

Why We're Moving to Best-in-Class Fund Families: Avantis and DFA

For years, our best-in-class ETF recommendations have asked you to assemble a portfolio one fund at a time, mixing and matching from across the industry. That approach served us well. But after a lot of conversation between Chris Pedersen, Daryl Bahls, and me — and after watching what's happened in the marketplace over the last few years — we've reached a turning point.

Going forward, we are recommending **Avantis** and **DFA** as best-in-class fund *families*. Not just individual funds — entire portfolios you can build inside one or the other (or a blend of both) with the confidence that the work is being done the way the academic evidence says it should be done.

I want to walk you through why we're making this change, what the data shows, and how to think about whether — and how — you should follow us there.

Why Now?

Let me start with the honest backstory. When Chris first brought the idea to me, my first reaction was concern for the work he and Daryl have poured into our best-in-class ETF analysis over the years. They have spent enormous amounts of time evaluating individual funds, sometimes splitting hairs between options that were nearly identical. It felt unfair to retire that effort.

But Chris pointed out something I couldn't argue with. Two big things have shifted in the marketplace.

First, the breadth of fund offerings has expanded dramatically. When we first started building best-in-class portfolios, we had to reach into half a dozen different fund families to get the asset-class coverage we wanted. There was no single shop that had all the pieces. Today, both Avantis and DFA offer a wide enough lineup of equity asset classes that you can build a complete, properly diversified portfolio without leaving the family.

Second, DFA now has ETFs. That alone is a major development. DFA spent decades as an advisor-only firm. To get access to their funds, you generally had to pay roughly 1% a year to a financial advisor. Now their ETFs are available to anyone with a brokerage account — no gatekeeper required. That's a quiet revolution for do-it-yourself investors, and it changes what “best in class” can reasonably mean.

The third thing — and this is the one I keep coming back to — is that I'm 82 years old. I'd like to live to 100, and my wife may have something to say about that, but the reality is I'm building something that needs to outlast me. I want our students (we don't think of you as clients — you don't pay us anything) to have a strategy they can use for the next 50 years without having to monitor month-by-month fund changes. A family-level recommendation is a more durable answer than a constantly shifting list.

The Choices That Actually Matter

Before I get into the comparison numbers, Chris made a point during our discussion that I want every reader to sit with for a moment. Most investors get the order of importance wrong.

Choice number one is to save. Without savings, none of the rest matters.

Choice number two is stocks versus bonds. How aggressive will your equity allocation be, especially when you're young and your money has time to compound?

Choice number three is whether to tilt away from the total market — toward small cap, toward value, or both. This is where the academic literature offers a real, measurable opportunity.

Choice number four is which specific funds to use to implement your plan.

That last choice is the one investors fixate on, and it matters least — assuming you've picked low-cost, well-run index funds. The choice between an Avantis small cap value fund and a DFA small cap value fund is far less important than whether you're tilting toward small cap value at all. So when we recommend a family, we're acknowledging that reality. Once you've made the bigger decisions, the family choice gives you a coherent, well-built implementation without forcing you to second-guess every line item.

Traditional vs. Non-Traditional Index Funds

This is where a lot of investors get confused, and Chris explained it better than I ever have.

A **traditional index fund** — think Vanguard's S&P 500 or Total Stock Market — tracks a publicly published index. The S&P 500 is set by a committee, and when the index changes its holdings, every fund tracking that index has to make those same trades on roughly the same day. That transparency is a feature in some ways, but it's also a liability. Other traders know exactly what those funds will buy and sell, and they can front-run those trades, driving up the price the index fund pays. Academic studies suggest this hidden cost can run 1% or more of the fund's return.

A **non-traditional index fund** — like those at Avantis and DFA — builds its own index based on its own rules. It can decide, within disciplined criteria, when to trade a holding. For example, it might choose to hold onto a small cap stock that has appreciated past the “small” threshold for a while longer if its price momentum is still positive, capturing extra return. It can avoid telegraphing its trades to the rest of the market.

Now, some people call these funds “active” because the manager has a degree of discretion. I think that label is misleading. The kind of “active” that hurts investors is the kind built on guessing — picking individual stocks, trying to time the market, swinging in and out of cash. That's the active management that drives expense ratios up and returns down.

Avantis and DFA aren't doing that. Their work is rules-based and grounded in decades of academic research from people like Eugene Fama and Kenneth French. There are two pieces of evidence that show the discipline is real:

1. **Their expense ratios are low.** Generally 15 to 25 basis points. That's higher than Vanguard's 5 to 10 basis points, but it reflects the additional work of running a non-traditional index — not a roomful of expensive stock-pickers.
2. **Their R-squared values are very high.** R-squared is a statistical measure of how well a fund's returns can be explained by exposure to known market factors (size, value, profitability, and so on). Avantis and DFA funds typically score 97%, 98%, even 99%. That means there's almost no room for somebody behind a curtain to be making mystery decisions. The funds are doing what you bought them to do.

The Numbers Tell a Story

Let's look at some real returns. I pulled up Morningstar charts for one of DFA's small cap value funds going back to its inception in early 2000 — about 26 years of history.

A \$10,000 investment in the DFA small cap value fund grew to approximately **\$165,000** over that period.

That same \$10,000 in the Vanguard S&P 500 grew to approximately **\$82,000** — or roughly half as much.

That same \$10,000 in iShares Russell 2000 Value (a traditional small cap value index fund) grew to approximately **\$97,000**.

Now stop and look at that gap. Both DFA's fund and the iShares fund are technically “small cap value” funds. They occupy the same asset class, the same Morningstar style box. But the non-traditional approach — building its own index, using disciplined trading rules, capturing the full premium that academic research says is available in small cap value — produced *roughly \$68,000 more* over 26 years on a \$10,000 investment than the traditional cap-weighted approach.

Let me run a few more comparisons from that same period:

- **DFA Small Cap Blend:** ~\$96,000 (some growth exposure mixed with value, lower premium than pure value)
- **DFA Large Cap Value:** ~\$115,000 (large is supposed to make less than small, but value still beats blend handily)
- **DFA International Small Cap Value:** ~\$135,000 (the international diversification adds another piece)

This is exactly what the academic research predicts. Asset class drives return. Small beats large over long periods. Value beats growth. International diversification adds another dimension. And how those asset classes are implemented — traditional or non-traditional — makes a meaningful difference within each category.

A Recent One-Year Snapshot

I also wanted to look at what happened more recently. For the 12 months ending April 19, I compared a 10-fund portfolio built four different ways:

- **All Avantis:** 45.5%
- **All DFA:** 40.7%
- **All Vanguard:** 38.5%
- **Average mutual fund return in those categories** (per Morningstar): 36.9%

For the U.S. four-fund strategy over the same period:

- **Avantis:** 46.3%
- **Fidelity:** 41.9%
- **Schwab:** 40.9%
- **DFA:** 39.7%
- **Vanguard:** 39.6%
- **Category average:** 35.4%

A single year doesn't prove anything about the long-term — and I want to be clear that past returns don't guarantee future returns. But what the snapshot shows is that any of these approaches would have done fine. The differences between them, however, were not trivial. In a year when small cap

value performed strongly (international small cap value was particularly hot), the families that tilt more aggressively toward those factors pulled meaningfully ahead.

Should You Make the Switch?

This is the question every investor has to answer for themselves. Here's how Chris and I think about it.

If you're in tax-deferred accounts — IRAs, 401(k)s, Roth IRAs — the friction of changing funds is minimal. There's a tiny bit of trading cost, but no tax bill. If you're holding actively managed funds with 1% expense ratios in a tax-deferred account, moving to Avantis, DFA, or even Vanguard is close to a no-brainer.

If you're in a taxable account with significant embedded gains, the math gets more complicated. You have to estimate how long it will take for the improvement in expected return to pay back the tax bill from selling. If the difference is small, you may be better off staying put. If the difference is meaningful and you have decades ahead of you, switching is likely to pay off.

If you're invested through Vanguard and don't want to leave, you can still execute most of our portfolio recommendations using Vanguard ETFs. There's just one asset class — international small cap value — that Vanguard doesn't offer directly. For that one slot, I'd encourage you to use a DFA or Avantis ETF even if everything else stays at Vanguard. That single substitution can add several percentage points of return in a strong year for that asset class, as we just saw.

One more consideration that often gets overlooked: active funds tend to generate higher *tax* costs each year too, not just higher expense ratios. It's not unusual for an actively managed fund to have a 1% drag from taxable distributions in a taxable account. So when you're comparing total cost, remember to add tax inefficiency to the expense ratio.

What If Your 401(k) Doesn't Offer These Funds?

This is one of the most common questions we get. Most 401(k) and 403(b) plans don't have Avantis or DFA on the menu.

A few options to consider:

3. **Capture the match first.** Whatever's in your plan, contribute enough to get the full employer match. That's free money.

4. **After the match, look at your IRA.** Once you've captured the match, if your plan's lineup is weak, redirect the next dollars to an IRA or Roth IRA where you can buy any ETF you want. Then come back to the 401(k) for additional savings beyond what the IRA allows.
5. **Consider a brokerage account.** Especially if you're thinking about retiring early, having money outside of retirement accounts is genuinely valuable — you can access it without penalties or required minimum distributions.
6. **Check for a self-directed brokerage option inside your plan.** Many 401(k) plans now offer a “brokerage window” that lets you invest in a broader universe of funds. Ask your HR department.
7. **Ask about an in-service transfer.** Many plans allow you to transfer money you've contributed yourself out to an IRA, sometimes at any age and almost always after age 59½. Read your plan document.

If you're truly stuck with a limited menu, just make the best choice you can. Look for low-cost funds with a meaningful tilt toward small and value, and aren't actively managed. Morningstar and Portfolio Visualizer are good free tools for sorting through what's available.

What About Sustainable / Socially Responsible Investing?

We get this question regularly. Both DFA and Avantis offer sustainable equity ETFs — DFA has a U.S. sustainable core, an international sustainable core, and an emerging markets sustainable core. Avantis offers three as well.

The challenge is that these sustainable funds are essentially large cap. To follow our portfolio recommendations — which depend on tilts toward small cap and value — you'd either have to give up those tilts or augment with non-sustainable funds, which somewhat defeats the purpose.

Because of that, we don't currently recommend a complete socially responsible portfolio. If those values are important to you, you can build something using Vanguard, DFA, or Avantis sustainable funds. You may give up a little bit of expected return in exchange for living your values — and that may be a perfectly reasonable trade. I know people in my own family who have made that choice and feel good about it. The satisfaction of investing in line with your principles can be worth more than the additional return you might have earned.

What About a One-Fund Solution?

Some investors ask about funds like AVGE (Avantis All Equity Markets) or DFAW (DFA World Equity), or AVGV (Avantis Global Value). These are one-fund “tilted” portfolios that simplify implementation enormously.

They're reasonable choices for someone who genuinely can't manage a four-fund or ten-fund portfolio. But I want to be honest: compared to the portfolios we build, they're relatively weak sauce in terms of tilt. They're tilted, but not as aggressively. If you choose to use one of these one-fund solutions and you want similar long-term results, you might compensate by holding a slightly higher equity allocation — accepting a bit more volatility because your engine isn't as strong.

Why Recommending a Family Feels Right

I want to come back to where I started. Vanguard is a wonderful company. John Bogle changed the world of investing, and I'll be speaking at the Bogleheads Conference this November. I have nothing but respect for what he built. The Vanguard funds we've recommended over the years are still excellent.

But here's where I've landed: at the end of the day, the work that matters most is being done by the people running the funds — not by people writing about them. Avantis and DFA are doing more work, more carefully, with more attention to the things academic research says actually drives long-term returns. They're charging a bit more for that work, but a fraction of what an actively managed fund charges, and the evidence suggests it's earning its keep.

When I read the literature from Vanguard, from DFA, and from Avantis, I see three companies trying to do the right thing for investors. Two of them — Avantis and DFA — are explicitly building portfolios on top of decades of academic research, with disciplined rules and high R-squared values that prove the discipline is real. That is the framework we are recommending now, with the confidence that you should be able to use it for a lifetime.

What's Next

Our updated portfolio recommendations are live now. The tools at PaulMerriman.com — including the calculator that lets you compare portfolios across families — have been updated. Instead of recommending one specific best-in-class ETF per category, you'll now select a family (Avantis, DFA,

Vanguard, Fidelity, or Schwab) and see the complete portfolio that family would build for you. The M1 Finance pies and other resources are being updated and will be live shortly.

Chris has built a beautiful comparison view: when you click between Avantis, DFA, and Vanguard, you can see how each family positions on the value/growth and small/large axes. Avantis sits diagonally across the middle. DFA shifts toward larger companies. Vanguard shifts toward less value and slightly larger. Each family is internally coherent, and you can pick the one whose philosophy fits you best.

Coming next: we'll be doing a Q&A session — Chris, Daryl, and me — to answer the questions that come in from this change. Send them to us. We'll work through them.

In the meantime, thank you for trusting us with this work. We don't take it lightly. Our goal hasn't changed in fifteen years: to help do-it-yourself investors build portfolios they can hold for a lifetime, with confidence grounded in evidence. We just think we have a cleaner, more durable way to do that now.

All the best to a stronger and better financial future.

— Paul