MONEY

Go active to find picks that buck trend

Not every investment is poor when the market is flat – there is always value to be found.

Martin Hawes

I THINK the next few years will see activist, "stock-picking" type investors do better than passive ones. It is likely that, for the foreseeable future, investment markets (especially shares and property) will largely go sideways: sure, there will be some ups and downs as the markets wobble around, but major, permanent market gains seem unlikely to me.

This will mean investors cannot rely on the markets overall to deliver good returns, but will instead need to be very careful about the individual investments they buy. A passive investor is one who is happy to take what the markets dish out; an active investor, on the other hand, looks for the best investments and the best risk-adjusted returns they can possibly get.

Whether to take an active or a passive approach is a question of style. It is a question that all investors need to ask and answer for themselves – for my money, the call is "go active" at the moment.

Investor style is different from investor type. Investor type is about whether you are an aggressive, balanced or defensive investor: how much volatility you can tolerate and, therefore, the proportions you have in each main asset class.

Your investor type and the way you allocate your funds to each asset class is undoubtedly the most important part of investment – nevertheless, you should also be clear about your investment style, which manifests when deciding about which funds to invest in – or, if you do not want to manage your own investments, choosing between funds which are actively or passively managed.

Some managed funds simply track the index: computers tell the managers what they should buy or sell so that they perform exactly according to the index – management of the fund is entirely passive. Even some funds which call themselves "active" are little more than index huggers – they stay fairly close to the mainstream and do not make big investments that are much outside their weighting in the index.

On the other hand, there are managed funds that are very active – their managers make high conviction calls as they invest in companies which are outside the norm. These managers do a lot of research (including visits to companies) and are very careful which companies they include in their funds. They often have the ability to go to cash so that if they foresee a market fall, they can take defensive action.

There are several well-known fund managers in New Zealand that are active in this sense – for example Fisher Funds, Milford Asset Management, Elevation Capital and PIE Funds all try to add value beyond the average. Whether they are successful at this will depend on how good they are, but I think with markets unlikely to produce very good returns, an active approach is preferable at the moment.

This also applies to property investors: with a flat market, property is unlikely to be a lazy way to riches – it will not be one where you can buy any old thing and simply wait for a good return. Instead, property investors will need to be very careful about what they own, selecting properties very carefully according to their rental yields and in locations where they are likely to get good long-term rental growth.

To make money, property investors need to treat their investments like a business.

This means being in the right market and offering the "product" (that is, rental accommodation) that the customers (tenants) want. It also means very active management, looking after the property and its tenants, as well as keeping down costs and managing cash flow. With low returns driven by the overall market, you cannot afford to sit back and be passive.

Not every investment is poor when the market is flat – there is always value to be found and these will outperform the average. In fact, whether it is shares or property, good value is often more apparent when the overall market is lacklustre. Those prepared to look carefully for gems, whether fund managers or individuals, can do very well.

Martin Hawes is an authorised financial adviser and his disclosure statement is available free of charge at www.martinhawes.com. This article is of a general nature and no substitute for personalised financial advice.