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## Key Questions for the Long-Term Investor

Oct 15, 2021

**Whether you've been investing for decades or are just getting started, at some point on your investment journey you'll likely ask yourself some of the questions below.** Trying to answer these questions may be intimidating, but know that you're not alone. Your financial adviser is here to help. While this is not intended to be an exhaustive list, it will hopefully shed light on a few key principles, using data and reasoning, that may help improve investors' odds of investment success in the long run.

### 1. WHAT SORT OF COMPETITION DO I FACE AS AN INVESTOR?

The market is an effective information-processing machine. Millions of market participants buy and sell securities every day, and the real-time information they bring helps set prices.

This means competition is stiff, and trying to outguess market prices is difficult for anyone, even professional money managers (see question 2 for more on this). This is good news for investors though. Rather than basing an investment strategy on trying to find securities that are priced "incorrectly," investors can instead rely on the information in market prices to help build their portfolios (see question 5 for more on this).



*In USD. Source: Dimensional, using data from Bloomberg LP. Includes primary and secondary exchange trading volume globally for equities. ETFs and funds are excluded. Daily averages were computed by calculating the trading volume of each stock daily as the closing price multiplied by shares traded that day. All such trading volume is summed up and divided by 252 as an approximate number of annual trading days.*

### 2. WHAT ARE MY CHANCES OF PICKING AN INVESTMENT FUND THAT SURVIVES AND OUTPERFORMS?

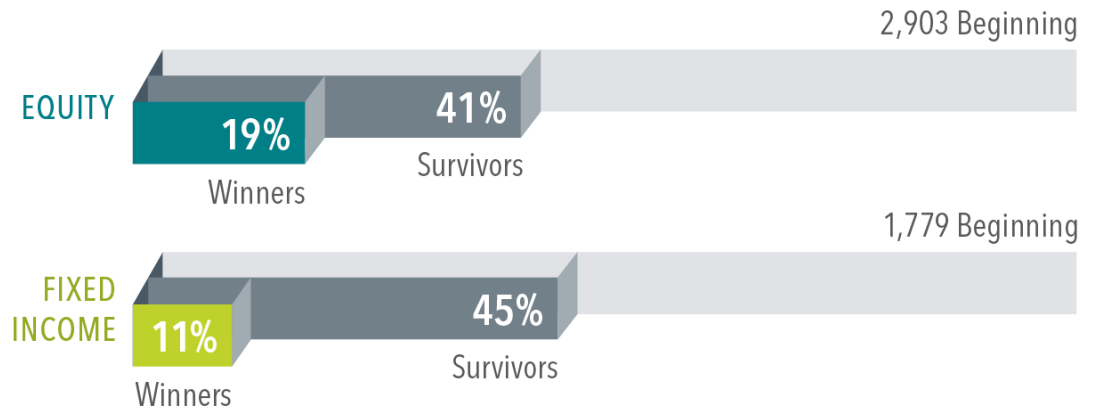
Flip a coin and your odds of getting heads or tails are 50/50. Historically, the odds of

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selecting an investment fund that was still around 20 years later are about the same. Regarding outperformance, the odds are worse. The market's pricing power works against mutual fund managers who try to outperform through stock picking or market timing. As evidence,<sup>1</sup> only 19% of US equity mutual funds and 11% of US fixed income mutual funds have survived and outperformed their benchmarks over the past 20 years.

**US-Domiciled Mutual  
Fund Performance**  
2001-2020



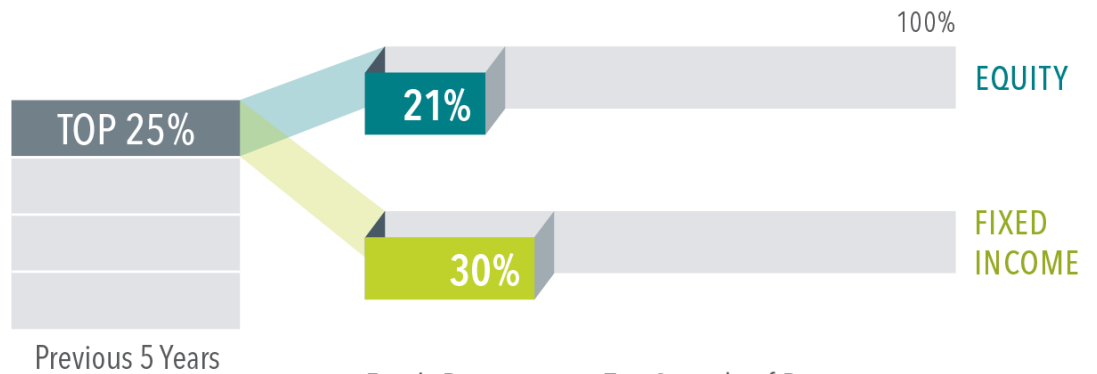
There is no guarantee investment strategies will be successful. Past performance is no guarantee of future results.

*Source: Mutual Fund Landscape 2021, Dimensional Fund Advisors. See Appendix for important details on the study.*

### 3. IF I CHOOSE A FUND BECAUSE OF STRONG PAST PERFORMANCE, DOES THAT MEAN IT WILL DO WELL IN THE FUTURE?

Some investors select mutual funds based on past returns. However, research shows that most US mutual funds in the top quartile of previous five-year returns did not maintain a top-quartile ranking in the following five years. In other words, past performance offers little insight into a fund's future returns.

Percentage of Top-Ranked US-Domiciled Mutual Funds That Stayed on Top



Funds Remaining in Top Quartile of Returns in the Following 5-Year Period (2010-2020 average)

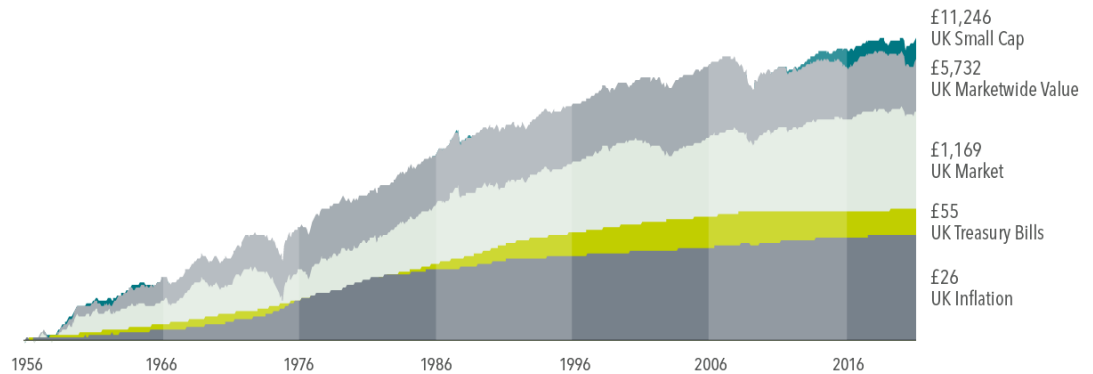
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*Source: Mutual Fund Landscape 2021, Dimensional Fund Advisors. See Appendix for important details on the study.*

#### 4. DO I HAVE TO OUTSMART THE MARKET TO BE A SUCCESSFUL INVESTOR?

Financial markets have rewarded long-term investors. People expect a positive return on the capital they invest, and historically, the equity and bond markets have provided growth of wealth that has more than offset inflation. Instead of fighting markets, let them work for you.

**Growth of a Pound**  
1956-2020  
(compounded monthly)



The graph is for illustrative purposes only; figures presented are hypothetical and not indicative of any investment. Past performance is no guarantee of future results.

*In GBP. UK Small Cap is the Dimensional UK Small Cap Index. UK Marketwide Value is the Dimensional UK Marketwide Value Index. UK Market is the Dimensional UK Market Index. UK Treasury Bills is UK One-Month Treasury Bills. UK Inflation is the UK Retail Price Index. The Dimensional and Fama/French indices reflected above are not “financial indices” for the purpose of the EU Markets in Financial Instruments Directive (MiFID). Rather, they represent academic concepts that may be relevant or informative about portfolio construction and are not available for direct investment or for use as a benchmark. Their performance does not reflect the expenses associated with the management of an actual portfolio. Index returns are not representative of actual portfolios and do not reflect costs and fees associated with an actual investment. Actual returns may be lower. See below for descriptions of the Dimensional and Fama/French indices. The Dimensional indices have been retrospectively calculated by an affiliate of Dimensional Fund Advisors Ltd. and did not exist prior to their index inception dates. Accordingly, results shown during the periods prior to each index’s inception date do not represent actual returns of the index. Other periods selected may have different results, including losses. Backtested index performance is hypothetical and is provided for informational purposes only to indicate historical performance had the index been calculated over the relevant time periods. Backtested performance results assume the reinvestment of dividends and capital gains.*

## 5. IS THERE A BETTER WAY TO BUILD A PORTFOLIO?

Academic research has identified these equity and fixed income dimensions, which point to differences in expected returns among securities. Instead of attempting to outguess market prices, investors can instead pursue higher expected returns by structuring their portfolio around these dimensions.

**Dimensions of Expected Returns**

EQUITIES			FIXED INCOME		
<b>Company Size</b> Market Capitalization	<b>Relative Price</b> Price/Book Equity	<b>Profitability</b> Operating Profits/Book Equity	<b>Term</b> Sensitivity to Interest Rates	<b>Credit</b> Credit Quality of Issuer	<b>Currency</b> Currency of Issuance

*Relative price is measured by the price-to-book ratio; value stocks are those with lower price-to-book ratios. Profitability is measured as operating income before depreciation and amortisation minus interest expense scaled by book.*

## 6. IS INTERNATIONAL INVESTING FOR ME?

Diversification helps reduce risks that have no expected return, but diversifying only within your home market may not be enough. Instead, global diversification can broaden your investment opportunity set. By holding a globally diversified portfolio, investors are well positioned to seek returns wherever they occur.

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### *Single Market Example*

**MSCI UK** Investable Market Index (IMI)



1 COUNTRY  
343 STOCKS

### *Global Market Example*

**MSCI ACWI** Investable Market Index (IMI)



50 COUNTRIES  
8,980 STOCKS

Past performance is not a guarantee of future results.

*Number of holdings and countries for the MSCI United Kingdom Investable Market Index (IMI) and MSCI ACWI (All Country World Index) Investable Market Index (IMI) as at 31 December 2020. MSCI data © MSCI 2021, all rights reserved.*

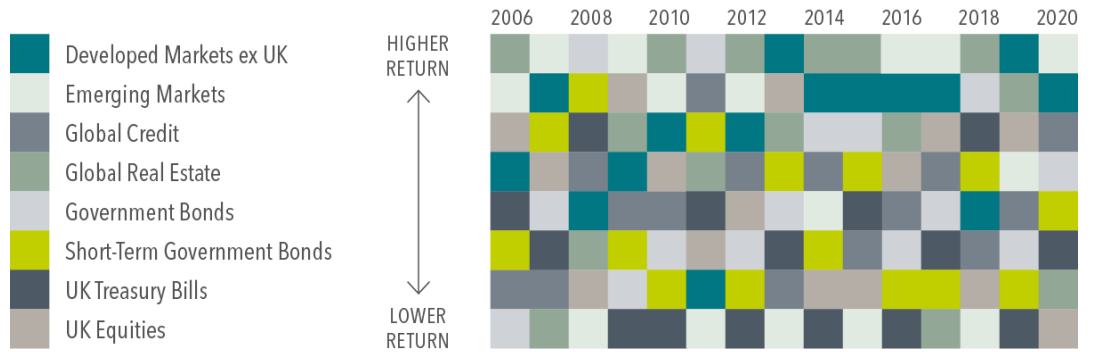
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## **7. WILL MAKING FREQUENT CHANGES TO MY PORTFOLIO HELP ME ACHIEVE INVESTMENT SUCCESS?**

It's tough, if not impossible, to know which market segments will outperform from period to period.

Accordingly, it's better to avoid market timing calls and other unnecessary changes that can be costly. Allowing emotions or opinions about short-term market conditions to impact long-term investment decisions can lead to disappointing results.

Annual Returns by Market Index



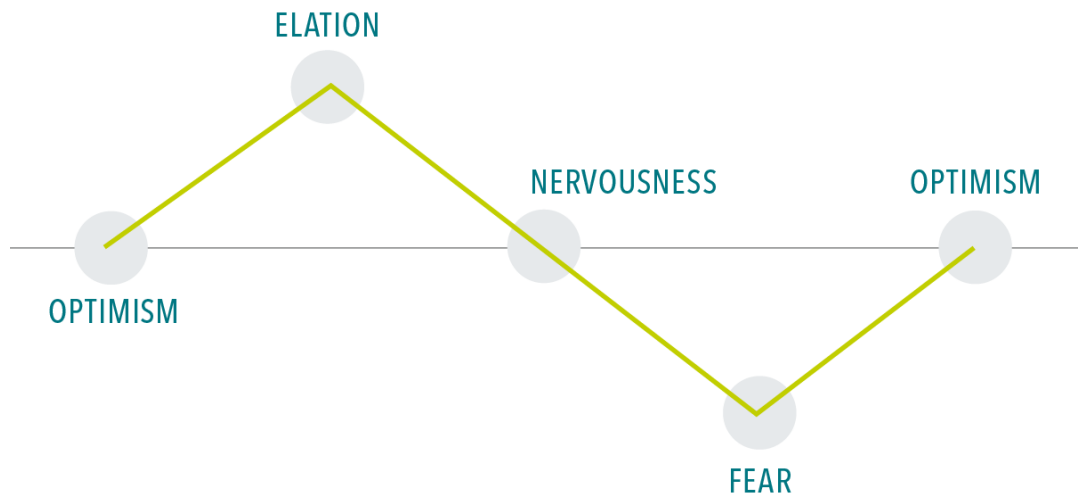
Past performance is not a guarantee of future results.

*In GBP. UK Equities is the MSCI United Kingdom Index (gross dividends). Developed Markets ex UK is the MSCI World ex UK Index (gross dividends). Emerging Markets is the MSCI Emerging Markets Index (gross dividends). Global Real Estate is the S&P Global REIT Index (gross dividends). UK Treasury Bills is UK One-Month Treasury Bills. Government Bonds is the FTSE World Government Bond Index (Hedged to GBP). Short-Term Government Bonds is the FTSE World Government Bond Index 1–5 Years (Hedged to GBP). Global Credit is the Bloomberg Barclays Global Aggregate Credit Bond Index (Hedged to GBP). MSCI data © MSCI 2021, all rights reserved. S&P data © 2021 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved. 1975–present: UK One-Month Treasury Bills provided by the Financial Times. Prior to 1975: UK Three-Month Treasury Bills provided by the London Share Price Database. FTSE fixed income indices © 2021 FTSE Fixed Income LLC. All rights reserved. Bloomberg Barclays data provided by Bloomberg.*

8. CAN MY EMOTIONS AFFECT MY INVESTMENT DECISIONS?

Many people struggle to separate their emotions from investing. Markets go up and down. Reacting to current market conditions may lead to making poor investment decisions.

Avoid Reactive Investing



9. SHOULD I MAKE CHANGES TO MY PORTFOLIO BASED ON WHAT I'M HEARING IN THE NEWS?

Daily market news and commentary can challenge your investment discipline. Some messages stir anxiety about the future, while others tempt you to chase the latest investment fad. If headlines are unsettling, consider the source and try to

maintain a long-term perspective.



## 10. SO, WHAT SHOULD I BE DOING?

Work closely with a financial adviser who can offer expertise and guidance to help you focus on actions that add value. Focusing on what you can control can lead to a better investment experience.

- Create an investment plan to fit your needs and risk tolerance.
- Structure a portfolio along the dimensions of expected returns.
- Diversify globally.
- Manage expenses, turnover and taxes.
- Stay disciplined through market dips and swings.

1. *Mutual Fund Landscape 2021*, Dimensional Fund Advisors. See Appendix for important details on the study. Past performance is no guarantee of future results.

## APPENDIX

**Question 2:** The sample includes funds at the beginning of the 20-year period ending 31 December 2020. Each fund is evaluated relative to its primary prospectus benchmark. Survivors are funds that had returns for every month in the sample period. Winners are funds that survived and outperformed their benchmark over the period. Where the full series of primary prospectus benchmark returns is unavailable,

non-Dimensional funds are instead evaluated relative to their Morningstar category index.

**Question 3:** This study evaluated fund performance over rolling periods from 2001 through 2020. Each year, funds are sorted within their category based on their previous five-year total return. Those ranked in the top quartile of returns are evaluated over the following five-year period. The chart shows the average percentage of top-ranked equity and fixed income funds that kept their top ranking in the subsequent period.

**Source (Questions 2 and 3):** US-domiciled, non-Dimensional open-end mutual fund data provided by Morningstar. Equity fund sample includes the following Morningstar historical categories: Diversified Emerging Markets, Europe Stock, Foreign Large Blend, Foreign Large Growth, Foreign Large Value, Foreign Small/Mid Blend, Foreign Small/Mid Growth, Foreign Small/Mid Value, Global Real Estate, Japan Stock, Large Blend, Large Growth, Large Value, Mid-Cap Blend, Mid-Cap Growth, Mid-Cap Value, Miscellaneous Region, Pacific/Asia ex-Japan Stock, Real Estate, Small Blend, Small Growth, Small Value, World Large Stock, and World Small/Mid Stock. Fixed income fund sample includes the following Morningstar historical categories: Corporate Bond, High Yield Bond, Inflation-Protected Bond, Intermediate Core Bond, Intermediate Core-Plus Bond, Intermediate Government, Long Government, Muni California Intermediate, Muni California Long, Muni Massachusetts, Muni Minnesota, Muni National Intermediate, Muni National Long, Muni National Short, Muni New Jersey, Muni New York Intermediate, Muni New York Long, Muni Ohio, Muni Pennsylvania, Muni Single State Intermediate, Muni Single State Long, Muni Single State Short, Muni Target Maturity, Short Government, Short-Term Bond, Target Maturity, Ultrashort Bond, World Bond, and World Bond-USD Hedged. See Dimensional's *Mutual Fund Landscape 2021* for more detail. Index data provided by Bloomberg Barclays, MSCI, Russell, FTSE Fixed Income LLC, and S&P Dow Jones Indices LLC. Bloomberg Barclays data provided by Bloomberg. MSCI data © MSCI 2021, all rights reserved. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. FTSE fixed income indices © 2021 FTSE Fixed Income LLC. All rights reserved. S&P data © 2021 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

## INDEX DESCRIPTIONS

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**DIMENSIONAL UK SMALL CAP INDEX:** January 1990–present Compiled by Dimensional from Bloomberg, LSPD securities data. Market-capitalisation-weighted index of small company securities in the eligible markets, excluding those with the lowest profitability and highest relative price within their country's small cap universe. The index also excludes those companies with the highest asset growth within their country's small cap universe. Profitability is defined as operating income before depreciation and amortisation minus interest expense divided by book equity. Asset growth is defined as change in total assets from the prior fiscal year to current fiscal year. The index monthly returns are computed as the simple average of the monthly returns of four sub-indices, each one reconstituted once a year at the end of each quarter of the year. Maximum index weight of any one company is capped at 10%. The country currently included is the UK. Exclusions: REITs and investment companies. The index has been retrospectively calculated by Dimensional and did not exist prior to April 2008. Accordingly, the results shown during the periods prior to April 2008 do not represent actual returns of the index. The calculation methodology for the index was amended in January 2014 to include profitability as a factor in selecting securities for inclusion in the index. The calculation methodology for the index was amended in November 2019 to include asset growth as a factor in selecting securities for inclusion in the index. July 1981–December 1989: Includes securities in the bottom 10% of market capitalisation excluding the bottom 1%. Rebalanced semiannually. Prior to July 1981: Elroy Dimson and Paul Marsh, Hoare Govett Smaller Companies Index 2009, ABN-AMRO/Royal Bank of Scotland, January 2009.

**DIMENSIONAL UK MARKETWIDE VALUE INDEX:** January 1990–present: Compiled by Dimensional from Bloomberg, LSPD securities data. Consists of companies whose relative price is in the bottom 33% of their country's respective constituents, after the exclusion of utilities and companies with either negative or missing relative price data. The index emphasises companies with smaller capitalisation, lower relative price and higher profitability, excluding those with the lowest profitability within their country's small cap universe. The index also excludes those companies with the highest asset growth within their country's small cap universe. Profitability is defined as operating income before depreciation and amortisation minus interest expense divided by book equity. Asset growth is defined as change in total assets from the prior fiscal year to current fiscal year. The index monthly returns are computed as the simple average of the monthly returns of four sub-indices, each one reconstituted once a year at the end of each quarter of the year. Maximum index weight of any one company is capped at 10%. The country currently included is the UK. Exclusions: REITs and investment companies. The index has been retrospectively calculated by Dimensional and did not exist prior to April 2008. Accordingly, the results shown during the periods prior to April 2008 do not represent actual returns of the index. The calculation methodology for the index was amended in January 2014 to include profitability as a factor in selecting securities for inclusion in the index. The calculation methodology for the index was amended in November 2019 to include asset growth as a factor in selecting securities for inclusion in the index. Prior to January 1990: Source: Large value and small value portfolio returns from Elroy Dimson, Stefan Nagel and Garrett Quigley “Capturing the value premium in the UK,” *Financial Analysts Journal*, 2003, 59(6): 35–45. Large value and small value portfolios combined at market cap weights. Created Returns, converted from GBP to USD using the WM/Reuters at 4 pm EST (closing spot), from PFPC exchange rate.



**DIMENSIONAL UK MARKET INDEX:** Compiled by Dimensional from Bloomberg, LSPD securities data. Market capitalisation-weighted index of all securities in the UK. Exclusions: REITs and investment companies. The index has been retroactively calculated by Dimensional and did not exist prior to April 2008.

**UK ONE-MONTH TREASURY BILLS:** January 1975–present: UK One-Month Treasury Bills provided by the Financial Times Limited. Prior to January 1975: UK Three-Month Treasury Bills provided by the London Share Price Database.

**UK RETAIL PRICE INDEX:** Provided by the Office for National Statistics. Crown copyright material is reproduced with the permission of the Controller of HMSO.

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