Nuts and Bolts
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buying high and selling low (Figure 3), with predictably disappointing results. Put differently, most long-term investors *do not stay the course*, thereby failing to reap the long-term benefits of investing in stocks.

Asset Allocation Is the Answer

Clearly, it is the short-term volatility, or risk, present in the market that prevents most investors from staying the course. Therefore, the solution appears to lie in developing a strategy that would help reduce the portfolio risk to the level with which the investor is comfortable. Put differently, for millions of investors who prefer to preserve their capital during market declines, reduce the volatility of their portfolio and actively participate in both the stock and bond markets, the use of asset allocation might well constitute the best strategy.

Almost unheard of several years ago, for investors, asset allocation services are rapidly becoming a standard feature, like dual air bags in new cars. This strategy provides the foundation for constructing a diversified portfolio of stocks, bonds, and money market instruments that optimizes the returns for the level of risk desired by the investor. And since the portfolio's risk is placed into the comfort zone, the investor can be expected to stay the course and participate in the benefits enjoyed by long-term investors.

Who Offers Asset Allocation?

Typically, an advisor measures your comfort level with risk and your investment time horizon, then creates a recipe for how much money should be invested in stocks, bonds, and money market.

Additionally, there are programs you can sign up for when you buy mutual funds and variable annuities. Samples include: Dreyfus Investment Allocation, Fidelity Portfolio Advisory Services, Pershing Peak II, Prudential Investment Allocation Strategy, American Skandia Asset Mix, and VALIC Portfolio Optimizer.

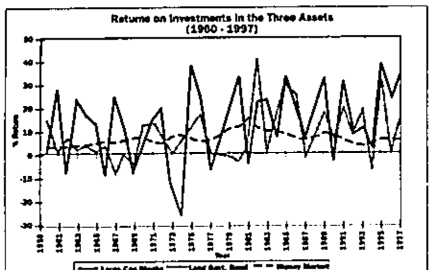

Fig. 2

In addition, many computer programs are now available that can explore the efficient frontier, maximize returns per unit of volatility, and allow you to deal with correlation between asset classes. Samples include: Allocation Master, Cadence Asset Mix Optimizer, Power Analyzer, The Power Center, and RAMCAP.

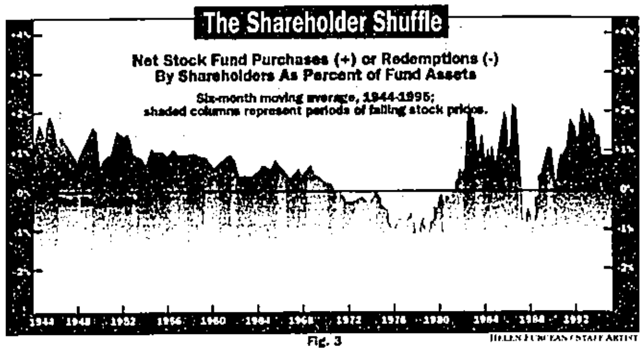

Fig. 3

Are They A Good Deal?

It all depends. While most programs boast that the asset allocation strategies are based on the work of Nobel prize-winning economists like Harry Markowitz and William Sharpe, for the most part you're simply plugged into one of the plethora of cookie-cutter formulas.

In addition, almost all of the software programs are used to develop a static, or at best, a modified static allocation which refers to a fixed percentage of funds allocated to the three asset classes.

For most investors, that's sufficient. It keeps them focused on risk, long-term goals, and the yin-and-yang of stocks and bonds, even if they don't understand any of that. These services can be especially valuable if they keep investors from having no strategy at all, or when they become excited about making market decisions based on something they heard at the watercooler, on the Internet or under the influence.

The Dynamic One model was designed to represent a bona-fide dynamic asset allocation strategy. Even more important, when used in conjunction with ancillary strategies, it can provide investors with an opportunity to uniquely combine their seemingly contradictory targets: Reduction of investment risk; optimization of investment return and conversion of market volatility as their friend.