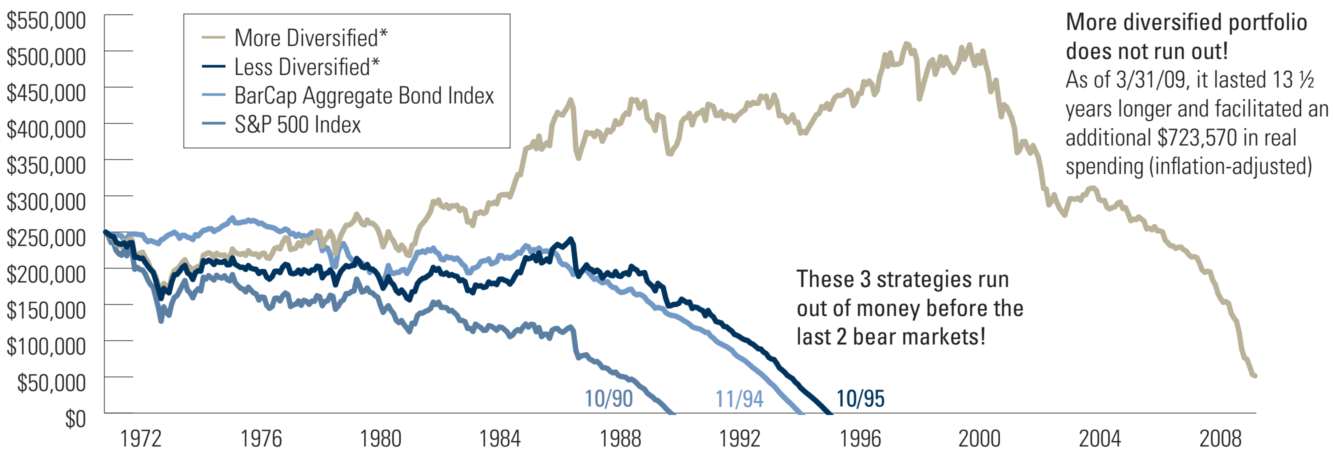
Conviction in Diversification: Benefits of Broad Diversification over Time

Distribution Phase

No longer in your working years, would you have been able to live on your investment savings for over a quarter century, throughout three of the worst Bear markets in history? The answer is yes, ***if*** you were invested for the long-term in a broadly diversified portfolio.

Hypothetical $250K investment beginning in 12/31/1972, net of a 5% drawdown through 3/31/2009

(5% drawdown off of initial portfolio value and inflation-adjusted using actual historical inflation[1])



Source: GSAM, Ibbotson

*The hypothetical historical returns were created with the benefit of hindsight using the percentage allocations shown in the appendix on page 3[2]. Simulated performance results do not reflect actual trading and have inherent limitations. Please see additional disclosures. Any changes will have an impact on the hypothetical historical performance results, which could be material. Hypothetical performance results have many inherent limitations and no representation is being made that any investor will, or is likely to achieve, performance similar to that shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved. Portfolios are comprised of underlying indices. See appendix for Benchmarks and Blend allocation.

When markets decline, it's tempting to throw in the towel and move your savings to cash or conservative bond investments. But history has proven that less diversified strategies that are missing exposure to the full spectrum of asset classes, including growth and value equities and less traditional asset classes — such as REITs, commodities and high yield bonds — ultimately do not create or sustain long-term wealth for investors.

As always, we remain convinced that broad diversification may not work all the time, but it works over time!

Conviction in Diversification: Roadblocks to Building Better Portfolios

The benefits of broad diversification over time are clear. However, in the recent challenging market environment, many investors are afraid to make adjustments to their portfolios in order to achieve a higher level of diversification. Instead, they are standing on the sidelines wondering, “What should I do now?”

But at GSAM, we want to know, “What’s stopping you now?” from taking advantage of an excellent opportunity to improve your investment portfolio.

In our view, the challenging market environment has actually eliminated many of the roadblocks to enhancing diversification that were previously preventing investors from realizing their asset allocation goals during less volatile times. Below, we take a closer look at these roadblocks then and now, and show investors why — with the roadblocks eliminated — they shouldn’t be afraid to stay invested in and/or reallocate to a well-diversified portfolio even in the midst of a Bear market.

Roadblocks to Building Better Portfolios

	Then	Now
Market is too expensive (“Valuation Dilemma”)	In the bull market, when stocks were flying high, investors were reluctant to reallocate to new investments and/or asset classes because they didn’t want to buy too high in fear that the run-up won’t last and their investment will lose value shortly after it’s purchased.	In down markets, such as the current bear, many investments are selling at discounted valuations providing investors with the opportunity to buy low and potentially sell high at a later date.
Tax costs of switching investments (“Tax Dilemma”)	In the booming market, changing allocations created a tax dilemma for clients. No one wanted to pay taxes on the sale of appreciated assets for the purpose of rebalancing portfolios that appeared to be doing fine as they were.	In today’s declining markets, the realization of tax losses can off-set future gains. With adequate planning, now more than ever, it’s an appropriate time to build better portfolios without the potential for significant tax consequences.
Reluctance to fix what’s not broken	When performance is strong, investors are happy. Even if they could be achieving better returns through improvements to their portfolio, most investors aren’t aware of it and, if they are, they are too content to do anything about it.	Today, with the dramatic decline in portfolio values, investors are now wondering if they should do anything differently and may be more open to considering asset classes that they have not been exposed to in the past.

Source: GSAM

One of the benefits of the recent Bear market is that many of the roadblocks to achieving broad diversification no longer exist. In fact, it’s during these times that investors are provided with the greatest opportunities to reassess and potentially reallocate and/or enhance their portfolios through increased diversification, ultimately building a greater source of wealth from which to draw from when needed.

Diversification does not protect an investor from market risk and does not ensure a profit.

For more information on how to diversify your portfolio in challenging times, please contact your Financial Advisor.

Appendix

[1] 5% spending was based off of initial corpus of $250,000 and drawn out monthly, at the end of each month. The actual inflation adjustment was based on monthly actual U.S. inflation, and was adjusted into each monthly drawdown. (U.S. inflation source: Ibbotson 1972 through 12/31/07, U.S. Census Bureau 1/2008 through 3/31/09)

[2] Portfolios rebalanced monthly.

Less Diversified and More Diversified Allocations

Asset Classes	Benchmark	Less Diversified Portfolio	More Diversified Portfolio
U.S. Large Cap	S&P 500	55.0%	—
U.S. Large Cap Value	Ibbotson Associates compiled	—	15.0%
U.S. Large Cap Growth	Ibbotson Associates compiled	—	15.0%
U.S. Small Cap Value	Ibbotson Associates compiled	—	7.5%
U.S. Small Cap Growth	Ibbotson Associates compiled	—	7.5%
International	MSCI EAFE	15.0%	15.0%
U.S. Fixed Income	Barclays Aggregate Bond Index	30.0%	20.0%
Commodities	S&P / GSCI	—	5.0%
U.S. REITs	FTSE NAREIT	—	5.0%
U.S. High Yield Bond	Ibbotson Associates compiled	—	10.0%
		100.0%	**100.0%**

Risk Considerations

Equity securities are more volatile than bonds and subject to greater risks. Small and mid-sized company stocks involve greater risks than those customarily associated with larger companies.

Bonds are subject to interest rate, price and credit risks. Prices tend to be inversely affected by changes in interest rates.

Investments in commodities may be affected by changes in overall market movements, commodity index volatility, changes in interest rates or factors affecting a particular industry or commodity.

Foreign securities may be more volatile than investments in U.S. securities and will be subject to a number of additional risks, including but not limited to currency fluctuations and political developments.

High-yield, lower-rated securities involve greater price volatility and present greater credit risks than higher-rated fixed income securities.

An investment in real estate securities is subject to greater price volatility and the special risks associated with direct ownership of real estate.

Index Definitions

The **S&P 500 Index** is the Standard & Poor's 500 Composite Index of 500 stocks, an unmanaged index of common stock prices. The Index is unmanaged and the figures for the Index do not include any deduction for fees, expenses or taxes. It is not possible to invest directly in an unmanaged index.

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