Commentary
Do Long-Term Investors Need Bonds?

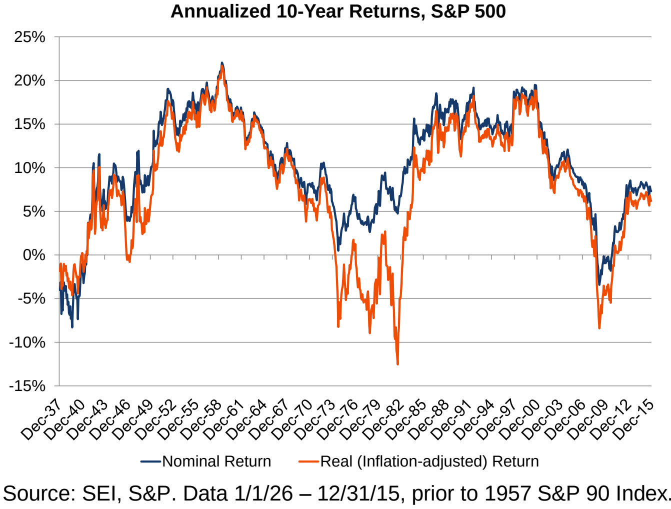
October 2016

Stocks are generally touted as the investment vehicle that offers the highest possible returns for the average investor. Bonds are paying next to nothing in the current low interest rate environment. This scenario has many investors wondering why they should invest in bonds at all. We understand that sentiment. We also believe there's strong case to be made for bonds in a diversified portfolio.

Stocks Don't Always Make Money, Even Over the Long-Term

Stocks are a risky investment and, contrary to conventional wisdom, their risk doesn't diminish the longer you hold them. *It grows.* As an investment is held longer the probability of a negative event rises and the variability of potential outcomes increase. Like interest, losses also compound, and a bad stretch in the stock market can be difficult to recover from.

Exhibit 1: Ten Years Isn't Always Long Enough

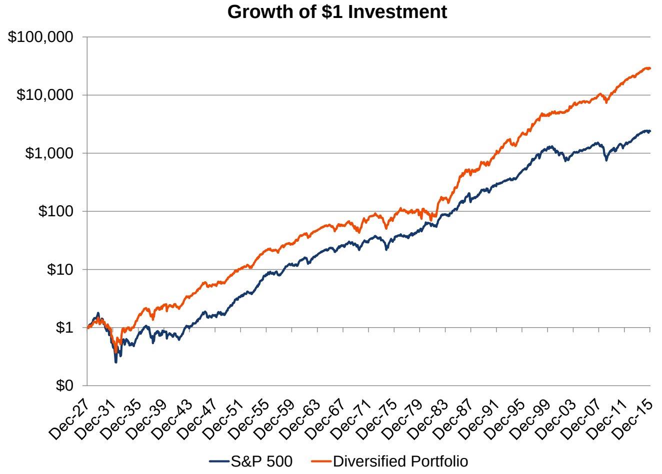


Source: SEI, S&P. Data 1/1/26 – 12/31/15, prior to 1957 S&P 90 Index.

Even When Stocks Make Money, Diversified Portfolios Usually Make More.

There's a common misconception that diversified portfolios are a "low risk, low return" alternative. The truth is investors of any risk tolerance can build a diversified portfolio that is more efficient than an all stock portfolio – meaning diversified portfolios have higher expected returns for any given level of risk.

Exhibit 2: Less Risk, More Return

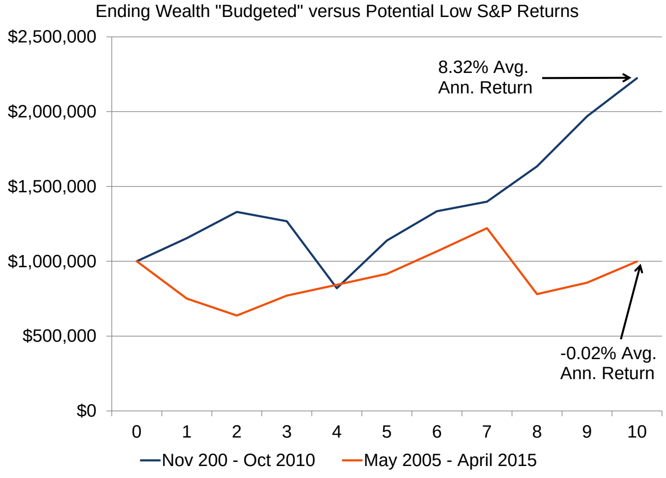


Source: SEI, S&P. Data 1/1/26 – 12/31/15, prior to 1957 S&P 90 Index. Diversified Portfolio = 80% S&P 500, 240% Ibbotson Associates Intermediate Term Government Bond Index, and -220% Ibbotson Associates SBBI 30-Day Treasury Bill Index (the latter being used to represent the financing cost of leveraged positions).

Timing Stock Market Cycles is Nearly Impossible, And Getting it Wrong Can be Disastrous.

Imagine you're an investor ten years from retirement. You are counting on stocks to earn their "typical" mid-to-high single-digit return, but they ended up flat after ten years. The result is a portfolio worth less than half of what was expected – and a retirement lifestyle that will suffer accordingly. This experience isn't rare.

Exhibit 3: It Can Happen To You



Source: SEI, S&P. Sample ten-year periods are for illustrative purposes only.

The Bottom Line: Diversification Helps

No investment can eliminate risk, but responsible investors can ensure that they give themselves the best chance of meeting their goals. Diversified portfolios help to make sure investors are compensated for all of the risks that they take. And this is true regardless of the investment horizon – even long-term investors will benefit from diversifying away from portfolios concentrated in stock-market risk.