The Investing Evolution: How We Got Here

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by Robert Isbitts
of Sungarden Investment Research

This week I attended the annual Schwab IMPACT conference in Denver. This event is one of the biggest and longest-running events for the investment industry. I have gone most years since the turn of the century, and the evolution of thought among independent investment advisors is astonishing to see.

One of the main themes of the conference was the urgency the industry feels to go beyond traditional asset allocation. I could not agree more with that concept. But as for the execution of it, I see what I have seen so many times before…a good idea to help investors, which the industry then bludgeons to death with complexity, excessive fees and a bunch of me-too products. I will devote much more space in this blog and in my Marketwatch Retirementors column to this in the coming weeks and months.

There is no question that what has been accepted as industry standard has changed over the decades. The question is where should we be going next? For now, just understand where we have come from:

1. In the beginning of what we will call the modern investment era (the 1990s is when I feel investors outside of the uber-wealthy first started looking beyond stockbrokers for help preserving and accumulating wealth), they looked at the stock market as a reference point. The S&P 500 Index, which was mainly used by pros gradually, replaced the Dow Industrials as the most popular benchmark.
2. In time, investors started to look to balance their stock portfolios with bonds. Borrowing from the pension world, investors discovered the 60%/40% stock/bond approach. The 60% was S&P 500 and the 40% was the then-named Lehman Bond Index.
3. A combination of research and marketing convinced investors that one type of stock and one type of bond was not sufficient in a global, evolving market. The science and art of asset allocation exploded into a complex set of "asset classes." Keeping up with Jones's meant owning 12, 15 or more types of securities. The goal of diversification–to reduce volatility, seemed lost in the battle over whose asset allocation scheme was the best. Benchmarks like the Dow Jones Relative Risk Indexes have been a good proxy for this very popular approach to investing.

Perhaps it's time to step back and take a look at the labyrinth that has been created for the beleaguered investor.

At Sungarden, we think that investors are ready to simplify the pursuit of income growth with lower expected volatility. But rather than revert to two "generations" ago and return to the basic stock-bond paradigm, we see value in constructing portfolios in this way:

1. Own individual stocks to avoid mutual fund expense ratios (stocks do not have them). Depending on the investor's risk tolerance, the stocks are dividend or growth-oriented.
2. Alongside the stocks, hedge against major declines by owning inverse ETFs against perceived areas of excessive valuation in the market.
3. Actively manage the portfolio between these two segments, understanding that they are separate decisions. "Active" means whatever the lowest turnover rate is to get the job done.

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