



These 6 ETFs Are All You Need for 8% Returns

Description

In the world of endowments, Yale University’s David Swensen is a god.

When Swensen was hired by the university in 1985 to manage the endowment, it was US\$1 billion. Today, more than 30 years later, it’s at US\$25.4 billion. Over the past 20 years, Swensen and his investment team delivered an annual return of 12.6%—510 basis points better than the 7.5% average return of college and university endowments in the U.S.

With numbers like that, it’s not surprising how revered Swensen is, both in academia and investment management circles. He’s truly helped transform Yale into one of the best educational institutions anywhere.

Here in Canada, the University of Toronto Asset Management Corporation has done a good job managing the endowment and pension funds of one of Canada’s biggest and best universities.

Over the last 13 years, it’s managed to deliver positive returns in every year but one, 2008, when it lost 29.4%—380 basis points worse than its benchmark portfolio, a shadow portfolio of six asset classes that can be easily duplicated by individual investors with ETFs.

“The principle underlying the Benchmark portfolio’s composition requires exposures that are passive, low-cost, easily implementable and generally representative of the investable universe,” stated its 2015 management discussion and analysis within its annual report.

I recommend you read its report and those of other endowments. They’re very informative and educational.

UTAM benchmark portfolio asset mix

Asset	Weight
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Canadian Equity

(S&P/TSX Composite Total Return Index) 16%

US Equity

(S&P 500 Total Return Index) 18%

International Developed Markets Equity

(MSCI EAFE Net Total Return Index) 16%

Emerging Markets Equity

(MSCI EM Net Total Return Index) 10%

Credit

(FTSE TMX Corporate Bond Total Return Index) 20%

Rates

(FTSE TMX Government Bond Total Return Index) 20%

Source: UTAM 2015 Annual Report

To make this as simple and cost effective as possible, I've selected the ETFs with the lowest management expense ratio that best correspond to each of the indexes used by the university.

In the case of the U.S. equity and international developed markets, the foreign currency is 65% hedged to the Canadian dollar. In the case of the emerging markets equity, it has 100% unhedged foreign currency exposure. We won't be able to completely duplicate this, but it will be close enough.

Benchmark ETF portfolio

Asset

Weight

Canadian Equity

iShares S&P/TSX Capped Composite Index Fund 16%

[\(TSX:XIC\)](#)

US Equity

Vanguard S&P 500 Index ETF CAD Hedged 18%

[\(TSX:VSP\)](#)

International Developed Markets Equity

iShares Core MSCI EAFE IMI Index ETF 16%
(TSX:XFH)

Emerging Markets Equity

iShares Core MSCI Emerging Markets IMI ETF 10%
([TSX:XEC](#))

Credit

iShares Canadian Corporate Bond Index ETF 20%
([TSX:XCB](#))

Rates

iShares Canadian Govt Bond Index ETF 20%
([TSX:XGB](#))

If you'd invested \$100,000 last November in the six ETFs above at the same weights, today you'd have almost \$109,000 and an 8.6% annual return. Although this is considerably lower (700 basis points) than if you'd put all of the money in the XIC; long term, especially in years like 2008, when there was no place to hide for equities, you'll be very happy that you're 30-40% in bonds.

How'd the XCB and XGB do in 2008? They generated total returns of 0.08% and 8.9%, respectively, compared to a negative return of 33.3% for the XIC.

Warren Buffett suggests most investors should put their money in this type of portfolio because it's simple and relatively safe over the long haul. The University of Toronto's asset managers believes this benchmark allows for a proper analysis of its "active" management, which beat the benchmark over the past four years by 290 basis points, 11.2% to 8.3%.

If it's good enough to be a benchmark for a multi-billion dollar endowment and pension, it ought to be good enough for the average investor.

These six ETFs are all you really need.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:XIC (iShares Core S&P/TSX Capped Composite Index ETF)

Category

1. Investing

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Author

washworth

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