



Index Fund Strategies

ASSET CLASS

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

Index Returns

	1997	1998	1999	Last 7 yrs.	6/14 2000
Bonds					
Short-term	6.0	5.7	4.6	5.3	+ 2.5
Intermediate	9.2	10.5	-3.6	6.0	+ 2.9
Long-term	14.3	12.0	-7.9	7.4	+ 6.2
Global	8.3	8.4	3.7	7.6	+ 2.4
U.S. stocks					
Large Market	33.2	28.7	20.8	21.3	+ 0.5
Large Value	28.1	12.0	4.8	16.3	- 0.9
Small Market	22.8	-7.3	29.8	16.5	+ 6.8
Small Value	30.7	-7.3	13.1	15.6	+ 5.0
Real estate	19.3	-15.4	-2.0	6.7	+ 15.9
Int'l stocks					
Large Market	5.5	18.2	28.5	14.3	- 3.6
Large Value	-3.1	14.9	16.3	13.9	- 1.1
Small Market	-23.7	8.2	21.9	6.6	+ 1.6
Small Value	-22.7	5.3	19.0	5.8	+ 0.7
Emerg. Mkts.	-18.9	-9.4	71.7	13.0	- 11.9

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 9-10 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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Markets Update Thursday, June 15, 2000

(No Market Update this issue)

A View of Dimensional Fund Advisors

Jeff Troutner, TAM Asset Management, Inc.

I just returned from three days of backpacking in the heart of Yosemite National Park. Yosemite, as many of you know, is an incredible scenic jewel consisting of huge granite monoliths like Half Dome and El Capitan and beautiful waterfalls like Yosemite, Vernal, Nevada, and Bridelveil Falls. All of these landmarks, including lesser-known ones such as Lost Arrow Spire¹ pictured on the right, can be seen from the top of Yosemite Falls—a 4 ½ mile hike 3,000 feet above the valley floor. Most of the visitors to Yosemite (and there are more than four million every year!) never venture more than a few feet from their tour buses or hotel rooms. It's just too easy and comfortable to stay where they are and look up.



I have to admit that during the trip when, among other things, I watched a dance troupe dangling from ropes off a sheer granite cliff a few thousand feet from solid ground (wallroom dancers, perhaps?), saw a bear run off through the woods afraid of *us*, and nearly stepped on a very annoyed rattlesnake, I thought of investments *maybe* once. But as I reflect on it, my experience in Yosemite can serve as a metaphor for an article I have been wanting to do on Dimensional Fund Advisors (DFA).

Like the landmarks of Yosemite, DFA rises above the crowd and has a quality and pureness to it that is very unique. And like the hike to the top of Yosemite Falls, David Booth and Rex Sinquefeld, DFA's founders, did not take the easy route when they decided to start an investment firm in 1981. "Indexing" was not the hot topic it is today and Rex and David took one more very large step away from the mainstream by indexing small company stocks. Their timing couldn't have been worse. Not only did they have to fight the Wall Street crowd long dominated by "active" investment strategies, but small company stocks experienced their worst stretch of performance relative to large company stocks from 1984-1990. Despite these obstacles, DFA attracted billions of dollars in assets from institutional investors. Today, the firm manages almost \$40 billion.

In 1991, Dan Wheeler, who had the fortunate experience of working for Merrill Lynch at one time, decided that DFA's investment strategy could and *should* be offered to "retail" investors through qualified investment advisors. Since then, the Financial Advisor Services division of DFA has grown to over \$10 billion in client assets.

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Ten billion dollars in index fund assets might not seem like a lot when you consider that the Vanguard 500 Index Fund alone has over \$100 billion in assets, but that says something else about DFA that is worth mentioning. They *don't care* about being the biggest fund company. They don't care about slick marketing, "incubator" funds, hot guru-of-the-months, or new "products" designed first and foremost to generate more fees for the company. In fact, some investors think they try too hard *not* to take their money and confuse this for arrogance. But DFA is simply *focused* and they are more motivated by being on the right side of the active/passive debate than being financially richer than they already are. (Even the Vanguard Group, which I admire, cannot wean itself completely from the false promises of active management despite the constant pro-indexing speeches of its former chairman, John Bogle).

With this focus comes complete transparency. There is nothing said to me or any other advisor behind the doors of DFA's Santa Monica office that cannot be said to a client's face. I assure you, this is not true of almost every other fund company and Wall Street brokerage firm. The following message from Dan Wheeler to advisors is a good example. As Dan suggests, investors can take the easy route and simply believe the slick performance-touting ads, or they can climb higher, above the crowd, where the noise disappears and the air is much clearer.

Having just finished giving a talk to a group of BAM advisors here in St. Louis, it occurred to me that in the controlled environment of a financial advisor conference the logic of what we all do seems incredibly obvious. How could any thinking person believe differently? But then I remembered seeing an ad for Investors Business Daily that I had read on the flight into St. Louis. (This particular ad was in Time magazine, although it probably appeared in numerous publications.) It began with the following declaration: "Only 2% of stocks will make you rich, so why do you keep buying the other 98%?" The ad then goes on to say that IBD's data makes it possible for anyone to identify those stocks: "With the right information, you'll see the opportunity of a lifetime about every two weeks." (Jay Leno could use these writers.) It closes with "Just when everybody but you is getting rich, an opportunity to set things right. Call for your free two-week trial subscription." If that last line doesn't make you see red, then perhaps you are in the wrong profession.

This type of advertising goes beyond the usual claims about finding the next Microsoft or the next Peter Lynch -- the material Weston calls "investment pornography". No, this ad reinforces one of the all time great lies currently being perpetuated by many in

our industry. It is the "everybody but you is getting rich" myth. It is analogous to drug dealer telling high school students all their peers are doing drugs and they are the only ones missing out. Perhaps one day these people will be held accountable for the damage they do, but, in the interim, we need to be talking to our clients just as we talk to our children about the myth being spread by the drug dealers. We may think our clients are far too sophisticated to be seduced by these ads, but don't count on it.

We do have a "new economy" and the enormous gains in productivity have created a new level of prosperity. Unfortunately, too many people are buying into the idea that this "new economy" has created a new stock market where high returns can be earned with little risk. And, conversely, stocks representing the "old economy" are riskier yet offer lower returns. Well, "pigs will fly" before risk and return are inversely related. I know it, you know it, and your clients intuitively know it. But rational people engage in all kinds of destructive irrational behavior. Our job is to keep that from happening.

Perhaps it is time to go on the offensive. This market has given new life to the active management crowd. No, they haven't been beating the market, but they are able to claim that with active management investors have a chance to win big. I can hear the brokers talking to your clients now: "Who wants to settle for mediocrity when things are booming?" With over six thousand actively-managed funds out there, brokers can always find a few that are hitting it big.

As I look at the year-to-date NAVs, I recall how I used to tell my clients they could learn about risk, return, diversification and discipline in two ways: from me or from the markets. But I also told them the "tuition" I charged was a lot less than what the markets would charge. Sure enough, this past few weeks the "Market School of Investing" has been sending out some pretty big tuition bills.

Who knows where we are headed next? No one does. This is a great time to be talking about diversification because there is so much uncertainty in people's minds. The sad thing is that it takes markets like this to make people realize that there is always uncertainty. They just choose to ignore it periodically.

There are a lot of investors walking around out there with their newly-minted degrees from the Market School of Investing. Now is the time to talk to them about the cost of a graduate degree.

¹ This is considered one of the 50 Classic Climbs of North America. I can see why. The climber in red is making a "Tyrolean Traverse" back to the canyon wall on a fixed rope.