Wilshire Funds Management

October 6, 2008

Memo to the Wary Investor:

History Shows The Value Of Staying Committed

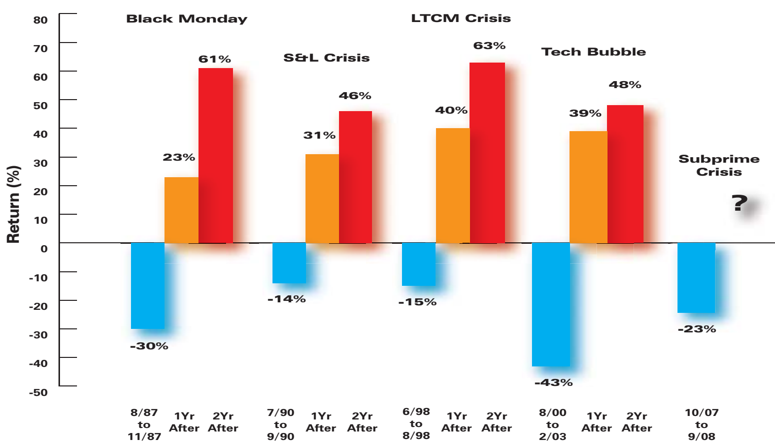
September 2008 will undoubtedly go down as one of the most volatile and challenging months for investors in market history. The deterioration of the U.S. banking and credit environment plunged global markets into crisis, taking as victims iconic institutions that many assumed could never fail. From the government takeovers of Fannie Mae and Freddie Mac, to the transformation of investment banks Goldman Sachs and Morgan Stanley into bank holding companies, and the controversy surrounding the government's original $700 billion bailout plan, investor confidence continues to be eroded by a steady stream of market-altering news.

Wilshire Funds Management's response to these events, as well as the response of the investment advisory community at large, has been for investors to "stay the course." While recent events have not changed the fundamentals of asset allocation and diversification, we are aware that some investors are considering temporarily moving their investments to cash, or getting out of the market all together. These investors argue that volatility is too high and markets are too uncertain, and although their positions are understandable, history has shown that abandoning a long-term investment strategy in a time of crisis can be costly.

Exhibit 1

Market Rebounds Can Be A Source Of Significant Return

S&P 500



Source: Wilshire Compass.

Our goal in this note is to help investors gain perspective on the current market crisis against a backdrop of major financial crises of the past. Whenever a major market dislocation occurs there are always some who decry "Armageddon" and the string of major market dislocations this September readily lend themselves to those inclined to doomsday scenarios. While the effects of the recent crisis have been profound, the fact that the market has always recovered after periods of stress remains unchanged. From acute market shocks like 9/11, to more systemic market collapses such as the S&L crisis and the tech bubble, the market has always rebounded to levels higher than they were pre-crisis, as seen in Exhibit 1.

When thinking about one's investment portfolio, the importance of taking a long-term perspective is paramount. Regardless of whether we find ourselves in a bull or bear market at a given moment, it is critical to remember that, over time, U.S. markets have been up more than they have been down, as is illustrated in Exhibit 2.

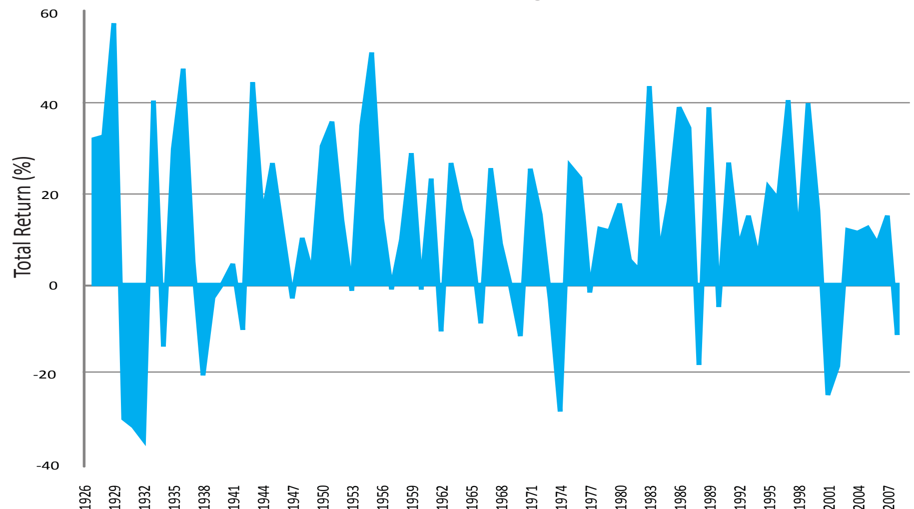
The current crisis has punished equities across the board, both in the U.S. and abroad. Although the recent returns of even historically low-correlated asset classes appear tightly interwoven, our conviction in the long-term benefits of diversification remains unchanged. Though the short-term volatility we have witnessed this September is testing for even the most experienced investors, it is precisely times like these, when investors must adhere to time-tested asset allocation strategies.

Exhibit 2

Markets Go Up More Than They Go Down

S&P 500 Annual Return

December 31, 1925 to August 31, 2008



Source: Wilshire Compass

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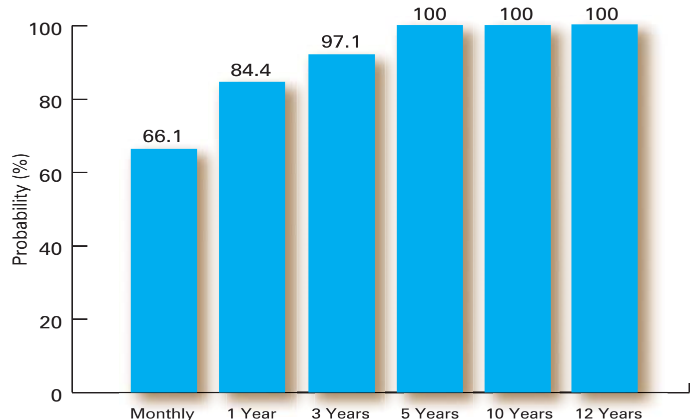
Exhibit 3 shows the percentage of time that a balanced portfolio (as measured by a hypothetical 60/40 percent mix of the S&P 500 Index and the Lehman U.S. Aggregate Index) had positive returns over various time periods. By staying invested in a balanced portfolio for at least five years, the historical frequency of positive results is 100 percent -- even at a three year horizon, the frequency of a positive outcome have been over 90 percent.

Although the urge to cash out of investments when the market is down is tempting, the possibility of missing the market's eventual rebound may prove detrimental to an investor's long-term goals. Now more than ever, it is important to remind ourselves that timing the market can be a very difficult and potentially costly endeavor. For example, an investor who stayed invested in the S&P 500 over a ten year period ending December 31st, 2007 would have seen an initial investment of $1,000 grow to $1,777. However, missing just the best 3 month period during the 10 years would have cost the investor $321. It is also noteworthy that the best consecutive 3, 6 and 12 month periods happened to follow the Asian financial crisis of 1998.

Exhibit 3

Probability of Positive Returns over Different Time Periods

April 30, 1990 to June 30, 2008

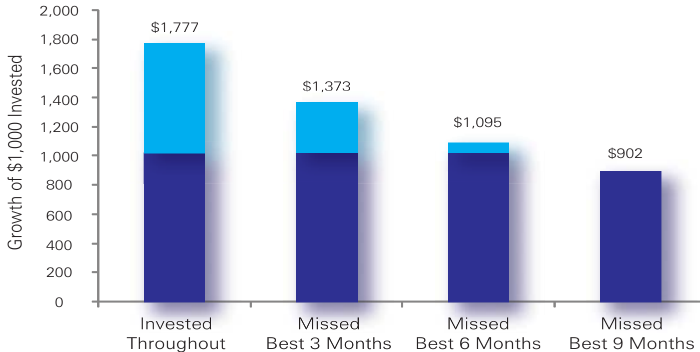


Source: Wilshire Compass
Balanced 60/40 Portfolio: 60% S&P 500, 40% Lehman U.S. Aggregate Bond

Exhibit 4

It Pays to Stay Invested

S&P 500 (Ten Years Ending December 31, 2007)

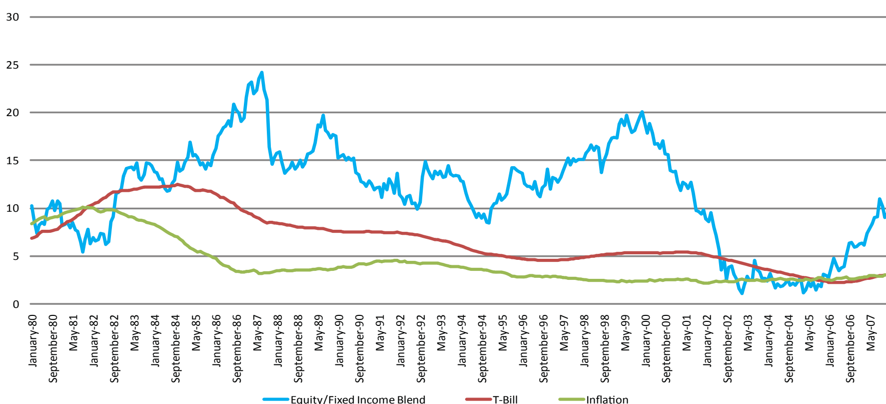


Source: Wilshire Compass

History has rewarded investors committed to a long-term strategy who exhibit discipline and steadfastness, even in the face of turmoil. Reactionary responses, like moving investments to cash, for example, have proven to negatively impact long-term performance, as shown in Exhibit 4.

Exhibit 5

5 Year Rolling Return



Source: Wilshire Compass
Balanced 60/40 Portfolio: 60% S&P 500, 40% Lehman Aggregate Bond

While the importance for investors to stay the course during down-market environments is well-documented, we must rely on professional investment managers to constantly monitor their portfolios and diligently manage their risk exposure. Wilshire Funds Management has been and will continue to be in frequent communication with our clients' investment managers. Our mandate is to understand their perspectives on the market, how they are positioning their portfolios to manage risk, and how they are taking advantage of attractive opportunities.

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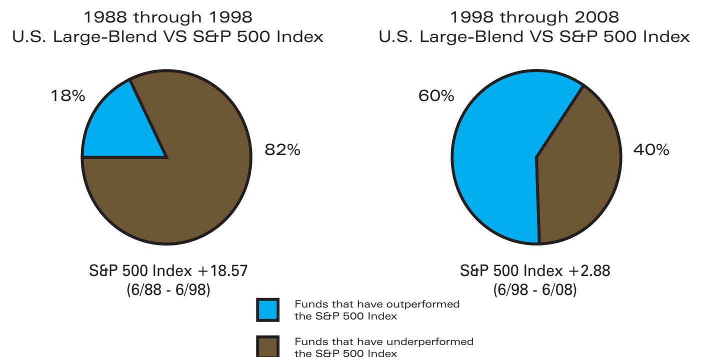
Most notably, we have seen active managers add the most value in low-return market environments. As Exhibit 6 illustrates, 60 percent of actively managed large-blend funds were able to beat the S&P 500 from July 1998 through June 2008, far exceeding the 18 percent of funds that outperformed in the preceding 10-year period. This comparison underscores the fundamental value proposition of active management combined with disciplined asset allocation- namely, that even in inhospitable market conditions, skilled active managers are able to potentially beat the broad market while managing risk.

Current market conditions are unprecedented, causing legitimate concern in even the most seasoned investors. In spite of how difficult it can be to keep an historical perspective in mind when looking at one's investments today, this is exactly what Wilshire Funds Management recommends. From the Great Depression, to the S & L crisis and 9/11, the market has proven its resiliency, compensating the long-term investor in turn. We understand that pulling out of the market during times of heightened volatility may seem like a good solution in the heat of the moment. However, history has shown us that staying invested through crises pays off in the long-term, rewarding investors for their fortitude when the market invariably turns around.

Exhibit 6



Source: Morningstar. Large-blend funds represented by Morningstar Large Blend category, excluding index funds.

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