Taking the Scary Out of Stocks

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One of the most effective marketing strategies being used by active investment managers to alter the way individuals invest for retirement is to point out that the S&P 500 has been essentially flat for *eleven* years. Compared to bank CDs and long-term Treasury bonds, stocks don't appear to be worth the risk.

Stock pickers are using this information to suggest that this is exactly why you need to hire them to be more *selective* in your stock investing. After all, not *all* stocks were flat or down over that period. Market timers are using the information to claim that they can get you in and out of the market at the right time. And the media is all too happy to play along with this game, rather than do the extra legwork to counter these claims.

We've done some of the extra legwork in previous *Asset Class* articles by pointing out, as always, that there's more to the stock market than the big U.S. growth stocks that dominate the S&P 500. In fact, U.S. and foreign large and small value stock indexes performed much better over this period, as reflected in the global index mix returns below.

Index	Annual Return 2000-2010	Monthly Volatility
One-Month CDs	3.0%	0.2%
Five-Year Treasury Bonds	6.3%	1.4%
Long-Term Treasury Bonds	7.9%	3.3%
S&P 500	0.4%	4.7%
Global Stock Mix	7.7%	5.7%
Global Balanced Mix	8.3%	3.4%

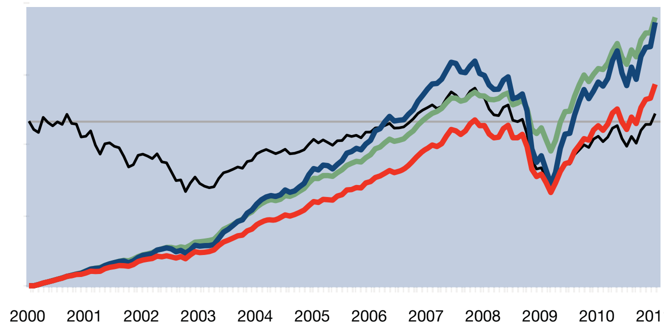
Global Stock Mix = 21% S&P 500 index, 21% DFA US Large Value index, 28% DFA US Small Value index, 18% DFA Int'l Value index, and 12% DFA Int'l Small Value index. **Global Balanced Mi**x = 35% Five-Year Treasury Bond index, 13.5% S&P 500 index, 13.5% DFA US Large Value index, 18% DFA US Small Value index, 12% DFA Int'l Value index, and 8% DFA Int'l Small Value index. Mixes are rebalanced to targets annually.

Monthly Volatility is the standard deviation of monthly returns. The returns and performance data are for illustration purposes only and do not represent actual Equius client performance. There are limitations inherent in model allocations. In particular, model performance may not reflect the impact that economic and market factors may have had on the advisor's decision making if the advisor were actually managing the client's money. Mutual fund and portfolio mixes are net of mutual fund fees and expenses but are not net of Equius investment advisory fees. **Past performance is no guarantee of future results.**

Given that most investors build their portfolios over time, we thought it would be helpful to look back on these eleven years from that perspective. After all, because of scary anti-stock headlines and poorly researched articles, many investors altered their stock allocations or quit buying stocks altogether. They shouldn't have.

We ran a simulation from 2000-2010 of a $1,000 monthly contribution into the S&P 500 and the more diversified indexed mixes shown in the table versus a onetime investment in the S&P 500. The following chart shows the results.

Chart: Growth of $132,000



Line	Index	End Value	$ Return
black	S&P 500 ($132,000 up front)	$138,057	$6,057
red	S&P 500 ($1,000/mo.)	$161,392	$29,392
blue	Global Stock Mix ($1,000/mo.)	$210,644	$78,644
green	Global Balanced Mix ($1,000/mo.)	$214,677	$82,677

The time-weighted rate of return, which reflects the actual *investment* return of the index, is the same for both of the S&P 500 simulations. But a steady monthly investment in the index over this period resulted in a higher ending value. This shows the power of dollar-cost averaging over periods with flat to down returns, and the advantage of the "buy low, sell high" effect of a portfolio rebalancing discipline.

Consider this chart also in terms of the emotional value of dropping regular contributions into the portfolio. During the first decline and up to mid-2007, the "accumulators" saw very few dips in total portfolio value. Yes, they, like everyone else, took a big hit during the worst decline in eighty years that followed. But in each case, previous portfolio highs were reached again *and* sooner than the onetime investment in the index.

The moral of this story is that investors should not answer the siren calls of active managers or be intimidated by the fear-mongering media. Invest steadily in a broadly diversified asset class portfolio that reflects your personal risk and return objectives, be patient, and spend your time with family and friends instead of *Mad Money* Cramer and his ilk.