

THE TORTOISE AND THE HARE

A Study in Volatility

By Ted Schwartz, Chief Investment Officer
Capstone Investment Financial Group

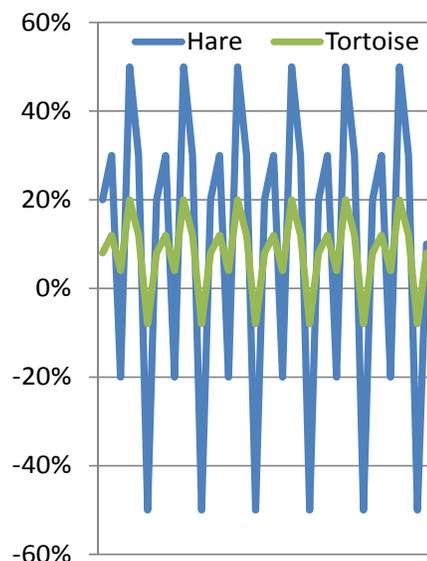


The pursuit of the top performing investments typically backfires on investors when they encounter the impact of increased volatility.

Given the choice of an investment that returns an average of 10% over six years, earning 30% in two of those years, 20% one year and 50% in a fourth year offset by a one-time 20% loss and a one-time 50% loss, and an investment with an average annual return of 8% with yearly results ranging from a 20% gain to a loss of 8%, which would you choose?

If you opted for the first, you, like many investors, have underestimated the impact of volatility on a portfolio. The term volatility indicates how much and how quickly the value of an investment, market, or market sector changes.

The hypothetical example here, which repeats the six-year pattern of returns over 36 years, clearly shows the value of slow but steady when it comes to growing a portfolio.



The hare falls behind because of the mathematics of gains and losses. It doesn't take a 50% gain to recover from a 50% loss. It takes 100%.

Low Volatility and Steady Gains Win the Race

Growth of a Hypothetical \$100,000 Portfolio

Year	Hare	Total	Tortoise	Total	Difference
1	20%	\$120,000.00	8%	\$108,000.00	(\$12,000.00)
2	30%	\$156,000.00	12%	\$120,960.00	(\$35,040.00)
3	-20%	\$124,800.00	4%	\$125,798.40	\$998.40
4	50%	\$187,200.00	20%	\$150,958.08	(\$36,241.92)
5	30%	\$243,360.00	12%	\$169,073.05	(\$74,286.95)
6	-50%	\$121,680.00	-8%	\$155,547.21	\$33,867.21
7	20%	\$146,016.00	8%	\$167,990.98	\$21,974.98
8	30%	\$189,820.80	12%	\$188,149.90	(\$1,670.90)
9	-20%	\$151,856.64	4%	\$195,675.90	\$43,819.26
10	50%	\$227,784.96	20%	\$234,811.08	\$7,026.12
11	30%	\$296,120.45	12%	\$262,988.40	(\$33,132.04)
12	-50%	\$148,060.22	-8%	\$241,949.33	\$93,889.11
13	20%	\$177,672.27	8%	\$261,305.28	\$83,633.01
14	30%	\$230,973.95	12%	\$292,661.91	\$61,687.96
15	-20%	\$184,779.16	4%	\$304,368.39	\$119,589.23
16	50%	\$277,168.74	20%	\$365,242.07	\$88,073.33
17	30%	\$360,319.36	12%	\$409,071.11	\$48,751.75
18	-50%	\$180,159.68	-8%	\$376,345.42	\$196,185.74
19	20%	\$216,191.62	8%	\$406,453.06	\$190,261.44
20	30%	\$281,049.10	12%	\$455,227.43	\$174,178.32
21	-20%	\$224,839.28	4%	\$473,436.52	\$248,597.24
22	50%	\$337,258.92	20%	\$568,123.83	\$230,864.91
23	30%	\$438,436.60	12%	\$636,298.69	\$197,862.09
24	-50%	\$219,218.30	-8%	\$585,394.79	\$366,176.49
25	20%	\$263,061.96	8%	\$632,226.37	\$369,164.42
26	30%	\$341,980.55	12%	\$708,093.54	\$366,112.99
27	-20%	\$273,584.44	4%	\$736,417.28	\$462,832.84
28	50%	\$410,376.66	20%	\$883,700.74	\$473,324.08
29	30%	\$533,489.65	12%	\$989,744.83	\$456,255.17
30	-50%	\$266,744.83	-8%	\$910,565.24	\$643,820.41
31	20%	\$320,093.79	8%	\$983,410.46	\$663,316.67
32	30%	\$416,121.93	12%	\$1,101,419.71	\$685,297.79
33	-20%	\$332,897.54	4%	\$1,145,476.50	\$812,578.96
34	50%	\$499,346.32	20%	\$1,374,571.80	\$875,225.49
35	30%	\$649,150.21	12%	\$1,539,520.42	\$890,370.21
36	-50%	\$324,575.11	-8%	\$1,416,358.79	\$1,091,783.68

Average Annual Return
10%

8%

This is a hypothetical example designed to illustrate the impact of volatility on a portfolio and does not represent the actual returns of any index or managed portfolio. There can be no assurance that any portfolio will match the returns shown here. All investments have the potential for loss as well as gain. Past performance is not indicative of future returns.