

# THE RETIREMENT INCOME COMPASS

BECAUSE THERE ARE BIG RISKS ON THE ROAD AHEAD

*Investing Challenge/Compass Advantage*

## Why Diversification Matters: The Randomness of Returns

Best-Performing Asset-Class Index (at top) to Worst-Performing (at bottom) from 1991-2011

1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Asset-Class Index Color
35.2%	28.6%	66.4%	31.0%	14.0%	7.6%	69.2%	35.1%	34.5%	36.0%	39.8%	8.8%	79.0%	28.1%	9.4%	US Real Estate
33.4%	23.1%	33.0%	22.8%	12.3%	5.1%	66.8%	33.2%	24.1%	33.0%	8.2%	6.6%	48.6%	26.9%	3.4%	5-yr US Government Fixed
31.8%	15.6%	30.2%	9.0%	8.4%	3.8%	60.2%	32.1%	22.6%	32.6%	8.0%	4.7%	47.8%	24.5%	2.3%	5-yr Global Fixed
22.4%	10.2%	21.5%	8.3%	7.3%	3.6%	56.3%	30.6%	15.1%	27.5%	6.3%	-24.1%	44.8%	20.7%	2.1%	US Large Cap
19.7%	9.7%	21.3%	7.3%	6.4%	3.4%	47.3%	26.0%	13.8%	26.3%	6.3%	-28.9%	28.6%	19.2%	0.6%	Diversified Portfolio
13.8%	8.4%	21.0%	7.0%	3.8%	-2.9%	46.0%	22.3%	8.2%	23.5%	6.2%	-33.8%	28.5%	19.2%	0.4%	1-yr US Fixed
7.3%	7.8%	14.0%	4.0%	2.5%	-6.0%	36.2%	18.3%	7.0%	22.2%	5.9%	-36.8%	27.2%	15.5%	-4.2%	US Large Cap Value
7.1%	6.8%	7.4%	0.2%	-2.4%	-6.8%	30.7%	16.5%	4.9%	18.4%	5.5%	-37.0%	26.5%	15.1%	-5.1%	US Small Cap
5.9%	5.9%	4.0%	-2.0%	-5.6%	-11.4%	30.0%	14.9%	4.7%	16.5%	2.8%	-39.2%	20.6%	13.9%	-5.5%	US Small Cap Value
0.4%	-2.6%	3.6%	-3.0%	-6.5%	-13.8%	28.7%	10.9%	4.6%	15.8%	-0.2%	-42.5%	19.7%	13.3%	-15.1%	Int'l Small Cap Value
-11.6%	-6.4%	1.9%	-9.1%	-11.9%	-15.5%	2.0%	2.7%	3.1%	4.3%	-1.6%	-45.1%	2.3%	3.7%	-15.6%	Int'l Small Cap
-14.5%	-17.0%	-1.5%	-12.3%	-15.4%	-20.5%	1.9%	1.3%	2.4%	4.1%	-9.8%	-47.1%	0.8%	2.0%	-17.1%	Int'l Large Cap Value
-15.1%	-25.3%	-2.6%	-30.6%	-16.7%	-22.1%	1.5%	0.8%	1.3%	3.8%	-17.6%	-53.2%	0.2%	0.8%	-18.2%	Emerging Markets

Source: DFA Matrix Book 2012. Past performance is no guarantee of future results. You cannot invest directly in an index. Diversification does not insure a profit or guarantee against a loss.

### The Investing Challenge

Although asset classes around the world do not behave consistently or predictably, combining them in diversified balanced strategies can eliminate much of this randomness.

The chart features annual performance for indexes of major asset classes in the U.S., international, and emerging markets over a fifteen-year period:

- The chart ranks the annual returns (from highest to lowest) using a different color box to represent each asset class.
- The white box displays the annual return for a diversified portfolio; balanced with a 60% allocation to stock asset classes, and a 40% allocation to bonds.

In both U.S. and non-U.S. markets, there is little predictability in asset class performance from one year to the next. The history strengthens the case for a portfolio diversified across many asset classes.

### The Compass Advantage

Madden's managed portfolios are built using global diversification across multiple asset classes. By maintaining diversification, managed portfolios have these advantages:

- **Less Variability**—each year's portfolio performance would be in the mid range of asset class rankings since the portfolio's return is a composite of all asset classes;
- **Greater Tax Efficiency**—taxable accounts switching to the best performing asset class would have a capital gains tax liability each year. The managed diversified portfolio will have much smaller tax liability since only a portion of gains would be recognized in annual rebalancing of the portfolio's asset classes.

While there are no guarantees, it's reasonable to assume that a diversified portfolio strategy can be expected to provide a superior return with less volatility and greater tax efficiency over the long run.

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What to know...  
and how to go

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