

MARKET TIMING: It's back – as “tactical asset allocation”

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PALM BEACH, Fla. -- Market timing, which fell out of favor among institutional investors more than a decade ago, is making a comeback under a new moniker, “tactical asset allocation.”

Greater emphasis on global investing and an outpouring of new derivatives based on foreign stock-market indexes now make it more feasible to boost returns by jumping in and out of markets, say money managers attending the ninth annual Asset Allocation Congress here.

“This year we're starting to see (tactical asset allocation) applied in emerging markets, where results can be very interesting,” says Robert Arnott, president of First Quadrant Corp., a leading practitioner.

Foreign markets give managers additional opportunities to hunt for mispriced assets. And the surge in global derivatives is rapidly bringing down trading costs. “It seems as though every single country now has a stock-index-futures contract and a bond futures contract,” says Mark Riepe, vice president at Ibbotson Associates.

Panagora Asset Management launched a global tactical asset allocation product three years ago. It's offered a similar product comprising US stocks and bonds for 11 years and has outperformed a passive benchmark in 10 of those years, says marketing director Bob Casey.

Many investors remain skeptical. “Any deviation from a long-term position is a bet,” says William Jacques, executive vice president and chief investment officer of Martingale Asset Management. “It's market timing--and a rose by any other name still has thorns.”

Catching the next market blip is out

Speaking at the three-day conference that began Monday, Jacques cited well-known academic studies from the 1960s, '70s and '80s, which found that mutual-fund managers rarely improve their results when they try to time the stock market.

But Robert Marchesi, president of consulting firm DeMarche Associates, says a longer time horizon makes “tactical asset allocation” essentially different from long-discredited market timing.

Marchesi defines a tactical move as one with a span of six months to three years. He says such asset shifts aren't predicated on catching the next immediate blip in the market. That is the province of market timing, which Marchesi defines as changes in asset mix based on a time horizon of up to six months or, alternatively, attempts to capture or sidestep a 5% market move.

Marchesi says he's never found a manager who's able to anticipate short-term swings in either the stock or bond markets with a high degree of regularity.

On the other hand, he says managers can aid portfolio returns through tactical shifts designed to catch swings of 10% to 15% within a longer market cycle -- as well as "strategic" shifts covering up to two market cycles, or a maximum of 10 years.

Tactical managers rely on comparisons between measures such as earnings yields and interest rates, to identify asset classes that appear undervalued or overvalued.

"This is a discipline that tends to do best in weak and turbulent markets -- and tends to be rather boring for those years in between," says First Quadrant's Robert Arnott.