



**RAPPAPORT REICHES**  
CAPITAL MANAGEMENT, LLC

## VALUE ADDED INDEXING<sup>SM</sup> PERSPECTIVES

**Pursuing a Better Investment Experience**

MAY 2015

## 1 Embrace market pricing

The market is an effective, information-processing machine. Millions of participants buy and sell securities in the world markets every day, and the real-time information they bring helps set prices.

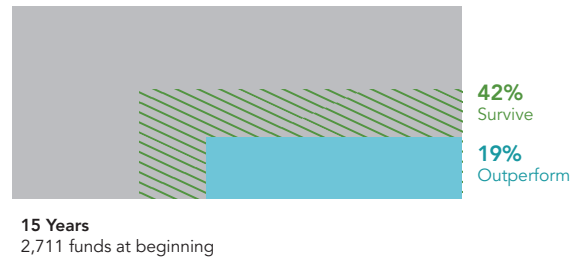
### World Equity Trading in 2014

	Number of Trades	Dollar Volume
Daily Average	60 million	\$302 billion

## 2 Don't try to outguess the market

The market's pricing power works against mutual fund managers who try to outsmart other participants through stock picking or market timing. As evidence, only 19% of US equity mutual funds have survived and outperformed their benchmarks over the past 15 years.

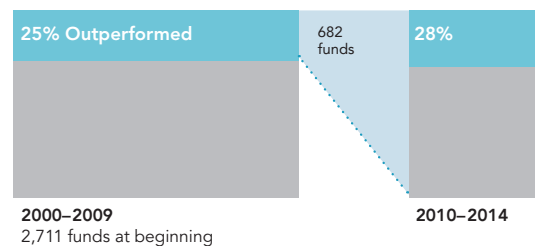
### US Equity Mutual Fund Performance



## 3 Resist chasing past performance

Some investors select mutual funds based on past returns. However, funds that have outperformed in the past do not always persist as winners. Past performance alone provides little insight into a fund's ability to outperform in the future.

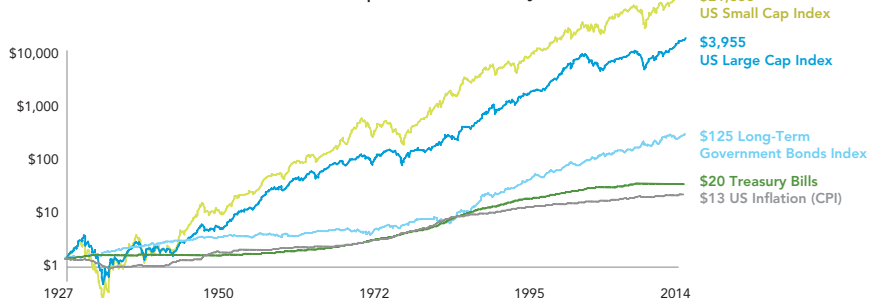
### Do Outperforming US Equity Mutual Funds Persist?



## 4 Let markets work for you

The financial markets have rewarded long-term investors. People expect a positive return on the capital they supply, and, historically, the equity and bond markets have provided growth of wealth that has more than offset inflation.

### Growth of a Dollar, 1926-2014 (Compounded monthly)



## 5 Consider the drivers of returns

Academic research has identified these equity and fixed income dimensions, which point to differences in expected returns. These dimensions are pervasive, persistent, and robust and can be pursued in cost-effective portfolios.

### Dimensions of Expected Returns

#### EQUITIES

<b>Market</b> Equity premium—stocks vs. bonds
<b>Company Size</b> Small cap premium—small vs. large companies
<b>Relative Price</b> Value premium—value vs. growth companies
<b>Profitability</b> Profitability premium—high vs. low profitability companies

#### FIXED INCOME

<b>Term</b> Term premium—longer vs. shorter maturity bonds
<b>Credit</b> Credit premium—lower vs. higher credit quality bonds

## 6 Practice smart diversification

Diversification helps reduce risks that have no expected return, but diversifying within your home market is not enough. Global diversification can broaden your investment universe.

### Home Market Index Portfolio



S&P 500  
1 country, 500 stocks

### Global Market Index Portfolio

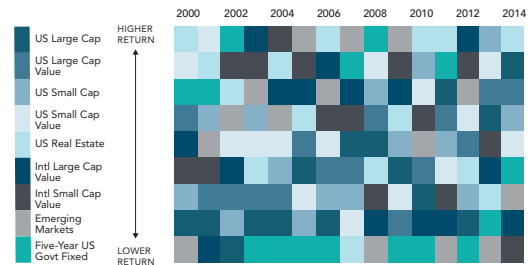


MSCI All Country World Index (IMI)  
46 countries, 8,603 stocks

## 7 Avoid market timing

You never know which market segments will outperform from year to year. By holding a globally diversified portfolio, investors are well positioned to seek returns wherever they occur.

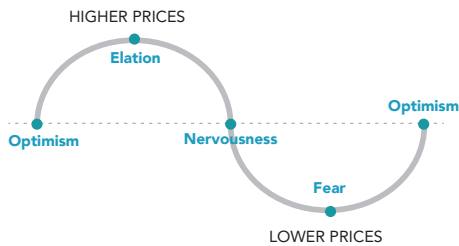
### Annual Returns by Market Index



## 8 Manage your emotions

Many people struggle to separate their emotions from investing. Markets go up and down. Reacting to current market conditions may lead to making poor investment decisions at the worst times.

### Reactive Investing in a Market Cycle



## 9 Look beyond the headlines

Daily market news and commentary can challenge your investment discipline. Some messages stir anxiety about the future while others tempt you to chase the latest investment fad. When tested, consider the source and maintain a long-term perspective.



## 10 Focus on what you can control

A financial advisor can create a plan tailored to your personal financial needs while helping you focus on actions that add value. This can lead to a better investment experience.



**Disclosures:**

**Exhibit 1:** In US dollars. Global electronic order book (largest 50 exchanges). Source: World Federation of Exchanges.

**Exhibit 2:** Beginning sample includes US equity mutual funds as of the beginning of the 15-year period ending December 31, 2014. Survivors are funds that were still in existence as of December 31, 2014. Non-survivors include funds that were either liquidated or merged. Outperformers are funds that survived and beat their respective benchmarks over the period.

**Exhibit 3:** The graph shows the proportion of US equity mutual funds that outperformed and underperformed their respective benchmarks (i.e., winners and losers) during the initial 10-year period ending December 31, 2009. Winning funds were re-evaluated in the subsequent five-year period from 2010 through 2014, with the graph showing winners (outperformers) and losers (underperformers). Fund count and percentages may not correspond due to rounding.

**Data Source (Exhibits 2 and 3):** The US Mutual Fund Landscape 2015, Dimensional Fund Advisors. US-domiciled mutual fund data is from the CRSP Survivor-Bias-Free US Mutual Fund Database, provided by the Center for Research in Security Prices, University of Chicago. Benchmark data provided by MSCI, Russell, and S&P. MSCI data © MSCI 2015, all rights reserved. Russell data © Russell Investment Group 1995–2015, all rights reserved. The S&P data are provided by Standard & Poor's Index Services Group. Benchmark indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Mutual fund investment values will fluctuate, and shares, when redeemed, may be worth more or less than their original cost. Diversification neither assures a profit nor guarantees against a loss in a declining market.

**Exhibit 4:** In US dollars. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. US Small Cap Index is the Fama/French US Small Cap Index; US Large Cap Index is the Fama/French US Large Cap Index; Long-Term Government Bonds Index is 20-year US Government Bonds; Treasury Bills are One-Month US Treasury bills; Inflation is the Consumer Price Index. Fama/French data provided by Fama/French. Eugene Fama and Ken French are members of the Board of Directors for and provide consulting services to Dimensional Fund Advisors LP. Bonds, T-bills, and inflation data © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefeld). Past performance is no guarantee of future results.

**Exhibit 5:** Relative price is measured by the price-to-book ratio; value stocks are those with lower price-to-book ratios. Profitability is a measure of current profitability, based on information from individual companies' income statements.

**Exhibit 6:** Number of holdings for the S&P 500 and MSCI All Country World Index–Investable Market Index (MSCI ACWI IMI) as of December 31, 2014. Indices are not available for direct investment and their performance does not reflect the expenses associated with the management of an actual portfolio. International investing involves special risks such as currency fluctuation and political instability. Investing in emerging markets may accentuate these risks. Past performance is not a guarantee of future results. The S&P data are provided by Standard & Poor's Index Services Group. MSCI data © MSCI 2015, all rights reserved.

**Exhibit 7:** In US dollars. Chart is for illustrative purposes only. Index descriptions for asset groups: US Large Cap is the S&P 500 Index, provided by Standard & Poor's Index Services Group. US Large Cap Value is the Russell 1000 Value Index. US Small Cap is the Russell 2000 Index. US Small Cap Value is the Russell 2000 Value Index. Russell data © Russell Investment Group 1995–2015, all rights reserved. US Real Estate is the Dow Jones US Select REIT Index, provided by Dow Jones Indexes. International Large Cap Value data provided by Fama/French from Bloomberg and MSCI securities data. International Small Cap Value data compiled by Dimensional from Bloomberg and Style Research securities data. Emerging Markets is the MSCI Emerging Markets Index (gross dividends), © MSCI 2015, all rights reserved. Five-Year US Government Fixed is the Barclays Capital Treasury Bond Index 1–5 Years, formerly Lehman Brothers, provided by Barclays Bank PLC. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.

Dimensional Fund Advisors LP is an investment advisor registered with the Securities and Exchange Commission.



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