Investing is boring:

If you want excitement, go to Vegas

Jonathan Chevreau, Financial Post · Jun. 29, 2011

Successful investing should be boring, which may explain why so many excitement-seeking investors suffer disappointing returns.

If you want excitement, go to Las Vegas.

If you want to be a rich crashing bore, read a little book self-published by Edmonton-based wealth counsellor Marshall McAlister. It's titled The Brilliance of Boring Investing: An Academic Approach to Portfolio Design.

It begins with a quote from Nobel laureate Paul Samuelson: "Investing should be dull. It shouldn't be exciting." But there's a paradox, writes McAlister: The portfolio process that requires less work from investors can actually deliver the best long-term investment returns.

Boring doesn't mean lazy, he hastens to add. It requires discipline and a process, which is the true value of what financial advisors provide. The kind of advisors I often meet at conferences sponsored by index fund maker DFA Canada, which is where I met McAlister last week.

The featured speaker at the Toronto event was prolific U.S. author and money manager Larry Swedroe, who views investing very much like McAlister and DFA. St. Louis-based Buckingham Asset Management (BAM) is one of DFA's largest clients.

Swedroe's talk focused on his recently published The Quest for Alpha: The Holy Grail of Investing. "Alpha" refers to the goal of "adding value" by security selection, relative to "beta" or market returns delivered by index funds or ETFs.

I'm surprised he didn't title it The Futile Quest for Alpha since that's the book's main thrust. Like McAlister, he believes timing the market is impossible, forecasts are for the gullible, and stock-picking is a mug's game.

Both advocate the "boring" route of low-cost "asset class" investing, which means creating portfolios built on lowcost index mutual funds (like DFA's, tilted in favour of value and small-cap stocks) or enhanced or fundamental-indexbased exchange-traded funds.

Swedroe says there are two main theories about markets: the conventional wisdom that they are inefficient so can be "beaten" versus modern portfolio theory's belief that markets are efficient and stocks priced roughly where they should be.

If markets are inefficient, the winning strategy would be to identify past "persistent alpha" and select managers with proven ability to add value through market timing and security selection.

Swedroe demolishes that school by reviewing the poor track records of actively managed mutual funds and venture-capital managers. Hedge funds are worse, he says, because they are illiquid, taxinefficient, lack transparency and offer no persistent outper-formance beyond what might be randomly expected. The result is risk-adjusted returns similar to treasury bills.

But his most telling argument involves pension plans. If anything could beat the market, it should be them, since they pay lower fees than retail investors, use the world's top managers and hire gatekeepers to monitor and replace managers if performance lags.

Sadly, all their activity has been for naught: They'd be better off imitating Rip Van Winkle and doing nothing. Swedroe concludes markets are indeed efficient, so efforts to "beat" it are futile after fees, trading costs and tax drag.

Therefore, the winning strategy is the "boring" one of focusing on low-cost fund construction and tax-efficiency, tuning out the noise and sticking to a long-term plan.

Not everyone believes alpha fails to add value. "It is difficult for most investors, amateur or professional, to consistently produce alpha," concedes Bob Cable, director of ScotiaMcLeod's The Cable Group. But while difficult, it's not impossible. One way is to take advantage of seasonal patterns (such as "sell in May and go away"), a strategy Cable says is particularly pronounced in the Canadian market.

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