

# 5 Steps

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T O B E T T E R I N V E S T M E N T P E R F O R M A N C E

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Before we start, please access our live poll here: [www.dentistadvisors.com/poll](http://www.dentistadvisors.com/poll)

*(raise your hand if you need help)*



DENTISTADVISORS.COM

# Investor Returns vs Market-Index Returns

*For the period ending December 31, 2015*

	INVESTOR EQUITY RETURNS	S&P 500	DIFFERENCE
10 Year	4.23	7.31	(3.08)

# Morningstar Study

*For the 10-year period ending December 31, 2015*

FUND RETURN	INVESTOR RETURN	DIFFERENCE
6.45%	4.81%	-1.64

Notes: Morningstar Investor Return assumes that the growth of a fund’s total net assets for a given period is driven by market returns and investor cash flow. To calculate investor return, a fund’s change in assets for the period is discounted by the return of the fund to isolate how much of the asset growth was driven by cash flow. A proprietary model, similar to an internal rate-of-return calculation, is then used to calculate a constant growth rate that links the beginning total net assets and periodic cash flows to the ending total net assets. Discrepancies in the return “difference” are due to rounding.

Source: Morningstar, Inc.

**WHY?**



# Poll Question Responses

## What are you hoping to learn from our session today?

 Respond at **PollEv.com/dentistadvisors**

“Should I pay down debt or invest?”

2 minutes ago

“What sort of investments should I have?”

2 minutes ago

“How should my portfolio be constructed?”

2 minutes ago

“What does a diversified portfolio look like?”

1 minute ago

“Is permanent life insurance a good investment?”

1 minute ago

“What should I do with extra money?”

1 minute ago

“How can I limit my investment risk?”

1 minute ago

# 5 Steps to Better Investment Performance

**1** Overcome common investor psychology

# 9 Categories of Irrational Investor Behavior

## **LOSS AVERSION**

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Expecting to find high returns with low risk

## **NARROW FRAMING**

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Making decisions without considering all implications

## **MENTAL ACCOUNTING**

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Taking undue risk in one area and avoiding rational risk in another

## **ANCHORING**

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Relating to the familiar experiences, even when inappropriate

## **HERDING**

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Copying the behavior of others even in the face of unfavorable outcomes

## **REGRET**

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Treating errors of commission more seriously than errors of omission

## **MEDIA RESPONSE**

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Tendency to react to news without reasonable examination

## **OPTIMISM**

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Belief that good things happen to me and bad things happen to others

## **DIVERSIFICATION**

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Seeking to reduce risk, but simply using different sources

# Vanguard Research Paper

*“Vanguard research and other academic studies have concluded that behavioral coaching can add 1% to 2% in net return.”*



*“The investor’s chief problem-and even his worst enemy-is likely to be himself.”*

**~ Benjamin Graham**

“GRAHAM, BENJAMIN, 1894-1976. THE INTELENT INVESTOR: A BOOK OF PRACTICAL COUNSEL.  
NEW YORK: HARPER 1959. PRINT.

*You have:*  
**\$32,500 Extra Cash  
Equipment Loan at  
6% Interest**

**A**

**Pay down equipment loan for a  
guaranteed return of 6%**

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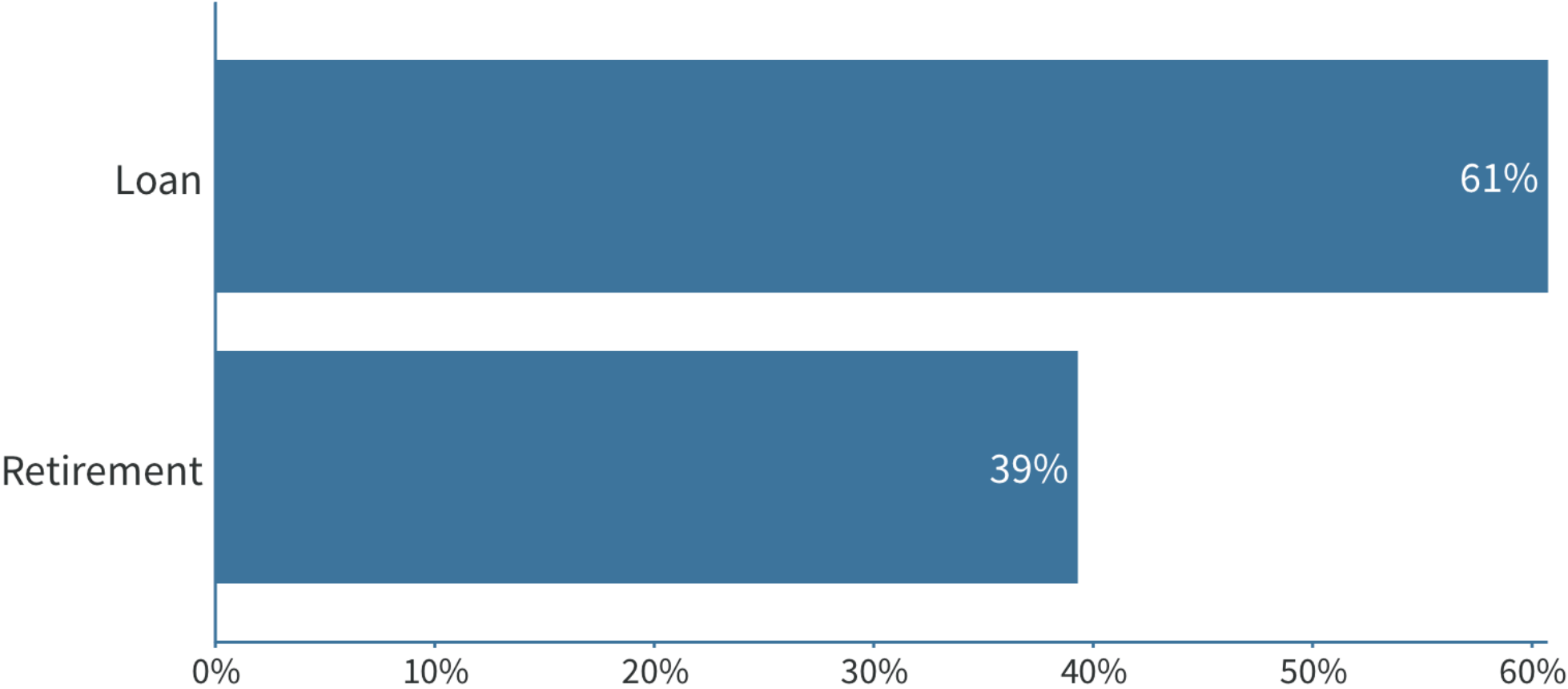
**B**

**Invest in a retirement plan  
which could return anywhere  
from 0% - 8%**

# Poll Question Responses

**Would you pay down the 6% loan (A) or invest the money into your retirement plan?  
(B)**

 Respond at **PollEv.com/dentistadvisors**



Tails you lose \$20

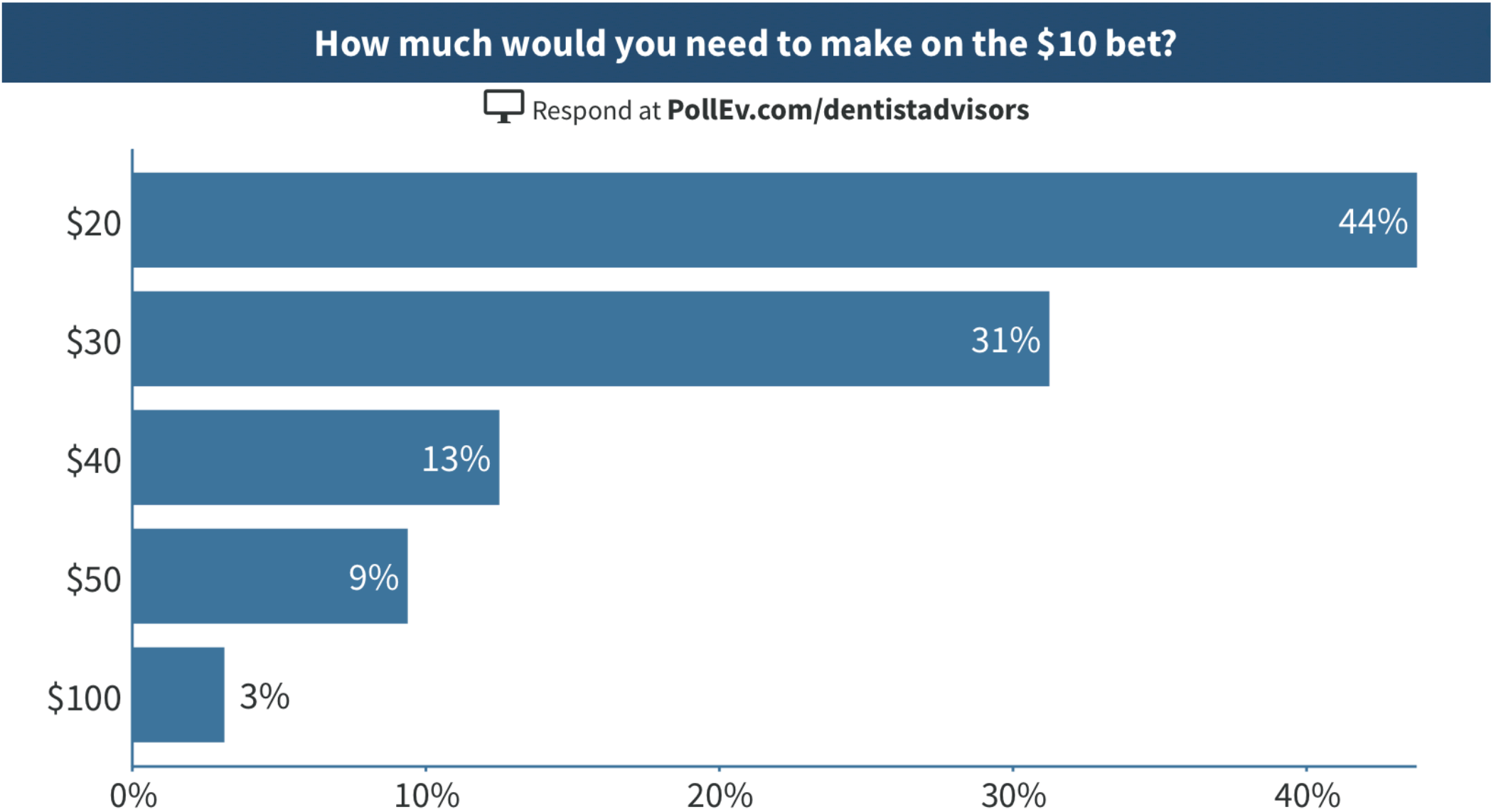


If it lands on heads, how much would you need to win for the bet to be worth it?

**\$?**



# Poll Question Responses

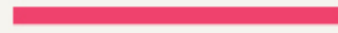


# 9 Categories of Irrational Investor Behavior

**LOSS AVERSION**



**ANCHORING**



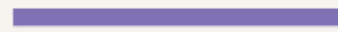
**MEDIA RESPONSE**



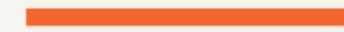
**NARROW FRAMING**



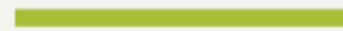
**HERDING**



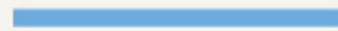
**OPTIMISM**



**MENTAL ACCOUNTING**



**REGRET**



**DIVERSIFICATION**



*“You make more money selling advice than following it. It’s one of the things we count on in the magazine business - along with the short memory of our readers.”*

**~ Steve Forbes**

STEVE FORBES, PUBLISHER, FORBES MAGAZINE, PRESENTATION TO UCLA (15 APRIL 2003).

*“Pundits forecast not because they know,  
but because they are asked.”*

**~ John Kenneth Galbraith**

FUTURE BABBLE: WHY EXPERT PREDICTIONS FAIL - AND WHY WE BELIEVE THEM ANYWAY  
[TORONTO: MCCLELLAND AND STEWART, 2010].



*Listen to:*

## **DENTIST MONEY™ SHOW #16:**

The Mind Games You  
Play with Your  
Money



Get it on iTunes or visit **DentistAdvisors.com/iTunes**

# 5 Steps to Better Investment Performance

- ① Overcome common investor psychology
- ② Hire a properly-incentivized advisor

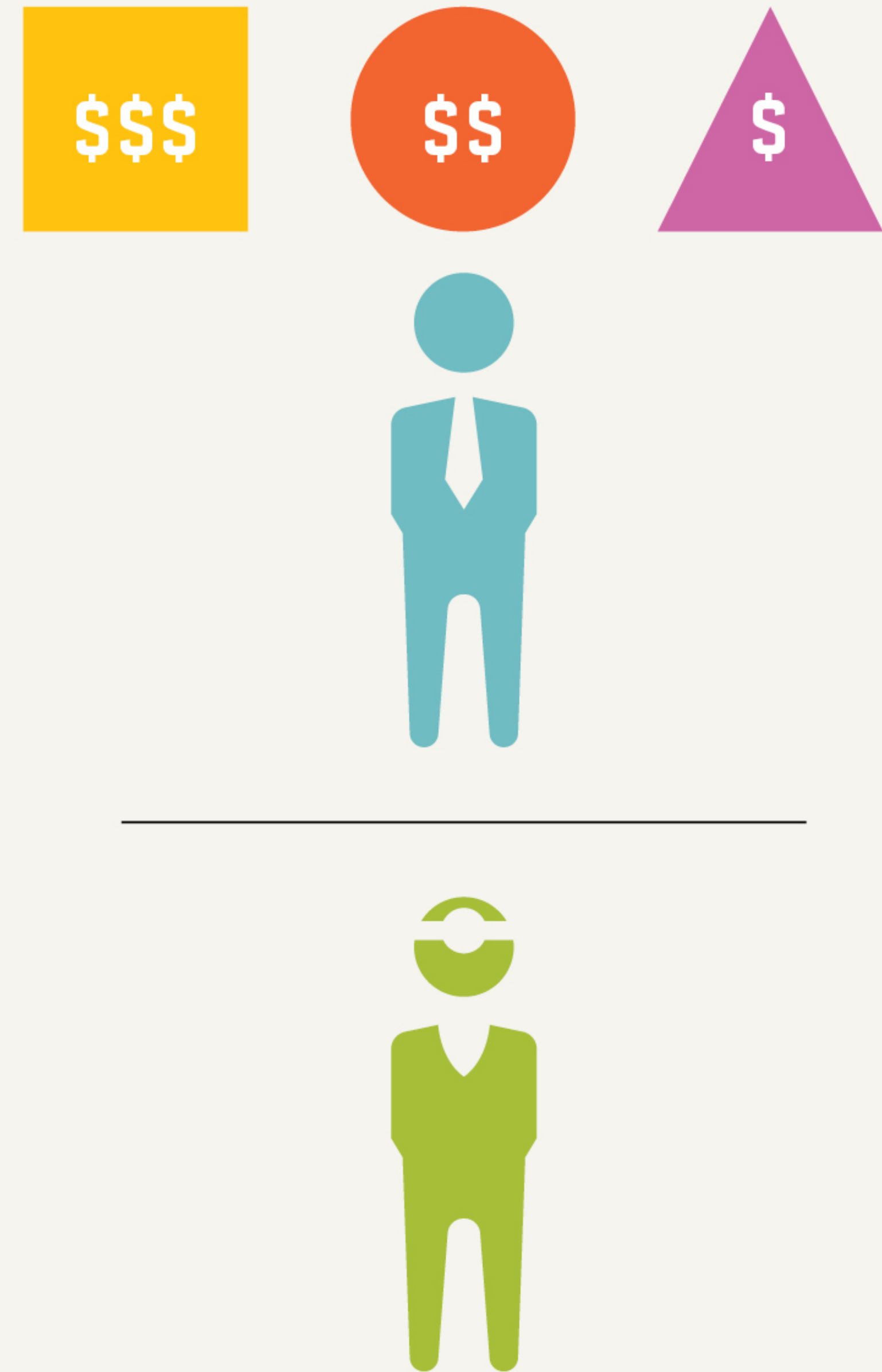
**FIDUCIARY**

Advisor → Fiduciary Standard

Broker → Suitability Requirement



# Broker Payment Structure



# Advisor Payment Structure



*See full article:*

## **DENTAL ECONOMICS:**

7 Questions to  
Ask Before Hiring a  
Financial Advisor



Read full article at [DentistAdvisors.com/DE](https://DentistAdvisors.com/DE)

# 5 Steps to Better Investment Performance

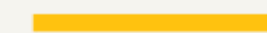
- ① Overcome common investor psychology
- ② Hire a properly-incentivized advisor
- ③ **Discover your investment DNA**

What types of  
investments do  
the wealthiest  
people and  
endowments  
use?

PRIVATE EQUITY



PRIVATE DEBT



HEDGE FUNDS



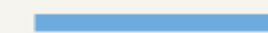
COMMODITIES



PUBLIC EQUITY



PUBLIC DEBT



REAL ESTATE



CASH & LIQUID ASSETS



**A**

**B**

**C**

Expected Return

**3%**

**6%**

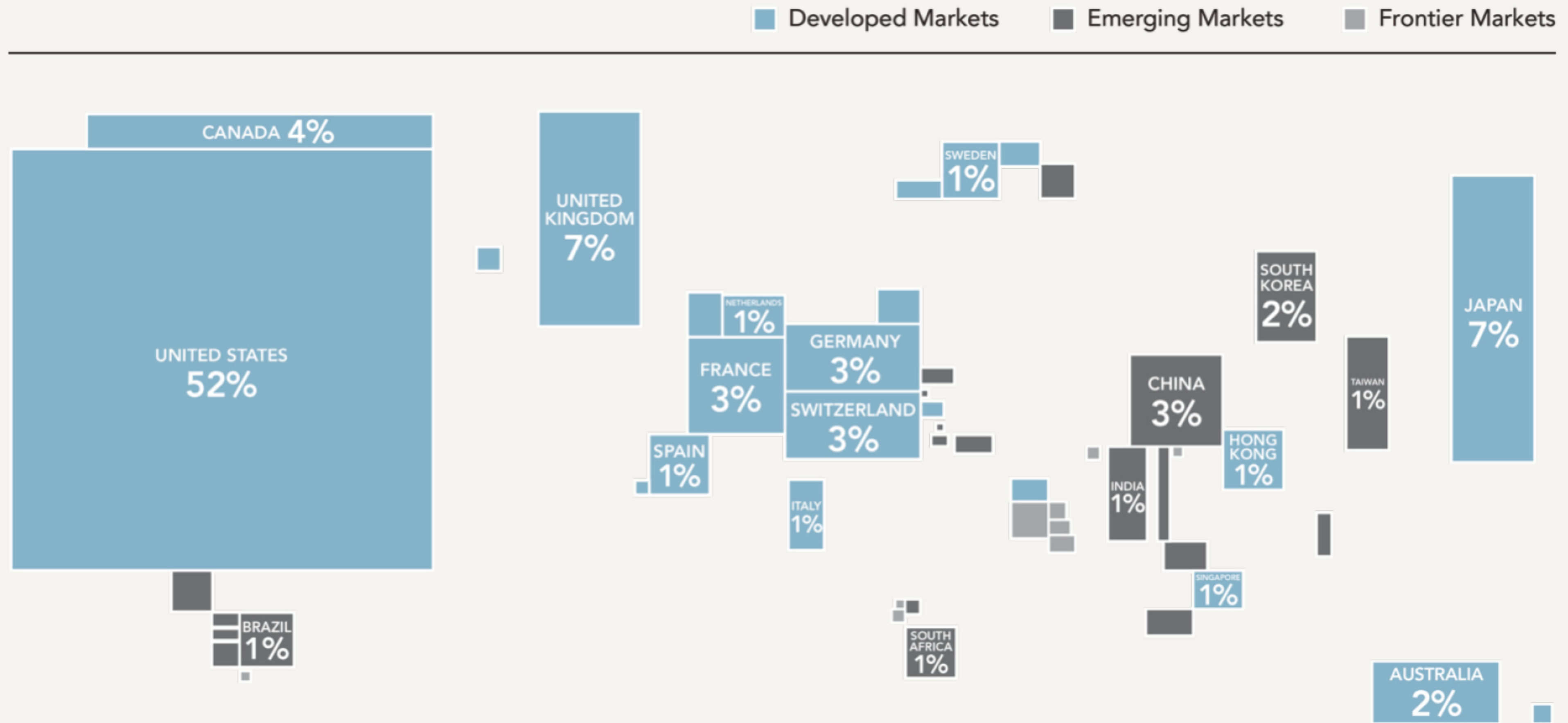
**9%**

Expected Volatility

**± 5%**

**± 12%**

**± 25%**



**0.4%**

S&P 500 (United States)

2000 – 2010

**10.9%**

Emerging Markets (Brazil, Russia, India, China)

2000 – 2010



# Value vs. Growth

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# Small vs. Big

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# Sample Portfolio

## PERFORMANCE

1-Year Return (%)	5.03
3-Year Annualized Return (%)	11.30
5-Year Annualized Return (%)	9.94
10-Year Annualized Return (%)	7.97
20-Year Annualized Return (%)	8.94

## VARIANCE

Lowest 1-Year Return (%) (3/08 - 2/09)	-30.91%
Highest 1-Year Return (%) (3/09 - 2/10)	44.33%
Lowest 3-Year Annualized Return (%) (3/06 - 2/09)	-7.00%
Highest 3-Year Annualized Return (%) (4/03 - 3/06)	21.23%

# 5 Steps to Better Investment Performance

- ① Overcome common investor psychology
- ② Hire a properly-incentivized advisor
- ③ Discover your investment DNA
- ④ Choose Investments like a Nobel Laureate**

# Following the Science of Investing



**Harry Markowitz, UCSD**  
1990 Nobel Prize  
Modern Portfolio Theory



**William F. Sharpe, Stanford**  
1990 Nobel Prize  
CAPM, Sharpe Ratio



**Eugene Fama, Chicago**  
2013 Nobel Prize  
Fama-French 3 Factor Model



**Kenneth French, Dartmouth**  
Fama-French  
3 Factor Model



**Gary Brinson, Author**  
Asset Allocation Theory, 1986 Paper  
“Determinants of Portfolio Performance.”



**Rogert Ibbotson, Yale**  
Author, “Stocks, Bonds, Bills,  
and Inflation.”



**Richard Thaler, Chicago**  
“Quasi-Rational Economics,”  
and “The Winner’s Curse.”



**Daniel Kahneman, Psychologist**  
2002 Nobel Prize  
Behavioral Economics



**Amos Tversky, Psychologist**  
Behavioral Economics



**Robert C. Merton, MIT**  
1997 Nobel Prize



# Active vs. Passive

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*“The most important single central fact about a free market is that no exchange takes place unless both parties benefit.”*

**~ Milton Friedman**

## Fund A

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37 Companies

## Fund B

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3,236 Companies



*“Put 10% of the cash in short-term government bonds and 90% in a very low-cost S&P 500 index fund. (I suggest Vanguard’s.) I believe the trust’s long-term results from this policy will be superior to those attained by most investors.”*

**~ Warren Buffet**

LETTER FROM WARREN E. BUFFET TO THE SHAREHOLDERS OF BERKSHIRE HATHAWAY INC.  
BERKSHIRE HATHAWAY INC.: SHAREHOLDER LETTERS (2013)



*“All the time and effort that people devote to picking the right fund, the hot hand, the great manager, have in most cases led to no advantage.”*

**~ Peter Lynch**

BEATING THE STREET (NEW YORK: SIMON & SCHUSTER, 1993), 60.

*“Wall Street’s favorite scam is  
pretending luck is skill.”*

**~ Ron Ross**

THE UNBEATABLE MARKET: TAKING THE INDEXING PATH TO FINANCIAL PEACE OF MIND (GEORGE ROSS, 2001).



*“The most important thing about an investment philosophy is that you have one you can stick with.”*

**~ David Booth**

*Listen to:*

**DENTIST MONEY™ SHOW #55:**

Six Keys to Building  
Powerful Investment  
Portfolios

**DENTIST MONEY™**

*with* **REESE HARPER, CFP®**



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# 5 Steps to Better Investment Performance

- ① Overcome common investor psychology
- ② Hire a properly-incentivized advisor
- ③ Discover your investment DNA
- ④ Choose Investments like a Nobel Laureate
- ⑤ Continuously adjust your portfolio to reduce tax and optimize return**



1

# Be Thoughtful about Asset Location to Minimize Taxes

**May add 0 - .75% in annual return**

VANGUARD. "PUTTING A VALUE ON YOUR VALUE: QUANTIFYING VANGUARD ADVISOR'S ALPHA<sup>®</sup>"  
WWW.VANGUARD.COM, VANGAURD, SEPTEMBER 2016, [HTTPS://WWW.VANGUARD.COM/PDF/ISGQVAA.PDF](https://www.vanguard.com/pdf/ISGQVAA.PDF)

2

## Spend your Assets in the Right Order

**May add 0 - 1.10% in annual return**

VANGUARD. "PUTTING A VALUE ON YOUR VALUE: QUANTIFYING VANGUARD ADVISOR'S ALPHA<sup>®</sup>"  
WWW.VANGUARD.COM, VANGAURD, SEPTEMBER 2016, [HTTPS://WWW.VANGUARD.COM/PDF/ISGQVAA.PDF](https://www.vanguard.com/pdf/ISGQVAA.PDF)

3

# Rebalance Effectively with New Cash Flow where Possible

**May add up to .35%  
in annual return-risk adjusted**

VANGUARD. "PUTTING A VALUE ON YOUR VALUE: QUANTIFYING VANGUARD ADVISOR'S ALPHA<sup>®</sup>"  
WWW.VANGUARD.COM, VANGAURD, SEPTEMBER 2016, [HTTPS://WWW.VANGUARD.COM/PDF/ISGQVAA.PDF](https://www.vanguard.com/pdf/ISGQVAA.PDF)

4

## Don't be Distracted by Income-based Investing

**May be significant  $> 0\%$   
but highly dependent on individual circumstances**

VANGUARD. "PUTTING A VALUE ON YOUR VALUE: QUANTIFYING VANGUARD ADVISOR'S ALPHA<sup>®</sup>"  
WWW.VANGUARD.COM, VANGAURD, SEPTEMBER 2016, [HTTPS://WWW.VANGUARD.COM/PDF/ISGQVAA.PDF](https://www.vanguard.com/pdf/ISGQVAA.PDF)

5

# Reduce Your Capital Gains When you Make Charitable Donations

**May be significant > 0%  
but highly dependent on individual circumstances**

VANGUARD. "PUTTING A VALUE ON YOUR VALUE: QUANTIFYING VANGUARD ADVISOR'S ALPHA<sup>®</sup>"  
WWW.VANGUARD.COM, VANGAURD, SEPTEMBER 2016, [HTTPS://WWW.VANGUARD.COM/PDF/ISGQVAA.PDF](https://www.vanguard.com/pdf/ISGQVAA.PDF)

# 5 Steps to Better Investment Performance

1	Overcome common investor psychology	1.5%
2	Hire a properly-incentivized advisor	* > 0%
3	Discover your investment DNA	* > 0%
4	Choosing investments like a Nobel Laureate	.40% +
5	Continuously adjust your portfolio to reduce tax & optimize return	2.55%

*\*A significant factor, but highly dependent on individual circumstances, and to unique to quantify.*