
BOOK REVIEW



Mark Kritzman, Senior Editor

GLOBAL ASSET ALLOCATION: A SURVEY OF THE WORLD'S TOP ASSET ALLOCATION STRATEGIES

Mebane Faber

Kindle Edition (April 20, 2015)

(Reviewed by Javier Estrada, IESE Business School, Barcelona, Spain)

It is no secret that finance and economics have been suffering from ‘physics envy’ for quite some time. Articles in academic, and even in practitioner-oriented journals seem to be increasingly driven more by the desire to introduce a new ‘sophisticated’ model, or a slight econometric tweak that alter the results of a widely-read article, than by the desire to help investors and policy makers to make better decisions. From this perspective, Meb Faber’s *Global Asset Allocation: A Survey of the World’s Top Asset Allocation Strategies*

is a very refreshing and welcome reading.

Faber would have found it nearly impossible to publish his short book, which is no longer than many articles regularly published in many journals, in a widely-read academic or practitioner-oriented journal. And this is, unfortunately, because his approach is direct, easy to follow, and devoid of methodological sophistication. However, the book and its ultimate message are extremely instructive and useful.

Ultimately, the book aims to compare the performance of several global asset allocation strategies, many of them explicitly or implicitly recommended by well-known investors such as Ray Dalio, David Swensen, and Rob Arnott, among others. Interestingly, the two main findings of the book can simply be summarized as follows:

First, most of these seemingly-different strategies have similar exposures; and second, the costs of investing are a critical determinant of performance. Regarding the latter, Faber shows that the best-performing of the strategies considered underperforms the worst-performing strategy if the former is implemented inefficiently without due attention to fees. Hence, smart investing requires carefully considering both asset allocation and the costs of investing. Simple, direct, and critical advice.

Faber starts off with a brief discussion of the long-term performance of stocks, bonds, and bills, not just in the US but also in several other countries. Then he moves to consider the performance of his benchmark portfolio, a 60-40 combination of stocks (the S&P 500) and bonds (10-year US Treasury Notes), discussing not only

its historical performance but also its expected performance given the current conditions of relatively high multiples in the stock market and very low yields in the bond market.

Faber's forecast for the 60-40 strategy over the next ten years is bleak: Expect annualized nominal returns around 3.5% for stocks, 2.2% for bonds, and 2–3% for the 60-40 portfolio. If these assumptions are coupled with expected annual inflation of a bit over 2%, then investors should expect annual real returns in the 0-1% range from the 60-40 portfolio. Very far from exciting, and yet fairly in line with forecasts from AQR, Bridgewater, Research Affiliates, and GMO.

In fact, this depressing expected performance of the 60-40 portfolio is Faber's justification for exploring other asset allocation strategies that on the one hand are more global and on the other include other assets beyond stocks and bonds. All in all, Faber considers 13 assets as the building blocks of several portfolios whose performance he evaluates over the 1970–2013 period; these include stocks (US large cap, US small cap, developed markets, and emerging markets), bonds (US Bills, US 10-year Notes, US 30-year Bonds, and US corporate

bonds, as well as 10-year foreign government bonds), and real assets (TIPS, commodities, gold, and REITs).

Having discussed the building blocks, Faber moves to consider several strategies that combine some of these assets, directly or indirectly recommended by well-known investors. Space limitations make it impossible to get into the details of these strategies and their performance, but it suffices to say here that the asset allocations considered include Ray Dalio's risk parity and all seasons strategies, Harry Browne's permanent portfolio, and portfolios suggested by Rob Arnott, Marc Faber, David Swensen, Mohamad El-Erian, and Warren Buffett, among others.

Interestingly, Faber finds that over the 1973–2013 period there is no dramatic difference in performance across these strategies, most of which are within one percentage point from each other in terms of annualized returns. Even more interestingly, he finds that implementing the best-performing strategy inefficiently (with mutual funds instead of ETFs and with advisory fees tacked in) turns it into the worst-performing strategy. In Faber's words: "Think about

that for a second. Fees are far more important than your asset allocation decision!"

In fact, Faber goes farther; again in his words: "This is the main point we are trying to drive home in this book — if you are going to allocate to a buy and hold portfolio you want to be paying as little as possible in total fees and costs." And he adds as basic advice that diversification is the only free lunch; real assets such as commodities, real estate, and TIPSs provide such diversification; a global 60-40 portfolio is a better choice than a US-centric 60-40 portfolio; and investors should choose an asset allocation and stick with it, save for some periodic rebalancing. (In his words: "Live your life and don't worry about your portfolio!")

In short, I found Faber's short book to be very easy to read and instructive. It reaffirms many points often stressed by advisors but not so often implemented by investors, and it does so based on an extensive evaluation of many different strategies. All in all, it will not take readers long to finish this book and it may yield great benefits to implement Faber's essential conclusions.