

Index Fund Strategies

# ASSET CLASS

A monthly update of asset class performance, trends, & topics for long-term investors

## Index Returns

|                     | 1996 | 1997  | 1998  | Last 6 yrs. | 6/23 1999 |
|---------------------|------|-------|-------|-------------|-----------|
| <b>Bonds</b>        |      |       |       |             |           |
| Short-term          | 5.8  | 6.0   | 5.7   | 5.4         | + 2.0     |
| Intermediate        | 2.4  | 9.2   | 10.5  | 7.7         | - 4.3     |
| Long-term           | -1.3 | 14.3  | 12.0  | 8.9         | - 7.1     |
| Global              | 10.8 | 8.3   | 8.4   | 8.3         | + 2.3     |
| <b>U.S. stocks</b>  |      |       |       |             |           |
| Large Market        | 22.9 | 33.2  | 28.7  | 21.4        | + 9.1     |
| Large Value         | 20.2 | 28.1  | 12.0  | 18.3        | + 14.4    |
| Small Market        | 18.2 | 24.6  | -5.5  | 12.4        | + 6.4     |
| Small Value         | 22.3 | 30.7  | -7.3  | 16.0        | + 8.3     |
| Real estate         | 33.8 | 19.3  | -15.4 | 8.2         | + 7.5     |
| <b>Int'l stocks</b> |      |       |       |             |           |
| Large Market        | 6.4  | 5.5   | 18.2  | 12.1        | + 6.3     |
| Large Value         | 7.8  | -3.1  | 14.9  | 13.5        | + 7.6     |
| Small Market        | 2.6  | -23.7 | 8.2   | 4.2         | + 16.8    |
| Small Value         | 1.0  | -22.7 | 5.3   | 3.7         | + 18.7    |
| Emerg. Mkts.        | 11.4 | -18.9 | -9.4  | 5.4         | + 42.5    |

### Descriptions of Indexes

|                    |                                 |
|--------------------|---------------------------------|
| Short-term bonds   | DFA One-Year Fixed Income fund  |
| Intermediate bonds | DFA Intermed. Gov't Bond fund   |
| Long-term bonds    | Vanguard Bond Index Long-term   |
| Global bonds       | DFA Global Fixed Income fund    |
| U.S. Large Market  | Vanguard Index 500 fund         |
| U.S. Large Value   | DFA Large Cap Value fund        |
| U.S. Small Market  | DFA US 6-10 fund                |
| U.S. Small Value   | DFA US 6-10 Value fund          |
| Real Estate        | DFA Real Estate Securities fund |
| Int'l Large Market | DFA Int'l Large Cap fund        |
| Int'l Large Value  | DFA Int'l Large Cap Value fund  |
| Int'l Small Market | DFA Int'l Small Company fund    |
| Int'l Small Value  | DFA Int'l Small Cap Value fund  |
| Emerging Markets   | DFA Emerging Markets fund       |

"Last 6 yrs." returns for U.S. Large Value (3/93), U.S. Small Value (3/93), Int'l Large Value (3/93), Int'l Small Market (10/96), Int'l Small Value (1/95), and Emerging Markets (5/94) include simulated data prior to fund inception (in parentheses).

This information is obtained from sources we believe are reliable, but we cannot guarantee its accuracy.

Past performance does not guarantee future returns.

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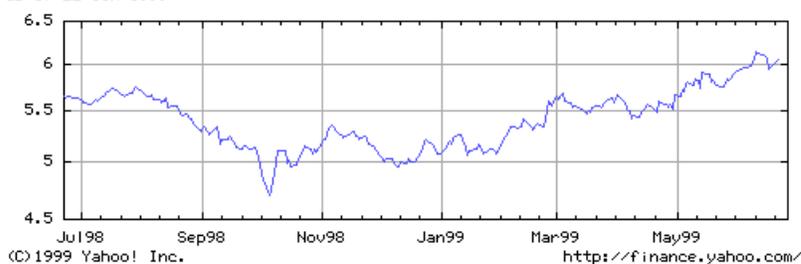
Editor: Jeffrey C. Troutner

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## Markets Update Wednesday, June 23, 1999

Value stocks have maintained their lead over growth stocks across all of the stock asset classes year-to-date. Small company stocks continue to lag, but are showing signs of strength. Overall, rising interest rates appear to be putting a damper on investor enthusiasm and causing some choppiness in the markets.

CBOE 30-year Yield as of 22-Jun-1999



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## Do-It-Yourself Investors Face a Harsh Reality

*Too many investors shoot themselves in the foot as they seek higher returns.*

*Jeff Troutner, TAM Asset Management, Inc.*

DALBAR Financial Services, an investment research company, released a study in 1994 that showed that do-it-yourself investors realized lower returns than investors using the services of "financial advisors." The study was originally funded by Merrill Lynch and the distinction between "do-it-yourselfers" and clients of advisors was basically one of no-load fund investors on the one hand and load fund investors on the other.

The manner in which the data from this study is used by some advisors can only be described as irresponsible, at best. To give you an idea of how good data can lead to good advice, but poor implementation, consider an article titled "Financial Advice Pays Bigger Returns" by Trimark Investments (a Canadian distributor of load funds). Here is the good advice:

Financial advisers can bring real value to investors because most people just don't have the time," says Elizabeth Hoyle, vice-president of marketing for Trimark Mutual Funds.

Financial advisers can help you determine your risk level, develop a plan and stick to it. Most importantly, financial advisers prevent people from panicking. It's reacting to short-term ups and downs that causes do-it-yourself investors to lose out by selling low and buying high.

As proof the article refers to the DALBAR study, updated through June 30, 1995, which showed that investors on their own realized an average total return of 79.5% compared to 96.4% for those working through an advisor.

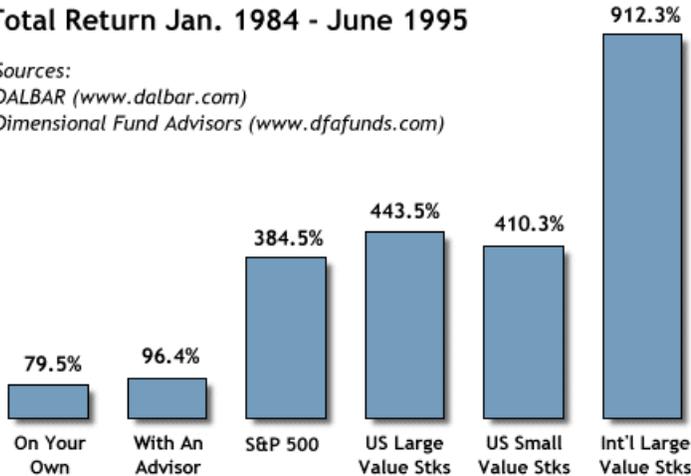
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Unfortunately, the article stops there. But there's more to the story:

### Total Return Jan. 1984 - June 1995

Sources:  
DALBAR ([www.dalbar.com](http://www.dalbar.com))  
Dimensional Fund Advisors ([www.dfafunds.com](http://www.dfafunds.com))



The DALBAR study found that do-it-yourself investors did not hold their equity mutual funds as long as clients of brokers and advisors. But what the chart above shows is that an investor who bought and held an *index fund* targeting any of the above asset classes (or all of them in a portfolio) would have done substantially better.

This is the approach most advisors specializing in indexed strategies espouse. The sad fact is investors who realize the pitfalls of active fund management and dealing with brokers who are compensated by fund sales loads, and choose instead to index, too often choose to index on their own. The biggest difference in the above returns is not due to the difference in passive (indexed) or active management, it's due to the lack of discipline, confidence, or experience that cause investors to give up too soon on a long-term strategy—all qualities a good advisor will possess.

When DALBAR updated their study for 1997 they eliminated the distinction between load and no-load fund investors. The reason for this is that the distinction has rapidly diminished due to the introduction of "Class" shares and the trend toward fee-based advice. Instead, they focused on "the average equity fund investor" and a "buy-and-hold" indexed investor.

Although the copy of the study I received does not provide the details of their methodology, it appears that DALBAR measures the performance of the average equity fund investor by looking at fund performance and inflows and outflows over the period measured. Based on their analysis, DALBAR concluded that:

***"Mutual fund investors earn far less than reported returns, due to their investing behavior.***

*While the Standard & Poor's 500 index returned over 17% per year (including reinvested dividends) for the 14-year period from 1984-1997, equity fund investors earned real returns of only 6.71% per year.*

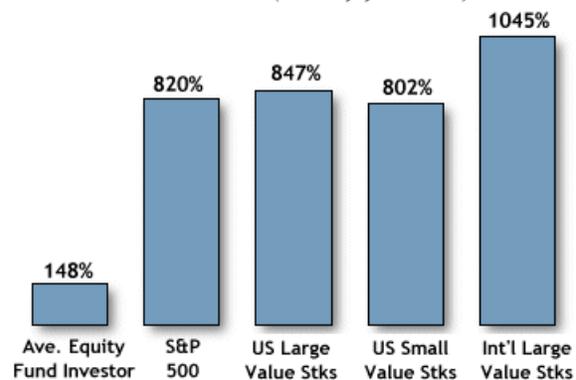
*This gap of 10% is explained by the behavior of equity fund investors. In their attempt to cash in on the impressive stock market gains, investors jump on the bandwagon too late, and switch in and out of funds trying to time the market. By not remaining invested for the entire period, they do not benefit from the majority of the equity market appreciation."*

DALBAR found that the retention rates for equity fund investors have actually fallen since the first study was completed. This is in spite of the fact that there has been a proliferation of educational materials and media coverage on the benefits of long-term investing.

Needless to say (I hope), the ten percent per year gap in returns cited by DALBAR is huge. On a total return basis, the numbers look like this:

### Total Return Jan. 1984 - Dec. 1997

Sources:  
DALBAR ([www.dalbar.com](http://www.dalbar.com))  
Dimensional Fund Advisors ([www.dfafunds.com](http://www.dfafunds.com))



A buy-and-hold investor in an S&P 500 fund would have realized returns 5 1/2 times higher than the average investor over this period! U.S. large value, U.S. small value, and international large value stock asset classes also performed exceptionally well over this period.

This study quantifies the difficulty individual investors have in staying with a long-term asset allocation and avoiding the temptation of market timing. I personally know how difficult it is because I have clients who sit through three hours of "reality training" initially and sometimes years of ongoing communication on the importance of "buy-and-hold", and still fall prey to the temptations of the "Dark Side."

Nevertheless, for those who lack the time, discipline, experience, or knowledge to implement and maintain an indexed portfolio over the long-term, a good advisor can add significantly to your bottom line.