

What to do about your January portfolio disaster

Although the overall news is bad we wouldn't be writing about this if we didn't have something of value for you. Let us start with the bad news.

As of this writing, Jan. 23, 2008, the S&P 500 is down over 11 percent year-to-date, the Dow Jones is down over 10 percent and the Nasdaq is down over 15 percent. Not only have all the major markets suffered a correction (defined as a loss of 10 percent or more); they are on the verge of becoming Bear markets (defined by a loss of 20 percent or more).

We don't know where the markets will be by the time you read this article but here is a table to illustrate losses based on year-to-date S&P 500 and Nasdaq volatility using different portfolio values:

Portfolio value on 1/1/2008	Loss based on S&P volatility	Loss based on Nasdaq volatility
\$3,000,000	\$330,000	\$450,000
\$5,000,000	\$550,000	\$750,000
\$10,000,000	\$1,100,000	\$1,500,000
\$25,000,000	\$2,750,000	\$3,750,000

You can use the table to extrapolate losses based on higher portfolio values.

Politicians and the media are starting to talk about a recession or a stagnation (recession with inflation), huge corporations are suffering tens of billions of dollars in losses due to subprime investments, unemployment is on the rise and housing starts are at a 16-year low. How do you think your money will fare going forward and what steps are you taking to protect your wealth?

Why do you suppose this is probably not the first time you have suffered such losses? This may be a good time to evaluate, isolate and fix the problem.

Now the good news.

David Swensen is Yale University's chief investment officer for its \$18 billion endowment fund. On his 22-year watch, Yale's endowment has grown tenfold and has spun off enough cash to fund about one-third of the university's annual operating budget.

Swensen has cranked out an average



Chris Snyder & Hutch Ashoo

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annual return of 16.1 percent – the best performance of any college endowment in the land; by comparison, the S&P 500 posted an average annual gain of 12.3 percent during that period.

Swensen is managing an endowment with a time horizon best measured in decades rather than years. As wealth managers we help clients face many of the same issues Swensen does. We depend upon the “spendable” funds our nest eggs produce yet like to see the values growing.

Swensen actually strives to produce equity market-like results for the Yale endowment. The expected return of his target portfolio is 10.1 percent a year.

While Swensen aims for the broad market's return, he diversifies the portfolio's assets to provide insulation from the equity market's potential for outsized losses in any given year.

Swensen's biggest allocations are to

private equity, real assets and absolute return strategies, representing nearly 70 percent of the Yale target portfolio. How does this compare with your portfolio?

Yale Endowment asset allocation targets

Real assets	27 percent
Absolute return	25 percent
Private equity	17 percent
Foreign equity	15 percent
Domestic equity	12 percent
Fixed income	4 percent

Source: Yale Foundation

In his book, “Unconventional Success: A Fundamental Approach to Personal Investment,” Swensen concludes the best thing investors can do for their portfolios is to steer clear of active management. It's too expensive and most portfolio managers aren't very talented.

Very interesting coming from an active manager who has achieved outstanding performance results.

Besides, individuals “tend to behave in ways that undermine the effects of active management,” writes Swensen, “You've got a lot of people crashing around doing dumb things.”

Most affluent investors are guided by advisers who are typically making the

Things to ponder

1. Why do experienced investors continue to lose money?
2. World-class investment management is independent and considers the view from 30,000 feet.
3. It is always greener on the other side; past performance is no indication of future performance.

investment decisions on their behalf. So are you really to blame when all you are doing is following your professional investment adviser's advice? One thing is for sure, you are paying for their mistakes with your hard-earned money and this may affect how you and your family live the rest of your lives.

In our opinion world-class money management must rise above the noise (see our past articles titled “What should smart investors do?”); it is managed independent of the adviser and provides you with high confidence of achieving everything that is important to you. For details download “Four Factors the Affluent Must Know to Avoid Financial Disaster and Secure Their Dreams” through our Web site.

You, too, might benefit from investments that diversify the stock market risk while providing you income and stock market-like returns. Mind you, this is a very complicated area where very few have succeeded.

Before you take any action, remember to evaluate the investment decision-maker; hopefully it isn't you. Also remember, it is always greener on the other side. Be sure that you and your investment advisers are qualified to take the 30,000-foot look before you make changes on the ground. Just because an investment has done well through this rough time period doesn't mean it will continue to perform well. Be skeptical and ask a lot of questions.

We welcome any questions and may answer the good ones in a future article.

Haitham “Hutch” E. Ashoo and Christopher G. Snyder are the principals of Pillar Financial Services, a wealth management firm in Walnut Creek. Contact them at 925-356-6780 or www.pillaronline.com.