Russell Investments

All was not lost

The case for diversification

MARCH 2011

Consulting Services Group

Investing during the first decade of the millennium was memorable. Events like the dot-com bubble bust, 9/11, Enron, and the Great Recession all left an indelible mark in the minds of investors. With annualized U.S. equity returns near zero from 2000-2009, the media conjured up terms like “the lost decade” to describe investing over that period. Investors were left to wonder whether or not participating in the markets could help them reach their financial goals.

Even now, this question persists as headline news cloud the greater story of growth and global recovery. In order to address investor fears, let’s fast forward one year and look at the ten year period from 2001-2010. What a difference a year can make. For those investors who held a balanced portfolio – with exposure to equities, fixed income and real assets – the last ten years was not lost.

Exhibit 1: Diversification rewarded balanced investors

10 year period returns (2001-2010)

Asset Class	10 yr annualized return (ending 12/31/2010)	10 yr cumulative return* (ending 12/31/2010)
U.S. Equity: Russell 3000® Index (R3000®)	2.2%	23.8%
Non-U.S. Equity: MSCI Europe, Australasia, Far East (MSCI EAFE)	3.5%	41.1%
Emerging Markets: MSCI Emerging Markets (MSCI EM)	15.9%	337.0%
Fixed Income: Barclays Capital Aggregate (BC Agg)	5.8%	76.3%
Real Estate: FTSE National Associate of Real Estate Investment Trusts (FTSE NAREIT)	10.8%	178.0%
60/40 Balanced Index Portfolio**	5.3%	67.4%

*Cumulative return – The aggregate amount that an investment gained or lost over time, independent of the period of time involved.
**60/40 Balanced Index Portfolio: 36% R3000®, 16% MSCI EAFE, 3% MSCI EM, 5% FTSE NAREIT, 40% BC Agg

Exhibit 1 shows 10-year returns for five asset classes and a balanced index portfolio. Please remember, indexes are unmanaged and cannot be invested in directly, but are used for illustration purposes. Over that time, the U.S. equity market had a cumulative return* of 23.8%. Hypothetically, this meant that $100,000 invested in U.S. Equities (represented by the Russell 3000® Index) on January 1, 2001 would have been worth

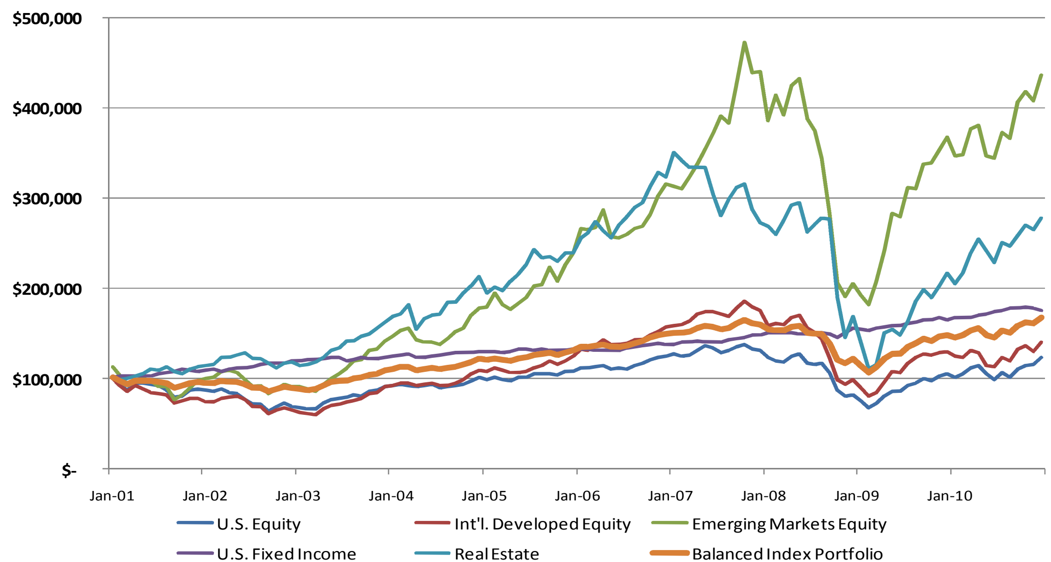
$123,800 on December 31, 2010 (earning a 2.2% return annually). While investors desire higher returns, the ending portfolio value was far from the depleted, never-to-be-recovered portfolios that the media has been talking about.

Balanced investors fared even better as $100,000 invested in a balanced index portfolio on January 1, 2001 would have potentially grown to $167,430 on December 31, 2010 (earning a 5.3% return annually). Diversification rewarded balanced investors. Please remember, returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment.

We know staying invested through volatile markets can be difficult. Exhibit 2 shows the same asset classes and balanced portfolio over the same time period from 2001-2010. It is interesting to see how most of the individual asset classes experienced greater fluctuation than the balanced index portfolio. The highest returns came from the Emerging Markets (MSCI Emerging Market Index) and Real Estate (FTSE NAREIT Equity Index) asset classes, but the volatility, or fall from the highs, was incredibly steep. These steep decreases may make it difficult for investors to stick to their financial plan. Balanced investors, though, had a smoother ride.

Exhibit 2: Balanced investors may have had a smoother ride

Growth of $100,000 from 2001 - 2010



Inevitably, the market will continue to fluctuate. We don't know for certain the direction on any given day, week or year but a diversified portfolio may help you avoid that volatility and stay invested. It is important for investors to focus on a long-term investment strategy and to not let short-term fluctuations and headlines impact long-term goals.

Please remember that all investments carry some level of risk, including the potential loss of principal invested. They do not typically grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

Diversification does not assure profit or protect against loss in declining markets.

Indexes are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment.

The Russell 3000® Index measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market.

Barclays Capital Aggregate Index, with income reinvested, generally representative of intermediate-term government bonds, investment grade corporate debt securities, and mortgage-backed securities. (Specifically: Barclays Capital Government/Corporate Bond Index, the Asset-Backed Securities Index, and the Mortgage-Backed Securities Index.)

The MSCI EAFE Index, with dividends reinvested, is representative of the securities markets of twenty developed market countries in Europe, Australasia, and the Far East.

MSCI EM Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in emerging market country indices.

FTSE NAREIT, an Index designed to present investors with a comprehensive family of REIT performance indexes that span the commercial real estate space across the US economy, offering exposure to all investment and property sectors. In addition, the more narrowly focused property sector and sub-sector indexes provide the facility to concentrate commercial real estate exposure in more selected markets.

The trademarks, service marks and copyrights related to the Russell Indexes and other materials as noted are the property of their respective owners. The Russell logo is a trademark and service mark of Russell Investments.

Copyright © Russell Investments 2011. All rights reserved. This material is proprietary and may not be reproduced, transferred, or distributed in any form without prior written permission from Russell Investments. It is delivered on an "as is" basis without warranty.

Russell Investment Group, a Washington USA corporation, operates through subsidiaries worldwide, including Russell Investments, and is a subsidiary of The Northwestern Mutual Life Insurance Company.

Russell Financial Services, member FINRA, part of Russell Investments.

First used: March 2011

RFS 11-5379