

The Joseph Wealth Counsel Journal

November 2005

ABOUT THIS PUBLICATION. Reviewing the historical returns of various asset classes, as well as projecting future returns of asset classes, can lead to a better understanding of the strategies underlying the design of your investment portfolio. In this publication we present various historical data on the returns of various asset classes, and the returns of select mutual funds and indices. This data is presented for educational purposes only.

This publication is designed for the use of our clients and prospective clients and is updated quarterly. The data herein is presented for educational and reference purposes only.

Joseph Capital Management, LLC employs research from Nobel-Prize winning financial economists and other academics, as well as its own proprietary research as to asset class valuation levels relative to historic levels, to design and construct investment portfolios for our clients. Utilizing low-cost investment products and tax-efficient investment portfolio design, we seek to reduce the various risks to which our clients may otherwise be exposed while achieving each client's desired long-term after-tax rate of return.

If you have any questions or suggestions regarding the content of this publication, or other questions regarding the design of your investment portfolio, please feel free to give me a call, or e-mail me at rrhoades@josephpartners.com.

Thank you! Ron A. Rhoades, B.S., J.D., CFP®, Director of Research
Joseph Capital Management, LLC
A Member of the Joseph Financial Group

Newsletter Publications of the Joseph Financial Group

Joseph Financial Group's Wealth Counsel & Perspectives: Articles from our directors and team members in each issue address aspects of tax, financial, and estate planning. Published four times a year. Publication dates vary depending upon tax and other developments.

Joseph Capital Management's Quarterly Capital Markets Commentary: A 4-page publication providing succinct analysis for our investment advisory clients. Published in January, April, July and October.

The Joseph Wealth Counsel Journal: This publication provides a detailed article in each issue on an aspect of investment theory or investment portfolio design, as well as charts on historical and expected future asset class returns. It is designed for our investment advisory clients who desire greater insights into Modern Portfolio Theory. Published in February, May, August, and November.

Inside this issue:

Feature Article: Examining Best and Worst Case Scenarios With Hypo- thetical Portfolios	2
Periodic Table of Historical Asset Class Returns	6
Historical Returns of Our Hypothetical Model Portfolios	8
Historical Returns for Select Mutual Funds and Commercial Indices	12
Illustrating The Small Cap and Value Effects: Historical Data Using Fama/French Indices	15
Appendix: Important Disclosures	18
Appendix: Sources of Data	20
About The Joseph Financial Group; Our Code of Ethics	24

Copyright © 2005 by Joseph Capital Management, LLC, a fee-only investment advisory firm providing sophisticated, objective and integrated tax, financial and estate planning and investment counseling services.

For more information about our firm and our services, please visit our web site, www.JosephPartners.com, or call us for a no-obligation initial conference to ascertain if our professional services can benefit you.



Feature Article: Best and Worst Cast Scenarios

How much “up” and “down” can you accept in your investment portfolio? That’s a key question in determining your ability to “stick with the discipline” – especially during times when stock prices fall or bond prices fall (due to interest rate increases). Your ability to counter the emotional aspects of investing is, perhaps, the largest determinant of your success as an individual investor. In other words, you need to possess the emotional fortitude to “buy” more of an asset class when it goes down in value (and not be “fearful”). Just as importantly, you also need to be able to “sell off” part of an asset class holding when it has risen in value (and not be “greedy”).

Knowledge is power. To that end, in this edition of The Joseph Wealth Counsel Journal we examine ten hypothetical portfolios over the January 1970 to June 2005 time period. We do this with a desire to determine the probable range of “ups” and “downs” for each portfolio. In the chart below we illustrate five portfolios (U100, U80, etc.) which are composed solely of a broad U.S. stock market index (“CRSP Market”) and a hypothetical 5-year constant maturity T-bill. We also illustrate five portfolios (100SV, 80SV) which possess a substantial tilt toward value and small cap stocks as well as some international holdings.

CHART: TEN HYPOTHETICAL SIMULATED PORTFOLIOS - HISTORICAL PORTFOLIO RETURNS AND STANDARD DEVIATION

PORTFOLIO CONSTRUCTION: USING INDEX DATA, NO DEDUCTION FOR INVESTMENT ADVISORY FEES, TRANSACTION FEES, MUTUAL FUND MANAGEMENT FEES, NOR REFLECTING ANY IMPACT OF TAXES

January 1970 - June 2005

Each Portfolio Rebalanced

	<u>U100</u>	<u>100SV</u>	<u>U80</u>	<u>80SV</u>	<u>U60</u>	<u>60SV</u>	<u>U40</u>	<u>40SV</u>	<u>U20</u>	<u>20SV</u>
CRSP Market (Decile 1-10)	100		80		60		40		20	
Fama/French US Large		20		16		12		8		4
Fama/French US Large Value Index Port.		20		16		12		8		4
Fama/French US Small		20		16		12		8		4
Fama/French US Small Value Index Port.		20		16		12		8		4
DFA Int'l. Large Company Index		10		8		6		4		2
DFA Int'l. Small Co. Simulated Index		10		8		6		4		2
5 Year Treasury Notes		0	20	20	40	40	60	60	80	80
Total	100	100	100	100	100	100	100	100	100	100
ANNUALIZED DATA:										
Portfolio Return	10.98	14.2	10.7	13.4	10.3	12.3	9.88	11.2	9.2	9.9
Standard Deviation*	17.87	18.7	14.5	15.2	11.4	11.8	8.65	8.83	6.7	6.77

*Annualized standard deviation is presented as an approximation by multiplying the monthly or quarterly number by the square root of the number of periods in a year. Please note that the number computed from annual data or monthly data may differ materially from this estimate.

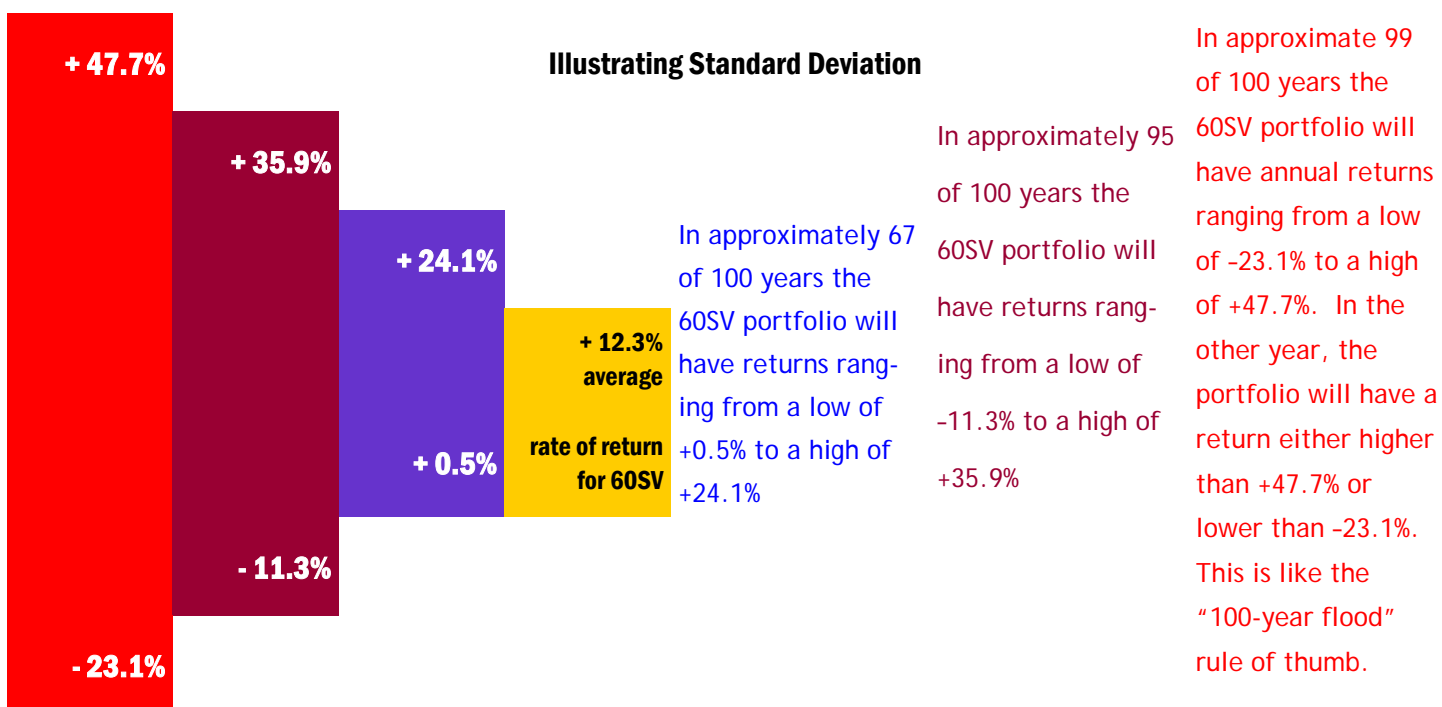
This data is provided solely for educational use, and does not represent the performance of any actual portfolio. See important disclosures in the Appendices. **Past performance is not a guarantee of future results.** Annual returns stated above include an exceptional period of stock/bond market history that is unlikely to be repeated.

-cont. Best and Worst Case Scenarios

In the chart on the left page we set forth the “average annualized returns” of each hypothetical portfolios as well as the “standard deviation” of each portfolio. Each portfolio is assumed to be rebalanced (on a quarterly basis) back to its original “target percentages” for each asset class. Investors, of course, want to see higher “average annualized returns.” Investors would also like to see “standard deviation” — a measure of the “volatility” or “ups and downs” of a portfolio — to be low..

The Small Cap / Value Tilted Portfolios “Win” - As To Returns. One compelling result of this analysis is the significantly higher annual returns of the small cap/value tilted portfolios when compared to the portfolios with the same overall percentage of stock holdings but only holding a broad U.S. stock market portfolio. For example, the U60 portfolio has an average annualized return over this period of 10.3%. By contrast, the 60SV portfolio with its value and small cap tilt has an average annualized return of 12.3% — a whopping 2% a year greater. To put that in dollar terms, \$1.00 invested in the U60 portfolio in January 1970 would have grown to a nice \$33.43 by the end of June 2005. However, \$1.00 invested in the 60SV portfolio, with its small cap and value tilt, would have grown to a whopping \$63.13 — nearly twice as much. These results are not unanticipated. Over very long periods of time (15 years or more), academic research reveals that a broad basket of “value” stocks will usually outperform a broad basket of “growth” stocks, and a broad basket of “small company stocks” will outperform a broad basket of “large company” stocks. (Please note that this is true only if the costs of investing in value stocks and small cap stocks is carefully controlled through limited trading, and hence low transaction costs. Many mutual funds which invest in value stocks and small company stocks do a poor job of minimizing these costs, often to the point of completely offsetting the positive benefits of the value and small company asset classes.)

Examining Volatility. The broad U.S. stock market portfolios have slightly less standard deviation (“volatility”) than the more diversified portfolios which have a substantial value and small cap tilt. This is to be expected, as small cap stock asset classes are very volatile, in and of themselves. For example, the “U60” portfolio, which consists of 60% broad U.S. stock market index and 40% fixed income investments, has a standard deviation of 11.4%. The more broadly diversified portfolio, “60SV,” has a higher standard deviation of 11.8%. **What does standard deviation mean?** To illustrate the concept, let’s again look at our 60SV portfolio, which has an average annualized return of 12.3% and a standard deviation of 11.8%. Based upon “standard deviation” - what is the likely “upper range” and “lower range” of the portfolio’s returns (based upon Jan.70 to June 05 data)?





-cont. Best and Worst Case Scenarios

As shown on the prior page, “standard deviation” is a statistical prediction of the range of possible returns of an investment portfolio. It is useful “shorthand” for comparing the relative expected “ups and downs” of two different portfolios. In constructing portfolios, we desire to reduce standard deviation, so that the investment portfolio does not fluctuate in its returns greatly. This is especially true during retirement since undertaking withdrawals from a highly volatile portfolio can actually reduce returns over time (as withdrawals get taken out during sometimes-prolonged “down” markets).

So how did our hypothetical portfolios actually do? Let’s examine each year’s annual returns of these portfolios, on a calendar-year basis, from 1970 through 2004:

CHART: TEN HYPOTHETICAL SIMULATED PORTFOLIOS - RANGE OF RETURNS

January 1970 - Dec. 2004 Number of Years That The Calendar-Year Returns Fell Within Stated Range of Returns

RANGE OF RETURNS	U100	100SV	U80	80SV	U60	60SV	U40	40SV	U20	20SV
-30% to -25%	1	1								
-25% to -20%	1	1	1	0						
-20% to -15%	1	2	0	2						
-15% to -10%	2	0	2	2	1	2				
-10% to -5%	1	1	2	0	2	2	1	2		
-5% to 0%	3	0	4	1	4	1	4	2	2	3
0% to 5%	3	3	2	3	3	2	5	2	7	4
5% to 10%	2	4	3	4	5	4	6	7	11	13
10% to 15%	2	1	4	3	6	8	8	10	8	7
15% to 20%	4	3	6	4	5	7	6	5	4	6
20% to 25%	5	10	3	9	5	3	3	4	2	1
25% to 30%	3	3	5	3	4	3	2	3	1	1
30% to 35%	5	2	3	2		3				
35% to 40%	2	2		0						
40% to 45%		0		2						
45% to 50%		1								
50% to 55%		1								

This data is provided solely for educational use, and does not represent the performance of any actual portfolio. See important disclosures in the Appendices. **Past performance is not a guarantee of future results.** Annual returns stated above include an exceptional period of stock/bond market history that is unlikely to be repeated.

Now consider your own portfolio. For example, if you have a 60% allocation to stock mutual funds, it would be likely that you would have 1 or 2 years (out of 35 years) in which your portfolio had a *negative 10% to negative 15% return*? With the same 60% allocation to stock mutual funds, could you tolerate 5-7 years out of 35 years in which the portfolio’s annual return would be less than zero?

There is an inherent relationship between risk and return in the capital markets. A greater exposure to stock mutual funds, or to value stocks, or to small cap stocks, or other “risk factors” — can yield greater average annual returns — over the very long term. However, the greater the exposure to these risk factors, generally the greater the volatility in a portfolio. **Consider, in light of the percentage allocation to stock mutual funds in your investment portfolio, the potential range of returns in the chart above. Can you tolerate the inevitable “ups” and “downs” of the stock market?**

-cont. Best and Worst Case Scenarios**Annual Returns of Hypothetical Portfolios, January 1970 through December 2004**

(No deduction for mutual fund fees, investment advisory fees, or transaction costs)

YEAR	U100	100SV	U80	80SV	U60	60SV	U40	40SV	U20	20SV
1970	0.03	0.73	3.4	3.96	6.76	7.18	10.12	10.4	13.49	13.63
1971	16.18	25.51	14.69	22.16	13.21	18.8	11.72	15.45	10.23	12.09
1972	16.93	21.5	14.58	18.24	12.23	14.97	9.88	11.71	7.52	8.44
1973	-18.14	-20.04	-13.59	-15.11	-9.04	-10.18	-4.49	-5.25	0.06	-0.32
1974	-27.17	-25.89	-20.6	-19.58	-14.03	-13.26	-7.46	-6.95	-0.89	-0.64
1975	38.68	52.09	32.51	43.24	26.34	34.38	20.16	25.53	13.99	16.68
1976	26.73	36.86	23.96	32.06	21.19	27.27	18.42	22.47	15.65	17.67
1977	-4.21	19.56	-3.09	15.93	-1.97	12.29	-0.85	8.66	0.27	5.03
1978	7.48	20.3	6.68	16.93	5.88	13.57	5.08	10.21	4.29	6.85
1979	22.96	24.84	19.19	20.69	15.42	16.54	11.64	12.39	7.87	8.25
1980	32.67	29.08	26.91	24.04	21.16	19.01	15.4	13.97	9.65	8.93
1981	-3.7	5.87	-1.07	6.58	1.56	7.29	4.18	8.01	6.81	8.72
1982	20.84	23.69	22.49	24.77	24.15	25.85	25.8	26.94	27.45	28.02
1983	21.98	31.66	19.06	26.81	16.15	21.96	13.24	17.11	10.32	12.26
1984	4.48	7.54	6.39	8.84	8.3	10.13	10.21	11.43	12.12	12.73
1985	32.16	37.19	29.79	33.82	27.43	30.45	25.07	27.08	22.7	23.71
1986	16.12	24.68	15.92	22.77	15.72	20.86	15.52	18.95	15.33	17.04
1987	1.72	5.4	1.96	4.9	2.19	4.4	2.43	3.9	2.67	3.4
1988	18.03	24.5	15.64	20.82	13.26	17.14	10.87	13.45	8.48	9.77
1989	28.85	23.08	25.74	21.12	22.62	19.16	19.5	17.2	16.39	15.23
1990	-5.97	-16.2	-2.83	-11.01	0.32	-5.82	3.46	-0.63	6.6	4.56
1991	34.68	31.84	30.8	28.53	26.93	25.22	23.05	21.92	19.18	18.61
1992	9.79	14.42	9.27	12.97	8.76	11.53	8.24	10.09	7.72	8.64
1993	11.12	22.93	11.14	20.59	11.17	18.25	11.19	15.91	11.21	13.58
1994	-0.05	1.37	-1.06	0.07	-2.08	-1.23	-3.1	-2.53	-4.11	-3.83
1995	36.79	28.29	32.65	25.85	28.52	23.42	24.38	20.98	20.25	18.55
1996	21.37	15.85	17.51	13.1	13.66	10.35	9.8	7.6	5.95	4.85
1997	31.41	23.27	26.8	20.29	22.2	17.31	17.59	14.33	12.99	11.36
1998	24.33	8.83	21.51	9.11	18.69	9.39	15.87	9.66	13.04	9.94
1999	25.41	18.24	19.98	14.24	14.54	10.24	9.11	6.24	3.67	2.24
2000	-11.49	-6.38	-6.67	-2.58	-1.86	1.21	2.96	5.01	7.78	8.81
2001	-11.12	4.91	-7.37	5.45	-3.63	5.99	0.12	6.53	3.87	7.07
2002	-21.17	-19.02	-14.35	-12.62	-7.52	-6.23	-0.7	0.17	6.13	6.56
2003	31.61	49.6	25.76	40.16	19.92	30.72	14.08	21.28	8.24	11.84
2004	11.93	20.51	10.19	17.05	8.44	13.59	6.69	10.13	4.95	6.66