VALUES FIRST PLANNING

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More than Money

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LPL Weekly Market Commentary

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Index Investing

We talk a lot about the market indexes - the Dow, NASDAQ and of course the S&P500. If you want to know how the market did on any certain day, you will likely be looking at one of these indices to get the answer. But what are they, how are they constructed, and how does one use these tools to build portfolios?

First, the actual market indices (like the S&P500 or just the S&P) only really exist on a spreadsheet. The Standard and Poor's company built this tool to measure the performance of a basket of stocks in the US stock market. In 1923 the original index was introduced with 233 companies. Then in 1957 it was increased to 500 companies. If you want to take a deeper dive into this topic click here. Many people suppose that if there are 500 companies then each company represents 1/500 of the total index. Like many things in life, it's more complicated than that.

The S&P is a capitalization weighted index (don't leave yet!). All it means is the bigger the company, the bigger their portion of the index. They did this since bigger companies have a bigger impact on the economy. Of course, all indexes are not weighted the same. This becomes very important as an investor if you are trying to control risk by not being overexposed to any one company or part of the market!

Originally if you wanted to invest in the S&P, you had to go buy all the companies in the correct

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weighting. That required a very large portfolio and lots of transaction costs. Then in August of 1976, Vanguard offered the very first Index Fund. It was the first-time average investors could actually “own the index”. Over the years the market has been flooded with many different index investing options. But what is so magical about index investing?

Most mutual fund managers struggle to beat the index that is most like their portfolios and there are some great reasons why. Here are two big ones:

*Index funds are very inexpensive to operate. There is no research department. You just mimic the index. That lower cost vs normal, actively mutual funds is significant over time.

*Indexes stay 100% invested for the long haul. There is no temptation to sell when things are challenging or make too many changes to the investments. It’s not rocket science, those who stay in are rewarded over time.

The challenge now is that several companies have become so large that they have skewed the index quite a bit. Right now, about 30% of the S&P is in the top 10 holdings – with the top two making up almost 7% each! So, it may be representative of the economy, but it is not as diversified as you might have expected.

There are dozens of important indexes, representing different types of investments all over the world. Understanding how these indexes are curated is vital to building portfolios with acceptable risk (volatility) over time. If you want more information about how you are invested and what risks you are carrying – Let us help!

The Standard and Poor’s 500 (SandP 500) is an unmanaged group of securities considered to be representative of the stock market in general. You cannot directly invest in this index.

Gratitude

From credit utilization, to balance transfers, to understanding what affects your score, credit can be a confusing subject. In this episode, Jeff and John give an overview of everything you need to know about credit.

Click **here** to listen.

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