

# 2012: The Year in Review

---

by **Jay D. Franklin** Wednesday, January 02, 2013

Unlike 2011, 2012 was a year in which risk was rewarded. It is important to bear in mind that if risk were rewarded every year, it wouldn't be risk and investors would have no right to expect a positive real return. The market climbed not just a wall of worry, but a "fiscal cliff" of worry that turned out to be much ado about nothing, at least from the market's perspective. However, the U.S. government continues to run trillion dollar deficits and may face the prospect of another downgrade by one of the rating agencies. On the international front, we still have uprisings in Arab countries (particularly Syria) and the continuing questionable financial stability of the European Union. Both of these stories will continue to play out in 2013.

## **Domestic Equities**

As shown in the table below, 2012 was a good year for both small cap and value indexes:

Returns of IFA Domestic Equity Indexes for 2012

Size/Style	Value	Blend	Growth
Large	22.05%	15.82%	17.04%
Small	19.19%	18.39%	17.68%

Source: [dfa.us.com](http://dfa.us.com), [vanguard.com](http://vanguard.com), and [ifaindexes.com](http://ifaindexes.com)

For the mixture of domestic equity indexes used in the majority of IFA's Index Portfolios, the 2012 return was 18.89%, which is 2.47% higher than the 16.42% return of the IFA US Total Stock Market Index.

## **International (Developed) Equities**

As shown in the table below, 2012 was also a good year for international equities, particularly in the small cap blend and small cap value segments:

Returns of IFA International Equity Indexes for 2012

Size/Style	Value	Blend
Large	16.61%	17.75%
Small	22.26%	18.86%

Source: dfaus.com and ifaindexes.com

For the mixture of international equity indexes used in the majority of IFA's Index Portfolios, the 2012 return was 18.58%.

### **Emerging Markets Equities**

As shown in the table below, emerging markets provided a strong showing in 2012:

Returns of IFA Emerging Markets Indexes for 2012

Emerging Markets	19.16%
Emerging Markets Value	19.36%
Emerging Markets Small	24.44%

Source: www.dfaus.com and ifaindexes.com

For the mixture of emerging markets indexes used in the majority of IFA's Index Portfolios, the 2012 return was 21.33%.

### **Real Estate**

For 2012, the IFA real estate index was up 23.17%. This index is a blend of domestic and international real estate investment trusts (REITs). Domestic REITs were up 17.48%, while international REITs were up 33.41%. International REITs rebounded nicely from a difficult 2011 where they suffered from the strengthening of the US dollar and the financial crisis in Europe.

## Fixed Income

Continuing to play its role as a risk reducer with respect to equities, all of IFA's fixed income indexes ended 2012 with positive returns:

Returns of IFA Fixed Income Indexes for 2012

One Year	0.93%
Two Year Global	1.03%
Short-Term Government	1.59%
Five Year Global	4.80%

Source: [www.dfaus.com](http://www.dfaus.com) and [ifaindexes.com](http://ifaindexes.com)

The higher duration fixed income funds enjoyed a higher return than the lower duration funds due to their increased sensitivity to changes in interest rates, which fell in 2012. Interest rates began the year 2013 at very low levels relative to their historical averages. For the mixture of fixed income indexes used in the majority of IFA's Index Portfolios, the 2012 return was 2.09%.

## IFA Index Portfolio Returns

Putting it all together, the 2012 returns of six of the IFA Index Portfolios are shown below:

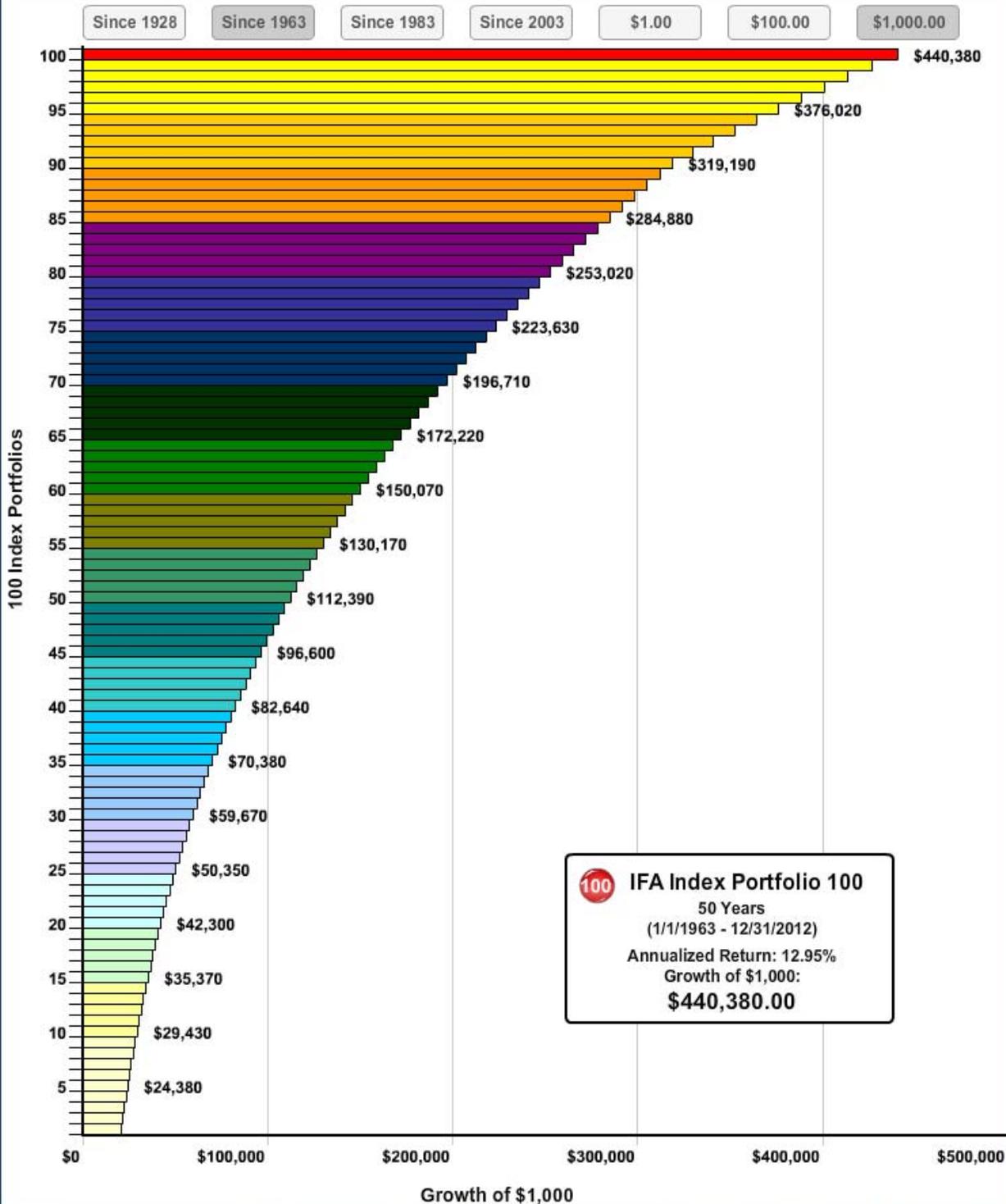
Returns of IFA Index Portfolios for 2012 (net of a 0.90% advisory fee)

<b>IFA Index Portfolio 100</b>	<b>18.38%</b>
<b>IFA Index Portfolio 90</b>	<b>18.43%</b>
<b>IFA Index Portfolio 70</b>	<b>14.98%</b>
<b>IFA Index Portfolio 50</b>	<b>11.53%</b>
<b>IFA Index Portfolio 30</b>	<b>8.08%</b>
<b>IFA Index Portfolio 10</b>	<b>4.62%</b>

Source: [www.ifabt.com](http://www.ifabt.com) (Returns not yet finalized)

# Growth of \$1,000 in 100 Index Portfolios

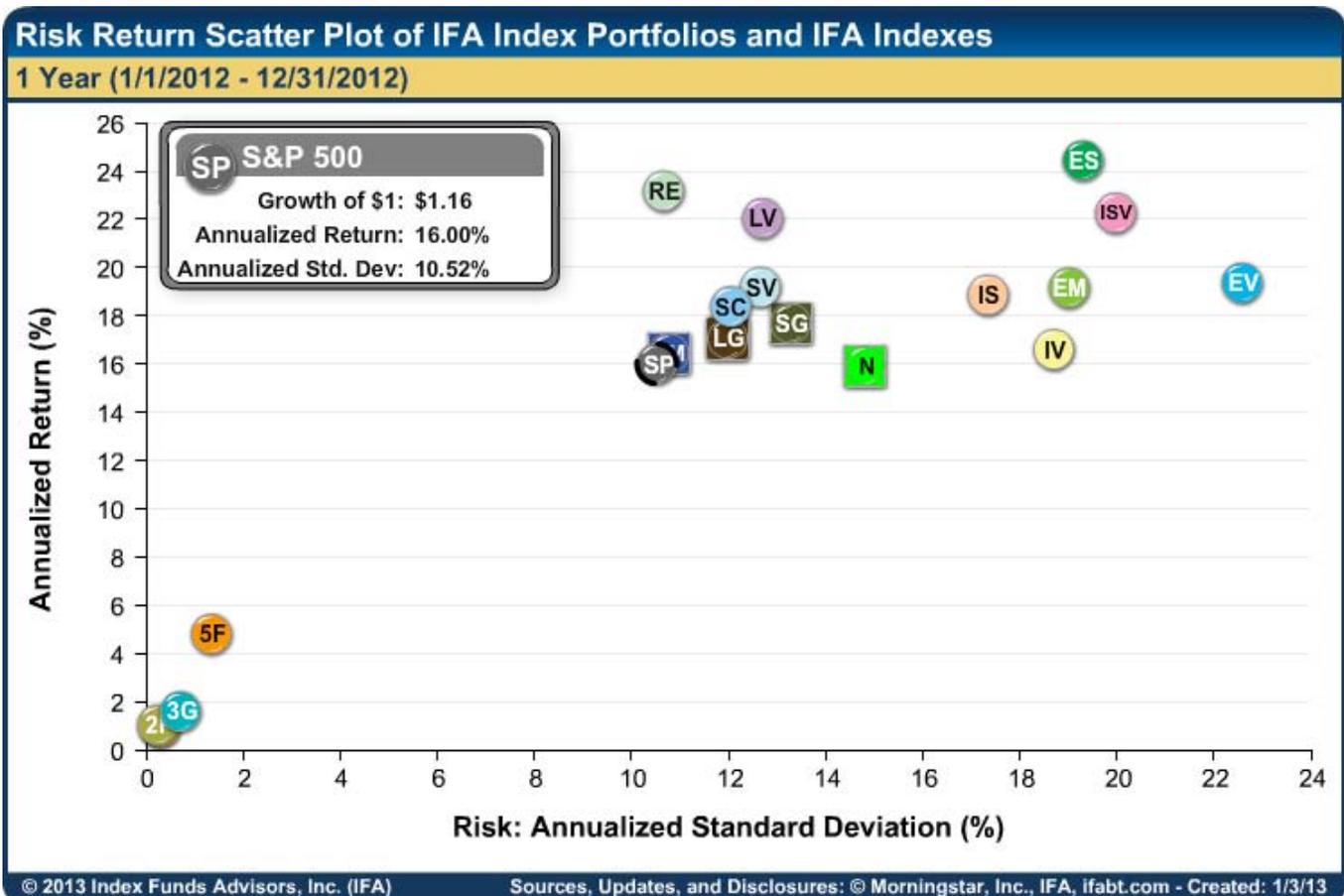
50 Years (1/1/1963 - 12/31/2012)



To summarize, 2012 was a good year for equity investors, especially those who were internationally diversified and tilted towards the compensated risk factors of small cap and value. Regarding IFA's outlook for 2013, it's the same

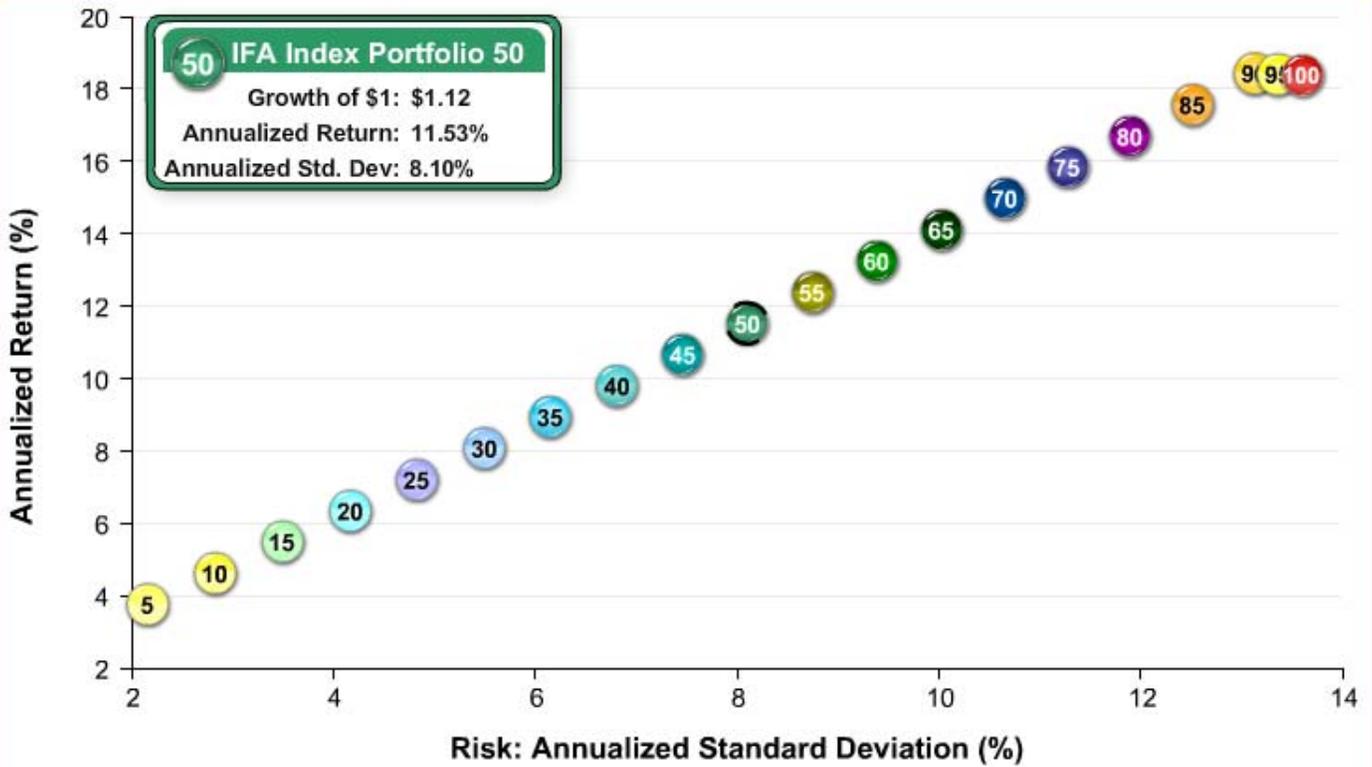
as it is at the beginning of every year (or every day for that matter). The market has done its job of setting prices so that investors can expect an appropriate return to compensate them for the risks they take. What will actually happen will depend on the news which nobody knows in advance.

The two charts below provide a pictorial summary of what happened in 2012. The first chart shows the return and risk (annualized standard deviation) of the asset classes discussed above, with the addition of NASDAQ. Overall, it shows a strong relationship between risk and return. The next chart shows twenty of IFA's Index Portfolios that are created by blending the indexes in the first chart, excluding the ones plotted as squares. Note the straight line relationship between risk and return for the portfolios going up to IFA Index Portfolio 90. The equity mix in IFA Index Portfolio 90 is utilized in all the IFA Index Portfolios below 90. IFA Index Portfolios 91 through 100 are also 100% equity portfolios, but with steadily increasing degrees of tilt towards the risk factors of small cap and value. All of these portfolios had very similar returns and risks in 2012.



# Risk Return Scatter Plot of IFA Index Portfolios and IFA Indexes

1 Year (1/1/2012 - 12/31/2012)



© 2013 Index Funds Advisors, Inc. (IFA)

Sources, Updates, and Disclosures: © Morningstar, Inc., IFA, ifabt.com - Created: 1/3/13

DISCLAIMER: Past performance does not guarantee future results. The actual performance of your portfolio may differ from what is shown here. Please see [here](#) for a further explanation.