

NAME: _____

DATE: _____

READING

Who's Driving?

What + Why: Compare two different investing strategies to figure out how decisions, fees, and long-term performance can impact how much your money actually grows.

Instructions:

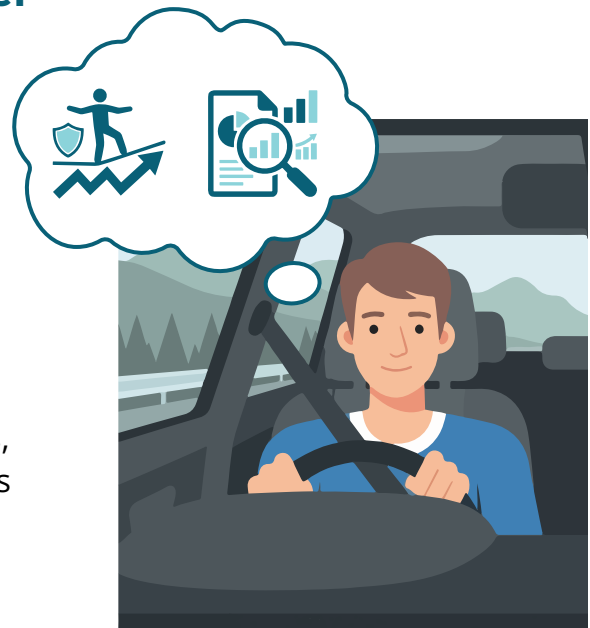
1. Read the provided text and be prepared to discuss with the class.
2. As you read, complete the Active vs. Passive Investing chart to organize your thinking.

Active vs. Passive Investing

When people invest, they bring different goals, values, and priorities to their decisions. For many, the goal is to grow money over time. But how they pursue that, and what they're willing to trade off to get there, can look very different. Some investors take a very hands-on approach, making deliberate choices about where their money goes. Others take a step back and let their money follow the broader market over time.

Active Investing: Taking the Wheel

Active investing is like trying to “drive” your investments to a better outcome. In this strategy, investors or professional fund managers make decisions about what to buy and sell. They use research, market trends, and predictions to try to beat the market, meaning they aim to earn higher returns than a benchmark like the overall stock market. A benchmark is a standard used to measure performance. Common examples include the S&P 500, which tracks 500 large U.S. companies, and the Dow Jones Industrial Average, which follows 30 major companies. When an active investor says they want to “beat the market,” they typically mean outperforming one of these benchmarks.

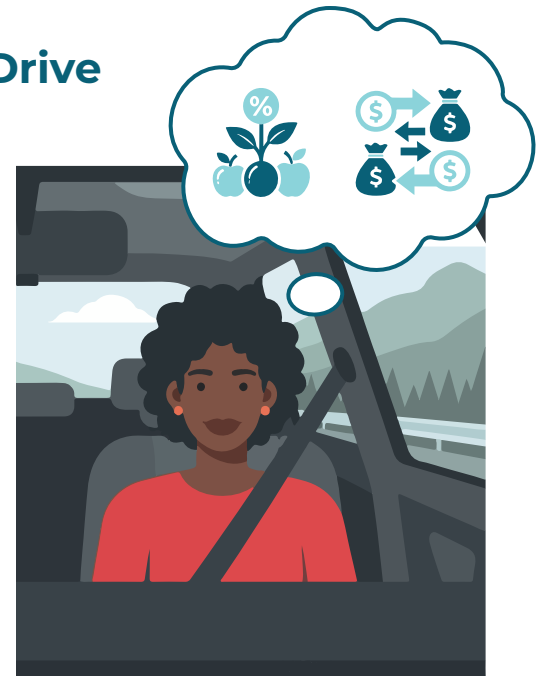


Because active investing involves frequent buying and selling along with ongoing decision making, it usually comes with higher fees. These fees pay for the time, research, and expertise required to manage the investments. One potential advantage of active management is that a fund manager can attempt to shift assets during a market downturn to limit losses, though this is not always effective and does not guarantee better outcomes than simply staying the course. However, even with all that effort, active investing does not guarantee better results. In fact, many active funds do not consistently outperform the market over long periods of time.

Passive Investing: Letting the Market Drive

Passive investing takes a different approach. Instead of trying to beat a benchmark like the S&P 500, passive investing aims to match it. Investors using this strategy typically invest in index funds or ETFs, which are designed to mirror the performance of a benchmark rather than outperform it. These funds automatically include a wide range of investments, creating built-in diversification.

Because there is little buying and selling, passive investing has lower fees and requires less ongoing management. Over time, passive investing focuses on long-term market growth over time rather than on trying to outperform the market in the short term, and it is designed to closely follow the performance of the market.



Looking at the Big Picture

Both active and passive investing aim to grow money over time, but they take different approaches to doing it. Some investors focus on making decisions to try to outperform the market. Others focus on following the market over time with fewer changes.

Because these strategies work differently, investors often look closely at how each one behaves over time when deciding which approach to use. Many investors don't stick to one strategy. Instead, they combine both. The mix of active and passive investments an investor chooses, along with how they divide money across stocks, bonds, and other assets, is called their asset allocation. How money is spread across and within different asset types helps determine the level of diversification.

Active vs. Passive Investing Chart

	Active Investing	Passive Investing
Goal <i>(What is this strategy trying to achieve?)</i>		
Trading Frequency <i>(How often are investments bought and sold?)</i>		
Fees (expense ratio) <i>(What costs are involved? Are they higher or lower?)</i>		
Risk of Underperforming Benchmark <i>(How likely is it to do worse than the market?)</i>		
Best suited for . . . <i>(What type of investor or goal does this strategy fit best?)</i>		

Key Terms

- **active investment strategy:** an approach to investing in which a manager or investor makes frequent decisions about buying and selling investments in an effort to outperform a market benchmark
- **asset allocation:** the process of spreading money across different types of investments (such as stocks, bonds, and cash) to manage risk and help achieve financial goals
- **benchmark:** a standard used to measure how well an investment performs relative to a particular market (stock, bond, REIT, etc.)
- **diversification:** the practice of spreading one's money across a range of investments to reduce the impact of a loss in any particular investment
- **passive investment strategy:** an approach to investing that aims to match the performance of a specific market index or benchmark, rather than trying to outperform it