

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

Asset Class Returns

November 30, 2014

	YTD 2014	2013	2012	2011	Past 10 yrs.*
Bonds (%)					
One-Year	0.4	0.3	0.9	0.6	2.2
Five-Year	3.3	-0.4	4.8	4.5	3.6
Intermediate	5.3	-3.5	3.7	9.4	4.7
Long-Term	19.6	-11.4	3.3	28.2	6.1
U.S. stocks (%)					
Large Market	13.9	32.3	15.8	2.1	7.4
Large Value	9.3	40.3	22.1	-3.1	8.9
Small Market	2.1	42.2	18.4	-3.2	10.2
Small Micro	-0.4	45.1	18.2	-3.3	9.3
Small Value	1.2	42.4	21.7	-7.6	10.0
Real Estate	28.8	1.4	17.5	9	8.2
International stocks (%)					
Large Market	-1.6	20.7	17.8	-12.3	7.0
Large Value	-3.4	23.1	16.6	-16.9	8.1
Small Market	-5.1	27.4	18.9	-15.4	10.3
Small Value	-3.9	32.4	22.3	-17.5	10.9
Emerg. Mkts.	3.0	-3.1	19.2	-17.4	11.6

All returns except "YTD" (Year to Date) are annualized.

Descriptions of Indexes

One-Year 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	Long-term Gov't Bond Index
U.S. Large Market	DFA U.S. Large Co. fund
U.S. Large Value	DFA Large Cap Value fund
U.S. Small Market	DFA U.S. Small Cap fund
U.S. Small Micro	DFA U.S. Micro 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

"Past 10 yrs." returns are ended 12/31/13.

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Past performance is not a guarantee of future results.

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Yearly Returns Are Random

Jeff Troutner, Equius Partners

When the investing planets are properly aligned, asset class returns accurately reflect their relative risk: stocks beat bonds, small stocks beat large stocks, and value stocks beat growth stocks. We've illustrated these relationships over reasonably long investment time horizons in many articles over the years.

For short periods, like one year, however, the planets are rarely aligned. Yearly returns are random and unpredictable. An effective way to illustrate this is with a "Periodic Table of Returns." We've done this for the period 1995 to 2013 on the next pages.

The key to the left of the main table shows each asset class in a particular color and its annualized return for the total period. The main chart then ranks each asset class from the highest to lowest return *each year*. The result is a mosaic with no discernible trends or patterns.

The Equius Team uses this graphic, along with others, as a way to illustrate several points:

1. *Market timing is a waste of time.*

Pick any asset class color and draw a line connecting that color each year on the Periodic Table of Returns. See a pattern? We don't.

2. *Asset class selection is important.*

The small cap and value return dimensions can add significantly to portfolio performance over time. Growth stocks? Not so much.

Draw a line connecting the Emerging Markets returns across the years (start with the light purple box at the bottom of 1995). You'll find it was the highest 4 times and the lowest 5 times. Extreme volatility and an annual return of over 2% less than U.S. large stocks for 19 years. Worth the risk? We think not.

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		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013		
1995-2013 Asset Class Annual Return		41.3%	37.1%	38.0%	54.4%	69.6%	31.0%	28.2%	17.8%	68.1%	38.7%	31.8%	36.0%	44.2%	25.9%	83.9%	32.0%	28.2%	19.9%	47.0%	Highest	
Fixed Income	U.S. T-Bills	2.8%	37.5%	25.8%	37.8%	27.9%	58.6%	21.5%	16.6%	12.9%	66.7%	33.8%	24.4%	35.1%	16.6%	13.1%	53.7%	28.6%	9.5%	19.8%	43.4%	↓
	U.S. T-Notes	6.0%	37.1%	25.5%	32.4%	20.9%	49.9%	19.9%	12.3%	3.9%	60.5%	33.2%	23.9%	30.0%	16.3%	1.6%	53.3%	28.4%	9.4%	19.5%	42.7%	
	U.S. T-Bonds	7.9%	36.0%	25.1%	31.1%	17.8%	49.4%	12.6%	7.6%	3.6%	59.4%	31.8%	23.5%	29.7%	12.6%	-35.8%	47.2%	28.1%	5.3%	19.2%	38.7%	
U.S. Large Stocks	Growth	7.2%	31.7%	22.6%	29.9%	16.9%	39.3%	12.4%	3.8%	1.6%	55.6%	29.6%	17.0%	25.3%	10.1%	-36.5%	46.3%	26.0%	1.4%	19.1%	33.9%	
	All	9.9%	31.5%	22.1%	19.7%	13.1%	36.8%	11.3%	3.7%	-1.8%	54.9%	26.6%	16.8%	25.2%	9.9%	-36.7%	45.0%	22.6%	0.0%	18.1%	29.8%	
	Value	11.9%	30.8%	9.6%	15.9%	12.8%	28.0%	5.9%	3.1%	-6.3%	54.8%	24.7%	14.8%	22.5%	8.8%	-39.2%	42.3%	21.5%	-2.5%	17.9%	29.5%	
U.S. Small Stocks	Growth	6.2%	16.8%	9.3%	8.8%	10.2%	27.5%	0.9%	-0.6%	-6.4%	49.1%	22.9%	13.8%	22.0%	8.3%	-40.0%	39.3%	20.5%	-3.0%	17.6%	28.9%	
	All	13.9%	12.2%	9.2%	8.4%	10.2%	22.2%	-2.3%	-3.0%	-8.4%	43.3%	22.7%	11.0%	21.6%	7.3%	-40.4%	35.1%	20.1%	-4.1%	17.4%	25.8%	
	Value	15.7%	10.2%	6.7%	5.3%	9.7%	20.6%	-9.0%	-12.7%	-10.2%	36.4%	19.4%	7.8%	21.5%	6.8%	-42.7%	33.4%	18.3%	-6.1%	17.2%	23.9%	
Int'l Large Stocks	Growth	6.5%	10.1%	5.7%	1.4%	6.5%	18.0%	-10.1%	-13.3%	-11.5%	36.2%	18.8%	7.7%	19.6%	6.1%	-44.5%	30.3%	15.9%	-7.6%	17.2%	23.1%	
	All	6.9%	8.3%	5.6%	1.3%	4.9%	8.0%	-16.7%	-13.6%	-12.2%	36.1%	11.4%	7.1%	15.2%	4.9%	-44.7%	29.7%	12.6%	-12.7%	17.1%	22.7%	
	Value	8.8%	5.6%	5.4%	-0.9%	1.2%	7.6%	-18.6%	-15.6%	-13.1%	28.9%	11.1%	6.2%	8.7%	4.7%	-45.2%	28.5%	12.4%	-12.9%	16.3%	1.2%	
Int'l Small Stocks	Growth	7.3%	3.1%	5.2%	-10.3%	-3.4%	4.7%	-25.8%	-21.7%	-13.2%	18.6%	8.5%	3.8%	7.2%	-4.1%	-45.9%	27.7%	11.5%	-14.8%	14.2%	0.0%	
	All	8.1%	2.5%	5.1%	-11.6%	-5.6%	-1.8%	-30.8%	-23.7%	-21.8%	2.4%	7.5%	3.5%	4.8%	-6.4%	-46.9%	0.1%	10.1%	-16.4%	3.3%	-0.6%	
	Value	10.3%	2.1%	2.1%	-11.7%	-17.0%	-2.6%	-33.4%	-24.8%	-25.0%	1.4%	2.3%	3.0%	3.1%	-11.2%	-48.1%	-2.4%	7.1%	-16.9%	2.1%	-1.1%	
Alternative	E. Markets	7.3%	-10.4%	-0.9%	-16.5%	-23.0%	-9.0%	-37.7%	-41.2%	-32.7%	1.0%	1.2%	1.4%	1.2%	-17.6%	-51.7%	-14.9%	0.1%	-19.1%	0.1%	-11.4%	
	REITs	10.6%																				

Yearly Returns Are Random.

Asset Class Returns Ranked Highest to Lowest Each Year

Annual Return is 1995-2013. Index Description and (Source): U.S. T-Bills = One-Month US Treasury Bills (Morningstar); U.S. T-Notes = Five-Year US Treasury Notes (Morningstar); U.S. T-Bonds = Long-Term Government Bonds (Morningstar); U.S. Large Stocks, Growth = Dimensional US Large Cap High Price-to-Book Index (Dimensional); U.S. Large Stocks, All = Dimensional US Large Cap Index (Dimensional); U.S. Large Stocks, Value = Dimensional US Large Cap Value Index (Dimensional); U.S. Small Stocks, Growth = Dimensional US Small Cap High Price-to-Book Index (Dimensional); U.S. Small Stocks, All = Dimensional US Small Cap Index (Dimensional); U.S. Small Stocks, Value = Dimensional US Small Cap Value Index (Dimensional); Int'l Large Stocks, Growth = Dimensional International Large Cap Growth Index (Dimensional); Int'l Large Stocks, All = Dimensional International Large Cap Index (Dimensional); Int'l Large Stocks, Value = Dimensional International Large Cap Value Index (Dimensional); Int'l Small Stocks, Growth = Dimensional International Small Cap Growth Index (Dimensional); Int'l Small Stocks, All = Dimensional International Small Cap Index (Dimensional); Int'l Small Stocks, Value = Dimensional International Small Cap Value Index (Dimensional); Alternative, E. Markets = Dimensional Emerging Markets Index; Alternative, REITs = Dow Jones US Select REIT Index (Dow Jones). Asset Class Investing, Inc. does not guarantee the accuracy or completeness of this information. Past performance is no guarantee of future returns. © 2014 Asset Class Investing, Inc.

2. *Asset class selection is important (cont.)*

The Emerging Markets experience offers another lesson. Having a low correlation to other asset classes in the portfolio might be enough for a robo-advisor, but not for us. So while we generally embrace the message conveyed by the following graphic by Carl Richards of [Behavior Gap](#),¹ it's only part of the story.



3. *The asset class planets align over time.*

The returns for the core asset classes structured around the market, size, and price (value) dimensions have met our *relative* expectations over this period based on their expected risk. Most have also met our *absolute* return expectations based on historical experience. Looking at the table below, we see that the annual return for U.S. Large Stocks, for example, was only 0.5% higher for the last 19 years than it was for the previous 67 years. The big outliers were U.S. Treasury Bonds (3.2% difference), U.S. Small Value Stocks (2.4%), and U.S. Small Growth Stocks (-2.6%).

Canada, France, Switzerland, Germany, and Australia is unwise?

If you're John Bogle, the former chairman of the Vanguard Group, evidently the answer is yes. In a recent article Bogle stated that he "wouldn't invest outside the U.S."²

This reminds me of a quote from Cliff Asness, founder of AQR, in his recent article [Efficient Frontier "Theory" for the Long Run](#):³

The point is that the very basic tenets of our field are better than what's often casually asserted, implied, inferred, imputed, and assumed; and that those assailing these basic tenets are too short-term oriented and sometimes far too triumphalist.

Bogle is considered an investing god by many investors, which almost guarantees that long-term portfolio allocations of his followers will begin to shift dramatically away from foreign stocks, reducing portfolio diversification.

At Equius, in contrast, we know that not all asset classes move in the same direction or to the same degree all the time—that's why we diversify. So we're confident that the foreign developed markets will have their day again. Besides, just like on the U.S. side, we've maintained a significant small cap and value tilt since 1995 (something John Bogle also continually advises against).

After a solid 2013 in terms of performance, 2014 might seem disappointing to some

Difference in Annual Returns for Periods 1928-1994 & 1995-2013

Fixed Income			U.S. Large Stocks			U.S. Small Stocks		
U.S. T-Bills	U.S. T-Notes	U.S. T-Bonds	Growth	All	Value	Growth	All	Value
-0.9%	0.9%	3.2%	-0.5%	0.5%	0.8%	-2.6%	2.0%	2.4%

The above comparison cannot be made with the international and REIT indexes due to much shorter data series. But using the MSCI EAFE Index (inception 1970) as a proxy for the non-U.S. developed markets stock indexes, we find a significant difference of 7.2% from the 1970-1994 period to the 1995-2013 period.

Foreign developed markets are 37% of the total global market capitalization. Should we conclude from the 1995-2013 experience that an allocation to the major foreign developed markets like Japan, United Kingdom,

investors. At Equius, we are committed to the basic tenets of asset class investing, rebalancing allocations and harvesting losses as appropriate, and remaining confident that core financial markets will reward risk taken over time. We wish all of you a happy, healthy, and prosperous New Year!

¹ www.behaviorgap.com

² "Jack Bogle: I Wouldn't Risk Investing Outside the U.S.," Bloomberg, Dec. 9, 2014

³ www.aqr.com/cliffs-perspective/efficient-frontier-theory-for-the-long-run