Strategic vs. Tactical Investing

How do these investment approaches differ?

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Ever heard the term "strategic investing"? How about "tactical investing"? At a glance, you might assume that both these phrases describe the same investment approach.

While both approaches involve the periodic adjustment of a portfolio and holding portfolio assets in varied investment classes, they differ in one key respect. Strategic investing is fundamentally passive; tactical investing is fundamentally active. An old saying expresses the opinion that strategic investing is about time in the market, while tactical investing is about timing the market. There is some truth to that.[1]

Strategic investing focuses on an investor's long-range goals. This philosophy is sometimes characterized as "set it and forget it," but that is inaccurate. The idea is to maintain the way the invested assets are held over time, so that through the years, they are assigned to investment classes in approximately the percentages established when the portfolio is created.[1]

Picture a hypothetical investor. Assume that she starts investing and saving for retirement with 60% of her invested assets held in equities and 40% in fixed-income vehicles. Now, assume that soon after she starts investing, a long bull market begins. The value of the equity investments within her portfolio increases. Years pass, and she checks up on the portfolio and learns that much more than 60% of the value of her portfolio is now held in equities. A greater percentage of her portfolio is now subject to the ups and downs of Wall Street.

As she is investing strategically, this is undesirable. Rebalancing is in order. By the tenets of strategic investing, the assets in the portfolio need to be shifted, so that they are held in that 60/40 mix again. If the assets are not rebalanced, her portfolio could expose her to more risk than she wants – and the older she gets, the less risk she may want to assume.[1]

Tactical investing responds to market conditions. It looks at the present and the near future. A tactical investor attempts to shift the composition of a portfolio to reduce risk exposure or to take advantage of hot sectors or new opportunities. This requires something of an educated guess – two guesses, actually. The challenge is to appropriately decide when to adjust the portfolio in light of change and when to readjust it back to the target investment mix. This is, necessarily, a hands-on style of investing.[1]

Is it better to buy and hold, or simply, to respond? This question has no easy answer, but it points out the divergence between strategic and tactical investing. A strategic investor may be inclined to "buy and hold" and ride out episodes of Wall Street turbulence. The danger is in holding too long – that is, not recognizing the onset of a prolonged downturn that could bring losses without much hope for a quick recovery. On the other hand, the tactical investor risks buying high and selling low, for figuring out just when to increase or decrease a portfolio position can be difficult.

Investors have debated which strategy is better for decades. One approach may be better suited than another at a particular point in time. Adherents of strategic investing point to the failure of active asset management to beat the equity benchmarks. A 2018 Dow Jones Indices SPIVA Report noted that across the five years ending June 30, 2018, more than 76% of U.S. large-cap funds failed to return better than the S&P 500. A proponent of tactical investing might counter that by arguing that this percentage might be much lower within a shorter timeframe. Ultimately, an investor has to consider their risk tolerance, objectives, and investing outlook in evaluating both approaches.[2]

Citations.

1 - money.usnews.com/investing/investing-101/articles/2018-07-25/whats-the-difference-between-strategic-and-tactical-asset-allocation [7/25/18]
2 - us.spindices.com/spiva/#/reports [2/5/19]