EQUIUS PARTNERS

Adding Balance to Wealth℠

ASSET CLASS℠

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

February 2013

Asset Class Returns

January 31, 2013

	YTD 2013	Last 10 yrs.*	2012	2011	2010
Bonds (%)					
One-Year	0.1	2.3	0.9	0.6	1.2
Five-Year	-0.5	4.0	4.8	4.5	5.3
Intermediate	-0.8	5.3	3.7	9.4	6.9
Long-Term	-3.3	7.4	3.5	29.3	8.9
U.S. stocks (%)					
Large Market	5.2	7.0	15.8	2.1	14.9
Large Value	6.9	8.4	22.1	-3.1	20.2
Small Market	6.3	10.9	18.4	-3.2	30.7
Small Micro	5.7	10.4	18.2	-3.3	31.3
Small Value	6.6	11.3	21.7	-7.6	30.9
Real Estate	3.5	11.4	17.5	9.0	28.7
International stocks (%)					
Large Market	4.1	8.4	17.8	-12.3	9.3
Large Value	4.6	10.2	16.6	-16.9	10.6
Small Market	4.4	12.8	18.9	-15.4	23.9
Small Value	5.1	13.5	22.3	-17.5	18.1
Emerg. Mkts.	0.5	17.4	19.2	-17.4	21.8

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	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 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

"Last 10 yrs." returns are ended 12/31/12.

Equius Partners is an investment advisor registered with the Securities and Exchange Commission. Consider the investment objectives, risks, and charges and expenses of any mutual fund and read the prospectus carefully before investing. Indexes are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. **Past performance is not a guarantee of future results.**

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Balance Is Better

Jeff Troutner, Equius Partners

Weston Wellington, one of our friends at Dimensional Fund Advisors, recently wrote an article that pointed out that the S&P 500, with dividends reinvested, finally reached a new high in March 2012—4½ years after the previous mark was set in October 2007. Weston pointed out that despite the frustration many investors have expressed about the market fluctuations in recent years, this market recovery is broadly consistent with past cycles. As he said in the article, "We can draw some measure of solace in acknowledging that past generations of investors often found their patience sorely tested, as well." Weston included the table below in the article to show how long it took the market to recover to previous highs.

Market Cycles Based on Month-End Value of S&P 500 Index with dividends reinvested

Peak Month	Trough Month	Loss at Trough	Recovery Month	Years to Recovery
Oct 2007	Feb 2009	-50.9%	Mar 2012	4.4
Mar 2000	Sep 2002	-43.8%	Oct 2006	6.6
Aug 1987	Nov 1987	-29.5%	May 1989	1.8
Dec 1972	Dec 1974	-37.2%	Jun 1976	3.5
Dec 1961	Jun 1962	-22.3%	Apr 1963	1.3
Feb 1937	Mar 1938	-50.0%	Mar 1944	7.1
Aug 1929	Jun 1932	-83.4%	Jan 1945	15.4

Using the movement of the S&P 500 index as the gauge of investor pain or pleasure makes sense, given that the index (and the more popular Dow Jones average) is what the financial media references every day and most indexers use as their core stock investment. But the index does not represent what Equius clients experience with a more balanced asset class approach. (In fact, it remains a mystery to me that after decades of successful "value investing" by renowned investor Ben Graham and his disciples, such as Warren Buffett, in which they purchased stocks at low prices to their book values, combined with the breakthrough 1992 "three factor" research of Fama and

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French, more investors generally—and particularly "indexers"—don't tilt their portfolios more toward value stocks.)

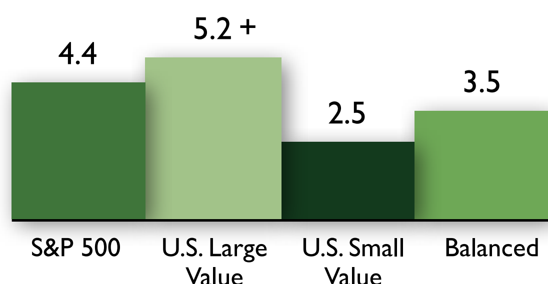
To track more closely the experience of Equius clients, I expand on Weston's analysis in this article by including U.S. large and small value stock indexes and a combination[1] of those indexes and the S&P 500 for the same time periods he reviewed.

If you tend to get lost within (or are bored by) the data, here's the conclusion: value stocks and, therefore, the balanced mix of the indexes generally recovered more quickly and ended with higher returns at the end of each period than did the S&P 500 index. In other words, a more balanced asset class portfolio would have resulted in a superior investment experience for investors during these very difficult markets.

Period 1: October 2007-March 2012

This most recent period saw the S&P 500 drop almost 51% from its monthly peak in October 2007 to the bottom in February 2009, and it didn't fully recover until the end of the period, in March 2012. U.S. large and small value stocks and the balanced asset class portfolio also bottomed in February 2009 and all experienced bigger declines than did the market. This reflects the unique nature of this bear market, which hit financial stocks (a larger component of value indexes than the market index) harder.

Years to Recovery From Previous High
October 2007-March 2012



Although small value stocks declined 62%, they recovered in April 2010, almost two years earlier than did the overall market. Large value stocks, weighted more heavily to the big financial stocks, have yet to recover fully from the decline. As of year-end 2012, they were still down 16% from the October 2007 high (while small value is *up* 21.4%). The balanced asset class portfolio fully recovered its losses almost a full year ahead of the market.

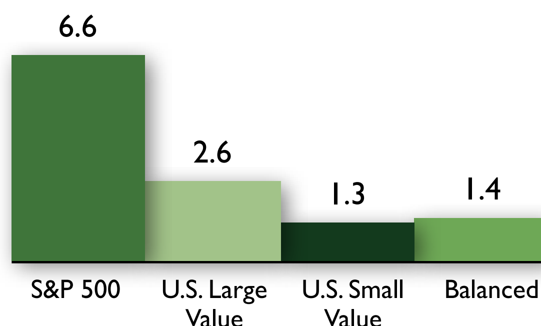
Period 2: March 2000-October 2006

This cycle was unique in that it was essentially a correction in one dimension of the market—large, high-priced stocks. As a result, it took the S&P 500, which is dominated by these kinds of stocks, more than 6½ years to recover from the March 2000 high.

In contrast, after a brief decline within a couple of months of the March 2000 high for the S&P 500, U.S. large and small value stocks continued to *climb* until May 2001 and April 2002, respectively. After reaching new highs, these indexes declined alongside the S&P 500 to the low at the end of September 2002.

During this bear market, U.S. large value stocks declined 15%, U.S. small value stocks *gained* 9%, the S&P 500 declined 44%, and the balanced portfolio declined 16%.

Years to Recovery From Previous High
March 2000-October 2006



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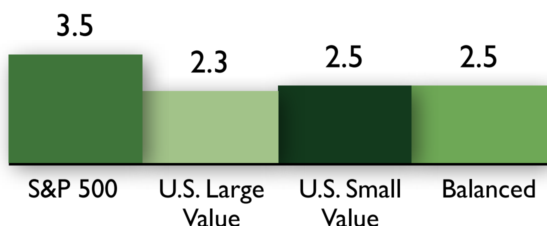
Period 3: August 1987-May 1989

This period is notable for the market "crash" in October 1987. By May 1989 all the indexes recovered from their lows at the end of November 1987 and recovered from five months sooner than the market (U.S. large value stocks) to one month sooner (U.S. small value stocks).

Period 4: December 1972-June 1976

Prior to the more recent "dot com" and "global financial crisis" declines, the 1973-1974 period was the worst market environment since the 1930s. From its high in December 1972 until its low in September 1974, the S&P 500 fell more than 37%.

Yet the recovery time was relatively short. U.S. large value stocks bottomed during the same month as the S&P 500, but U.S. small value stocks continued to decline until December 1974. From their *lows*, U.S. large and small value stocks recovered to new highs in seven months and six months, respectively.

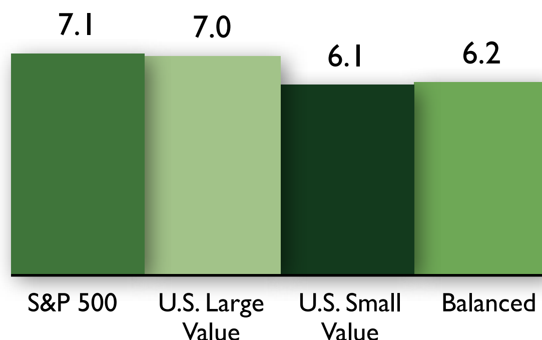


Period 5: December 1961-April 1963

Over the course of this period, the S&P 500 dropped 22.3% before it recovered 16 months later. U.S. large and small value stock prices continued to rise until February 1962 before declining to lows with the S&P 500 in June 1962 and then recovered three months before the market did.

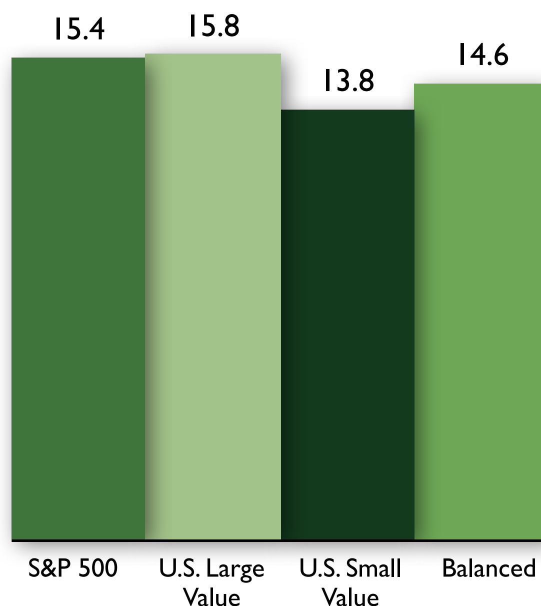
Period 6: February 1937-March 1944

This period was notable for the "great recession" within the Great Depression, and the recent global financial crisis bears an eerie similarity to this period (see Period 1 above). The market declined 50% before the recovery began in March 1938. Both large and small value stocks declined even more, with the latter down 68%. Compared to the recovery we just experienced, this period's recovery was much longer and more frustrating, coming on the heels of the last period we'll cover—the aftermath of the 1929 crash.



Period 7: August 1929-January 1945

This is the mother of all market declines. Stocks recovered almost all of their losses by February 1937 but they began to decline again (see Period 6) and did not reach a new high until January 1945. At the low in June 1932, the S&P 500 had dropped 83%, with



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U.S. small value stocks down an incredible 90% in just under three years. As we see time and time again, however, the hardest-hit asset classes tend to recover more quickly and more powerfully. When the S&P 500 hit its peak 15 years later, U.S. small value stocks were already up 63%.

Returns

Given the quicker recovery time after major declines for value stocks as compared to the overall market (large value being the occasional exception), I thought it would be interesting to look at the total returns for the value-tilted indexes over these periods (see table at right). Returns are month-end to month-end, which accounts for the slightly positive returns for the S&P 500 index.

The table shows that the riskiest asset class—small value stocks—tended to decline the most, recover most quickly, and reach substantially higher new highs by the time the overall market recovered fully. This trend was most evident during March 2000-October 2006. Unlike the most recent bear market and the markets of the Great Depression, this period was unique in the degree to which the S&P 500 and value stocks diverged. This was somewhat foreseeable (see the January 2000 *Asset Class*, "Should We Fear a Total U.S. Market Collapse—Or Is a Gradual "Rotation" Among Asset Classes More Likely?").

Conclusion

No one can predict when bear markets will begin, how far stocks will fall, how much the asset classes will diverge from one another, and how long it will take for markets to recover. But we know that stocks are multidimensional in terms of risk and expected return. A more diversified portfolio that is balanced among the core asset classes can provide investors with a better overall experience during severe market declines. In addition, investing among the value and small cap dimensions *globally* can further enhance diversification and the overall investing experience.

Total Returns at End of Each Period	
Period 1: October 2007-March 2012	
S&P 500 index	0.3%
U.S. large value stocks index	-21.0%
U.S. small value stocks index	14.6%
Balanced mix index	-0.3%
Period 2: March 2000-October 2006	
S&P 500 index	2.3%
U.S. large value stocks index	84.4%
U.S. small value stocks index	229.5%
Balanced mix index	96.7%
Period 3: August 1987-May 1989	
S&P 500 index	3.5%
U.S. large value stocks index	15.7%
U.S. small value stocks index	6.7%
Balanced mix index	8.7%
Period 4: December 1972-June 1976	
S&P 500 index	1.5%
U.S. large value stocks index	46.0%
U.S. small value stocks index	34.8%
Balanced mix index	28.8%
Period 5: December 1961-April 1963	
S&P 500 index	1.9%
U.S. large value stocks index	11.6%
U.S. small value stocks index	6.3%
Balanced mix index	6.7%
Period 6: February 1937-March 1944	
S&P 500 index	0.9%
U.S. large value stocks index	3.2%
U.S. small value stocks index	27.4%
Balanced mix index	14.7%
Period 7: August 1929-January 1945	
S&P 500 index	0.6%
U.S. large value stocks index	-12.2%
U.S. small value stocks index	63.0%
Balanced mix index	27.8%

[1]Source: Dimension Fund Advisors. U.S. large value stocks = Dimensional US Large Cap Value index; U.S. small value stocks = Dimensional US Small Cap Value index; and Balanced mix = 30% S&P 500, 30% Dimensional US Large Cap Value index, and 40% Dimensional US Small Cap Value index. Indexes are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio.

Past performance is not a guarantee of future results.