TAM Asset Management, Inc.

Asset Class[sm]

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

October 2006

Asset Class Returns

September 30, 2006 (YTD)

	2003	2004	2005	Last 10 yrs.	YTD 2006
Bonds					
One-year	1.6	0.9	2.3	4.3	3.5
Five-Year	3.0	2.9	1.7	6.1	2.8
Intermediate	2.5	4.3	1.6	6.2	2.7
Long-term	2.7	7.1	6.6	7.1	1.4
U.S. stocks					
Large Market	28.5	10.7	4.9	8.9	8.4
Large Value	34.4	18.2	10.2	11.9	11.2
Small Micro	60.7	18.4	5.7	13.6	6.0
Small Market	51.5	17.9	6.1	11.8	6.9
Small Value	59.4	25.4	7.8	15.9	10.4
Real estate	35.6	32.1	13.2	15.1	24.2
Int'l stocks					
Large Market	36.7	18.8	13.5	6.2	13.8
Large Value	49.4	28.8	15.3	9.2	19.7
Small Market	58.8	30.9	22.0	N.A	10.9
Small Value	66.5	34.8	23.2	10.2	13.1
Emerg. Mkts.	60.2	29.9	29.9	8.5	10.2

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 US Large Co. fund
U.S. Large Value	DFA Large Cap Value fund
U.S. Small Micro	DFA US Micro Cap fund
U.S. Small Market	DFA US Small Cap fund
U.S. Small Value	DFA US 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 12/31/05.

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The Evolution Continues (Part 1)

Jeff Troutner, TAM Asset Management, Inc.

Lately it occurs to me: What a long, strange trip it's been.[1]

I have now been in the investment business for 25 years. Coincidently, my favorite mutual fund management firm, Dimensional Fund Advisors (DFA), is celebrating its 25th anniversary this year. To honor the occasion, I thought I would reflect on how my career and the investment approach TAM embraces have evolved over time.

It's no accident that *we* find ourselves benefiting from an "asset class" investment philosophy. I'm sure our journeys to this place have been similar in many ways (albeit mine as purveyor and yours as consumer of investment services). If I can be so bold, I think "survival of the fittest" is an apt description of the result so far.

My Evolution

From as early as I can remember, I wanted to be in the investment business. Maybe it was due to the fact that my dad was a banker, or maybe I stopped one day to read the financial section of the newspapers I was delivering every morning at 5:00 am.[2] Whatever the motivation, I ended up pursuing a business/finance degree at Indiana University and graduated in 1980 ready to deal with the real world of financial advice.

As it turns out, the first phase of my evolution as an investment advisor was accelerated by the fact that I *wasn't* hired by either a local bank trust department (inhabited by investment dinosaurs) or the local Merrill Lynch office (I couldn't relate to their boiler room "training"). Instead, I found myself in the nurturing bosom of Headford & Company, Incorporated. George Headford was a well-respected and highly ethical broker of local economic development bonds and bank stocks and, as it turned out, his style contrasted sharply with what I observed at Merrill Lynch twenty floors below us.

Despite George's valuable mentoring and friendship, however, I left Headford & Company in late-1981 to join Shearson Lehman Brothers (now Smith Barney).[3] My goal was to expand the investment opportunities and options for my clients and me. After about a year within the Shearson environment, I had achieved a goal of moving away from "product sales" and closer to the world of investment advice by focusing on an obscure (at the time) specialty I'll call "managed money."

The business of managed money involved referring my high net-worth and corporate retirement plan clients to outside, fee-based investment advisors I had screened for unique investment styles and successful track records. At the same

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time, I was embracing a concept that was very foreign to brokerage firms then and, unfortunately, is still an issue with them today—accountability. Using one of the first Macintosh computers, I developed a system for *calculating and reporting the performance of each of my client's managed accounts*.

Despite the fact that I was only one of a relative handful of brokers specializing in this kind of business in the mid-80's and receiving no support for my efforts from Shearson (except, importantly, from the local branch manager who clearly saw the potential), my business expanded rapidly over the next five years. After I left Shearson to join one of my recommended advisors in late 1988, I saw the commitment to managed money business explode at all the major Wall Street firms.

As luck would have it (!), the advisor I joined in 1988 was a "tactical asset allocator," which is simply a fancy name for "market timer." I have to admit that I thought these guys were on to something when they moved to 100% Treasury Bonds about six months prior to the October, 1987 stock market crash[4]. I learned two years later how lucky that call was after a third of the advisor's $1.5 billion under management walked out the door due to two years of lousy performance. They were then forced to close the San Francisco office I had been hired to help open and develop.[5]

The next and current stage in my career evolution occurred when I had the fortunate experience of meeting Dan Wheeler. Dan was an independent investment advisor who had worked for Merrill Lynch previously and, like me, was witness to a constant parade of "superior" money managers becoming inferior over time. Acknowledging the futility and lack of value-added of switching managers for clients in a quest for the next Peter Lynch or Warren Buffett, Dan discovered the benefits of indexing through his own research and came upon an obscure institutional firm in Santa Monica called Dimensional Fund Advisors. DFA appeared to be on the cutting edge of an "asset class investing" revolution and, after much prodding, they allowed Dan to use their funds to build his clients' portfolios. Not long after, Dan convinced DFA to open their funds to other enlightened advisors like him and (to all of our benefit) he now heads the Financial Advisor side of DFA's investment business.

TAM was founded in October of 1992 based on my evolution as an advisor, *not* on an evolution within my industry. At the time, few investment advisors (and even fewer stockbrokers) were even aware of the benefits of indexing or its more sophisticated version, asset class investing. And most potential clients greeted my presentations of the benefits of indexing with reactions ranging from indifference to total disdain.

Despite the growth of firms like Vanguard and DFA; the plethora of very good investment books written on the subject of indexing the past ten years; the happy coincidence in 1992 of the publication of the core Fama/French research and the third revision of The Prudent Investor Rule; and the phenomenal growth of indexed Exchange Traded Funds (ETF's), the majority of serious investment asset are *still* actively managed. In fact, (true to their nature) the only "progress" most active managers, advisors, and stockbrokers have made in embracing indexing as a strategy is to exploit its increased visibility by using ETF's to promote even more *market timing*.[6]

My personal experiences and the knowledge I've gained over time have created a passion for asset class investing that has allowed TAM and our clients to thrive for these 14 years. This passion has been enhanced by the peerless research, integrity, and commitment of the professionals at DFA. Appropriately, next month's *Asset Class* will review the evolution of the science of asset class investing and introduce you to DFA's new "Core" fund strategies.

As this was being written, Forbes. com published an article entitled, "The Index Insurgents" that describes "the race to build a better index fund" and features David Booth, the CEO of Dimensional Fund Advisors. The article can be found on the web here: www.forbes.com/business/forbes/2006/1030/064.html. Free registration is required on the Forbes site.

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[1] Lyrics from Robert Hunter/Grateful Dead song "Truckin'."

[2] My Dad was such a stickler for personal responsibility that he insisted that I deliver my morning papers one day despite being doubled over in pain. Afterward, we went to the hospital to have my appendix removed.

[3] George passed away in 1992. His wife, Daisy, became the first TAM client and my relationship with her remains one of my most cherished.

[4] Influenced, no doubt, by the fact that my annual meeting with my biggest client was on the day of the crash (October 19) and I had placed all of their money with this advisor.

[5] The lucky part (for me and my clients) was experiencing the downside of market timing *before* I founded TAM. I also feel lucky for having moved my family of six to Marin County, California where I enjoy a very balanced life that includes a passion for mountain biking, sea kayaking, and snowboarding, *and* I met my business partner, Phil Jonckheer.

[6] But now, rather than moving in and out of stocks in general, the emphasis is more on major shifts among industries, sectors, countries, or asset classes. Market timing has many faces and they're all ugly.