EQUIUS
PARTNERS
Adding Balance to Wealth℠

ASSET CLASS℠

An update of performance, trends, research & topics for long-term investors

Asset Class Returns

May 31, 2010 (YTD)

	2009	2008	2007	Last 10 yrs.*	YTD 2010
Bonds (%)					
One-year	1.9	4.0	5.2	3.7	0.4
Five-year	4.2	4.0	5.2	4.8	2.6
Intermediate	-0.7	12.9	9.5	6.9	2.8
Long-term	-12.1	22.5	9.2	7.4	8.1
U.S. stocks (%)					
Large Market	26.5	-37.0	5.4	-1.0	7.1
Large Value	30.2	-40.8	-2.8	4.4	13.3
Small Market	36.3	-36.0	-3.1	5.7	17.5
Small Micro	28.1	-36.7	-5.2	6.3	17.5
Small Value	33.6	-36.8	-10.8	9.1	21.0
Real Estate	28.2	-37.4	-18.7	10.5	17.9
International stocks (%)					
Large Market	30.6	-41.4	12.5	1.4	-0.5
Large Value	39.5	-46.3	10.2	6.7	0.3
Small Market	42.0	-43.9	5.6	8.7	7.0
Small Value	39.5	-41.7	3.0	11.3	6.4
Emerg. Mkts.	71.8	-49.2	36.0	9.5	4.2

Descriptions of Indexes

Short-term bonds	DFA One-Year Fixed Income fund
Five-Year bonds	DFA Five-Year Global Fixed
Intermediate bonds	DFA Intermed. Gov't Bond fund
Long-term bonds	Vanguard Long-term U.S.Treas.
U.S. Large Market	DFA U.S. Large Co. fund
U.S. Large Value	DFA Large Cap Value fund
U.S. Small Micro	DFA U.S. Micro Cap fund
U.S. Small Market	DFA U.S. Small Cap fund
U.S. Small Value	DFA U.S. Small Value fund
Real Estate	DFA Real Estate Securities fund
Int'l Large Market	DFA Large Cap Int'l fund
Int'l Large Value	DFA Int'l 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 10 yrs." returns are ended 12/31/09.

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Meeting the Legacy Challenge

Phil Jonckheer, Equius Partners

This year my Stanford business school classmates and I will celebrate our 30th reunion (ouch!). As I reconnect with these old friends—many of whom are extraordinarily successful in their chosen careers—I have become much more aware of the concept of "legacy" and the challenge of defining, preserving, and growing one within the context of significant wealth and a culture of risk-taking. (Jeff's article about Oprah Winfrey in last month's *Asset Class* is an interesting perspective in this regard.)

> *The goal isn't to live forever, it's to create something that will.*
>
> Chuck Palahniuk

But extraordinarily successful businesspeople are not the only ones with legacy challenges. As our team at Equius Partners continues to build investment plans and counsel clients into and through their retirement years, we appreciate more than ever that *everyone* has a legacy, irrespective of the size of his or her estate. After much research, we have teamed with a group of outside experts to develop a structure around legacy and inheritance planning that should serve our current and future clients through many generations.

Improving the Odds (Again)

One outcome of our research has been the realization that without careful planning, a legacy can be quickly lost. In fact, studies indicate that 60% of new wealth is gone by the second generation and 90% of that wealth does not survive the third generation. This pattern is not new: it has endured for centuries and through all cultures. Why?

The reason is that our legacies are much more than our money. Enduring legacies preserve not only material wealth, but also the history, purpose, and values behind that wealth. In order to increase the odds of preserving your legacy so that it passes in perpetuity and with meaningful purpose to people and/or causes that you care about, a process needs to be adopted that guides your legacy in a serious and deliberate way.

> *Wealth stays with us a little moment if at all: only our characters are steadfast, not our gold.*
>
> Euripides

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That process is bolstered by three complementary pillars: estate planning, inheritance planning, and investment planning and counseling.

Legacy's First Pillar: Estate Planning

All our legacies share a common heir: our government, which most likely will claim some portion of our material wealth when we're no longer here. A tremendous amount of brainpower and effort have been directed toward creating elaborate estate planning techniques focused on channeling the flow of wealth into hands other than the government's. The business of estate planning continues to thrive, since deciphering the tax code has not become any easier and benefactors are still committed to optimizing the after-tax transfer of their financial wealth to designated beneficiaries.

Ironically, estate planning's obsession with protecting material wealth is the very reason it does not work: many estate plans fail long-term because they do not formally link the assets they protect with what those assets are meant to support.

Legacies that last for centuries are distinguished by structures that recognize that their material assets need to support the principles, fabric of mores and traditions, and standards that have shaped the histories of their benefactors and beneficiaries. Cultivating a meaningful and long-lasting legacy demands more than simply growing and passing on material wealth through cleverly crafted estate plans and brilliant trust management. It means formalizing a process that defines the soul of all legacies through a code of principles and ethics that extends meaning, not just wealth, to future generations.

Legacy's Second Pillar: Inheritance Planning or The Legacy of Values

Estate planning attempts to protect a legacy's wealth. Inheritance planning increases the odds of a legacy's survival by codifying what that wealth is meant to support.

What results from that process is a document that defines your wealth through an understanding and articulation of your experiences, the principles that have defined your culture, and the road that brought you to this point in your life. Documenting that story lays the foundation for conversations with your beneficiaries so that fundamental guiding principles can be expressed, shared, and owned through multiple generations.

In order to increase the odds of preserving your legacy, inheritance planning also needs to establish a system of governance that manages the conveyance of shared values through multiple generations so as to optimize returns on the human, intellectual, and social capital defined by you and your beneficiaries.

Money will buy a luxurious bed, but it cannot guarantee a good night's sleep. It can buy a magnificent library but not the discipline to educate oneself. Money can purchase a house but never a home; luxuries but not culture or taste; temporary amusements but not lasting happiness.

Rod Zeeb

Human capital is the knowledge, talents, experiences, values, skills, and judgment of those most invested in and affected by your legacy. Acknowledging and articulating these traits is an important step in defining your legacy.

Gary Becker, professor of economics and sociology at the University of Chicago and a Nobel laureate, observes in his book *Human Capital* that "education and training are the most important investments in human capital. These investments improve skills and knowledge and thereby raise psychic incomes."

To realize the full potential of human capital, each member's sense of self-worth needs to be supported by the dignity of work, in whatever form, in order to enhance each member's definition and pursuit of happiness. All such work, irrespective of its financial reward, is of equal value to the legacy.

Intellectual capital is built as each member learns, communicates, and makes decisions. This capital also grows as all members of the legacy communicate, resolve conflict, make joint decisions, and mentor one another.

In order for families to thrive over time, a formal system of governance based on well-stated goals and principles needs to be instituted. The challenge here, writes the former dean of Harvard Graduate School of Education, Paul Ylvisaker, in his book *Conscience and Community*, is that "governance can become an anguishing issue. In the first generation, the question is how to overcome the tendency to bow obsequiously to the founding donor; in subsequent generations, it's how to include a spreading avalanche of beneficiaries without being exclusive or overwhelmed."

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To realize the full potential of intellectual capital, a means for collecting and disseminating the accumulated knowledge of all members needs to be created. Passing on your family story to those who are in line to take representative and leadership roles in perpetuating your legacy is also crucial in maximizing returns on this capital.

Social capital is built as members of the legacy and the group as a whole engage with their communities. The components of social capital are the aspects of social life that allow individuals to commune with each other through networks, norms, and trust in order to pursue shared objectives.

Successful inheritance planning draws on fundamental strategic planning models, therefore its effectiveness can be gauged by how completely the following questions are answered by you and your beneficiaries (including designated charities):

- What is your legacy's vision and mission?
- How should those responsible for that vision and mission communicate with each other now and after your passing?
- How should those members make decisions?
- How does your legacy address its members' emotional and intellectual growth?

With a thorough awareness of shared values embedded in all generations, whoever defines your family will more effectively promote your guiding principles, advocate and expand your philanthropic ventures, and appreciate the importance of prudent investment management so as to preserve your legacy.

To the extent that charity is an important component of your legacy, we have established the Equius Foundation to apply our investment philosophy within the structure of a donor-advised fund so that all elements of this part of your legacy are purposefully and prudently managed.

Legacy's Third Pillar: Investment Planning & Counseling

Financing a legacy requires an investment approach built on enduring and irrefutable investment principles that have stood the test of time and can transcend the vagaries of any era and biases of any individual.

Educating beneficiaries on how their assets are managed such that the odds of investment success are placed squarely in their favor instills in them the confidence that will keep them committed to their prudently crafted plan. If that plan is strictly implemented, it will preserve your/their legacy's material assets through multiple generations.

> *If we would have new knowledge, we must get a whole world of new questions.*
>
> Susanne K. Langer

Maintaining a portfolio of highly concentrated individual stock positions and/or higher-risk, active strategies (hedge funds, private equity, venture capital) at their core carry extraordinarily high odds of underperforming simple market benchmarks over time. These types of portfolios also introduce negative elements such as illiquidity, lack of transparency, high costs, excessive leverage, and unnecessary complexity, all of which your heirs and/or your chosen charities are forced to struggle with after your passing. In addition, portfolios concentrated in low-risk, fixed-income investments such as municipal bonds are unlikely to provide real (net of inflation) growth for you or your beneficiaries.

Preserving and growing a legacy is best accomplished with portfolios that are broadly diversified among the public global financial markets, using the very best institutional-level, low-cost, and tax-efficient "asset class" funds. This ensures more predictable and consistent growth of your assets, while also ensuring that your heirs or your selected charities will inherit a fully transparent, manageable, and timeless investment process. This kind of strategy dramatically increases the odds of preserving financial assets through many generations.

Our firm's success and the success of our investment approach are not dependent on any one individual. Instead, this success is a function of a well-justified belief in markets (long term), a commitment to the evidence-based research of leading financial economists, and a team approach to all aspects of our client relationships. This allows for a more stable, reliable, and, ultimately, successful experience for your heirs and the generations that follow. Core investment principles and specific strategies are more easily and clearly articulated in a way that preserves and grows your family's wealth.

One of the more satisfying aspects of our business is connecting with second- and third-generation clients

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and managing their wealth. The more your heirs are educated about how their assets are managed in a way that puts the odds of success in their favor, the less likely they will be seduced by the wealth-deflating siren calls of Wall Street's highly effective marketing machine.

Recognizing how emotions can wreak havoc on an investment plan, our investment counseling helps all involved and affected by your legacy avoid the behavioral mistakes common to investors so as to enhance the preservation of your legacy's financial assets through multiple generations. As all our clients are aware, our counseling is bolstered by the research and insights of leading behavioral economists at major universities.

The peace of mind, relative simplicity, and full transparency that characterize our investment approach allow you and your beneficiaries to concentrate on continuing to foster the *principles* and *meaning* that drive your legacy.

What Is Your Legacy?

If communicated effectively, the hardships that you overcame to create your wealth and the principles and ethics that guided you as you defined your legacy can be passed on to important people and causes. These beneficiaries foster a ripple effect as they extend your wealth with meaning—not just money—to those causes and generations that define your and their heritage. Benefactors and beneficiaries that successfully extend their legacies meaningfully and in perpetuity have the following common characteristics:

- They share a mutually defined mission and vision.
- They communicate effectively and trust each other.
- They appreciate and support the group's and each individual's human, intellectual, and social capital.
- They meet frequently and have fun at those gatherings.
- They know their shared histories.
- There is a well-defined and active mentoring system.
- They celebrate their shared values, accept their differences, and honor each member's pursuit of happiness.
- Their time frame for success is long-term.
- They understand that wealth is much more than money.

More than creating a model about giving back, we want to perpetuate a structure about ongoing giving to all your beneficiaries through purposeful legacy planning. What we're advocating is not simply passing on your wealth; we want to support the essence of what built your wealth and make sure that whatever material wealth you wish to bestow on your heirs supports the principles that are important to you and your beneficiaries.

In that way we believe your legacy will be one that you can enjoy now and that will help your designated beneficiaries flourish. Forever. We look forward to elaborating on these processes and helping you extend and expand your legacy as you define it.

The Bottom Line...

- Everyone leaves a legacy! In this case, size (of wealth) doesn't matter.
- 90% of new wealth does not survive the third generation.
- Enduring legacies preserve the history, purpose, and values behind wealth.
- Traditional estate planning is only one step in preserving your legacy. Inheritance planning and a *timeless* investment strategy are also critical components.
- Inheritance planning requires structure and ongoing family governance.
- An investment approach that is not dependent on a "guru," is fully transparent, and is based on principles that can be effectively communicated to heirs and charities can preserve and grow a legacy in perpetuity.