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Bogleheads guide to the three fund portfolio analysis answer sheet example



It includes "USD-denominated, taxable bonds that are rated either investment grade or high-yield." As of 2015, 87% of the Universal index is made up of bonds in the Aggregate index, but the other 13% includes "U.S. Corporate High Yield Index, Investment Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index." People who have strong feelings about wanting to be more "total" than the Vanguard Total Bond Index Fund might prefer the Barclay's Universal index. Avoids "front running." Easy to rebalance. On the one hand, a three-fund portfolio involves a do-it-yourself aspect that makes it more complicated than using an all-in-one fund. One sensible option is to hold domestic and international stocks in the same proportions as they represent in the total world economy. On the other hand, it is assumed that every investor should hold both domestic and international stocks. The term has been popularized by Paul B. Other variations See also: Variations on Bogleheads® investing A three-fund combination can serve as the core of a more complex portfolio, where you add a small play money allocation or a tilt to some corner of the market that interests you. When transferring to a different brokerage, the fund will have to be liquidated, thereby creating a taxable event.[3] † The Fidelity ZERO International Index Fund (FZILX) does not include international small-cap stocks. As of October 2014, that would be about 50% U. Vanguard funds in this category include the Target Retirement funds, the LifeStrategy funds; perhaps the actively-managed Wellington and Wellesley funds would qualify, too. † 3.0 3.1 Fidelity ZERO funds are not recommended for use in taxable accounts due to their lack of portability. This article contains details specific to United States (US) investors. This option is recommended by Burton Malkiel and Charles Ellis, both of whom have longstanding ties to Vanguard, in their book The Elements of Investing. † An investor in the Thrift Savings Plan seeking to gain US small cap and mid cap exposure must add the S fund (an S&P completion index fund) to the TSP three-fund portfolio. TAYLOR LARIMORE is a sage on the Boglehead forums for everyone who wants to discover "the Boglehead way." Crowned the "King of the Bogleheads" by Jack Bogle, he has spent more than seven decades in finance and investing, in such positions as revenue officer for the IRS, chief of the Financial Division for the Small Business Administration in South Florida, and a director of the Dade County Housing Finance Authority. Suggestions 2 and 3 are adjustments that don't radically change the risk of the bond component. † Investors using The Vanguard FTSE All-World ex-US ETF for international stock allocation need to recall that the fund does not provide exposure to small cap international stocks. † The Stock fund is comprised of 70% Total US Stock market, 30% total international (excluding US) market, which is 2/3 of a three-fund portfolio. It is assumed that cash is not counted within the investment portfolio, so it is not included. Investors wanting to include small cap international stocks in the portfolio can add the Vanguard FTSE All-World ex-US Small-Cap ETF (VSS) . Thus, the Bogleheads forum and Wiki tends to be Vanguard-oriented. The International Index (tracking the EAFE index) does not include emerging market stocks, Canadian stocks, and has minimal exposure to international small cap stocks. † The T. there is a certain elegance in the simplicity of it." In her Forbes article, "How To Diversify With Just Three Funds", Boglehead Laura F. (Refer to the associated wiki article for additional information.) Three-fund Portfolios using Mutual Funds Fund Source Example Portfolios Charles Schwab With Schwab, investors can construct a three-fund portfolio using: [note 1] Schwab Total Stock Market Index (SWTSX) Schwab International Index (SWISX) Schwab U.S. Aggregate Bond Index Fund (SWAGX) Dreyfus When using Dreyfus index funds, investors can build a three-fund portfolio using: [note 2] S&P 500 Basic Index (DSPSX) International Index (DIPSX) Bond Index Basic (DBIRX) Fidelity With Fidelity, for example, you could construct a three-fund portfolio using: Fidelity ZERO Total Market Index Fund (FZROX)[note 3] or Fidelity Total Market Index Fund (FSKAX) Fidelity ZERO International Index Fund (FZILX)[note 3][note 4] or Fidelity Total International Index Fund (FTIHX) Fidelity U. For the record, it should be stated that Burton Malkiel and Charles Ellis, in the 2013 edition of their book Elements of Investing, made a controversial and much more radical suggestion, which shocked many forum members. Not to the legions of investors who have already amassed fortunes following the philosophy of iconic investor and founder of The Vanguard Group, Jack Bogle. Taylor Larimore is recognized as a bona fide expert on Jack Bogle's low-cost, buy-and-hold investment strategy. On the other hand, three-fund portfolios are simpler than the genres called "Coffeehouse portfolios" (William Schultheis's term), "couch potato" portfolios, or "lazy portfolios," which are intended to be easy for do-it-yourselfers but are nevertheless slice-and-dice portfolios using six or more funds. The tool is entitled Get a recommendation to fit your goals; you can navigate to it by way of Vanguard.com, Go to personal investors' site, What we offer: Mutual Funds, Get a Recommendation. There are "completion index" funds such as Vanguard's Extended Market fund (available as an open-end fund as VEXAX and as an ETF as VXF) which can be added to an S&P 500 fund in a specified ratio to produce a hybrid which should perform like a Total Stock Market fund. Contains every style and cap-size. Other authorities suggest holding less than that, and Vanguard currently allocates 40% of stock to international in its Target Retirement funds, and in their research, advise holding 20% - 40% international allocations.[4]. For example, one could use Total Stock Market ETF (VTI) [1], Vanguard Total International Stock Index Fund (VXUS) [2] for international, and Vanguard Total Bond Market ETF (BND). No definitive answer can be given to this controversial question, but we can sketch out some of the prevalent conflicting opinions on the matter. You may need to hold the same (or equivalent) funds in multiple accounts to have ideal asset allocation and asset location. Choosing your asset allocation Even if you are going to use a single Target Retirement fund, you should not take the shortcut implied by the use of a retirement year in the name; you need to decide for yourself what percentage of your portfolio you want to invest in stocks, and choose the fund that matches it. And unbeatable. Vanguard perplexes investors by offering two virtually interchangeable international stock market index funds: Vanguard Total International Stock Index Fund (VTIAX) and Vanguard FTSE All-World ex-US (VFWAX). It's 2016. Acting on fund or ETF suggestions in it may have harmful US tax consequences for non-US investors. Aggregate Bond Index ETF (SCHZ) State Street SPDRs When using SPDRs, investors can build a three-fund portfolio using: [note 12] SPDR Russell 3000 ETF (THRK) SPDR MSCI ACWI ex-US ETF (CWJ) SPDR Bloomberg Barclays Aggregate Bond ETF (AGG) Vanguard When investing in Vanguard ETFs, investors can create a three-fund portfolio using: [note 13] Vanguard Total Stock ETF (VTI) Vanguard Total International Stock ETF (VXUS) Vanguard Total Bond Market ETF (BND) Other considerations A total stock market index fund represents the whole market, while an S&P 500 fund does not. Dogu describes this investing and comments "With only these three funds (Vanguard Total Stock Market Index fund, Vanguard Total International Stock Market Index fund, and the Vanguard Total Bond Index fund), investors can create a low cost, broadly diversified portfolio that is very easy to manage and rebalance.... In general, the international fund should go into a taxable account, the bond fund should go into a tax-advantaged account, and the domestic equity fund should fill in the remaining space. Very low cost. What about bonds? If your own preference is for a "total world" weighting, then the portfolio can obviously be simplified using Vanguard's Total World Stock Index fund, which is exactly what Malkiel and Ellis suggest. Watch out for high expense ratios, particularly in the bond funds. Rowe Price T.Rowe Price investors can create a simple indexed three-fund portfolio using the following three funds: [note 6] Total Equity Market Index Fund (POMIX) International Equity Index Fund (PIEQX) US Bond Enhanced Index Fund (PBIDX) Thrift Savings Plan Participants of the Thrift Savings Plan can create a three-fund portfolio using the following three funds, for example: [note 7] C fund I fund F fund, or alternately, the G Fund TIAA TIAA annuities plans participants can create a three-fund portfolio with only two funds:[note 8] CREF Stock (70% Russell 3000 / 30% MSCI Allworld ex-US) CREF Bond (Barclays U.S. Aggregate Bond)[note 9] TIAA mutual fund (retail) participants can use:[note 10] Equity Index (TNRX) Emerging Markets Stock Index Fund (TEQXX) Bond Index Fund (TBILX) With Exchange-traded funds: Three-fund Portfolios using ETFs Fund Source Example Portfolios Blackrock iShares When using iShares ETFs, investors can build a three-fund portfolio using: iShares Core S&P Total Market ETF (ITOT) iShares Core MSCI Total International ETF (IXUS) iShares Core Total U.S. Bond Market ETF (AGG) Charles Schwab With Schwab, investors can construct a three-fund portfolio using: [note 11] US Broad Market ETF (SCHB) International Equity Index ETF (SCHF) U. This is a conservative rule, and leads to smaller percentages of stocks than Vanguard chooses for its Target Retirement series. Now, the bond portion has been modified to include international bonds; specifically, the bond allocation is now 70% Vanguard Total Bond Market Index Fund and 30% Total International Bond Index Fund. In addition, index purists should take note that the US Bond Enhanced Index Fund utilizes an active management component. Bond Index Fund (FXNAX) Northern Funds When investing in Northern Funds investors can create a three-fund portfolio using: [note 5] Stock Index (NOSIX) International Index (NOINX) Bond Index (NOBOX) T. Some would say that advocates of complex investing strategies always have reasons why simple approaches "once worked but don't work any more." Advocates of simplicity might say to ignore the noise and continue to stay the course; it may turn out that something else does better—something always does—but that a three-fund portfolio is still good enough. Sample three-fund portfolios Other than Vanguard, Boglehead-style The building blocks of Boglehead-style investing are low-expense-ratio index mutual funds and/or ETFs. Vanguard fans would suggest that Vanguard has the best and most complete lineup of such funds, and that the most convenient place to hold Vanguard mutual funds is directly at Vanguard. The investment manager has the authority to adjust certain holdings versus the benchmark index, which could result in the fund being marginally underweight or overweight in certain sectors, or result in the portfolio having a duration or interest rate exposure that differs slightly from those of the index. Contrasted with other approaches There are single, all-in-one, "funds of funds" that are intended to be used as an investor's whole portfolio. See Should I buy Total International or FTSE All-World ex-US for the details. Simplicity – Taylor Larimore, co-author, The Boglehead's Guide to Investing A three-fund portfolio is based on the fundamental asset classes, stocks and bonds. The differences are usually of no fundamental importance, and are usually the result of a) making choices between nearly identical, almost interchangeable funds, and b) simplifying further by using combination package funds. They seemed to be recommending the replacement of a traditional high-grade bond fund with a 50/50 mix of emerging markets bonds and a high-dividend stock fund. No style drift. Small cap international stocks make up only a minimal part of the portfolio. This implementation creates a six-fund portfolio, and 50% international. They are "lazy" in that the investor can maintain the same asset allocation for an extended period of time, as they generally contain 30-40% bonds, suitable for most pre-retirement investors. No overlap. Be aware of any minimum investment required by each fund; for instance, the Admiral shares of most Vanguard index funds require a minimum investment of \$3000.00; if you will have difficulty meeting these minimums, you may want to consider an all-in-one single-fund portfolio until you accumulate enough that this is not an issue. Even if you are going to use a single LifeStrategy fund, you need to decide which of them to use, based on the percentage of stocks each one holds. Note that the international indexes being tracked by the funds do not include Canadian stocks nor market weightings of small cap stocks. See Asset allocation for more details. Through step-by-step explanations, it shows you how to ensure your financial security by investing in the three market index funds—U.S. stocks, non-U.S. stocks, and U.S. bonds. Low turnover. One could, of course, use ETFs rather than mutual funds. Mathematically certain to out-perform most investors. This is a much less critical decision because U.S. and international stocks have similar risk profiles and have similar long-term returns. For people just entering the workforce as well as those closing in on retirement, this single resource ensures a brighter financial future by enabling you to: Eliminate a large handful of risks associated with other investing methods, including manager choice, individual stock and sector vulnerabilities, tracking error, and more Avoid the most common ways investors lose money trying to make it, including stock picking, market timing, useless newsletters, and expensive advisors Prepare yourself to invest real money by hearing from a diverse collection of everyday investors successfully using the approach, including model allocation strategies and tips Follow the simple path to financial security in The Bogleheads' Guide to the Three-Fund Portfolio. [note 14] The funds include: Vanguard Total Stock Market Index Fund Vanguard Total International Stock Index Fund Vanguard Total Bond Market Index Fund The International Index (which tracks the EAFE index). Sound too good to be true? The original "basic, humble, couch potato portfolio" consisted of two funds, "the Vanguard Index 500 fund, which mimics the Standard and Poors' 500 index, and the Vanguard Fixed Income Short Term Government Bond Fund." [8] Taylor Larimore was an early advocate of this approach, which he described in 1999 in a Morningstar posting. Which is better, 15 funds or 4? He is co-author of The Bogleheads' Guide to Investing and The Bogleheads' Guide to Retirement Planning. As of 2016 when this is being written, bond interest rates are near historic lows and there is a good deal of buzz to the effect that the "thirty-year bull market in bonds has ended" and that investing strategies that have worked for decades should be changed to reflect new realities. Now, with only four funds, it is possible to own all the securities in every asset-class, style, and cap-size, in exact proportion to their market weight. S. No manager risk. Read it, execute it, then retire in comfort and sleep like a baby." —William J. There is no magic in the number three; the phrase is shorthand for a style of portfolio construction that emphasizes simplicity, and is related to lazy portfolios. † TIAA plans are often customized by each employer, so you may have lower expense-ratio options that are not mentioned in this article. By adding an international stock fund, one could create a three-fund portfolio with two funds. Others would argue that the evidence for superiority of slice and dice, "small value tilting," and inclusion of classes like REITs is too strong to ignore. The LifeStrategy and Target Retirement funds are four-fund portfolios The Vanguard Target Retirement funds and LifeStrategy funds employ a four fund allocation matrix. Non-US investors can find related information at Simple non-US portfolios. Barclay's has a broader index, the Barclay's U.S. Universal Index. Choosing three funds For Bogleheads, the answer for "what mutual funds" to use in a three-fund portfolio is "low-cost funds that represent entire markets." If you ask different people to choose funds for a three-fund portfolio, you will get different fund choices. Some well-informed Bogleheads make a strong case that the "bond" component of a three-fund portfolio might well be filled with non-brokered bank CDs instead of a traditional bond fund. These four funds are: Total Stock Market Fund, Total Bond Market Fund, Total International Fund and a Money-Market Fund." Notes 1 The Schwab International Index is based on the MSCI EAFE index, which does not include emerging market stocks, Canadian stocks, and which has minimal exposure to international small cap stocks. Investors can broaden US stock diversification by adding the Mid Cap (PESPX) and Small Cap (DISJX) index funds to the portfolio allocation. † The Vanguard Target Retirement Income fund, and Target funds nearing target dates add a fifth fund, the Vanguard Short Term Inflation Indexed Bond Fund, to the allocation matrix. Alternatively, you can approximate a Total Stock Market fund by combining an S&P 500 index fund with one or more mid-cap and small-cap funds. † The SPDR MSCI ACWI ex-US Index provides exposure to 87% of the international stock market. Some people complain that the Aggregate index isn't really the "total" bond market. "Simple. Investors can add exposure to these markets by adding the Schwab Emerging Markets Equity ETF (SCHE) and the Schwab International Small Cap ETF (SCHC) to the portfolio mix. Investors desiring exposure to small cap international stocks can add the SPDR S&P International Small Cap ETF (GWL) and the SPDR S&P Emerging Markets Small Cap ETF (EWX) to the portfolio. Very tax-efficient. † Dreyfus Basic shares provide for lower expense ratios and a \$10,000 minimum investment. Some investors may be uncomfortable with holding only three funds and will question whether they are truly diversified. A three-fund portfolio is a portfolio which uses only basic asset classes — usually a domestic stock "total market" index fund, an international stock "total market" index fund and a bond "total market" index fund. The key to capturing the most return with this strategy lies in allocation, and the guidance inside offers an illuminating depth of coverage on the nuanced ways to balance a portfolio based on your age, income, goals, tolerance for risk, and personal comfort level with volatility. Some may find it appealing to follow Vanguard's lead. The fund does not include emerging market stocks or Canadian stocks. This option is still available, but is too complex to fully explain in this article. As of 2015, there is at least one product, the iShares Core Total USD Bond Market ETF, IUSB, that tracks the Barclay's Universal index, and with an 0.13% expense ratio, it qualifies as a "low-cost index fund." It could be used as the bond component of a three-fund portfolio. Establishing a three-fund portfolio ADVANTAGES OF THE THREE-FUND INDEX PORTFOLIO Diversification. † The Schwab International Index ETF does not include emerging markets nor international small cap stocks. But, because they were early champions of indexing, each with long associations with Vanguard, their suggestion should be noted. It is often recommended for and by Bogleheads attracted by "the majesty of simplicity" (Bogle's phrase), and for those who want finer control and better tax-efficiency than they would get in an all-in-one fund like a target retirement fund. In practice, the importance and magnitude of the difference is a subject of debate. Farrell, who writes MarketWatch columns about various simple portfolios. Whether you want to start investing or need better returns, this comprehensive guide walks you step-by-step through determining the proper allocation of your assets, choosing smart investments, and managing your portfolio over time—without losing sleep or money! In his inspiring Foreword, Jack puts his seal of approval on this powerful and easy-to-use resource, which provides: A five-step solution to securing wealth in Bull and Bear Markets Actionable plans for capturing more market returns than many professional investors Insights and commentary from celebrated and everyday Boglehead investors Discover the stress-free approach to reaching your financial goals with The Bogleheads' Guide to the Three-Fund Portfolio. But the more complicated your portfolio is, the more expensive and more prone to blow-ups it's likely to be — which also increases the odds that it will generate subpar returns," and suggested a "three-fund diversified portfolio: simply invest in the following three funds (or their ETF equivalents): a total U.S. stock market fund, a total international stock market fund and a total U.S. bond market fund." [7] Some would argue that a three-fund portfolio is good enough and that there is no real proof that more complicated portfolios are any better. Rowe Price International Index Fund is a developed market international index fund. The task, then, is to take these three basic non-cash assets — domestic stocks, international stocks, and bonds — decide how much of each to hold (your asset allocation); choose where to hold each of these asset classes, and

finally choose a mutual fund to use for each asset class. Also, the I fund (tracking the EAFE index) does not invest in emerging market stocks or Canadian stocks, and has minimal exposure to small cap international stocks (less worry). The Vanguard Total Bond Market Index Fund, and those of several other firms, track the Barclay's U.S. Aggregate Index (in Vanguard's case, the Barclay's U.S. Aggregate Float-Adjusted Index). Combining domestic and international stocks
The relative percentage of domestic and international stocks is a subject of intense discussion in the forum. Choosing your asset location
Since your portfolio may be split between multiple locations (one or more tax-advantaged retirement accounts, and one or more taxable accounts) you should look at Principles of tax-efficient fund placement to determine which funds belong in each account. The advantages are small but meaningful to some, and include: Improved tax efficiency for taxable investors by placing each fund in its best location Direct control over allocation percentages Independence from Vanguard's small course changes in the Target Retirement funds (as when they increased stock allocation in 2006, and changed domestic-to-international ratio in 2010, and added international bonds in 2013) Availability of slightly-lower-cost Admiral shares in the individual funds, but not the Target Retirement or LifeStrategy funds Lazy portfolios Lazy portfolios are specific portfolio suggestions, designed to perform well in most market conditions. Vanguard funds From Vanguard's list of "core funds," the funds that are best for a three-fund portfolio are: Vanguard Total Stock Market Index Fund (VTSAX) Vanguard Total International Stock Index Fund (VTIAX) Vanguard Total Bond Market Fund (VBTLX) So, a "three-fund portfolio" might consist of 42% Total Stock Market Index, 18% Total International Stock Index, and 40% Total Bond Market fund. He stated that "It is no longer necessary to own large portfolios. Most contain a small number of low-cost funds that are easy to rebalance. Vanguard's tool As of 2020, Vanguard provides a tool that recommends a balanced portfolio similar to the kind discussed here (Vanguard recommends a four fund portfolio), with percentages based on your responses to a short online questionnaire. Historic notes Scott Burns wrote a 1991 article, "Exactly How To Be A Couch Potato Portfolio Manager". In a 401(k) plan with limited choices one might very well opt for an S&P 500 index fund to serve as the domestic stock component of a three-fund portfolio. Such a two-fund portfolio would use these funds: Vanguard Total World Stock Index Fund (VTWSX) for both domestic and international stocks Vanguard Total Bond Market Index Fund (VBTLX) Combining stocks and bonds The Vanguard Balanced Index Fund holds 60% Total Stock Market Index Fund and 40% Total Bond Market Index Fund. Instead of going through the step of deciding on your own asset allocation, you accept the suggestion that, say, 2/3 stocks to 1/3 bonds and half-and-half domestic and international is a good enough, one-size-fits-all allocation. Using Vanguard's "risk potential" categories, that means they are recommending replacing a holding in risk potential category 2 with a mix of holdings in categories 3 and 4. In 2013, Vanguard altered the composition of its Target Retirement funds; from 2010 to 2013, most of them were literally three-fund portfolios as described here. This groundbreaking guide in the Boglehead series offers the most straightforward system for developing an indexed portfolio that will outperform actively-managed ones over time. In fact, there's a lot of data and analysis showing the most profitable portfolios are the simplest. He's substantially grown his own portfolio and shown many others how to do the same based on Bogle's philosophy, and in The Bogleheads' Guide to the Three-Fund Portfolio, he shares the blueprint to his personal approach to index investing approved by Jack himself. The second decision is what percentage of your stock allocation should be U.S. (domestic) and what should be international. Investing doesn't need to be complicated. Powerful. In 2010, Vanguard increased the international allocation of its Target Retirement and LifeStrategy funds from 20% of the stock allocation to 30%, and increased it again to 40% in 2015. In Barclay's words, this index tracks the "investment grade, US dollar-denominated, fixed-rate taxable bond market." The "bond market" is a somewhat diffuse concept. † The original fixed income option at TIAA was the TIAA Traditional account. With these three holdings the answer on diversification is a resounding 'YES'.^[6] In a 2015 article, "The only funds you need in your portfolio now", Walter Updegreave commented: "Of course, some advisers will suggest that you're missing out unless you spend your money among all manner of exotic investments (which they're more than happy to sell you). Over 10,000 world-wide securities. One traditional rough rule-of-thumb is "age in bonds," or percentage of stocks = 100 - age. Here are some suggestions on how to do it with other funds. Now that total stock market funds exist and have expenses just as low as S&P 500 funds, total stock market funds are preferable. Should the three-fund portfolio be modified? Adequacy of a three-fund portfolio One Marketwatch article^[5] quotes various non-Boglehead commentators as saying such things as "You can make it really simple, be well-diversified, and do better than two-thirds of investors" and "That three-pronged approach is going to beat the vast majority of the individual stock and bond portfolios that most people have at brokerage firms... Bernstein, bestselling author of The Investor's Manifesto: Preparing for Prosperity, Armageddon, and Everything in BetweenDiscover How Focused Investing Can Lead to Tremendous Financial GrowthThe Bogleheads' Guide to the Three-Fund Portfolio shows you how to get better returns than the majority of professional advisors with just three index funds and a buy-and-hold strategy. Taylor Larimore's " Lazy Portfolio" in fact, consists of these three funds based on the investor's desired asset allocation. For example, because different assets grow at different rates, any investor who chooses a do-it-yourself approach needs to "rebalance" occasionally — perhaps annually — in order to maintain the desired percentage mix. † The Northern Fund's three-fund portfolio can be expanded for greater US diversification by adding the Mid Cap Index (NOMIX) and Small Cap Index (NSIDX) to the Stock Index (S&P 500). But investing according to the Boglehead philosophy certainly does not require you to invest at Vanguard or use Vanguard products. Nothing Vanguard has published would lead one to believe that this is a big change or that it will have a big effect.

A pair of headphones

A pair of headphones