



THE SCIENCE BEHIND THE NUMBERS: PART 1 - WHY INDEX?

It is our responsibility here at Hummel Financial Group to provide clients with the greatest probability of long-term investment success. To do so, it is critical to understand the sources of returns, and the likelihood that we can deliver returns consistently over time. To shape our understanding we analyze stock market data to compare the investment returns between passive and active investing.

What is the difference between active and passive investing?

- **Passive (Index) Investing:** is a portfolio management strategy where the portfolio tracks a market weighted index, replicating the investment weighting and returns of a benchmark index.
- **Active Investing (Mutual Funds, Investment Counsel, Stock Picking Strategies):** is a portfolio management strategy where the manager makes specific investments with the goal of outperforming an investment benchmark index.

So what do the numbers say? Do actively managed funds outperform passively invested indexes, or is it against the odds to beat the market over a long time horizon? Our answer to these questions lies in dissecting numerous years of mutual fund and stock market data.

The Results...

- Based on one-year performance data, **63.43%** of U.S. Domestic Funds, and **93.22%** of CDN Domestic Funds underperform the market.
- Based on three-year performance data, **83.40%** of U.S. Domestic Funds, and **91.04%** of CDN Domestic Funds underperform the market.
- Based on five-year performance data, **86.72%** of U.S. Domestic Funds, and **81.69%** of CDN Domestic Funds underperform the market.
- Based on ten-year performance data, **86.65%** of U.S. Domestic Funds, and **91.86%** of CDN Domestic Funds underperform the market.

(See Exhibit 1 on page 2 for the specific performance data figures on the U.S. Equity Market, and Exhibit 2 for data on the CDN Equity Market and data sourcing.)





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Exhibit 1: SPIVA U.S. Scorecard - Percentage of U.S. Equity Funds Outperformed by Benchmarks

Fund Category	Comparison Index	1-Year (%)	3-Year (%)	5-Year (%)	10-Year (%)	15-Year (%)
All Domestic Funds	S&P Composite 1500	63.43	83.40	86.72	86.65	83.74
All Large-Cap Funds	S&P 500	63.08	80.56	84.23	89.51	92.33
All Mid-Cap Funds	S&P MidCap 400	44.41	86.34	85.06	96.48	94.81
All Small-Cap Funds	S&P SmallCap 600	47.70	88.83	91.17	95.71	95.73
Large-Cap Growth Funds	S&P 500 Growth	32.92	67.58	80.92	93.65	93.49
Large-Cap Core Funds	S&P 500	68.98	88.45	90.99	94.95	94.67
Large-Cap Value Funds	S&P 500 Value	46.88	80.37	85.07	70.44	85.71
Mid-Cap Growth Funds	S&P MidCap 400 Growth	18.05	91.46	81.13	97.69	95.32
Mid-Cap Core Funds	S&P MidCap 400	64.67	88.24	87.90	96.15	96.51
Mid-Cap Value Funds	S&P MidCap 400 Value	43.14	75.41	81.54	88.04	88.89

SOURCE: S&P DOW JONES INDICES LLC. DATA AS OF DEC. 29, 2017. RETURNS SHOWN ARE ANNUALIZED. PAST PERFORMANCE IS NO GUARANTEE OF FUTURE RESULTS. TABLE IS PROVIDED FOR ILLUSTRATIVE PURPOSES.



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Exhibit 2: SPIVA CDN Scorecard - Percentage of CDN Equity Funds Outperformed by Benchmarks

Fund Category	Comparison Index	1-Year (%)	3-Year (%)	5-Year (%)	10-Year (%)
All Canadian Equity	S&P TSX Composite	93.22	91.04	81.69	91.86
CDN Small/Mid Cap Equity	S&P TSX Completion	93.55	75.68	60.00	77.59
CDN Dividend & Income Equity	S&P TSX Canadian Dividend Aristocrats	42.11	53.66	59.52	100.00

SOURCE: S&P DOW JONES INDICES LLC. FUNDATA. DATA AS OF DEC. 29, 2017. CIFSC CATEGORIZATION ARE USED. FINANCIAL INFORMATION PROVIDED BY FUNDATA CANADA INC. TABLE IS PROVIDED FOR ILLUSTRATIVE PURPOSES. PAST PERFORMANCE IS NO GUARANTEE OF FUTURE RESULTS.

What the Numbers Tell Us, and our Resulting Strategy...

We base our investment strategy on empirical market research. The data tells us that the majority of active fund managers fail to outperform their respective indexes and that this underperformance trend increases as the investment time horizon lengthens. For this reason we construct the foundation of our client's portfolio's with index investments.

Market research reveals that passive investing provides consistently stronger returns over the long-run. The sometimes superior returns of actively managed funds are short-term in nature, and benchmark outperformance is more due to fortunate timing of the fund's investment style than the skill of the fund manager.

The science behind the numbers tells us that a well-constructed portfolio of diversified passive index investments has the highest probability of long-term success. This is why indexing is core to our investment philosophy, and directs our investment decision making.



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Sources:

1. S&P Dow Jones Indices LLC, a part of S&P global. (2018). SPIVA U.S. Scorecard. Retrieved from S&P Dow Jones Indices (<https://us.spindices.com/resource-center/thought-leadership/spiva/>)
2. S&P Dow Jones Indices LLC, a part of S&P global. (2018). SPIVA Canada Scorecard. Retrieved from S&P Dow Jones Indices (<https://us.spindices.com/resource-center/thought-leadership/spiva/>)

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