Smoother Ride Part II - Strategies & Historical Performance "Closed Captions"

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Hello again everyone. This is Matt Curfman from Richmond Brothers with the second edition of my series titled, "Smoother Ride." Thank you so much for tuning in. So if you watched my introductory video, you kind of got a feeling for what sorts of questions and solutions we're trying to come up with to help address the current environment and what we've seen over the last handful of years.

With that in mind, I just want to start off with some disclosures. One, the information I'm about to share is for informational and educational purposes only. It is not meant to be a recommendation for you or your specific circumstances. We really should have a one-on-one meeting or discussion with you or your advisor through Richmond Brothers to appropriately go through your tolerance for risk. We can use Riskalyze to address some of these questions and suitability. And just because we have an option that doesn't mean it fits everyone and this is not meant to be a cookie cutter approach.

So we're going to give some historical context. We're going to talk about back-tested performance really for most of my career, which goes back to the late '90s and early 2000s. Again, these strategies historically were not previously allowed or available, I should say, through Fidelity. So they have now become available and so I can start to create this video series to educate you. If you watch any of these videos and they intrigue further interest, you can certainly reach out to questions@richmondbrothers.com and we can make sure to set a follow-up call/video appointment to review with your advisor if these strategies could make sense. Also, past performance is not indicative of future results.

So with that, I'm going to do a quick screen share here. Don't get too dizzy. So here is the document I wanted to spend a little bit of time on and so with this in mind – I'm going to zoom out here – you can see Beacon Capital Management. So, who is Beacon? Beacon is a third-party money manager that is now available through Fidelity's platform and Beacon was founded by another financial advisor, who was a registered investment advisor. The founders name is Chris Cook and he was very much in a similar type of business as we are, and Chris used these and formulated these strategies with his clients over a lot of years. And these strategies became available or started to become available on larger platforms so other financial advisors could consider them where appropriate with their clients beginning, I believe, in the year 2011.

So what we're really looking at here is historical context. I want to kind of go through this. You can see this is data measured from January of 2000 through December 31 of 2021, so these are calendar year returns. You can see the calendar year over here on your left. On the far right you see the Vanguard 500 Index, and the symbol is VFINX, as you can see here. We included this on the document more to just

have a back drop on the context on what was happening in the environment and the markets during each of these calendar years. This is not meant to be a comparison. We're not looking to beat or outperform the market here. That's just there for backdrop and context. Now, each of these are three strategies that we'll have available that we can consider. So, Vantage 2.0 Conservative, Balanced, and Aggressive, and each of these has a target allocation.

The aggressive is an all equity, so all stock compensation target. Balanced is going to target a 70/30 mix and the conservative is going to actually target a 40/60 stock/bond mix. Now many of you know we speak in Riskalyze language and risk scores. So to give you some context, if you just had Vanguard 500 Index, that comes in, according to Riskalyze, at a risk score of 76. And that's on a scale of 1 to 99. The conservative model here comes in at a risk scale of a 38. Balanced comes in at a risk scale of 50. And aggressive comes in at a risk scale of 55, according to Riskalyze on the day of this recording.

So with that in mind, if you go back, many of you remember – if we kind of highlight the far right column – the S&P 500 or the Vanguard 500 Index in the early 2000s was coming out of the technology bubble from the 90s, and also September 11 happened and so that caused our economy to move into recession. Go back to 2008 and the Vanguard 500 Index dropped 37% and that was during the financial credit crisis, the real estate recession, otherwise known as The Great Recession, for context. You can kind of see each of these strategies have different returns, but the further you go from conservative balance to aggressive, the more equity exposure you typically have.

So what I wanted to spend some time on – and you'll have access to this exact document with all of these data points and then all of the disclosures – but, two things. If you look at the Vanguard S&P 500, one, it's a cap-weighted index. What does cap-weighted index mean? There's 500 constituents in the S&P 500 and cap-weighted means the bigger each constituent is, the more their return or loss matters to the market. So a really, really big entity that might be worth a trillion dollars in size, might have more impact both positively and negatively on the broad market in a cap-weighted index.

So there's data I have shared with you over the last year, where technology has become a really big portion of the overall market. And the top 5 size companies in the Vanguard 500 Index represent probably about 20 to 30% of the overall market in a cap-weighted index. That means 1% of the constituents can weight about 20 to 30% of the whole market. That used to not be a problem if you go back historically in the market, but since businesses have gotten bigger and bigger, we just want to be aware of it.

All three of these strategies, if we have equity exposure, there are actually 11 sectors of the market. Technology is one, utilities, consumer staples – and so I'll go through those here in just a minute. Any equity exposure we have in these three strategies we would want to equal weight them so we're not cap weighted, we would equal weight them. And then they'll be, any of these strategies that had bonds, we want to also equal weight those to start. And what's different is equal weighting – and then if the equal weighting of those benchmarks, any of the equity exposure, if they drop 10% from a previous high, it triggers a defensive move. And what does that mean? I'll talk about that in a minute. On the bond side, if bonds drop 4% then this triggers a defensive move.

So if we go back to this historical comparison, that's really what we're showing here. You can kind of see in extreme negative years all of these strategies have done reasonably well in the context of this back drop. In 2008, when the market did really poorly, these strategies ended positive. Now that seems a little off the wall, but it's possible the reason was at the first 10% drop in the markets, the equity strategies got more defensive and the worse the market went, the better those strategies ended up doing. Now again, past performance is not indicative of future results, but I wanted this for context. It's not always perfect either. If you look at the year 2011, you can see the S&P or the Vanguard 500 Index squeaked out a 1.97% gain. The conservative made 3, the balanced lost 1, and the aggressive lost nearly 5%. Even in 2013, the Vanguard 500 made 32%. The all equity allocation over here only made 25.5%.

So a cap-weighted index is not necessarily the bench mark. I just wanted this for comparison. In the year 2015, here's another year where the Vanguard 500 Index squeaked out an over 1% return. These strategies all lost. So with a little bit of historical context, what's happening is if the market drops or the equity portion drops 10% early in the year, the rest of the year in the calendar year return, like this document shows, is really trying to make that back up and it depends on a lot of outside circumstances. If the market were to drop 10% from its high in November, and we only have one month left until the end of the year, it's of course more challenging for these strategies to compete against the broad-based Vanguard 500 Index.

So there's a quick summary here at the bottom that shows annualized return for those 21 years, highest return in any given year, and the lowest return or lowest loss. You can see over here the S&P buy and hold strategy ended up at 7.41% a year for those 21 years. Now, that is a very stagnant number; money was not added, money was not taken out. It's just what did the Vanguard 500 Index perform in any of those given years. Highest return was 32%, lowest was minus 37. So many of you as clients know from a Riskalyze language that's quite a wide variant. If you pop over here to the aggressive strategy, you remember this targets an all equity approach, equal-weighted but with a 10% downside trigger. This ended up returning or averaging about 9.96%. The highest return was 25.49. The worst year was -8.58. And again, as you get more balanced, the numbers come down a little bit. As you get more conservative, they come down a little bit. If you get the sense of the title of my video, Smoother Ride, that's really what we're getting at. I'll go through in the next video – I'm going to take this exact same document, I'm going to go into some of the disclosures, and dive a little deeper into this, but this video is already at 10 minutes so I'm going to pause for now. And tune in to my next video for the next series of education. Thank you so much for checking in.

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Sources:

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