It's Time to Get Active Again!

Four reasons why active management makes sense now

Executive Summary

Index-based, passively-managed fund popularity does not compete with the value of disciplined active management for investors. Why?

- Market conditions are likely to change.
- Indexing may not make sense for all asset classes.
- Index popularity is producing stronger active managers.
- Statistics highlighting lackluster long-term results of the average active manager can blind plan sponsors to better-than-average active managers.

While it's no secret that passive investing has become hugely popular in recent years, long-term investing is complex, and one size rarely fits all. That is why MassMutual Funds advocates for a well-diversified approach that includes a prudent mix of active and passive investments tailored to the needs of long-term investors.

1 *Market conditions are likely to change.*

The long-running bull market in stocks since early 2009 has provided a favorable backdrop for passive investing, especially given the recent concentration of benchmark gains in a handful of the largest-capitalization stocks. In such an environment, a strategy that mimics an index will do well, whereas active managers may struggle to keep up.

However, markets are cyclical, and this situation can and probably will change. At the end of July 2017, the four largest components of the S&P 500® by index weight were Apple, Microsoft, Facebook, and Amazon.com. Alphabet, Inc.'s class A (GOOGL) and class C (GOOG) shares rounded out the top ten with the ninth- and tenth-largest components, respectively. All of these stocks have been on a tear lately, and any active manager who did not overweight them probably lagged the S&P 500®.

If the market were to enter a bear phase, or become choppier, or should market growth leadership rotate away from the largest index components noted above, the seemingly easy gains from indexing could become more problematic. In conditions like these, the top-down and bottom-up stock selection expertise of strong active managers may prove key to achieving benchmark beating results.

2 *Indexing may not make sense for all asset classes.*

When an asset class is less efficient, active managers may find more opportunities to add value for their clients. Bonds, for example, have long been acknowledged as an area where good managers can add value. On the equity side, a similar case can be made for smaller capitalization and international stocks, two groups where information is harder to come by, and comprehensive research can often uncover hidden value.

The strongest case for index-based investing can be made in the domestic large-cap equity space, where companies are thoroughly researched, and where there is little room for undiscovered value. Large-cap domestic index-based and passively managed funds make up important components of plan line ups. Even so, offering plan participants exposure to historically strong active, large-cap managers may prove favorable to long term returns.

3 *Index popularity is producing stronger active managers.*

Fee pressures and new fiduciary rules are forcing active managers to either up their game or close up shop. Gone are the days when investors willingly paid for active management and got "closet indexing" in return. What is left is a smaller core of high-conviction, highly skilled managers who are committed to delivering better-than-benchmark results (alpha) on behalf of long-term investors.

As a result, the current generation of active managers can potentially offer better results at a lower cost than previous generations of active managers. Although active management will nearly always cost more than passive management, the real test is whether an active manager can deliver benchmark-beating performance, net of fees, over a reasonably long period of time.

4 *Statistics highlighting active management's long-term under performance can be misleading.*

While past performance is no guarantee of future results, there are active managers whose funds perform favorably compared to their benchmarks over longer periods of time. For example, the MassMutual Funds include several funds in the domestic equity (even large-cap), international equity, and fixed-income categories that compare favorably with their benchmarks over 5- and 10-year periods as of June 30, 2017.

These funds are guided by some of the best-known money managers in the investment industry, managers who make it their explicit goal of delivering benchmark-beating results. MassMutual scours the investment landscape to bring clients what we consider to be the "cream of the crop" of proven portfolio management teams with specialized expertise in their respective areas, combining the best of both in-house and sub-advised single-manager and multi-manager funds.

How to "get active" again.

- ✓ **Look for benchmark beaters.** Research funds and managers who demonstrate a history of beating their benchmarks over longer periods of time and who demonstrate a process for doing so that you understand and in which you have confidence.
- ✓ **Focus on performance net of fees.** Passively managed funds always underperform their benchmark due to modest fees. An actively managed fund that beats its benchmark net of fees makes fees less relevant.
- ✓ **Diversify broadly**. Diversify across asset classes and subclasses (stocks versus bonds, large-caps versus small-caps, domestic versus international, etc.) and investment styles (growth versus value). We suggest diversifying across management styles (active versus passive) as well.
- ✓ **Maintain a long-term perspective.** Even great managers have off years and times when they are out of step with the markets.

For investors interested in getting more active management, the MassMutual Funds offer a broad selection of actively managed funds worth considering. Contact your MassMutual Funds representative and visit www.massmutualfunds.com for more information.

These funds are only available for sale to retirement plans and other eligible institutional investors. They are not available for sale to individual retail investors.

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from www.MassMutualFunds.com and should be read carefully before investing.

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MassMutual's focus is on maintaining the financial strength and stability of the company to meet future obligations and to serve the long-term interests of our customers. As a mutual company, MassMutual does not have stockholders, so our value as a company is not dependent upon short-term investor perception. The mutual structure also allows us to take a disciplined approach to growth.

- Mutually owned and independent for 165 years, providing retirement services for more than 60 years
- Named a top 100 company on the FORTUNE 500 (Fortune Magazine, 2016)
- $675 billion in assets under management as of 12/31/2016 (Assets under management include assets and certain external investment funds managed by OppenheimerFunds, Barings and other MassMutual subsidiaries)

Financial Strength Ratings:

- A.M. Best Company A++ Superior (top category of 15)
- Fitch Ratings AA+ Very strong (2nd highest category of 21)
- Moody's Investors Service Aa2 Excellent (3rd highest category of 21)
- Standard & Poor's AA+ Very strong (2nd highest category of 21)

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