ACTIVE PORTFOLIO MANAGEMENT

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The goal of any active portfolio manager is to get investment decisions right so that the returns of a portfolio are greater than a benchmark. The positive difference between the return for a portfolio relative to a benchmark is referred to as alpha. Active portfolio managers strive to create alpha, which long term, on average, is hard to do. In the short term, because of significant volatility, it is possible to "make the right bet," however, the ability to make accurate predictions is both intellectually and physically demanding. The selection of securities should be primarily driven by fundamental research and analysis and should be supported by quantitative techniques. Technical analysis is used as a tool in active tactical asset allocation. Technicians chart price movements, volume data, and changes of direction in both to learn something about the future direction of the market and individual securities.

If someone tells you that they are "active" in the stock market, you will want to know what tools and techniques they are using as the basis to make their active investment decisions. Understanding a 200-day Simple Moving Average (SMA) as an active technical analysis tool to make buy or sell decisions is an excellent foundation and starting point to start to better understand other active investment strategies. By simply understanding one active strategy, an average investor can begin to become not only knowledgeable but also eventually more critical on evaluating various tactical and active investment strategies.

There is a lot of investment "information" on social media now. Most of it is not good "advice". Be wary of unsolicited investment advice, ensure that your Investment Advisor is registered with Securities Board of India (SEBI). An active and qualified Portfolio Manager should be able to distill complex information and strategies and communicate them in a simple, understandable manner.

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The first and easiest technical chart for any investor to understand is the 200-Day Simple Moving Average (SMA). Charts are used to provide buy and sell signals. We will use the iShares MSCI India ETF (INDA), to show how the 200-Day Simple Moving Average (SMA) indicated buy & sell signals for three years and then use the Year-to-Date using the 50-day Simple Moving Average (SMA) to look at how changing one parameter impacts the frequency of the buy and sell signals.

Strategic Asset Allocation Versus Tactical Asset Allocation

Strategic Asset Allocation:
Strategic Asset Allocation seeks to identify and maintain a portfolio asset allocation appropriate for an investor's financial goals, investment objective, time horizon, and volatility tolerance. Strategic Asset Allocation:
• Makes no attempt to predict the direction or magnitude of short-term market volatility;
• Is characterized by a fixed target allocation to each asset class in an investor's portfolio; and
• Requires periodic portfolio rebalancing to maintain the target allocation to each asset class.

Tactical Asset Allocation:
Tactical asset allocation attempts to improve upon the performance of strategic asset allocation and attempts to predict the direction or magnitude of short-term price volatility. With a tactical strategy, the investor periodically alters the asset allocation based upon forecasts of regional, country, asset class, sector, and individual security returns. Fundamental and technical analysis are used in the investment decision making process.

In our example, we would expect that an Active Portfolio Manager, when comparing against the relevant benchmark of the iShares MSCI India ETF, using any strategy, would be outperforming the ETF performance of a 3-Year Return of 47.85% as the benchmark performance.

Fundamental Analysis
The purpose of looking at sectors and individual stocks is to determine which of those is the strongest and weakest within the broader market. Technicians do not perform any sort of fundamental analysis, since they believe this information is effectively already priced into the market. Technicians focus on price and volume movements and trends, rather than the inherent value of a security.

Fundamental analysis focuses on the intrinsic value of a security using various valuation models (FCFE, P/E, EV/EBITDA, P/BV, DDM) and compares the resulting price versus the market price to try to identify mispriced securities. Underpriced securities are bought and overpriced sold. Decisions are based on the strength of the valuation model.

Technical Analysis

**Introduction to Technical Indicators as an Active Buy or Sell Signal**
The most basic and easiest to understand technical indicator is the 200-Day simple moving average (SMA). Add up the prices of a security or index for 200 days and divide by 200. A 200-Day SMA smooths out shorter term volatility and creates a trend line that longer term on average is easy to see. Broad market movements like a bear market and then a bull market recovery will make the price or performance graph line cross the moving average line. A saying in technical analysis is "the trend is your friend." A 200-Day SMA longer term on average shows clear trend lines.

More frequent and therefore more active trading signals and strategies can be built. We will look at the 50-Day SMA as another easy-to-understand foundational example.

The "Rules" for using a Simple Moving Average (SMA) as a Buy or Sell Signal are:
• When the price or performance chart crosses the 200-Day SMA from below, it is a buy signal.
• When the price or performance chart crosses the 200-Day SMA from above, it is a sell signal.
• Using a 200-Day SMA provide a pretty good base for a more passive buy and hold strategy with periodic rebalancing.
• Easy to understand and long term on average, easy to implement for broader decision making.
• One issue is confusion in flat, sideways market - like Year-to-Date 2022 for example where the price line crosses back and forth more frequently.

iShares MSCI India ETF (INDA): 3-Year Performance Graph + 47.85%

https://app.koyfin.com/share/bbe4c5463f
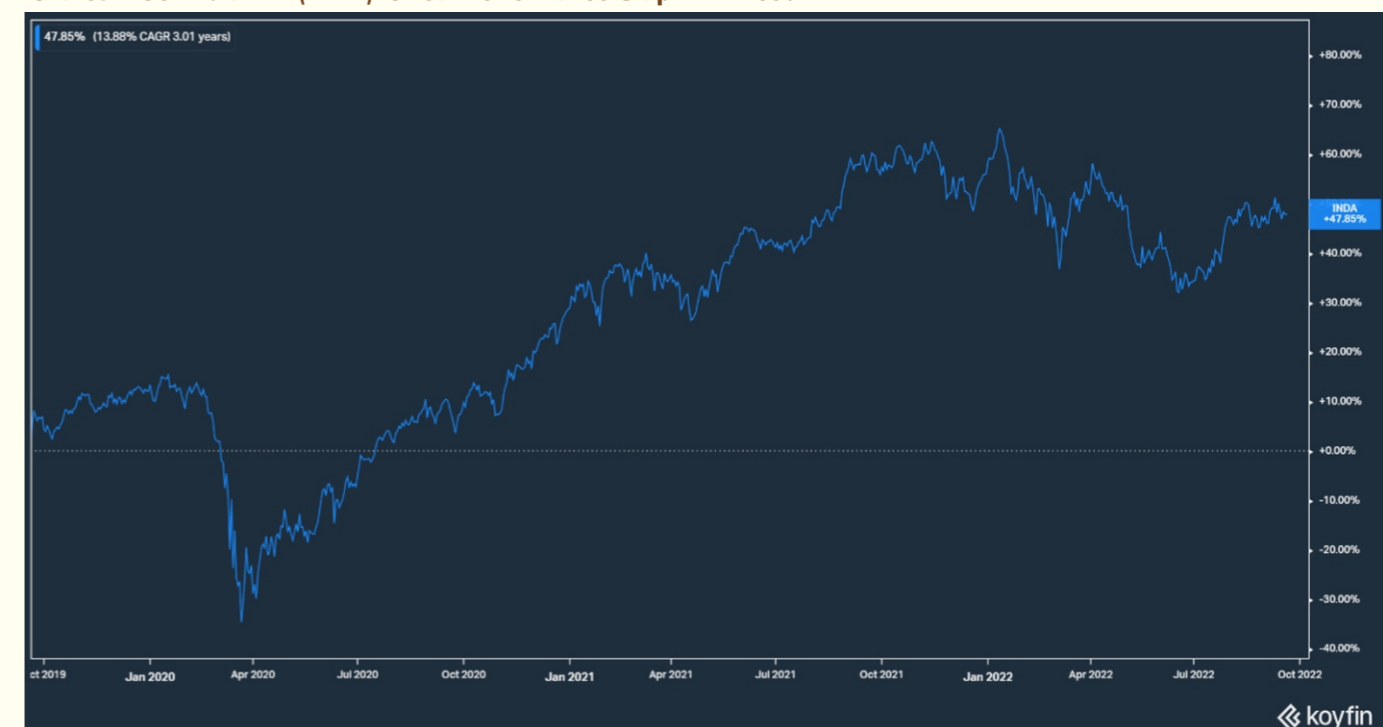
iShares MSCI India ETF (INDA):

- iShares MSCI India ETF (INDA) has a performance of a 3-Year Return of 47.85% September 20, 2022.
- That compares very well relative to the iShares S&P 500 ETF (IVV) of 34.73% for the same period.
- There is a very high correlation between the market movements of INDA vs IVV.

iShares MSCI India ETF (INDA): 3-Year Performance Graph with 200-Day Simple Moving Average (SMA)

https://app.koyfin.com/share/244e1f615b

- In the 3-Year INDA Performance Graph, there is a clear buy signal around July 2020.
- In the 3-Year INDA Performance Graph, there is a clear sell signal early in 2022.
- Year-to-Date (YTD) we can see the market direction is negative, that the trend line is dropping and that it crosses the price line more frequently in 2022.

Increasing Trade Frequency by Changing Technical Input Parameters.

iShares MSCI India ETF (INDA): 3-Year Performance Graph with 200-Day & 50-Day SMA

https://app.koyfin.com/share/c845ea63b2

- In the chart above, we added the 50-Day SMA, and you can see that it cuts the price line much more frequently than the 200-Day SMA. Many more.
- By changing a technical parameter, we changed the frequency for trading.
- Apply this principle to then any market data driven model - what are the rules and reasons for the buy and sell signals?
- In this example, we would expect that an Active Portfolio Manager, when comparing against the relevant benchmark of the iShares MSCI India ETF, using any strategy, would be outperforming the ETF performance of a 3-Year Return of 47.85% as the benchmark performance.

> **Understanding a 200-Day Simple Moving Average (SMA) as an active technical analysis tool to make buy or sell decisions is an excellent foundation and starting point to start to better understand other active investment strategies and to quickly visualize the broader market trend line.**

Summary & Conclusions

If someone is giving hot stock tips or investment advice, it means that they have a belief in a tool, and or a model, and a technique to predict the price movement. Security markets are efficient. Price movements come from not only systemic risks that affect the macro economies globally, but also from company specific risks. Long term on average it is very difficult to outperform the broader market by making active buy and sell decisions. It is very difficult to accurately predict future prices. There are too many macro and micro factors that affect security prices. However, understanding various tools, models and techniques can provide much insight for the average investor. Understanding a 200-Day Simple Moving Average (SMA) as an active technical analysis tool to make buy or sell decisions is an excellent foundation and starting point to start to better understand other active investment strategies and to quickly visualize the broader market trend line. Fundamental and Technical analysis is also used in a wide range of career opportunities as well such as Institutional Equity & Fixed Income Sales and Trading, Investment Banking, Research Analyst and Associate, Portfolio Manager, and other roles.

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His professional credentials include an MBA from the Ivey School of Business in Canada (1994), the Chartered Financial Analyst designation from the CFA Institute (2003) and Certified Financial Planner designation in 2010. He also held the CMA & CPA designations but now retired.

In addition to his teaching duties at George Brown College, Ted served as a consultant to Financial Planning Standards Board Ltd. (FPSB) as Head of Learning and contributed content to the new FPSB India Ltd. CFP Program.

Currently he is also a CFA® Exam Prep Training Provider with Wiley. For more information visit his website at WWW.ProfTed.com.