OSS Health

The Abernathy Group II

Family Office

2021 Mid Year Outlook

Quarterly Market Review

Second Quarter 2021

This report features world capital market performance and a timeline of events for the past quarter. It begins with a global overview, then features the returns of stock and bond asset classes in the US and international markets.

The report also illustrates the impact of globally diversified portfolios and features a Mid-Year Outlook and a quarterly topic.

Overview:

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Are the Markets Overvalued?

3 Techniques to Reduce Risks

The most common questions being asked today regarding the investment environment are the correct questions.

- Are the U.S. and Global stock and bond markets overvalued?
- How can I protect the value of my assets if we go into a downturn?

Trying to time the stock and bond markets is a "fools-game". It is well documented that professional investors and retail investors alike, are unable to predict the movements of the stock and bond markets.

What Should Investors Expect?

History, and PRŪF – The Science of Investing™ offers investors' valuable information when forming reasonable expectations for investment returns over the long-run.

As with any intelligent investment, the best starting point is understanding A) the risks I am taking with my investment capital, and B) the future returns myinvestment is likely to offer, in exchange for taking those risks.

The first step is to determine the cost and value of the investment, and how it compares to historical costs. For instance – if the current value of an investment is *higher* than historical values, it is reasonable to expect 1) the risks are higher, and 2) future returns are likely to be *lower* than historical returns.

And vice-versa.

If current values are *lower* than historical costs, it is reasonable to expect 1) the risks are lower and, 2) future returns are likely to be *higher* than historical returns.

Overvalued or Undervalued?

Which brings us back to the first question above - Where are the current valuations of the stock and bond markets – are they overvalued or undervalued?

There are many methods of determining the cost/value of an investment. While there are an almost countless number of considerations which are specific to each individual investment, there are broad measurements of the stock and bond markets which will help us answer this question. One of the broadest measurements is called the "Buffett Indicator"[1], which was used by Warren Buffett as a broad indicator of the investment marketplace.

[1] The "Buffett-Indicator" is NOT a market timing indicator. It is a broad-brush amalgamation of all market capitalizations of the S&P 500, compared with to the total value of ALL reported revenue produced in the U.S.

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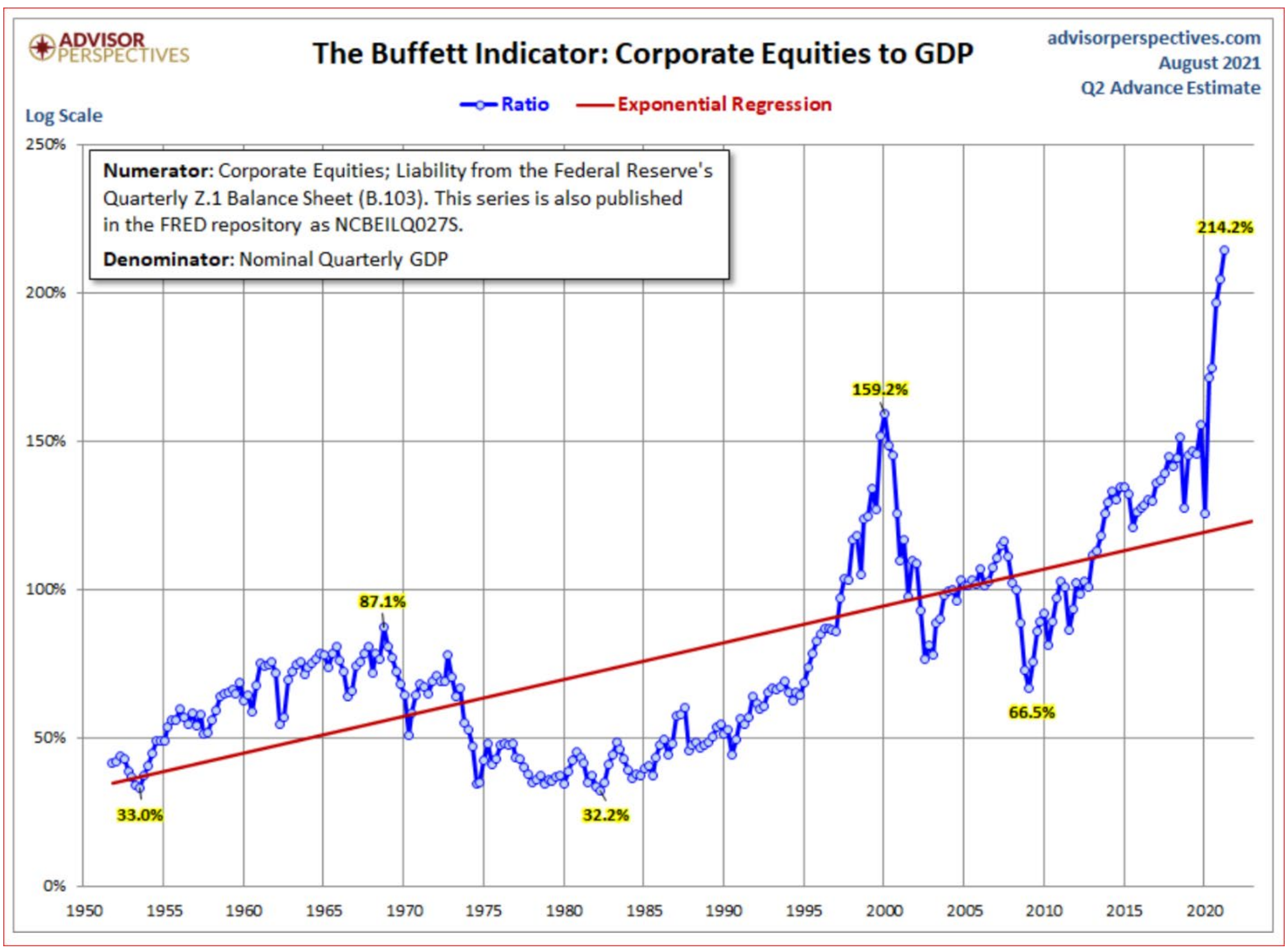
The Buffett Indicator compares the current market capitalization (the prices) of all securities in the S&P 500, with the U.S. Gross Domestic Product (the value of all goods AND services produced in the U.S.).

The “average” value of the “Buffett Indicator” since 1950 is 0.88. *As you will see from the chart below, the current value is 2.14*. *This indicates the current stock market’s value is more than twice as expensive as the average value of the history of this indicator. In short, current market prices offer higher risks and lower future returns… not an attractive combination.*



Reducing Risk

This brings us to question number 2. Since the risks of investing today are higher than average, how can I protect the value of my assets if we go into a downturn?

During market downturns, the vast majority of securities move to lower valuations. This means that most *current investments will decrease in value* – that is the bad news. However, there is good news. Downturns' end, and prices recover. And as prices move down, intelligent investors realize that downturns end. If you are a long-term investor, you will continue to invest at these lower prices with an understanding that all economies go through downturns, and the vast majority recover, and move to new heights in a short time. This means your former highly valued investments, which moved lower, will move back to higher levels, AND the new investments made during the downturn, at lower prices will also move higher. This combination is the "compounding" effect of consistent, long-term investing, and is commonly called "dollar cost averaging".

For those investors who would like to lower current risks, and potentially mitigate some of the downturn when it takes place, we can suggest 3 ideas.

Increase Diversification

The first idea is to *broadly diversify your stock and bond investments*. Most of the funds in the OSS 401k plan are widely diversified. So, we will not spend too much time on this topic – yet if you feel you are NOT well diversified, or if you would like to increase your diversification, please come and see us or give us a call. The OSS 401k plan has many highly diversified, high-quality investments specifically chosen to be *low-cost*, and available to all.

Increase Investment Allocations to Dividend-Paying Stocks

The second method to decrease risk is to add investments in dividend paying companies, which are likely to continue increasing their dividends.

Public companies that regularly increase their dividends are called dividend growth stocks. They often appreciate *and* provide stability in your portfolio because they deliver returns in two ways:

Capital Appreciation: Dividend growers tend to be high-quality, stable companies. They often provide a strong defense against market downfalls.

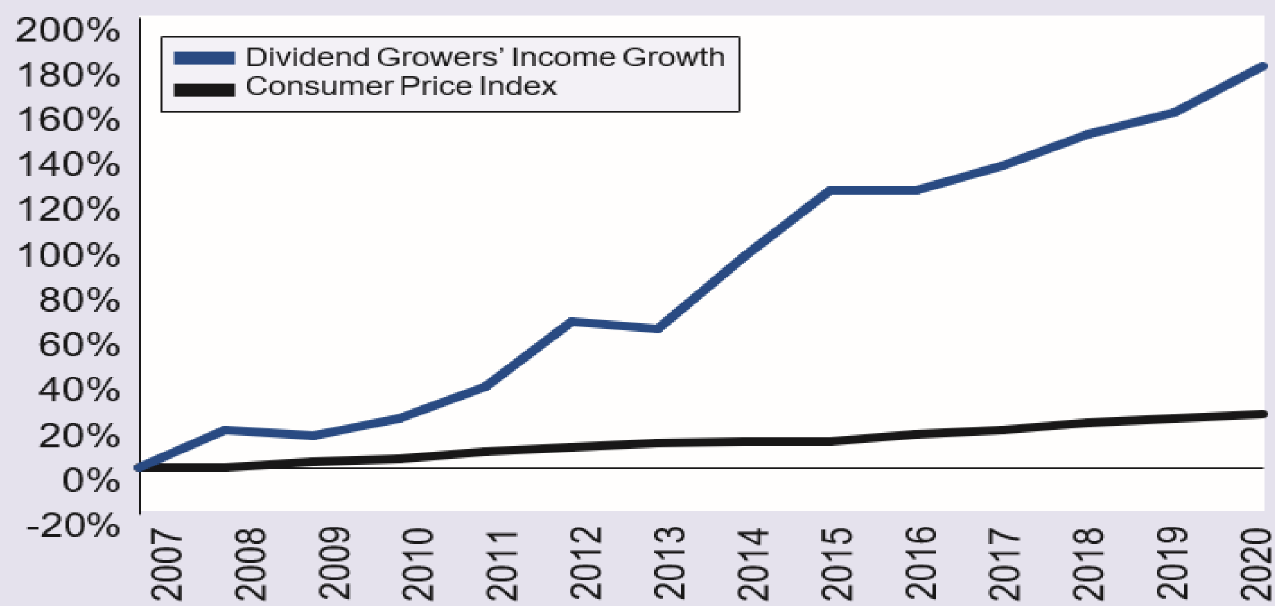
These stocks have delivered competitive returns with *less risk* than the overall stock market through full market cycles because dividends tend to reduce downside risk when markets fall. Below you will find a chart detailing the positive effect of dividends during “down” markets.

Year	Market Milestone	Percent Change	Number of Years	Annualized Return, No Dividends	Annualized Return with Dividends
1877	Low	-	-	-	-
1906	High	456%	29.3	5.1%	10.1%
1921	Low	-69%	14.9	-7.5%	-2.0%
1929	High	396%	8.1	21.9%	28.4%
1932	Low	-81%	2.7	-44.9%	-41.2%
1937	High	266%	4.7	32.1%	38.7%
1949	Low	-54%	12.3	-6.2%	-0.8%
1968	High	413%	19.5	8.8%	13.3%
1982	Low	-63%	13.6	-7.0%	-3.0%
2000	High	666%	18.1	11.9%	15.3%
2009	Low	-59%	8.5	-9.8%	-8.1%
Now	-	347%	-	N/A	N/A

Based on inflation-adjusted S&P Composite monthly averages of daily closes.

1) **Income Generation:** Dividend paying companies do NOT often lower their dividends during market downturns which typically limits price depreciation. While dividend paying companies generate helpful capital appreciation, dividend paying companies provide a steady stream of income while typically *growing the stream of dividends faster than inflation since 2007* as indicated in the **chart below**.

Growing Dividends Outpace Inflation



Note: Chart shows percentage growth of dividend payments for the NASDAQ U.S. Dividend Achievers Select index compared to the gain of the consumer price index from 2007 through 2020.
Source: Bloomberg.

Increase Investment Allocations to Non-U.S. Stock Markets

The third recommendation would be for those investors who have allocated the vast majority of their 401k plan to U.S. investments. Consider embracing a more significant allocation to non-U.S. investments in both "Developed" markets and in "Emerging Markets". Here's why:

1) The U.S. economy makes up approximately 25% of the "global economy". If you are NOT diversified globally, you are missing out on the growth from 75% of the countries making up the global economy.
2) Most of the "Developed" (largely made of Europe and Japan) and "Emerging" markets (made up of over 30 smaller countries), are significantly less expensive than the U.S. markets. Paying less for future earnings is likely to lower your risks *AND* offer higher future returns.
3) Most "Developed" and "Emerging" markets pay *higher dividends* than U.S. companies. As mentioned above, collecting dividends is an attractive method of assuring growth of your assets, as dividend paying companies tend to decline less during downturns and appreciate faster during the recovery phase of a typical market cycle.
4) Most of the "Developed" and "Emerging" markets are being affected by the current virus, just like the U.S. However, both "Developed", and "Emerging" markets are approximately 6 months behind the U.S. in their fight to bring back normal economic conditions. The combination of economic stimulus plans, and effective vaccine distribution is likely to allow both "Developed" and "Emerging" markets to follow the same path to economic recovery the U.S. is following, with a six-to-nine-month lag. Each recovering market is likely to appreciate materially, similar to the U.S.'s recovery, once recovery becomes apparent.

Summary

The current values of the U.S. stock and bond markets are near historic highs. This is likely to mean current investments offer higher than normal risks, and lower than normal future returns. As said, this is an unattractive combination.

With stock and bond market valuations at current levels, *investors must be effectively diversified to lower risks* and lessen the higher probability of downturns.

Investors can *lower their risks* by increasing allocations to dividend paying and dividend growing stocks.

It is equally likely that increasing investments in non-U.S. markets, both “Developed” and “Emerging”, will lessen exposure to the overvalued U.S. market, and provide higher long-term returns. Both “Developed” and “Emerging” markets are *less expensive than the U.S. markets*, and *pay higher dividends*. As a consequence, they are likely to offer *higher* future returns, with *less* risk, as they overcome the depressed economic conditions caused by the virus over the last year or so.

OSS 401K PLAN

The national average for 401k Plan advisory fees is slightly over 1% per year.

The OSS 401k Plan, which is available for all employees at OSS, has fees of less than 0.2%, which is 80% less than the national average, and has no conflicts of interest of any kind.

In addition to OSS management’s generous contributions to each employee’s 401k Plan, the investment choices available have been specifically chosen to *minimize fees and maximize investment returns*.

If you have any questions or would like to discuss investment choices, retirement strategies, or the proper contribution amounts to ensure you are saving enough for retirement, please fee free to make an appointment to see Steven Abernathy at the Powder Mill Road location or call 212-293-3469 for a telephone appointment.

Quarterly Market Summary

Index Returns

2Q 2021	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
	STOCKS				BONDS	
	8.24%	5.65%	5.05%	10.17%	1.83%	0.35%
Since Jan. 2001						
Avg. Quarterly Return	2.4%	1.7%	3.1%	2.6%	1.2%	1.1%
Best Quarter	22.0% **2020 Q2**	25.9% **2009 Q2**	34.7% **2009 Q2**	32.3% **2009 Q3**	4.6% **2001 Q3**	4.6% **2008 Q4**
Worst Quarter	-22.8% **2008 Q4**	-23.3% **2020 Q1**	-27.6% **2008 Q4**	-36.1% **2008 Q4**	-3.4% **2021 Q1**	-2.7% **2015 Q2**

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index [net div.]), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond Market ex US (Bloomberg Barclays Global Aggregate ex-USD Bond Index [hedged to USD]).

Long-Term Market Summary

Index Returns as of June 30, 2021

	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
	STOCKS				BONDS	
1 Year	44.16%	33.60%	40.90%	34.83%	-0.33%	0.05%
5 Years	17.89%	10.36%	13.03%	4.62%	3.03%	2.80%
10 Years	14.70%	5.70%	4.28%	6.85%	3.39%	4.12%

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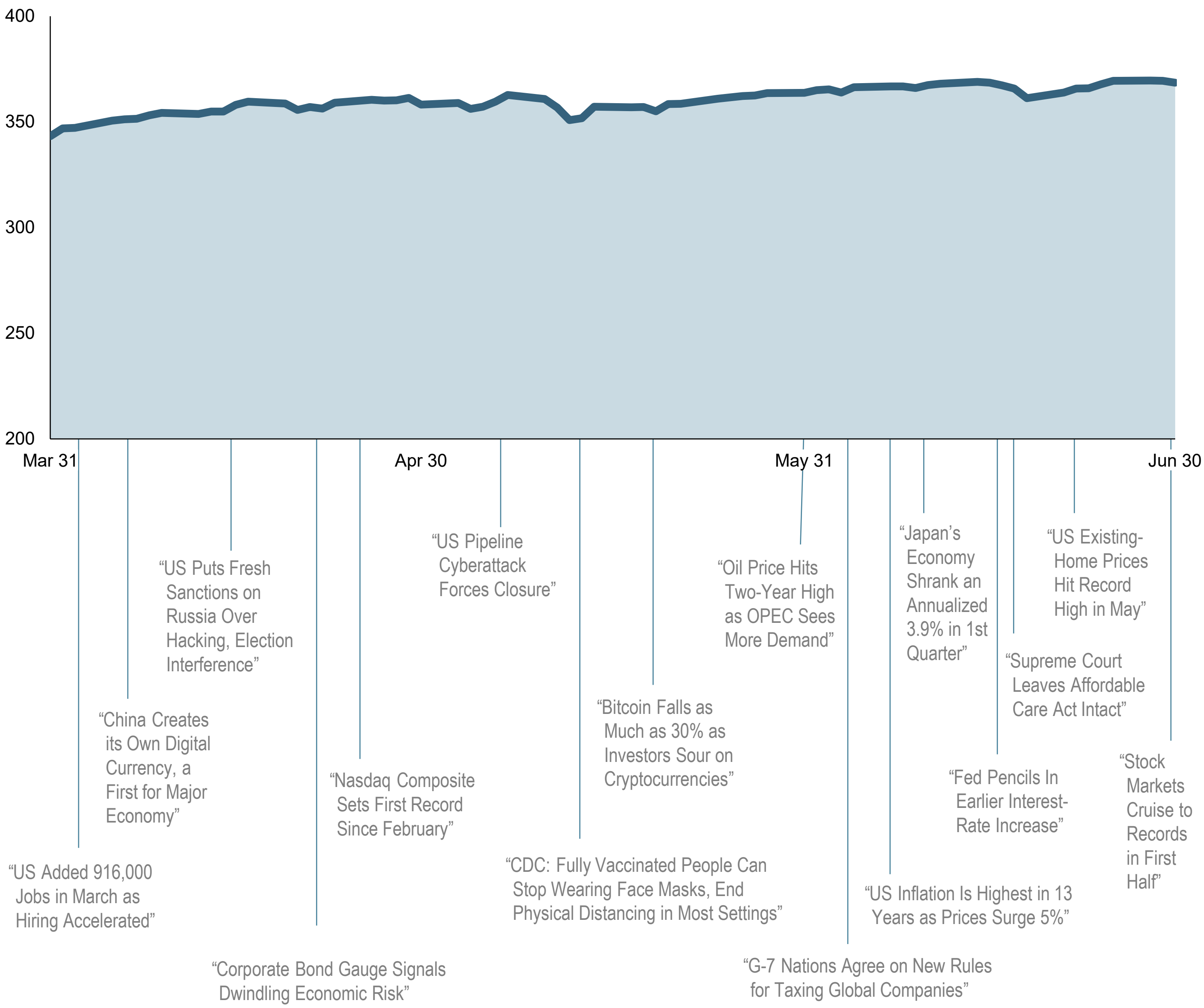
World Stock Market Performance

MSCI All Country World Index with selected headlines from Q2 2021

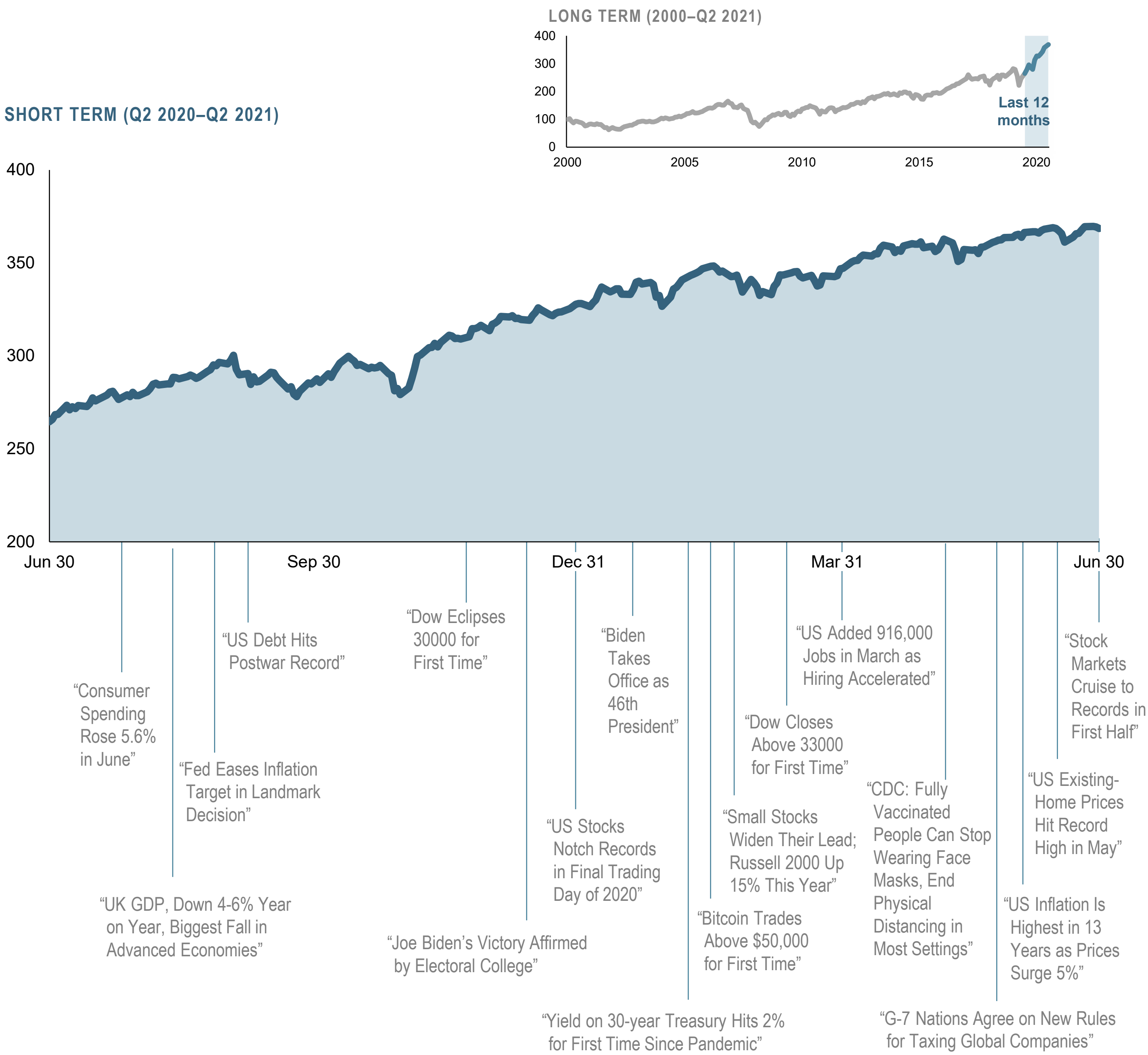


These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.

Graph Source: MSCI ACWI Index [net div.]. MSCI data © MSCI 2021, all rights reserved.
It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. **Past performance is not a guarantee of future results.**

World Stock Market Performance

MSCI All Country World Index with selected headlines from past 12 months



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Graph Source: MSCI ACWI Index [net div.]. MSCI data © MSCI 2021, all rights reserved.

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World Asset Classes

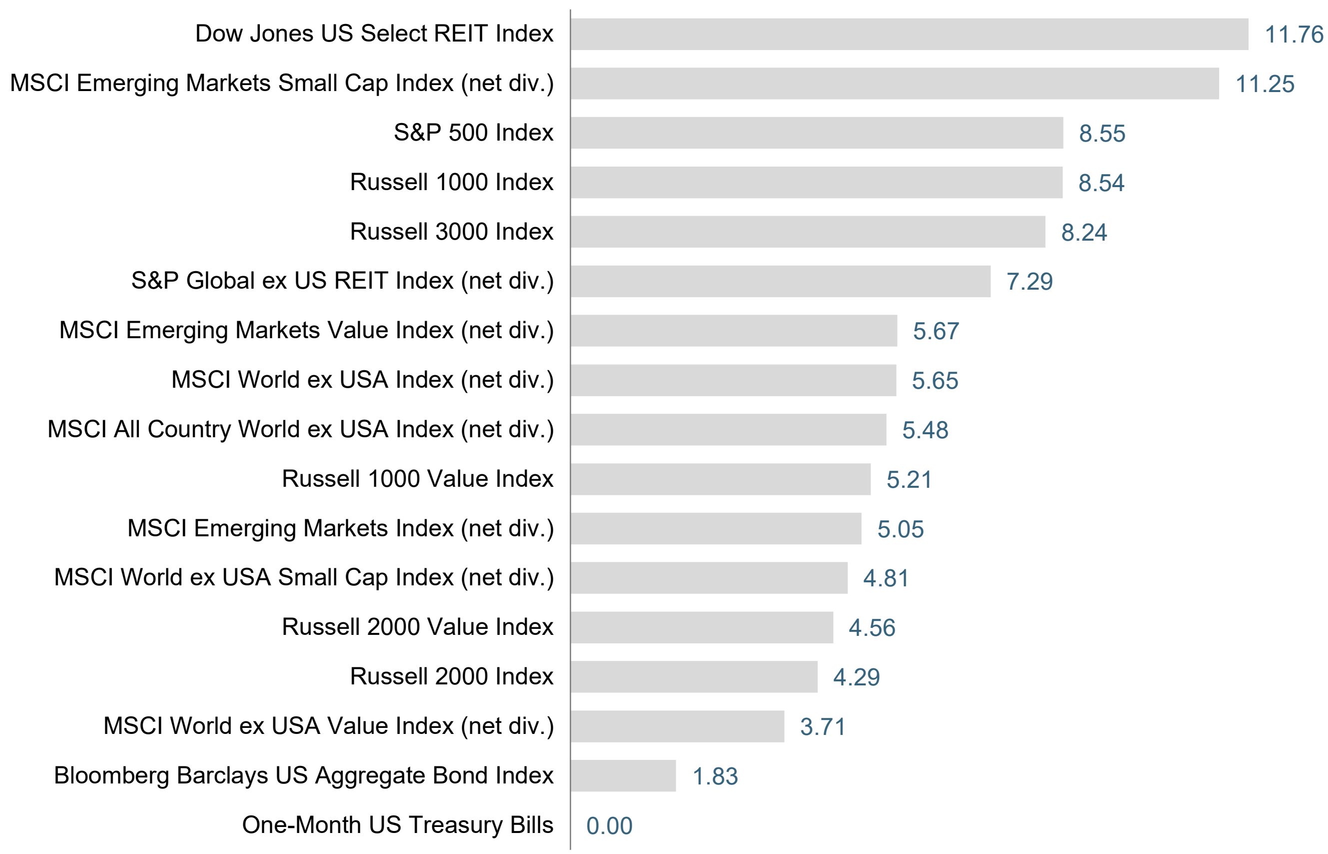
Second Quarter 2021 Index Returns (%)

Equity markets around the globe posted positive returns in the second quarter. Looking at broad market indices, US and non-US developed markets outperformed emerging markets for the quarter.

Value performance was mixed in the US, with small value outperforming small growth but large value underperforming large growth. Value underperformed growth in non-US developed markets and outperformed in emerging markets.

Small caps underperformed large caps in the US and non-US developed markets but outperformed in emerging markets.

REIT indices outperformed equity market indices in the US and non-US developed markets.



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US Stocks

Second Quarter 2021 Index Returns

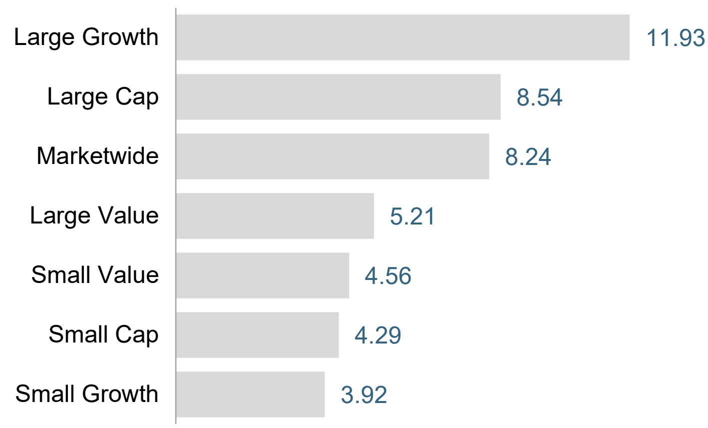
The US equity market posted positive returns for the quarter and outperformed non-US developed markets and emerging markets.

Value underperformed growth in large cap stocks but outperformed growth in small cap stocks.

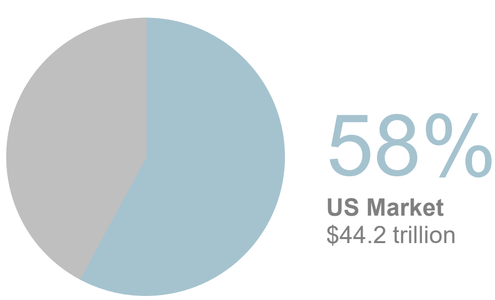
Small caps underperformed large caps.

REIT indices outperformed equity market indices.

Ranked Returns (%)



World Market Capitalization—US



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Growth	12.99	42.50	25.14	23.66	17.87
Large Cap	14.95	43.07	19.16	17.99	14.90
Marketwide	15.11	44.16	18.73	17.89	14.70
Large Value	17.05	43.68	12.42	11.87	11.61
Small Value	26.69	73.28	10.27	13.62	10.85
Small Cap	17.54	62.03	13.52	16.47	12.34
Small Growth	8.98	51.36	15.94	18.76	13.52

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International Developed Stocks

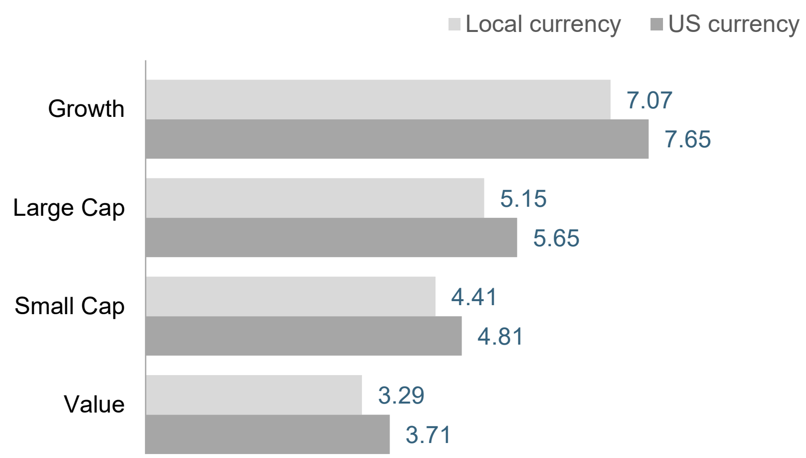
Second Quarter 2021 Index Returns

Developed markets outside the US posted positive returns for the quarter, underperforming US equities but outperforming emerging markets.

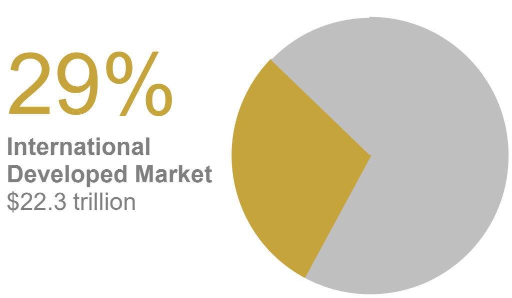
Value underperformed growth.

Small caps underperformed large caps.

Ranked Returns (%)



World Market Capitalization—International Developed



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Value	12.35	35.85	4.22	8.07	3.87
Large Cap	9.92	33.60	8.57	10.36	5.70
Small Cap	9.92	42.28	8.92	11.88	7.66
Growth	7.26	31.08	12.56	12.35	7.35

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Emerging Markets Stocks

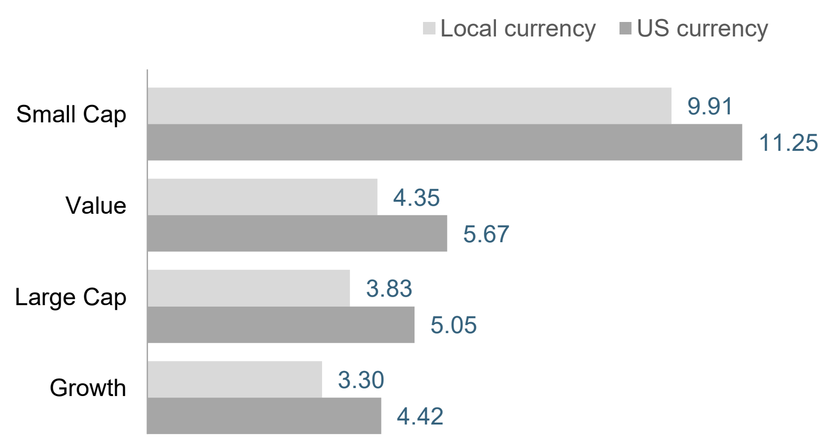
Second Quarter 2021 Index Returns

Emerging markets posted positive returns for the quarter, underperforming the US and non-US developed equity markets.

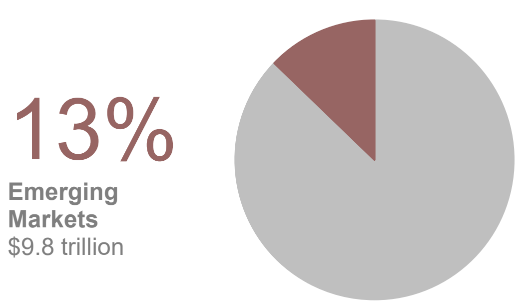
Value outperformed growth.

Small caps outperformed large caps.

Ranked Returns (%)



World Market Capitalization— Emerging Markets



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Small Cap	19.78	63.75	12.31	11.86	4.55
Value	10.01	41.59	7.81	9.70	1.80
Large Cap	7.45	40.90	11.27	13.03	4.28
Growth	5.04	40.08	14.44	16.14	6.63

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Select Market Performance

Second Quarter 2021 Index Returns

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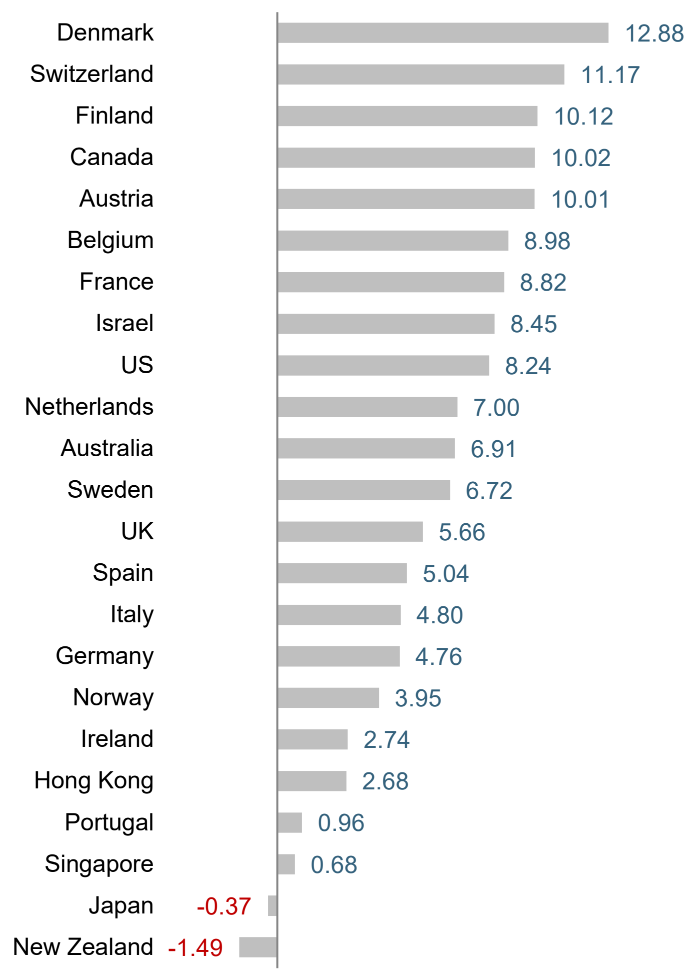
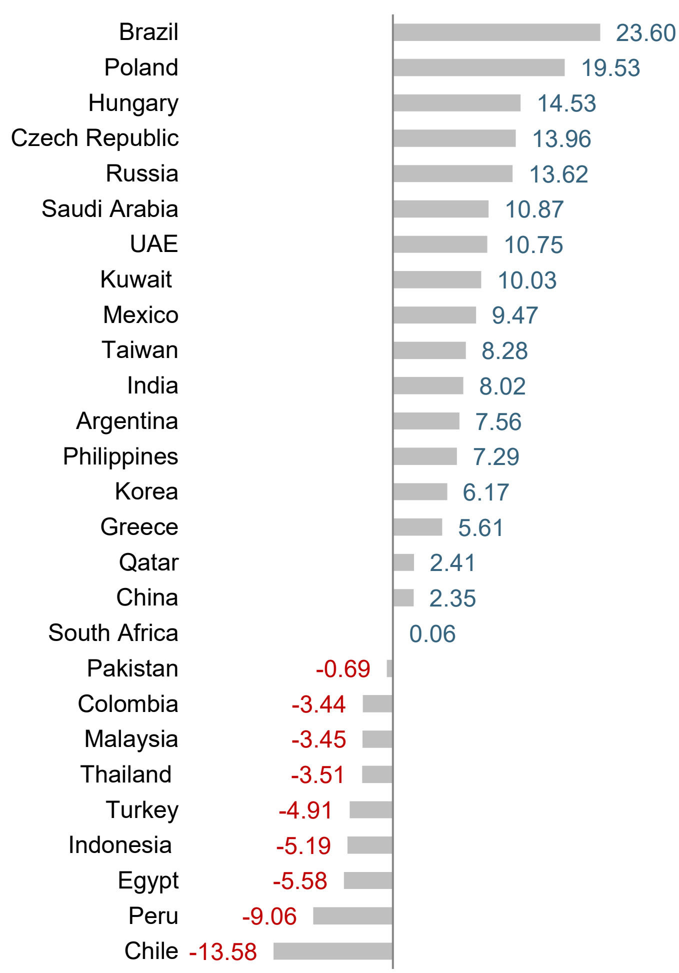
In US dollar terms, Denmark and Switzerland recorded the highest country performance in developed markets, while New Zealand and Japan posted the lowest returns for the quarter. In emerging markets, Brazil and Poland recorded the highest country performance, while Chile and Peru posted the lowest performance.

Ranked Developed Markets Returns (%)



Ranked Emerging Markets Returns (%)



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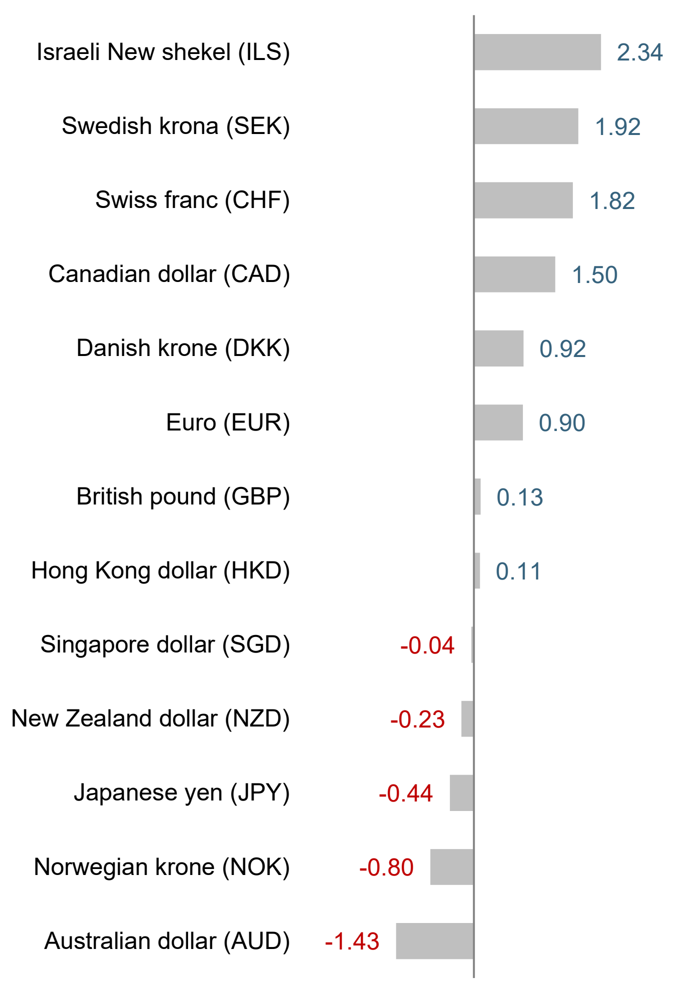
Select Currency Performance vs. US Dollar

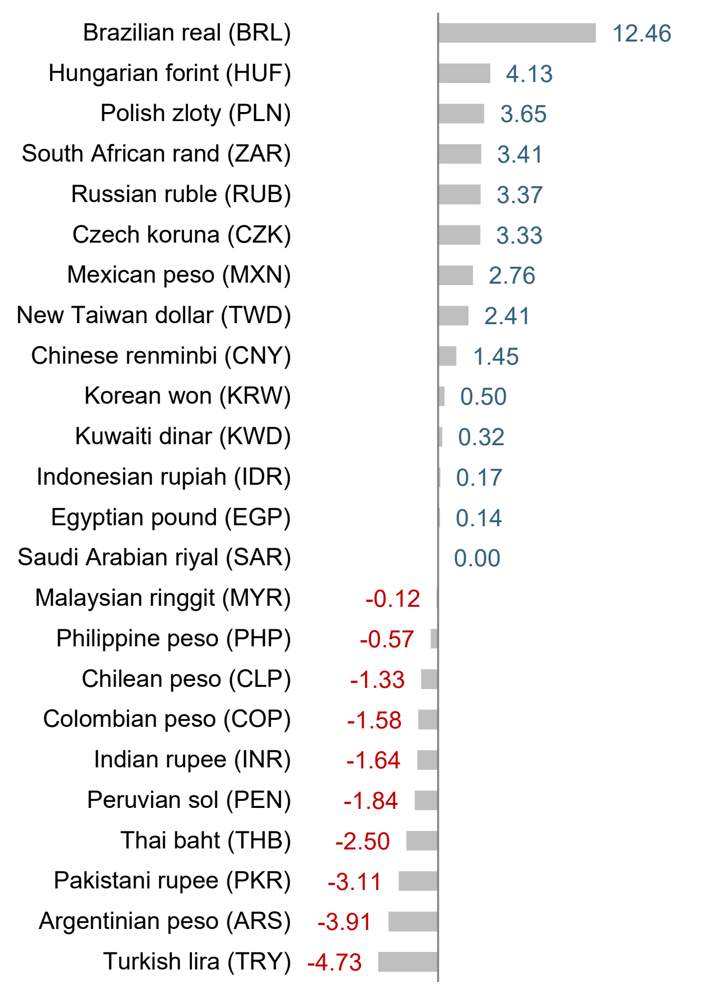
Second Quarter 2021

In developed markets, several currencies appreciated vs. the US dollar, but some, notably the Australian dollar, depreciated. In emerging markets, most currencies appreciated vs. the US dollar, but some, notably the Turkish lira, depreciated.

Ranked Developed Markets Returns (%)



Ranked Emerging Markets Returns (%)



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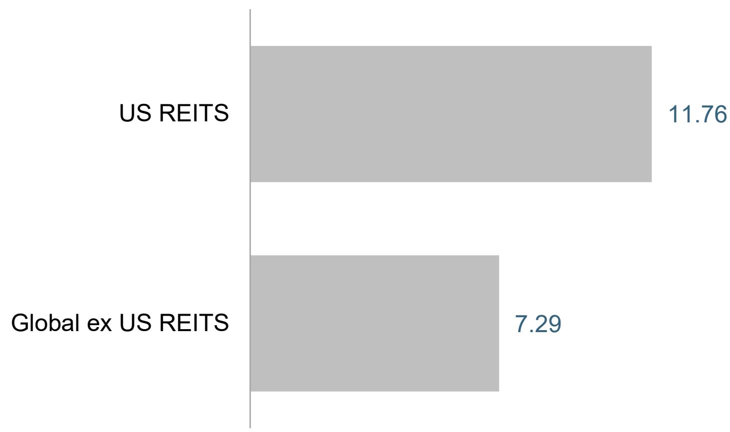
Real Estate Investment Trusts (REITs)

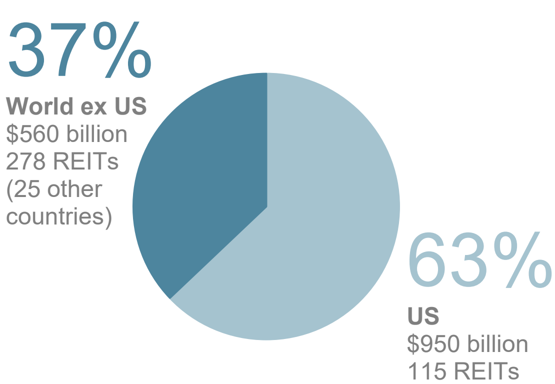
Second Quarter 2021 Index Returns

US real estate investment trusts outperformed non-US REITs during the quarter.

Ranked Returns (%)



Total Value of REIT Stocks



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
US REITS	22.94	39.98	8.13	5.16	8.67
Global ex US REITS	9.68	31.93	4.63	4.11	5.00

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Number of REIT stocks and total value based on the two indices. All index returns are net of withholding tax on dividends. Total value of REIT stocks represented by Dow Jones US Select REIT Index and the S&P Global ex US REIT Index. Dow Jones US Select REIT Index used as proxy for the US market, and S&P Global ex US REIT Index used as proxy for the World ex US market. Dow Jones and S&P data

Commodities

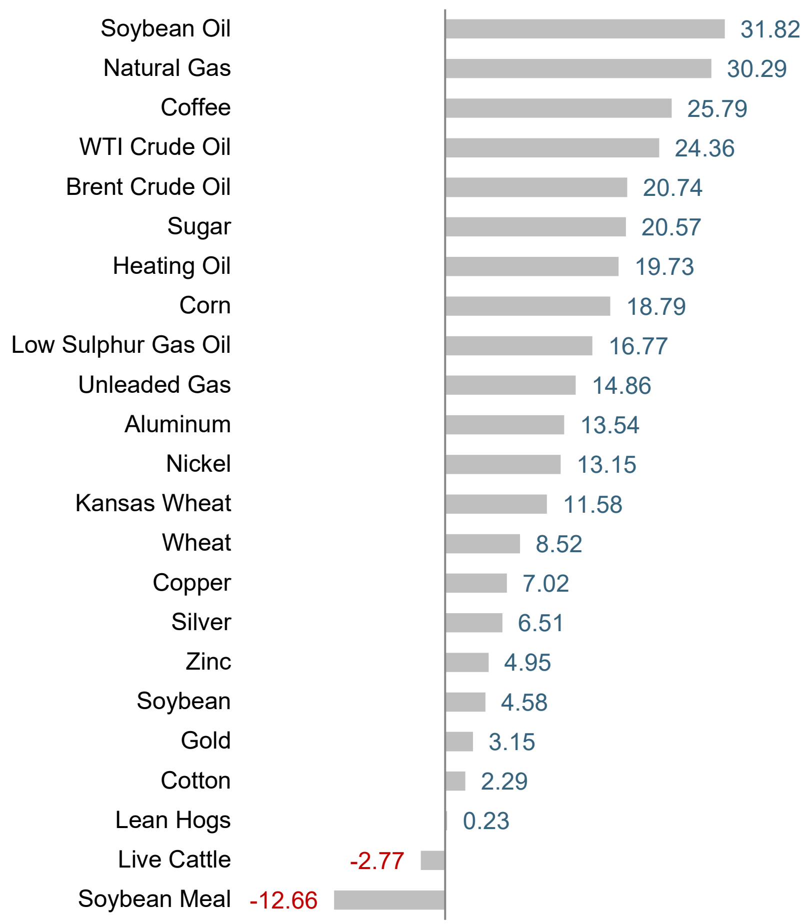
Second Quarter 2021 Index Returns

The Bloomberg Commodity Index Total Return returned 13.3% for the second quarter of 2021.

Soybean Oil and Natural Gas were the best performers, returning 31.82% and 30.29%, respectively.

Soybean Meal and Live Cattle were the worst performers, declining 12.66% and 2.77%, respectively.

Ranked Returns (%)



Period Returns (%)

** Annualized*

Asset Class	QTR	YTD	1 Year	3 Years*	5 Years*	10 Years*
Commodities	13.30	21.15	45.61	3.90	2.40	-4.44

Past performance is not a guarantee of future results. Index is not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Commodities returns represent the return of the Bloomberg Commodity Total Return Index. Individual commodities are sub-index values of the Bloomberg Commodity Total Return Index. Data provided by Bloomberg.

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Fixed Income

Second Quarter 2021 Index Returns

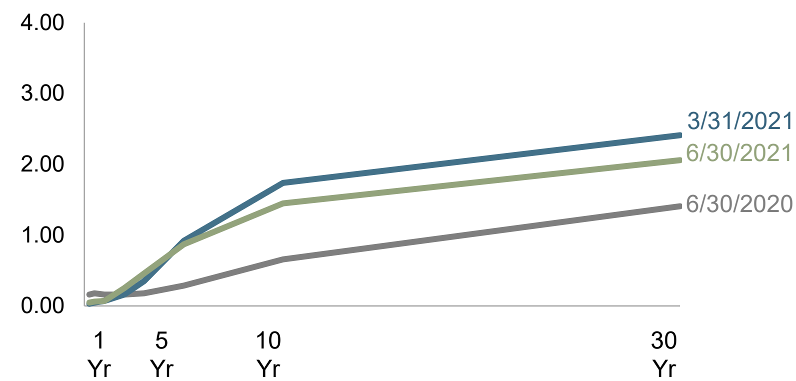
Changes in interest rates in the US Treasury fixed income market were generally mixed during the second quarter of 2021. The yield on the 5-Year Treasury note decreased 7 basis points (bps) to 0.88%. The yield on the 10-Year T-note decreased 28 bps to 1.46%. The 30-Year Treasury bond yield declined 35 bps to 2.04%.

On the short end of the yield curve, the 1-Month US Treasury bill yield remained unchanged at 0.05%, and the 1-Year T-bill yield increased 2 basis point to 0.10%. The 2-Year Treasury note increased 10 bps to 0.25%.

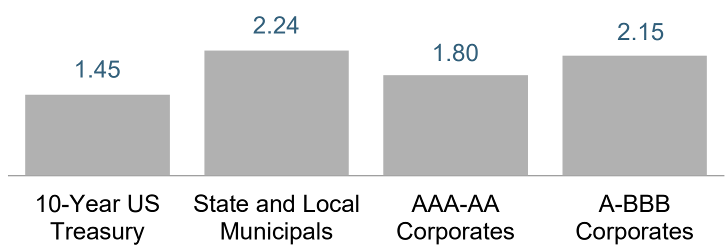
In terms of total returns, short-term corporate bonds gained 0.70%. Intermediate-term corporate bonds returned 1.70%.

The total return for short-term municipal bonds was 0.30%, while intermediate-term munis returned 0.80%. Revenue bonds outperformed general obligation bonds.

US Treasury Yield Curve (%)



Bond Yields across Issuers (%)



Period Returns (%)

*Annualized

Asset Class	QTR	YTD	1 Year	3 Years*	5 Years*	10 Years*
Bloomberg Barclays US Government Bond Index Long	6.43	-7.82	-10.42	7.97	3.18	6.62
Bloomberg Barclays US TIPS Index	3.25	1.73	6.51	6.53	4.17	3.40
Bloomberg Barclays US High Yield Corporate Bond Index	2.74	3.62	15.37	7.45	7.48	6.66
Bloomberg Barclays US Aggregate Bond Index	1.83	-1.60	-0.33	5.34	3.03	3.39
Bloomberg Barclays Municipal Bond Index	1.42	1.06	4.17	5.10	3.25	4.28
FTSE World Government Bond Index 1-5 Years	0.31	-2.08	2.08	2.31	1.27	-0.13
FTSE World Government Bond Index 1-5 Years (hedged to USD)	0.07	-0.30	0.11	2.82	1.92	1.88
ICE BofA 1-Year US Treasury Note Index	0.02	0.09	0.22	2.01	1.47	0.90
ICE BofA US 3-Month Treasury Bill Index	0.00	0.02	0.09	1.34	1.17	0.63

One basis point (bps) equals 0.01%. **Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.** Yield curve data from Federal Reserve. State and local bonds are from the S&P National AMT-Free Municipal Bond Index. AAA-AA Corporates represent the ICE BofA US Corporates, AA-AAA rated. A-BBB Corporates represent the ICE BofA US Corporates, BBB-A rated. Bloomberg Barclays data provided by Bloomberg. US long-term bonds, bills, inflation, and fixed income factor data © Stocks, Bonds, Bills, and Inflation (SBBI) Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefield). FTSE fixed income indices © 2021 FTSE Fixed Income LLC, all rights reserved. ICE BofA index data © 2021 ICE Data Indices, LLC. S&P data © 2021 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

Global Fixed Income

Second Quarter 2021 Yield Curves

Changes in government bond yields in the global developed markets were mixed for the quarter.

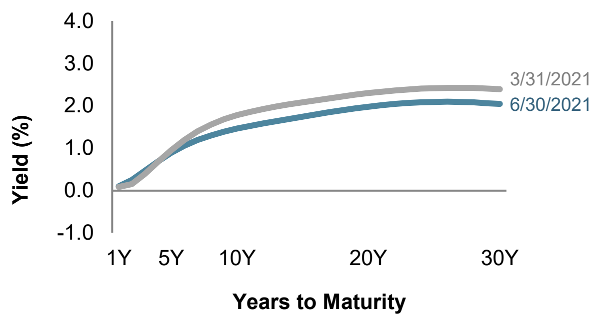
Term premiums were mixed in developed markets.

Short- and intermediate-term nominal interest rates were negative in Japan and Germany.

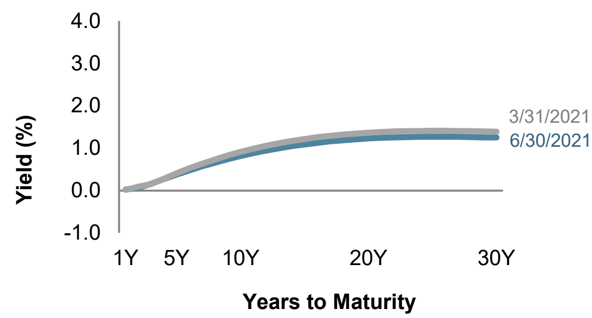
Changes in Yields (bps) since 3/31/2021

	1Y	5Y	10Y	20Y	30Y
US	1.8	-6.5	-31.9	-31.8	-35.0
UK	0.8	-3.1	-9.9	-13.8	-13.8
Germany	-2.2	5.4	5.1	4.4	1.5
Japan	1.9	-1.5	-4.4	-3.7	2.2
Canada	11.1	1.8	-16.0	-16.1	-12.8
Australia	-11.0	-3.2	-24.7	-37.3	-40.5

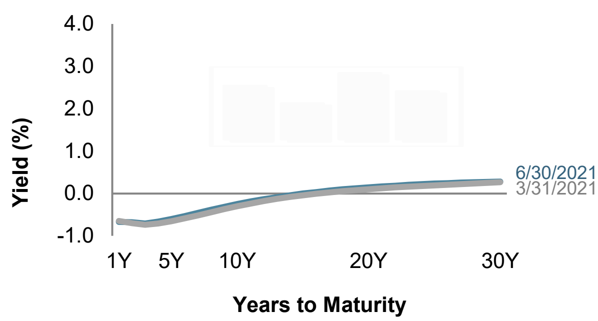
US



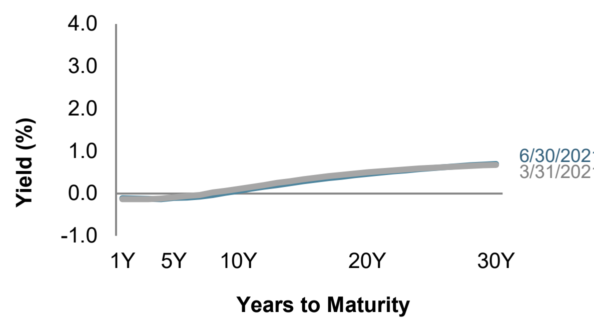
UK



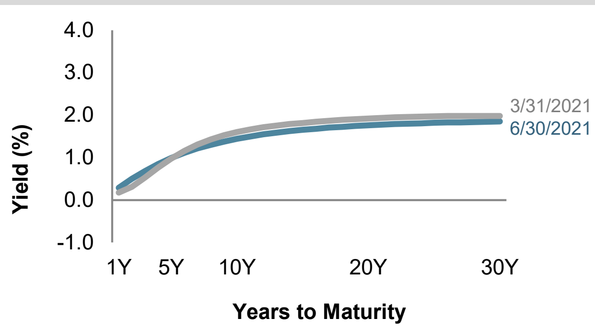
Germany



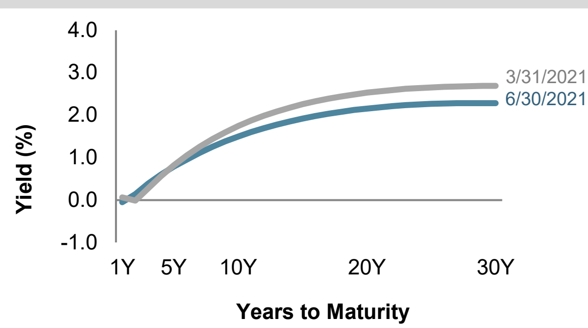
Japan



Canada



Australia



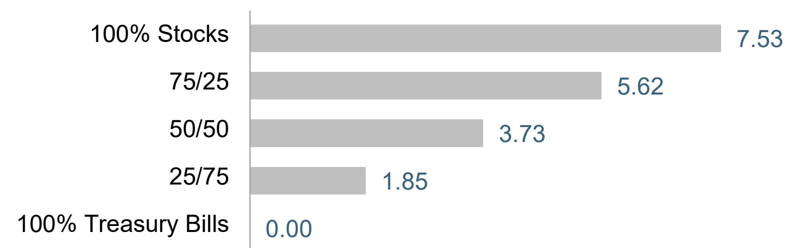
One basis point (bps) equals 0.01%. Source: ICE BofA government yield. ICE BofA index data © 2021 ICE Data Indices, LLC.

Impact of Diversification

Second Quarter 2021

These portfolios illustrate the performance of different global stock/bond mixes and highlight the benefits of diversification. Mixes with larger allocations to stocks are considered riskier but have higher expected returns over time.

Ranked Returns (%)

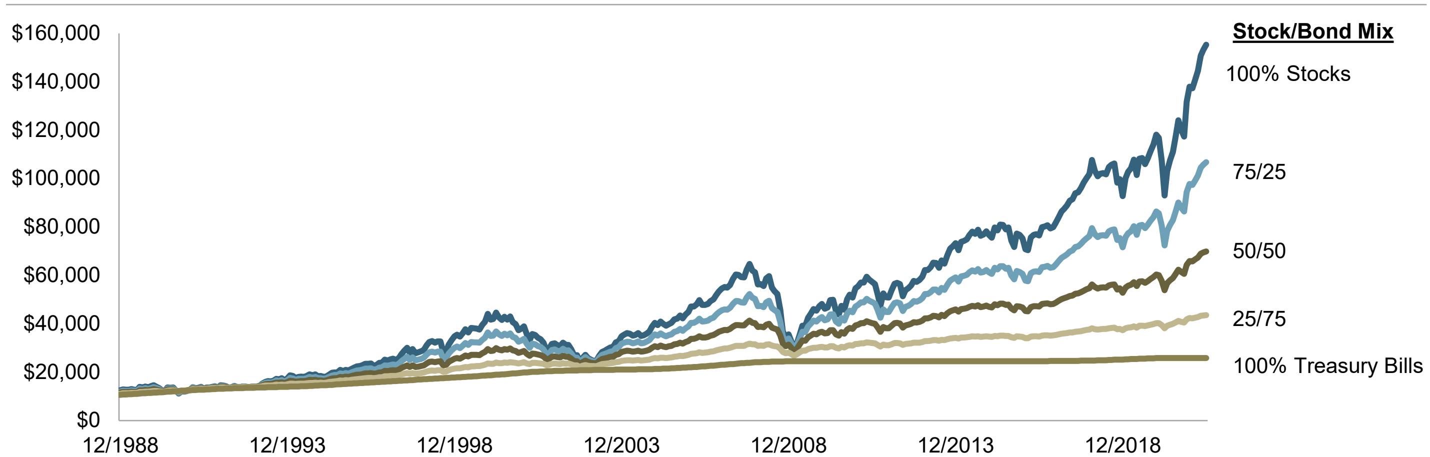


Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*	10-Year STDEV[1]
100% Stocks	12.56	39.87	15.14	15.20	10.48	14.03
75/25	9.32	28.96	11.84	11.73	8.12	10.52
50/50	6.15	18.71	8.40	8.20	5.67	7.00
25/75	3.05	9.08	4.85	4.64	3.14	3.49
100% Treasury Bills	0.01	0.06	1.21	1.06	0.55	0.23

Growth of Wealth: The Relationship between Risk and Return



1.STDEV (standard deviation) is a measure of the variation or dispersion of a set of data points. Standard deviations are often used to quantify the historical return volatility of a security or portfolio.

Diversification does not eliminate the risk of market loss. **Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio.** Asset allocations and the hypothetical index portfolio returns are for illustrative purposes only and do not represent actual performance. Global Stocks represented by MSCI All Country World Index (gross div.) and Treasury Bills represented by US One-Month Treasury Bills. Globally diversified allocations rebalanced monthly, no withdrawals. Data © MSCI 2021, all rights reserved. Treasury bills © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefield).

Inflation: An Exchange Between Eugene Fama and David Booth

David Booth, Executive Chairman and Founder

Eugene Fama, PhD, Nobel laureate, Director, and Consultant

With the economy starting to recover from the COVID-19 pandemic and investor concerns turning increasingly toward inflation, Dimensional Founder David Booth talked with Nobel laureate Eugene Fama about inflation and how investors should think about it in their portfolios. Excerpts from their conversation have been edited for clarity.

ON PREDICTING INFLATION

David Booth: Gene, you are a founding Director of Dimensional and have been involved in our research and corporate governance for more than 40 years. People may not know that you've also done a lot of research on inflation and interest rates.

We always tell people, "We don't try to forecast. We try to be prepared for various outcomes." Inflation is one of those things you want to be prepared for. There's a pickup in inflation risk that wasn't there, say, 10 years ago. Does that cause you to worry?

Eugene Fama: Historically what's happened is, when there's a spike, the spike persists for a long time. Inflation tends to be highly persistent once you get it. Once it goes down, it tends to be highly persistent on the downside. You've got to be prepared for that. Predicting next month's inflation may not be very hard because this month's inflation can be a pretty good predictor of next month's inflation, or next quarter's inflation, or even the next six months' inflation. Persistence is a characteristic of inflation.

We haven't been in a period of high inflation, or even moderate inflation, for at least 10 years, so I'm not particularly concerned that inflation will be high soon.

(continued from page 25)

ON HOW INVESTORS SHOULD THINK ABOUT INFLATION AND THEIR FINANCIAL GOALS

Booth: Conditions change, so is there anything about the current environment and the risk of inflation heating up that would cause you to change your portfolio?

Fama: I don’t think anybody predicts the market very well. Market timing is risky in the sense that you’ve always emphasized: You may be out of the stock market at precisely the time when it generates its biggest returns. The nature of the stock market is you get a lot of the return in very short periods of time. So, you basically don’t want to be out for short periods of time, where you may actually be missing a good part of the return.

I think you take a long-term perspective. You decide how much risk you’re willing to take, and then you choose a mix of bonds, stocks, Treasury Inflation-Protected Securities, and whatever else satisfies your long-term goals. And you forget about the short term. Maybe you rebalance occasionally because the weights can get out of whack, but you don’t try to time the market in any way, shape, or form. It’s a losing proposition.

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Eugene Fama is a member of the Board of Directors of the general partner of, and provides consulting services to, Dimensional Fund Advisors LP.

(continued from page 26)

Booth: As you get to the point in life where you actually need to use your portfolio, does that change the kinds of allocations you'd want?

Fama: The classic answer to that was, yes, you'd shift more toward short-term hedges, short-term bonds. Once you had enough accumulated wealth that you thought you could make it through retirement, you'd want to hedge away any uncertainty that might disturb that. That's a matter of taste and your willingness to take risk and your plans for the people you will leave behind, like your charities or your kids. All of that will influence how you make that decision. But the typical person who thinks they'll spend all their money before they die probably wants to move into less risky stuff as they approach retirement.

Booth: The notion of risk is pretty fuzzy. For example, if I decide that I want to hold Treasury bills or CDs when I retire, and you did that 40 years ago, when we started the firm, and you've got that 15% coupon, that's pretty exciting. With $1 million at 15%, you're getting $150,000 a year. Today you might get less than 1%.

Fama: Right, but I remember when inflation was running at about 15%, so not much better off!

Booth: Those are different kinds of risks.

Fama: When you approach retirement, you're basically concerned about what your real wealth will look like over the period of your retirement, and you have some incentives to hedge against that. You face the possibility, for example, that if you invest in stocks, you have a higher expected return, but you may lose 30% in a year and that might be devastating for your long-term consumption.

Booth: I think part of planning is not only your investment portfolio, but what to do if you experience unexpected events of any kind. We're kind of back to where we start our usual conversation: "Control what you can control." You can't control markets. What you can do is prepare yourself for what you'll do in case bad events happen. Inflation is just one of many risk factors long-term investors need to be prepared for.
