



# E Q U I T I E S

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## Why Not 100% Equities

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In a 1994 article “College and University Endowment Funds: Why Not 100% Equities?” Richard H. Thaler and J. Peter Williamson presented strong evidence documenting the historical superiority of investing in 100% equities compared with a more common investment policy of 60% equities and 40% bonds (60/40).

However, their recommendation that endowments invest in 100% equities actually mixes two distinctly different ideas: 1) endowments should take more risk than 60/40, and 2) they should take this added risk by investing 100% in equities.

Whether a long-term investor should take more risk is a fascinating and sometimes contentious subject that I do not address. Instead, this article focuses on whether 100% equities is the best way to gain more exposure to risk. The answer, generally, is that it is not, because a portfolio of 100% equities ignores the benefits of diversification.

Investors willing to bear the risk of 100% equities may do even better with a diversified portfolio, particularly when they are willing to lever. A diversified portfolio historically delivers more return, while not increasing risk (measuring risk along several different dimensions).

Regardless of which portfolio is chosen, this article argues that deciding how much risk to bear, and building a set of portfolios with the most expected return for a given amount of risk, are separate tasks. Choosing a portfolio of 100% equities based on their historical realized return misses this separation.

A long-term investment in 60/40 may, or may not, take enough risk. An investment in 100% equities almost guarantees an inefficient portfolio.

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