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Investment objectives vary among individuals, but the general idea in every case is to earn some sort of positive return on one's money. Except for those focused solely on income, the hope and expectation is that at some point in the future we will have more than we originally invested. Investing is based on the premise of delayed gratification in exchange for a larger future reward. But what determines our future reward?

There are three things that determine how much wealth one accumulates: the amount one invests, how long it is invested, and the rate of return. That's it. It can always be boiled down to those three variables.

What is so interesting about these three variables is that we have direct control over two of them – the amount we invest and how long it is invested – yet as humans we tend to focus most on the one variable we *can't* control – the rate of return. (Clarification: throughout this commentary, "we" refers to humans in general rather than Oak Funds.) We spend all sorts of time trying to figure out if the market is going to go up or down, shifting our investments among asset classes, and trying to identify the next hot stock. For the vast majority of people these efforts are counterproductive, as we tend to be drawn to investments at their peak and repelled at the bottom. Through a disciplined investment strategy, building wealth is surprisingly attainable, given the simple but effective concept of compounding.

We have established that future wealth is a function of three variables: amount, time, and return. We know we have control over the first two and can vary those based on our individual circumstances. But we still need to come up with an assumption for a rate of return before we can begin crunching numbers. Over the last 100 years or so the US stock market has returned roughly 10% per year. Based on this very long-term track record one could argue that 10% is a reasonable expectation for the future. On the other hand, one could argue that returns will be significantly lower in the future given the already-favorable starting point of low interest rates and high corporate profit margins. So, what return can we expect in the future? There is no correct answer, and while many people may have an opinion, nobody truly knows. Let's be conservative and use 7%, well below the historic average. If you'd like to use a different number, or change any of the inputs, you can make the adjustments using the calculator online at calculator.net. Now let's take a look at some examples. *Please note that examples 1 – 4 are hypothetical in nature.*

Example 1

Initial investment: \$10,000	Monthly investment: \$300
Time: 30 years	Total amount invested: \$118,000
Assumed annual return: 7%	Future value: \$429,000

In Example 1, we invest \$10,000 upfront and \$300 every month for thirty years, which equates to a total amount invested over the period of \$118,000. Over the period, assuming a 7% return, this grows to \$429,000, or about 3.6 times the amount we invested, even though the bulk of that investment was made along the way and not upfront. This illustrates the power of compounding. Now let's change some of the variables (in bold).

Example 2

Initial investment: \$20,000	Monthly investment: \$400
Time: 30 years	Total amount invested: \$164,000
Assumed annual return: 7%	Future value: \$623,000

In Example 2 we increase our initial investment from \$10,000 to \$20,000 and our monthly investment from \$300 to \$400. By doing this, we increase our future value, the amount we will have at the end of 30 years, from \$429,000 to \$623,000, or about 45%. This final sum is about 3.8 times what we invested.

Example 3

Initial investment: \$20,000	Monthly investment: \$400
Time: 40 years	Total amount invested: \$212,000
Assumed annual return: 7%	Future value: \$1,294,000

In Example 3 we increase the time period from 30 to 40 years but make no other changes. As you can see, adding those extra ten years has a massive impact on the size of our future nest egg, taking it from \$623,000 in year 30 to \$1,294,000 in year 40 – more than doubling it. Note too the effect on the ratio of how much we reap versus how much we invested. The \$1,294,000 exceeds the amount invested by over 6 times.

If we could add *another* ten years to Example 3, making our time horizon 50 years, we would again more than double the future value, taking it to \$2,677,000. In fact, for a 7% annual return, a rule of thumb is that an investment doubles in value every ten years. The effect of adding ten years is even greater if the average rate of return exceeds 7%.

When we “add ten years”, we tend to think of adding it to the end of the horizon. But it makes just as much sense to add it to the *beginning*. In other words, if we start investing ten years earlier, we double the amount that we have at the end of the period. While it is impossible to go back in time, in a way we can do this with our children/grandchildren by getting them started at an early age. Say your child/grandchild is going to start investing at age 25 when she is working and that, for simplicity, we estimate the value of her portfolio to be \$1,000,000 when she reaches 60 years of age. If instead, with a little help from her parents or grandparents, she started investing at age 15, the expected value of the portfolio at age 60 would be \$2,000,000! So, adding that ten extra years at the *beginning* has a huge impact on the value of the portfolio at the end of the horizon.

It is numbers like these that supposedly led Albert Einstein to call compounding “the most powerful force in the universe” and “the greatest invention in human history.” The numbers increase slowly at first, but then explode, which is why allowing time to work its magic is critical to investing.

So, the “secret” to building wealth is simple: time. Increasing the investment period dramatically increases the value at the end of the period. And time is something we can control, since we are the ones who decide when to start investing and when to stop. So often we become emotional or overthink things, which leads to poor decisions or failure to implement a sensible investment plan. Perhaps the most under-utilized investment strategy is the systematic investment plan, which entails automatically investing the same amount every month. This helps take the emotion out of investing by putting it on autopilot; for example, on the same day of every month the same amount is transferred from a savings account to a mutual fund. But many are turned off by this strategy because it makes us feel like we are relinquishing control, and if there is one thing we want to be able to control it is our money. The irony is that those who want to “maintain control” are almost always worse off in the long run than those who just stick with an automatic investment plan.

We at Oak always say that the most important decision is to be in the market, as opposed to what sectors or stocks to own. We also like to point out that hospital wings are never endowed by market timers; if they aren’t funded by longtime business owners they tend to be so by individuals who have held stocks in some form for a long period of time. It should be no surprise then that one of the tenets of Oak’s investment philosophy is to stay fully invested.

On to some hypothetical Q&A...

Q: I don’t have \$10,000 sitting around to invest, nor can I afford \$300 or \$400 a month, so is this even worth the effort?

A: Even if you start with zero and invest just \$100 per month, by year 40 you would have \$249,000. (See below.)

Example 4

Initial investment: \$0	Monthly investment: \$100
Time: 40 years	Total amount invested: \$48,000
Assumed annual return: 7%	Future value: \$249,000

The effect of time on a portfolio is almost magical. But it isn't magic; it's just math. Given the realities of these numbers, it begs the question why more people don't engage in such a plan. There are probably a lot of answers to that question.

- People just aren't aware of the effect of compounding.
- Inertia and procrastination. "One more day isn't really going to make a difference, so I'll just do it tomorrow." Before you know it, days turn into years, and no plan has been implemented.
- Bad economic news. "I don't like what is going on with the economy/Washington/Europe, etc. I'll just wait until things settle down." There are two problems with this. First, there are *always* issues to be concerned about, so this game can end up delaying a plan for years. Second, it is often the case that when conditions feel the worst, it is the best time to buy stocks because the bad news is priced in.
- As mentioned earlier, people like to have control over their money, and putting our investing on autopilot just doesn't jibe with those feelings.
- Humans value certainty, and in the stock market there are no guarantees about future returns. So it feels like we are making a blind leap of faith to commit our hard-earned money to something that might or might not work out. Not surprisingly, when viewed this way, many choose to sit on the sidelines. The problem with that thinking though is that it completely ignores history. For nearly 200 years investors in US large cap stocks have fared quite well. According to Barry Bannister, an Equity Investment Strategist at Stifel Nicolaus, from 1835-1919, returns averaged 7.6% (but an inflation-adjusted, or real, return of 7.2%, which is excellent), and from 1920-2012, returns averaged 10.1%, (6.6% real). While there were certainly ups and downs during those times, incredibly, there were essentially only two ten-year periods, for those 185 years, in which returns were negative: the Great Depression and the financial crisis five years ago. (I say "essentially" because the ten years ending 2008 and the ten years ending 2009 technically count as two such incidents.) Remarkably, while the average annual returns for these periods were negative, they were barely so, in the neighborhood of -1% to -2%. In our examples above we used 30 or 40 years as our time horizon. Amazingly, since 1900, the *worst* 35-year period, in terms of average annual return for the Dow Jones Industrial Average, was 6.1% (from observationsandnotes.blogspot.com). So even after all our nation has been through over the past 185 years (Civil War, two world wars, The Great Depression, Vietnam, stagflation (combination of recession and inflation), 9-11, etc.) stocks have always generated positive returns over long periods.

Q: If we just invest all our extra cash, keeping it tied up in the market, and we don't get to enjoy it, what is the point?

A: Good point. There is no sense in building your wealth to obscene levels and not enjoying it or using it to benefit others. There is a balance to be struck, based on each individual's circumstances. But whether your budget allows a monthly investment of \$50 or \$5,000, the key is getting started as early as you can and sticking to it, because the resulting financial security will not only open up different opportunities but will also bring financial peace of mind.

Q: It appears that it's really important to invest as much as I can up front, and I have a large chunk of cash just sitting in my bank account not earning anything. But I'm afraid that if I put it all into the market, there could be a correction and I could lose 15% right off the bat.

A: In order to mitigate the effects of something like this happening, you may want to invest half now and the rest in, say, six months. Of course there could still be a correction in six months, so you can not truly eliminate the risk. Also, the beauty of a systematic investment plan is that it consistently invests, so that over time the effects of these corrections may be minimal. One more way to think about the timing of getting started: The Dow Jones Industrial Average, the most widely followed stock index, is currently about 16,500. If it rises 7% per year on average for the next 40 years it will be 247,000. Given that context, whether we start investing when the Dow is 16,000 or 14,000 does not seem to be very important.

Q: I heard an expert on TV saying that a 25-year bear market is coming.

A: The market has always had its share of pessimists, and while they *sometimes* get it right in the short run, their long-term apocalyptic calls have never come to fruition. A bearish forecast always appeals to people, especially in difficult times, not only because it plays to our fears about uncertainty but also because it just *sounds* intelligent. For whatever reason, the case for a bear market tends to sound more intellectual than the case for a bull market. Of course 185 years of history is on the side of the bulls. So you can side with the bear, who, despite his confidence, like the rest of us does not possess a crystal ball, or you can side with 185 years of history.

Q: You use 7% as the rate of return, but you just said you don't have a crystal ball, so how do you know that is what we will end up earning?

A: I don't. It just seems like a reasonable estimate given history and the prevailing conditions. Stocks might return less than that, or even more than that. But history shows us the longer one is invested, the closer one can expect to get to an attractive rate of return, and the more the portfolio can grow. The key is allowing time to work.

Conclusion

The idea of investing is to have more tomorrow than we do today. There are three determinants of the value of the pot at the end of the rainbow: the amount one invests, how long it is invested, and the rate of return. As humans we tend to focus on the one thing we can't control (return), rather than the two we can (how much we invest and for how long). We can limit the damage our emotions have on our finances by implementing a systematic investment plan. By investing with discipline for a long period of time, one can maximize the chances of (and almost guarantee) achieving financial security. The examples we used sound too good to be true, which illustrates the power of compounding. The great thing is that, because of this compounding, significant wealth is within reach of not just the wealthy, but most Americans. It just comes down to implementing a plan and sticking to it.

Oak's marketing team might take me to task for saying this, but the choice of a fund manager is secondary to the decision/discipline to be in the stock market to begin with. That being said, if you would like to learn more about the benefits of a systematic investment plan, please contact us at www.oakfunds.com or 1-888-462-5386.

Kind regards,



To determine if this fund is an appropriate investment for you, carefully consider the fund's investment objectives, risk factors, charges and expenses before investing. This and other information can be found in the fund's prospectus, which may be obtained by calling 1-888-462-5386 or visiting our website at www.oakfunds.com. Please read it carefully before investing.

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