

L.R.Hasanova
educational affairs coordinator of Dual Degree Program,
Azerbaijan State Oil and Industry University PLE
ORCID 0000-0002-7596-0781
hasanova.leyla@asoiu.edu.az

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STRATEGIC APPROACHES TO INVESTMENT PORTFOLIO MANAGEMENT

Abstract

This article explores strategic approaches to investment portfolio management through a comparative analysis of active, passive, and hybrid models. The article is based on a structured literature review of studies on foundational portfolio theory, including research on developed, emerging, and frontier markets. Results of the review indicates that no single approach is universally superior. Passive strategies offer cost efficiency, broad diversification, and strong benchmark consistency, especially in relatively efficient markets and for long-term horizons. Active management, however, remains valuable in market environments where informational gaps, sectoral shifts, pricing anomalies, or macroeconomic instability create opportunities for security selection and tactical rebalancing. A central finding of the review is that hybrid strategies occupy an increasingly important place in portfolio management, especially core-satellite structures that combine a passive core with selective active overlays. Within cyclical framework of portfolio formation and management, portfolio management is treated not as a choice between opposing approaches, but as a continuous governance process of aligning objectives, risk preferences, market conditions, and managerial decisions.

Keywords: *portfolio management, active strategy, passive strategy, hybrid strategy, diversification.*

INTRODUCTION

Investment portfolio management holds a central place in modern financial decision-making because it translates broad investment objectives into a structured combination of assets, risk limits, and operating rules. From the traditional perspective of modern portfolio theory, the essential challenge is to obtain the most favorable relationship between expected return and risk through diversification, covariance management, and rational asset selection (Markowitz, 1952). At the same time, the strategic dimension of portfolio management extends well beyond mathematical optimization. Managers must determine how actively a portfolio should respond to market information, how often asset weights should be adjusted, which benchmark is the most appropriate, and whether consistent outperformance remains feasible once fees and transaction costs are taken into account.

The studies reviewed in this article suggest that the debate between active and passive management remains relevant, but its implications are more complex than a simple either-or choice. In an emerging-market simulation, Bama (2020) showed that a dividend-oriented buy-and-hold strategy could dominate speculative trading when price adjustment is slow and liquidity is limited. In contrast, studies on Indonesian equity markets found settings in which periodic active rebalancing and valuation-based selection improved portfolio performance relative to passive alternatives (Hidayat & Hendrawan, 2017; Hendrawan, Fadhyala, & Aminah, 2020). At the same time, cost-adjusted evidence from fund comparisons shows that passive investing often retains a structural advantage because expenses and turnover reduce the persistence of active alpha (Greenhill, 2014).

For enterprise investors, treasury departments, and institutional managers, the strategic question is therefore not simply whether active management is better than passive management. The more important question is how portfolio strategy should be matched with market efficiency, information quality, investment horizon, liquidity needs, and risk budget. Recent comparative discussions increasingly argue that a mixed architecture may be more effective than a pure binary choice, because a stable low-cost approach may be combined with tactical active positions aimed at specific opportunities or risk controls (Azouagh & Daoui, 2023; Baranova & Ivanov, 2023).

The purpose of this article is combine the reviewed studies into a coherent discussion of strategic approaches to investment portfolio management. The article first outlines the conceptual foundations of portfolio strategy, then compares active, passive, and hybrid models, and finally proposes a strategic cycle for portfolio formation and control. The contribution of the paper lies in showing that strategy should be treated as a continuous governance process rather than a one-time selection of portfolio style.

METHODOLOGICAL APPROACH AND THEORETICAL FOUNDATIONS

This study is conceptual in design and relies on comparative review and analytical synthesis. It is based on foundational theoretical sources and the selected studies dealing with active versus passive portfolio management, portfolio construction, valuation-based stock selection, emerging-market portfolio behavior, and performance evaluation. The reviewed studies cover different research designs, including theoretical comparison, simulation, fund analysis, and market-specific case studies. Their diversity is methodologically useful because it reveals not only the direct performance effects of strategic choices but also the contextual variables that shape these effects.

The analysis is based on three main pillars. First, modern portfolio theory establishes diversification as the core mechanism for reducing portfolio risk without sacrificing expected return. The strategic implication is decisive- portfolio quality cannot be inferred from isolated securities. It emerges from the interaction of securities within the portfolio as a system.

Second, the efficient market hypothesis provides the classical rationale for passive management. If prices absorb available information rapidly, repeated attempts to identify mispricing should, on average, fail to generate persistent abnormal return after costs (Fama, 1970). The rise in buy-and-hold and index replication techniques can be explained by this reasoning. The literature does, however, also highlight the drawbacks of rigid efficiency assumptions. Security selection and timeliness can be important in some situations due to behavioral considerations, informational frictions, and uneven price adjustment speed (Shefrin & Statman, 2000; Lo, 2004).

Third, strategic asset allocation broadens the discussion from security selection to policy design. Brinson, Hood, and Beebower (1986), and later Brinson, Singer, and Beebower (1991), argued that long-term asset allocation explains a very large share of return variation. Although the magnitude of this effect has been debated, the strategic lesson remains important - successful portfolio management depends not only on choosing securities, but also on determining policy weights, benchmark orientation, and the rules of revision. This insight is especially relevant in enterprise settings, where portfolio management is linked to overall capital allocation, liquidity preservation, and governance discipline.

Table 1

Comparative characteristics of strategic portfolio approaches

Criterion	Active management	Passive management	Hybrid
Strategic objective	Outperform a benchmark through selection, timing, and tactical repositioning.	Replicate or closely track benchmark return at low cost.	Combine market-matching stability with selective search for excess return.
View of market	Assumes exploitable inefficiencies or uneven information processing.	Assumes prices broadly reflect available information.	Accepts broad efficiency, but recognizes pockets of temporary mispricing.
Typical instruments	Stock picking, sector rotation, tactical asset allocation, valuation filters.	Index funds, ETFs, buy-and-hold, full or sampled replication.	Passive core with active satellite elements, factor tilts, or tactical overlays.
Main advantages	Flexibility, adaptation to volatility, customization, downside management.	Low fees, high transparency, broad diversification, tax and turnover efficiency.	Balances cost control with adaptability and strategic optionality.
Main limitations	Higher fees, turnover, model risk, benchmark underperformance after costs.	Limited outperformance potential, dependence on benchmark structure.	Requires governance discipline to prevent style drift and overlap.
Best strategic use	Less efficient, volatile, concentrated, or fast-changing market segments.	Long-horizon exposure to broad and relatively efficient markets.	Institutional or enterprise portfolios with layered objectives and active risk budgets.

Strategic Approaches to Portfolio Management

Active management

Active management aims to exceed the benchmark by making deliberate choices regarding securities, sectors, timing, and rebalancing intensity. The reviewed literature repeatedly associates active strategy with three operational levers: asset allocation, security selection, and market timing. In practical terms, this means that managers do not simply hold a diversified portfolio. They attempt to identify securities that are undervalued, sectors that may benefit from the business cycle, or moments when a change in portfolio weights can improve the expected risk-adjusted outcome.

Empirical evidence for active management is clearly conditional rather than universal. Hidayat and Hendrawan (2017) found that semiannual active portfolio strategies built with relative valuation indicators outperformed passive and annual active alternatives in their setting, suggesting that review frequency and the quality of valuation filters matter. Likewise, Hendrawan et al. (2020) showed that portfolios formed around selected financial ratios, especially low Tobin's Q and high PBV groups, could generate attractive combinations of return and risk, with active semester rebalancing being especially effective for investors willing to modify portfolio composition as information changes.

Active strategy becomes even more relevant in environments that are structurally less efficient. Bama (2020) examined an emerging market context and determined that the best strategic response depends on how price formation actually works in that market. In low liquidity environments with rare price changes, excessive trading may not be rewarded, but information about dividends, issuer quality,

and delayed price adjustment may still provide value for the investor. This indicates that active management should not be limited with rapid turnover only. In some contexts, active management is better understood as informed selectivity and disciplined tactical patience.

Nevertheless, active management faces structural disadvantages. Greenhill (2014) emphasized that management fees and turnover can neutralize much of the incremental gross return generated by active managers.

Passive management

Passive management is based on the view that a portfolio should reflect the market rather than consistently aim to beat it. Its core practices include buy-and-hold investing, index tracking, and low-turnover replication. From a strategic viewpoint, this method cuts through decision clutter by focusing efforts on benchmark choice, replication techniques, and sustained oversight of costs, taxes, and diversification over long-term period.

The literature provides strong support for the structural efficiency of passive management. Greenhill (2014) concluded that active equity funds were not, overall, a more cost-effective investment tool than passive funds, even though some short subperiods favored active products. Azouagh and Daoui (2023) also emphasize that passive management offers lower costs, greater simplicity, and broader diversification, especially when the investor's objective is not to maximize tactical alpha but to obtain stable exposure to a chosen benchmark. Mahmood (2025), writing in the context of the Iraqi securities market, demonstrates that passive portfolio design can still be analytical and sophisticated rather than naive, even within passive construction, beta sensitivity, concentration, and security selection remain strategically meaningful.

Passive management is especially attractive when three conditions are present. First, the market segment is sufficiently broad and liquid for index replication to be reliable. Second, the investor's horizon is long enough for the cost savings of passive implementation to compound over time. Third, the principal objective is policy consistency rather than tactical outperformance. In such cases, passive management is not a passive intellectual choice- it is a deliberate strategic decision to prioritize efficiency, transparency, and benchmark consistency.

At the same time, passive strategy has its limitations. Benchmark construction may concentrate capital in specific sectors or large issuers, and pure replication may underreact to regime changes, structural breaks, or enterprise-specific risk. That is why passive management should be viewed as efficient, but not sufficient in every context. Where the investment policy contains multiple objectives- such as inflation protection, liquidity tiers, capital preservation, or selective thematic exposure- passive exposure may need to be supplemented rather than used in isolation.

Hybrid approach

An increasingly common conclusion in the reviewed literature is that active and passive strategies should not be viewed as strict alternatives. Azouagh and Daoui (2023) explicitly recommend a hybrid structure in which the passive core captures average market performance at low cost, while actively managed satellites pursue selective opportunities. Baranova and Ivanov (2023) reach a similar conclusion by arguing that effective portfolio management should combine asset allocation as a passive component with security selection as an active component.

The hybrid approach is strategically attractive because it separates objectives. The core portfolio can be aligned with long-term policy exposure, liquidity thresholds, or market-equivalent return. Satellite sleeves can then be devoted to sector rotation, valuation anomalies, defensive hedging, ESG (environmental, social, and governance) preferences, or tactical inflation response. This layered structure also improves governance. Instead of asking active management to outperform everywhere, the enterprise can define where active risk is permitted, how much tracking error is acceptable, and under which conditions active positions must be reduced.

From the perspective of enterprise capital management, the hybrid model is especially useful because it combines the logic of strategic planning. Firms usually pursue multiple financial objectives.

They require income stability, capital preservation, liquidity for operating needs, and selective growth opportunities. A hybrid portfolio architecture allows these needs to coexist within one strategic system. In that sense, the future of portfolio management is a more disciplined integration of both.

Table 2

Analytical synthesis of selected reviewed studies

Study	Context	Approach	Main finding	Strategic implication
Bama (2020)	West African regional market	Simulation of dynamic vs. passive behavior	Buy-and-hold and dividend anticipation were more effective than speculation on price fluctuations.	Passive or low-turnover strategies may dominate when liquidity and price discovery are weak.
Hidayat & Hendrawan (2017)	Indonesia, LQ-45	Relative valuation portfolios under active and passive strategies	Semiannual active strategy produced the strongest overall performance sequence.	Active strategy can add value when valuation filters and review intervals are well designed.
Hendrawan et al. (2020)	Indonesia, SRI-KEHATI	Tobin's Q and PBV portfolio simulations	Low Tobin's Q generated high returns with high risk; high PBV showed attractive return with lower risk.	Risk tolerance should shape choice of ratio-based active or passive implementation.
Greenhill (2014)	US mutual fund evidence	Cost-adjusted active vs. passive fund comparison	Passive funds were not, overall, inferior after costs; active advantage was inconsistent across horizons.	Fees and turnover are central in strategic evaluation.
Hilsted (2012)	Benchmark-driven active management	Strategic + tactical asset allocation with mean-variance construction	Active portfolios did not beat the benchmark in raw return, but generated value in risk-adjusted terms.	Active management should be assessed net of benchmark risk, not only by headline return.
Azouagh & Daoui (2023)	Theoretical review	Comparative analysis of active and passive management	Active offers higher upside but with higher fees and uncertainty; passive is cost-efficient but limited in outperformance.	Core-satellite integration is a pragmatic compromise.
Baranova & Ivanov (2023)	Comparative review	Assessment of active and	Neither pure active nor pure passive	A combined framework of asset allocation and

		passive efficiency	dominates under all conditions.	security selection is preferable.
Mahmood (2025)	Iraqi stock market	Passive portfolio formation with fuzzy time series	High-beta passive portfolios achieved the best return-risk balance but remained sensitive to sector concentration.	Passive design still requires careful portfolio engineering in unstable markets.

4. Implications for Enterprise Portfolio Management

For enterprise investors, portfolio strategy cannot be separated from corporate financial policy. The portfolio is not merely a collection of securities - it is part of a broader system of capital preservation, income generation, liquidity planning, and strategic flexibility. Consequently, the choice of active, passive, or hybrid management should reflect the firm's operating cycle, cash-flow uncertainty, funding structure, and tolerance for valuation volatility.

A purely active strategy may be justified when the enterprise has strong internal analytical capacity, operates in markets characterized by weak efficiency, or seeks tactical positioning around sectoral and macroeconomic developments. However, such a strategy requires explicit governance mechanisms: benchmark choice, position limits, review frequency, stop-loss or replacement rules, and post-trade evaluation criteria. Without these, active management can deteriorate into discretionary trading without strategic coherence.

A purely passive strategy is more appropriate when the enterprise prioritizes transparency, low operational burden, and reliable market exposure. This is especially true for reserve portfolios, pension-related balances, or medium-term capital that should not be exposed to frequent tactical change. Yet the evidence reviewed in this article suggests that passive implementation should still be engineered carefully. Concentration risk, beta exposure, and liquidity profile must be monitored even if the portfolio broadly tracks a benchmark.

For many firms, the strongest strategic solution is a layered model. The core portfolio can be indexed or rules-based, ensuring stable diversification and lower cost. A satellite sleeve can then be devoted to valuation opportunities, sector tilts, or defensive adjustments during periods of macroeconomic stress. This arrangement preserves discipline while still allowing the portfolio to respond to changing conditions. In enterprise practice, such a model also improves accountability because active risk is visible, limited, and reviewable.

CONCLUSION

The comparative analysis of the reviewed literature leads to three main conclusions. First, the strategic debate in portfolio management should not be reduced to a simple active-versus-passive opposition. The relative performance of each approach depends on market efficiency, transaction costs, benchmark structure, information quality, and investment horizon. Second, passive management retains a strong structural advantage in cost efficiency, diversification, and long-term benchmark consistency. Third, active management remains strategically important where valuation dispersion, market conditions, or macroeconomic instability create opportunities that justify the assumption of active risk.

The most persuasive synthesis emerging from the reviewed studies is that portfolio management should be organized as a cyclical and layered process. A robust strategic system defines investment policy first, chooses an appropriate strategic architecture second, and only then proceeds to security analysis, construction, revision, and evaluation. Within such a system, hybrid models - especially core-satellite structures - appear particularly well suited to modern portfolio management because they combine the discipline of passive exposure with the selectivity of active intervention.

Accordingly, strategic approaches to investment portfolio management should be assessed not by ideological preference, but by their capacity to align portfolio behavior with investor objectives, risk tolerance, and market conditions. In academic as well as practical terms, the most effective portfolio strategy is the one that transforms diversification, information, and monitoring into a coherent management system.

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L.R.Həsənova

*İkili Diplom Proqramının tədris işləri üzrə koordinatoru,
Azərbaycan Dövlət Neft və Sənaye Universiteti PHŞ
ORCID 0000-0002-7596-0781*

İnvestisiya portfelinin idarə edilməsinə strateji yanaşmalar

Xülasə

Bu məqalədə investisiya portfelinin idarə olunmasına dair strateji yanaşmalar aktiv, passiv və hibrid modellərin müqayisəli təhlili əsasında araşdırılır. Tədqiqat portfel nəzəriyyəsinin fundamental əsaslarına, habelə inkişaf etmiş, inkişaf etməkdə olan və sərhəd bazarlarını əhatə edən elmi araşdırmaların strukturlaşdırılmış ədəbiyyat icmalına əsaslanır. Aparılmış icmalın nəticələri göstərir ki, heç bir yanaşma bütün şəraitlər üçün universal üstünlüyə malik deyildir. Passiv strategiyalar, xüsusilə nisbətən səmərəli bazarlarda və uzunmüddətli investisiya üföqlərində, xərc səmərəliliyi, geniş diversifikasiya və “benchmark” üzrə yüksək uyğunluq baxımından mühüm üstünlüklər nümayiş etdirir. Bununla yanaşı, informasiya boşluqları, sektorlararası dəyişikliklər, qiymət anomaliyaları və ya makroiqtisadi qeyri-sabitlik səbəbindən qiymətli kağızların seçilməsi və taktiki yenidən balanslaşdırma üçün imkanların yarandığı bazar mühitlərində aktiv idarəetmə öz aktuallığını qoruyub saxlayır. İcmalın əsas nəticələrindən biri ondan ibarətdir ki, hibrid strategiyalar, xüsusilə passiv əsas hissəni seçilmiş aktiv əlavələrlə tamamlayan “core-satellite” strukturları, portfel idarəçiliyində getdikcə daha mühüm mövqə tutur. Portfelin formalaşdırılması və idarə olunmasının dövrü təbiəti çərçivəsində portfel idarəçiliyi bir-birinə zidd yanaşmalar arasında seçim kimi deyil- məqsədlərin, risk toleranlığın, bazar şəraitinin və idarəetmə qərarlarının uzlaşdırılmasına yönəlmiş fasiləsiz idarəetmə prosesi kimi nəzərdən keçirilir.

Açar sözlər: portfel idarəçiliyi, aktiv strategiya, passiv strategiya, hibrid strategiya, diversifikasiya.