Building a strong foundation

A framework for diversification

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A critical step toward reaching your financial goals is to define well-diversified strategic allocations, which create the starting point for a well-designed investment portfolio. This helps keep your investments aligned with your risk and return objectives. Our strategic asset allocation guidance can assist you through this process. This guidance can help ensure your portfolio is appropriately diversified across a variety of asset classes according to your comfort with risk and financial goals, providing a strong foundation.

The most important factor

While many investors focus on the specific investments in their portfolio, the most important measure of how a portfolio's performance may vary over time is its asset allocation.* Whether constructing a portfolio for the first time or reviewing it to determine whether adjustments are needed, you'll want to make sure the end result fits your comfort level with risk and long-term financial goals. While it may be tempting to focus on the top-performing asset class, we encourage you to consider the following:

Asset classes behave differently over time.

The prices of different asset classes don't move in unison because they tend to react differently to market and economic events, outperforming and underperforming at different times. Since stock and bond prices can often move in opposite directions — meaning they aren't perfectly correlated — combining them may help reduce the volatility of your portfolio overall.

Asset class leadership rotates.

When different asset classes outperform and underperform at different times, you may be tempted to move your money into the best-performing asset class each year.

However, the leading asset class one year can become the worst performer the next year. If you build a portfolio invested in only one asset class, you have to be comfortable with both of these outcomes.

*Source: "Determinants of Portfolio Performance II: An Update," Gary P. Brinson, Brian D. Singer and Gilbert L. Beebower, *Financial Analysts Journal,* 1991.

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Performance by design

A well-diversified portfolio of asset classes won't outperform the top asset class of any one year, but it also won't underperform the lowest — and that is by design. The goal of asset allocation is to focus on achieving solid long-term performance and to balance return potential with the risk you're taking. We believe a portfolio spread across different asset classes can help reduce drastic swings in the value of your portfolio, putting you in a better position to achieve your long-term goals.

As you discuss your financial goals and comfort level with risk with your financial advisor, our long-term strategic asset allocation guidance can help you determine the mix of asset classes to use to align your portfolio with your goal. Our strategic asset allocation guidance represents our view of balanced diversification across a set of recommended asset classes based on our global outlook for the economy and markets over the next 30 years. The exact weightings of each asset class depend on the broad allocation to equity and fixed-income investments that most closely aligns with your financial goals and comfort with risk.

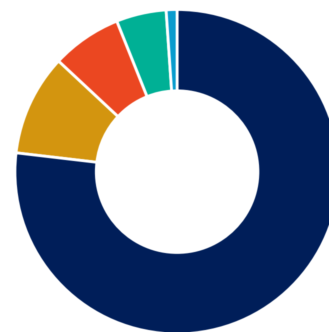
Keep in mind, however, the importance of diversification goes beyond asset allocation. We also recommend spreading your investments across a variety of sectors and securities within each asset class. Owning too much of a single sector, stock or bond increases your portfolio's sensitivity to the specific risks of that investment, increasing the chances of unexpected results.

Strategic asset allocation guidance

Equity diversification

- U.S. large-cap stocks
- International large-cap stocks
- U.S. mid-cap stocks
- U.S. small-cap stocks
- International small- and mid-cap stocks
- Emerging-market equity

Fixed-income diversification



- U.S. investment-grade bonds
- U.S. high-yield bonds
- International bonds
- Emerging-market debt
- Cash

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Best performance ↑ / Worst performance ↓

2014	2015	2016	2017	2018
U.S. large-cap stocks 13.7%	Int'l small- and mid-cap stocks 6.6%	U.S. small-cap stocks 21.3%	Emerging-market equity 37.3%	Int'l bonds 3.2%
U.S. mid-cap stocks 13.2%	U.S. large-cap stocks 1.4%	High-yield bonds 17.1%	Int'l small- and mid-cap stocks 30.8%	Cash 1.9%
50% stocks/ 50% bonds 9.8%	Int'l bonds 1.4%	U.S. mid-cap stocks 13.8%	Developed int'l large-cap stocks 25.1%	U.S. investment-grade bonds 0%
Int'l bonds 8.8%	Emerging-market debt 1.3%	U.S. large-cap stocks 11.9%	U.S. large-cap stocks 21.8%	High-yield bonds -2.1%
U.S. investment-grade bonds 6%	50% stocks/50% bonds 1%	Commodities 11.7%	U.S. mid-cap stocks 18.5%	50% stocks/50% bonds -2.2%
U.S. small-cap stocks 4.9%	U.S. investment-grade bonds 0.6%	Emerging-market equity 11.2%	U.S. small-cap stocks 14.7%	Emerging-market debt -2.5%
Emerging-market debt 4.8%	Cash 0.1%	Emerging-market debt 9.9%	50% stocks/50% bonds 12.7%	U.S. large-cap stocks -4.4%
High-yield bonds 2.5%	Developed int'l large-cap stocks -0.8%	50% stocks/50% bonds 7.3%	Emerging-market debt 8.2%	U.S. mid-cap stocks -9.1%
Cash 0.1%	U.S. mid-cap stocks -2.4%	Int'l bonds 4.9%	High-yield bonds 7.5%	U.S. small-cap stocks -11%
Emerging-market equity -2.2%	U.S. small-cap stocks -4.4%	U.S. investment-grade bonds 2.6%	U.S. investment-grade bonds 3.5%	Commodities -11.3%
Int'l small- and mid-cap stocks -3.3%	High-yield bonds -4.4%	Int'l small- and mid-cap stocks 1.3%	Int'l bonds 2.5%	Developed int'l large-cap stocks -13.8%
Developed int'l large-cap stocks -4.9%	Emerging-market equity -14.9%	Developed int'l large-cap stocks 1%	Commodities 1.7%	Emerging-market equity -14.6%
Commodities -17%	Commodities -24.7%	Cash 0.3%	Cash 0.9%	Int'l small- and mid-cap stocks -17%

- International bonds represented by the Bloomberg Global Agg Ex U.S. TR Hgd USD Index.
- U.S. investment-grade bonds represented by the Bloomberg U.S. Aggregate TR USD Bond Index.
- High-yield bonds represented by the Bloomberg U.S. HY 2% Issuer Cap TR USD Index.
- Cash represented by the Bloomberg U.S. Treasury Bellwethers 3Mon TR USD Index.
- Commodities represented by the Bloomberg commodities index.
- Emerging-market equity represented by the MSCI EM NR USD Index.
- U.S. small-cap stocks represented by the Russell 2000 TR USD Index.
- U.S. mid-cap stocks represented by the Russell Mid-cap TR USD Index.
- U.S. large-cap stocks represented by the S&P 500 TR USD Index.
- International small- and mid-cap stocks represented by the MSCI EAFE SMID Cap NR USD Index.
- International large-cap stocks represented by the MSCI EAFE NR USD Index.
- Emerging-market debt represented by the Bloomberg Emerging Market USD Agg TR USD Index.
- 50% stocks/50% bonds represented by the average of the S&P 500 TR Index and the Bloomberg U.S. Aggregate Bond Index. For illustrative purposes only, not a portfolio available for investment.

Source: Morningstar Direct, S&P, Bloomberg, FTSE, Russell, MSCI. Past performance does not guarantee future results. An index is unmanaged, is not available for direct investment and does not depict an actual investment. Performance does not include payment of any expenses, fees or sales charges, which would lower the performance results. Returns include reinvestment of dividends and interest. All investments carry a certain degree of risk, with various factors impacting performance. Investing in equities involves risks. The value of your shares will fluctuate and you may lose principal. Investing in bonds involves risks, including credit risk and market risk. Bond investments are also subject to interest rate risk such that when interest rates rise, the prices of bonds can decrease, and the investor can lose principal value if the investment is sold prior to maturity. Equity securities are generally more volatile than bond investments and subject to greater risks. The prices of small-cap stocks are generally more volatile than those of large-company stocks, and commodities can be even more volatile. There are special risks inherent in international investing, including currency fluctuations and political, social and economic risks.

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	2019	2020	2021	2022	2023
Best performance	U.S. large-cap stocks 31.5%	U.S. small-cap stocks 19.9%	U.S. large-cap stocks 28.7%	Commodities 16.1%	U.S. large-cap stocks 26.3%
	U.S. mid-cap stocks 30.6%	U.S. large-cap stocks 18.4%	Commodities 27.1%	Cash 1.5%	Developed int'l large-cap stocks 18.3%
	U.S. small-cap stocks 25.5%	Emerging-market equity 18.3%	U.S. mid-cap stocks 22.6%	Int'l bonds -9.8%	U.S. mid-cap stocks 17.2%
	Int'l small- and mid-cap stocks 24.9%	U.S. mid-cap stocks 17.1%	U.S. small-cap stocks 14.8%	High-yield bonds -11.2%	U.S. small-cap stocks 16.9%
	Developed int'l large-cap stocks 22%	50% stocks/50% bonds 12.9%	50% stocks/50% bonds 13.6%	U.S. investment-grade bonds -13%	50% stocks/50% bonds 15.9%
	50% stocks/50% bonds 20.1%	Int'l small- and mid-cap stocks 11.3%	Developed int'l large-cap stocks 11.3%	Developed int'l large-cap stocks -14.5%	Int'l small- and mid-cap stocks 15.1%
	Emerging-market equity 18.4%	Developed int'l large-cap stocks 7.8%	Int'l small- and mid-cap stocks 8.8%	Emerging-market debt -15.3%	High-yield bonds 13.5%
	High-yield bonds 14.3%	U.S. investment-grade bonds 7.5%	High-yield bonds 5.3%	50% stocks/50% bonds -15.6%	Emerging-market equity 9.8%
	Emerging-market debt 13.1%	High-yield bonds 7%	Cash 0%	U.S. mid-cap stocks -17.3%	Emerging-market debt 9.1%
	U.S. investment-grade bonds 8.7%	Emerging-market debt 6.5%	Int'l bonds -1.4%	U.S. large-cap stocks -18.1%	Int'l bonds 8.3%
	Commodities 7.7%	Int'l bonds 3.9%	U.S. investment-grade bonds -1.5%	Emerging-market equity -20.1%	U.S. investment-grade bonds 5.5%
	Int'l bonds 7.6%	Cash 0.7%	Emerging-market debt -1.7%	U.S. small-cap stocks -20.4%	Cash 5.2%
Worst performance	Cash 2.3%	Commodities -3.1%	Emerging-market equity -2.5%	Int'l small- and mid-cap stocks -20.8%	Commodities -7.9%

- International bonds represented by the Bloomberg Global Agg Ex U.S. TR Hgd USD Index.
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Source: Morningstar Direct, S&P, Bloomberg, FTSE, Russell, MSCI. Past performance does not guarantee future results. An index is unmanaged, is not available for direct investment and does not depict an actual investment. Performance does not include payment of any expenses, fees or sales charges, which would lower the performance results. Returns include reinvestment of dividends and interest. All investments carry a certain degree of risk, with various factors impacting performance. Investing in equities involves risks. The value of your shares will fluctuate and you may lose principal. Investing in bonds involves risks, including credit risk and market risk. Bond investments are also subject to interest rate risk such that when interest rates rise, the prices of bonds can decrease, and the investor can lose principal value if the investment is sold prior to maturity. Equity securities are generally more volatile than bond investments and subject to greater risks. The prices of small-cap stocks are generally more volatile than those of large-company stocks, and commodities can be even more volatile. There are special risks inherent in international investing, including currency fluctuations and political, social and economic risks.

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Asset allocation benefits — focusing on risk and return

Because asset classes perform differently over time, and leadership rotates, asset allocation can provide the following benefits compared to investing in just a few asset classes:

Reduces risk and volatility

Asset allocation can't eliminate risk, but it can help reduce it. Asset classes considered risky by themselves, such as small-cap stocks and emerging-market equity, can reduce portfolio volatility if they are part of a broadly allocated portfolio.

How is this possible? Refer again to the table. If different asset classes are outperforming or underperforming at different times, it is likely that while one part of your portfolio is down, another is up, helping reduce the volatility of your portfolio.

Competitive returns, lower volatility

Over the long term, an all-stock portfolio likely will outperform a blended portfolio, but it also will have much higher risk. That's because risk and return go hand in hand. In general, the less risk you take, the lower your potential returns and vice versa. But proper asset allocation can reduce risk as well as provide return benefits.

For example, you'd expect an all-stock portfolio to have much higher returns than a portfolio with an allocation to stocks and bonds. However, stocks and bonds tend to behave differently over time, with bonds often rising when stocks drop. Therefore, a stock and bond portfolio could achieve competitive returns in relation to an all-stock portfolio over the long term but with much less volatility. And even though asset allocation can't eliminate declines, it can help reduce the magnitude of these declines. This could help keep your emotions under control when the markets hit a rough patch.

Ultimately, by owning the right mix and a variety of asset classes, your portfolio is likely to experience less volatility and show more consistent performance over time compared to a more narrowly focused portfolio.

What really matters — aligning your asset allocation with your goals

The best asset allocation is one that is designed to help you reach your financial goals. Your portfolio's asset allocation should provide the returns necessary to help reach your goals while also aligning with your comfort with risk.

We've developed several portfolio objectives that incorporate our strategic asset allocation guidance. Each is designed with the optimal mix of asset classes for a given level of risk. As you discuss your goals and risk tolerance with your Edward Jones financial advisor, you can decide which is appropriate for you. Constructing your portfolio with the right combination of asset classes — and making periodic adjustments to help ensure it remains aligned — can help it be better positioned to weather potential issues along the way, helping you reach your long-term financial goals.

Diversification and asset allocation do not guarantee a profit or protect against loss in a declining market. Investors should understand the risks involved in owning investments, including interest rate risk, credit risk and market risk. The value of investments fluctuates, and investors can lose some or all of their principal.

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