EQUIUS PARTNERS
Adding Balance to Wealth℠

ASSET CLASS℠

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

Asset Class Returns

December 31, 2013

	YTD 2013	Past 10 yrs.*	2012	2011	2010
Bonds (%)					
One-Year	0.3	2.2	0.9	0.6	1.2
Five-Year	-0.4	3.6	4.8	4.5	5.3
Intermediate	-3.5	4.7	3.7	9.4	6.9
Long-Term	-13.0	5.7	3.5	29.3	8.9
U.S. stocks (%)					
Large Market	32.3	7.4	15.8	2.1	14.9
Large Value	40.3	8.9	22.1	-3.1	20.2
Small Market	42.2	10.2	18.4	-3.2	30.7
Small Micro	45.1	9.3	18.2	-3.3	31.3
Small Value	42.4	10.0	21.7	-7.6	30.9
Real Estate	1.4	8.2	17.5	9.0	28.7
International stocks (%)					
Large Market	20.7	7.0	17.8	-12.3	9.3
Large Value	23.1	8.1	16.6	-16.9	10.6
Small Market	27.4	10.3	18.9	-15.4	23.9
Small Value	32.4	10.9	22.3	-17.5	18.1
Emerg. Mkts.	-3.1	11.6	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

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

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The KISS of Death For "Alternatives"?

Jeff Troutner, Equius Partners

"It seems that perfection is reached not when there is nothing left to add, but when there is nothing left to take away."
Antoine de Saint-Exupéry

It hardly bears repeating that the 14 years from 2000 to 2013 were among the most volatile and challenging in our country's history. The ups and downs of the stock market were extreme, creating an emotional roller coaster for investors that caused many to jump in and out of stocks and bonds, change strategies and money managers frequently, and, in some cases, abandon traditional long-term investments altogether.

This period began with U.S. stock prices near an all-time peak. The "dot-com bubble" (as most experts referred to it after the fact) was about to pop and predictions of a "lost decade," or worse, were setting the stage for an exodus of investors from the market. Despite the very strong market resurgence over the 2003-2007 period, by the time the global financial crisis hit in 2008-2009, many investors had moved substantial sums out of basic stock portfolios and into the much more opaque, unproven, expensive, often speculative, and, ultimately, unsuccessful world of "alternatives" (gold, real estate, esoteric mortgage securities, commodities, hedge funds, and so on). Two major themes rose to prominence: diversify among as many asset classes and sectors as possible (resulting in the astounding growth of specialized ETFs) and shift allocations frequently and dramatically in reaction to short-term market forecasts and economic trends.

Our World, in Contrast

A little known secret about the Equius team is that we all have KISS (Keep It Simple Stupid) tattoos. Not anywhere on our bodies, of course, (at least that I know of) but etched permanently on our psyche. This has resulted in a more consistent, transparent, easy-to-understand, less stressful, more predictable, and ultimately very successful investment approach.

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By the year 2000, Equius Partners had a well-established and unique "asset class" approach centered on a thorough understanding of two key aspects of long-term investing:

- **Investment Risk**
- **Investor Behavior**

Our expertise in these vital pillars of long-term investing is based on a consistently rigorous examination and critique of the most respected academic research in financial economics (particularly efficient markets research) and behavioral economics. This is the basis for an investment strategy that combines market risk with a highly structured tilt to global "value" stocks; high-quality, short-term bonds (for most client portfolios); and a strict rebalancing discipline.

The "Dot-com" Crash

Our expectations at the beginning of this period were outlined in the January 2000 issue of *Asset Class* in an article titled *"Should We Fear a Total U.S. Market Collapse (or is a gradual "rotation" among asset classes more likely)?"*

Over the next 3¼ years, the S&P 500 dropped an alarming 39.6%, while U.S. large value stocks hardly corrected with a loss of 8.1% and small value stocks were *up* 12.1%. Not only were Equius clients better positioned to weather that market storm, they were well rewarded for the risk they accepted and their patience when the market turned around in the second quarter of 2003 and gained 95% by May 2007. U.S. large and small value stocks gained 147% and 208% over the period.

The "Global Financial Crisis"

By June 2007, the stock portion of balanced portfolios reflected the first symptoms of what came to be known as the global financial crisis. As with prior market declines marked by significant problems in the financial sector, this one was especially hard on value stocks. From June 2007 to February 2009, the S&P 500 crashed 50%. Global value stocks declined another 10%! Clearly, asset class diversification did not soften the blow investors took to their portfolios. But investors who had fled stocks (most, as indicated by mutual fund cash flows, near the bottom of the decline) in favor of alternatives found little, if any, shelter from this market tsunami.

Through focused and effective counseling, the Equius team worked with clients in maintaining their long-term allocations—even to the extent of rebalancing portfolios, by selling bonds and buying stocks in balanced portfolios during the decline—in order to once again reap the rewards of asset class diversification. This culminated in our February 2009 *Asset Class* article titled *"Past Declines & Their Recoveries."* The market decline ended abruptly on March 9, 2009.

From March 2009 to December 2013, the S&P 500 surged 179% (23.6% annually). U.S. large and small value stocks once again surpassed the market return by climbing 243% (29.0% annually) and 275% (31.4% annually), respectively.

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Table 1 Asset Class	Total Returns Jan 2000-Mar 2003	Apr 2003-May 2007	June 2007-Feb 2009	Mar 2009-Dec 2013	Full 14 Years (annualized)
S&P 500 Index	-39.6%	94.7%	-50%	178.9%	64.0% (3.6%)
U.S. Large Value Stocks	-8.1%	147%	-60.6%	242.6%	206.4% (8.3%)
U.S. Small Value Stocks	+12.1%	208.3%	-61.2%	274.6%	402.4% (12.2%)
MSCI EAFE Index	-47.5%	193.3%	-53.6%	127.1%	62.4% (3.5%)
Int'l Large Value Stocks	-28.5%	268.7%	-60.8%	143.4%	151.7% (6.8%)
Int'l Small Value Stocks	-2.3%	306.9%	-57.2%	170%	359.0% (11.5%)

The Full Fourteen Years: 2000-2013

It's almost impossible to know how the average investor fared over the past 14 years, given the significant portfolio shifts that undoubtedly occurred. What we do know is that in the midst of historically volatile markets and economic, political, and foreign policy turmoil, investors were constantly lectured by so-called experts to abandon simple asset class investing principles in favor of traditional stock picking and market timing strategies and nontraditional alternatives. The result? Active management and alternatives, in virtually every form, suffered through one of their worst periods ever.

In contrast, asset class investing did very well on both a relative and absolute basis. The core Equius 100% stock model produced an annual return of 8.8%, or 7.7% after a 1% annual advisory fee (billed quarterly). The S&P 500 Index and MSCI All Country World Index produced annual returns of 3.6% and 3.7%, respectively, over the same period.

Table 2 **Asset Class**	**Jan 2000-Dec 2013 (Annualized)**	**Jan 2000-Dec 2013 (Total)**
Equius 100% Stock Model	8.8%	224%
S&P 500 Index	3.6%	64%
MSCI All Country World Index	3.7%	66.1%

And how did the world's greatest stock picker do in comparison? Warren Buffett's Berkshire Hathaway stock returned 8.6% annually with a much more concentrated investment portfolio.

It's interesting to note also that even though U.S. value stocks outperformed their non-U.S. counterparts over the period, the globally diversified Equius 100% stock model outperformed a U.S.-only model 8.8% versus 8.6% before an advisory fee (both rebalanced annually). This illustrates clearly the power of combining asset class diversification with a rebalancing discipline.

Conclusion

The 2000-2013 period put asset class investing principles through their toughest challenge since the Great Depression. But it was Equius Partners' unique approach of limiting asset classes to an essential core, rebalancing portfolios in a systematic way, and keeping clients "in the game" by setting realistic expectations and providing consistent and effective counseling that set us apart from the crowd and provided a more rewarding investment experience.

Understanding and managing risk and investor behavior will remain our priorities no matter what challenges markets, economies, our industry, or the media present us.

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[1]*The Equius 100% stock model is 21% DFA US Large Company fund, 21% DFA US Large Value fund, 28% DFA US Small Value fund, 18% DFA International Large Value fund, and 12% DFA International Small Value fund. The model is the starting point for all client portfolios. Portfolios are tailored and managed to individual objectives and risk tolerance using fixed income funds (primarily the DFA Five Year Global Fixed fund), tax-managed funds, or other asset class funds with similar structure and objectives that were purchased and retained for tax-loss harvesting strategies. Actual client performance will vary based on asset allocations; the timing of contributions, withdrawals, and rebalancing; fund holdings; and advisory fees. For purposes of this article, the model was rebalanced to target allocations annually. Indexes are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. The returns of the Equius 100% stock model are based on simulations to demonstrate broad economic and investment principles. They were achieved with the benefit of hindsight and do not represent actual investment performance. There are limitations inherent in model performance; it does not reflect trading in actual accounts and may not reflect the impact that economic and market factors could have had on an advisor's decision making if the advisor were managing actual client money. Model performance is hypothetical and is for illustrative purposes only. The information provided is for educational purposes only. Consider the investment objectives, risks, and charges and expenses of all mutual funds carefully before investing. Past performance is not a guarantee of future results.*

Equius 100% Stock Model Characteristics (as of 9/30/2013)

Overall U.S. Non-U.S.

For investors who enjoy "looking under the hood," we offer the following data on the Equius 100% Stock model. A notable detail of our diversification is that risk is spread among 4,260 stocks—refuting the notion that superior returns can only be achieved through portfolio concentration.

Country Allocations (%) View All

	Mix
United States	70.01
Japan	6.48
United Kingdom	6.33
Canada	2.83
France	2.35
Germany	2.27
Switzerland	1.92
Australia	1.52
Sweden	0.99
Other	5.31

Equity Characteristics

	Mix
Aggregate Price-to-Book	1.34
Weighted Average Total Market Cap (in millions)	46,981.58

Expenses

	Mix
Weighted Average Expense Ratio	0.39

Asset Allocations (%)

Quarterly Average Weights	Mix	Market
Large Growth	5.82	16.27
Large Blend	18.67	36.26
Large Value	25.54	18.65
Medium Growth	0.92	4.93
Medium Blend	4.22	9.03
Medium Value	7.44	5.70
Small Growth	0.64	1.65
Small Blend	6.12	3.89
Small Value	30.64	3.62

Equity Characteristics

	Mix	Market
Aggregate Price-to-Book	1.48	2.17
Weighted Average Total Market Cap (in millions)	53,971.01	87,061.63

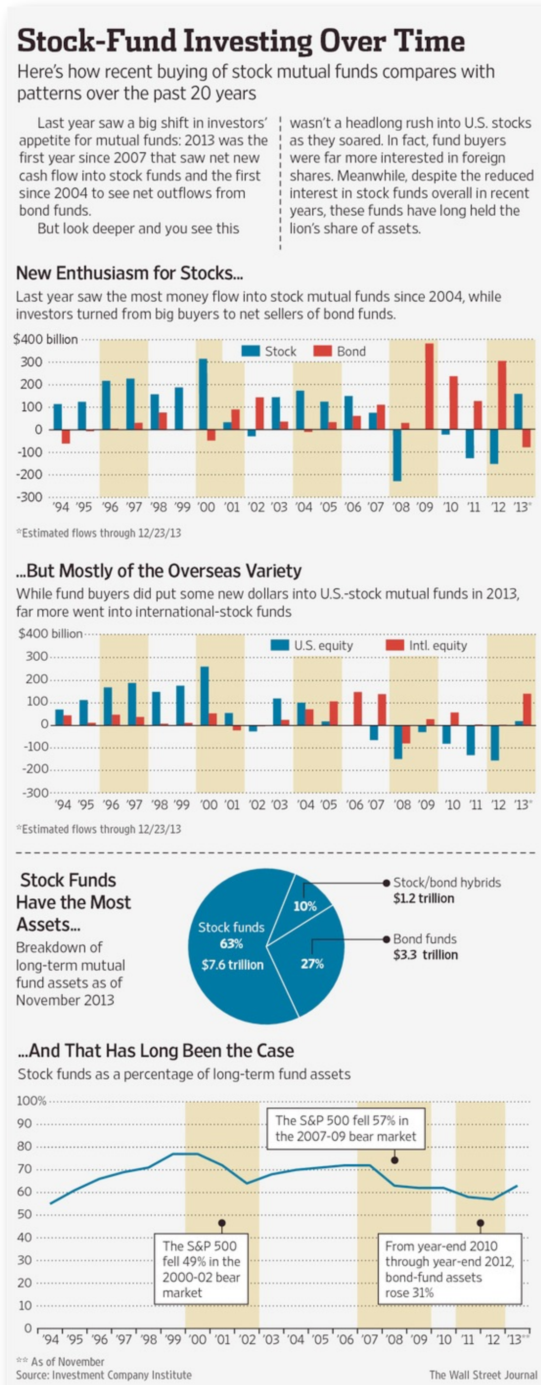
Asset Allocations (%)

Quarterly Average Weights	Mix	Market
Large Growth	0.00	14.58
Large Blend	11.47	33.44
Large Value	30.64	17.03
Medium Growth	0.16	6.38
Medium Blend	10.37	11.03
Medium Value	12.11	6.22
Small Growth	0.95	2.43
Small Blend	7.67	4.44
Small Value	26.62	4.44

Equity Characteristics

	Mix	Market
Aggregate Price-to-Book	1.03	1.71
Weighted Average Total Market Cap (in millions)	30,671.38	54,319.67

Investors Behaving Badly



Source: *The Wall Street Journal, January 6, 2014*