

Is Modern Portfolio Theory Dead?

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I don't believe MPT is dead. These are the theories derived from Modern Portfolio Theory:

1. Investors are risk adverse. The only acceptable risk is that which is adequately compensated by potential portfolio returns.
2. Markets are efficient. For the most part, markets are fairly priced. It is virtually impossible to know ahead of time (with any degree of certainty) the next direction of the market, as a whole, or of any individual security.
3. The portfolio, as a whole, is more important than individual security selection. The appropriate allocation of capital among asset classes (stocks, bonds, cash, etc.) will have far more influence on long-term portfolio results than the selection of individual securities.
4. Investing should be for the long-term. Investment horizons of ten years or more are critical to investment success because it allows the long-term characteristics of the markets to surface.
5. Every level of risk has an optimal allocation of asset classes that will maximize returns. Conversely, for every level of return, there is an optimal allocation of asset classes that can be determined to minimize risk.
6. Allocating investments among assets with low correlation to each other reduces risk if they're held long-term. Correlation is the statistical term for the extent to which two assets are similar to one another.

What can an investor disagree with here? The problem, as I see it, is that MPT is not applied appropriately by current advisors. Post-Modern Portfolio Theory and Behavioral Finance give investors and advisors a better road map for applying MPT. See www.isectors.com for additional information.

Vern Sumnicht has 25 years experience as a successful financial planner and has been recognized for four consecutive years by "Worth Magazine" as one of the Nation's Top Wealth Advisors. Vern and his team developed iSectors® diversified ETF allocation portfolios. For more information about iSectors ETF Allocation Portfolios, visit www.iSectors.com, email Vern at vern@isectors.com or call 1-800-iSectors.