When You're Serious…

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Looking Back To The Future

Many of the recent articles associated with planning for the New Year have been very narrow in their focus; how to reduce taxes or how to increase retirement savings. While reducing your taxation and increasing your level of ongoing savings will certainly not be detrimental to your long-term financial health, let's take a minute to focus on the impact of managing the dollars that you have already accumulated in an appropriate fashion.

Although the parting phrase for most investment related literature is 'past performance is no guarantee of future results', there is little doubt that continuing to make the mistakes of the past will not enhance your returns in the future.

To that end, here is a compendium of mistakes we have seen people continue to make; each of these will ultimately be very costly in the form of unnecessary volatility or poor investment performance.

Where Am I Going?

Some serious discussions and introspection needs to done before tackling some of the basic questions related to retirement planning and investing: How much should I save? What types of accounts should I utilize? Which investments best suit my needs?

A lack of detailed financial planning, either utilizing a cookie-cutter option or doing nothing, is the quickest way to set yourself up for failure. Not quantifying your needs in a detailed fashion will cause you to make all other retirement and investment related decisions in a vacuum and will increase your odds of making inappropriate choices.

Is The Juice Worth The Squeeze?

One of the most consistent mistakes we see is people taking more risk than is necessary to reach their goals. If you only need a 6% return to meet you goals, why have a portfolio structured with the inherent risk of returning 8%; at this point you are simply taking risk for risk's sake.

The most prudent approach is to reduce your volatility as much as possible while still generating the returns that will allow you to meet your goals. As you near retirement, your biggest concern should not be squeezing every last ounce of return out of your portfolio, it should be to protect yourself from the major potholes that could be lurking around the corner; think 'Tech Bubble' and 'Financial Crisis'.

Why Stay The Course?

The second biggest mistake is not adapting to a changing environment, if nothing else, the past decade should have taught us that volatile times call for active portfolio management.

Let's quantify some of the low hanging fruit that we have seen recently. A prime example is the dedicated foreign exposure that many people continue to hold, despite the major issues that continue to plague the foreign markets. The return advantage of the Morningstar™ Domestic Large Cap Blend category average over the Foreign Large Cap Blend for the past two years ending November 30th was 13.50% or 6.75% per year; who says that active management doesn't add value?

Are All Fees Bad?

As goes the answer to many of life's questions, it depends. The fees that add value, such as the fees paid to the manager of a mutual fund that regularly performs in the top quartile of its peer group, are good. However, sales and marketing charges that do not add direct value to the management and performance of your portfolio should be eliminated whenever possible.

Likewise, within the universe of 'good fees', the lowest fee may not necessarily provide the best value; evaluate the data on fees from the perspective of what the fee earns you versus what the fee costs you. For example, when comparing two Large Cap Value options with operating fees of 0.12% and 0.28%, it may surprise you that the more 'expensive' fund out performed its less 'expensive' counterpart by 3.5% per year for the past three years (9.1% vs. 12.6%); now that's an additional fee that was well spent.

'Those who do not learn from their mistakes are bound to repeat them' or 'lessons are presented repeatedly until they are learned'; take your pick, but if you have not experienced success in the past, you should not expect better results without making changes, often dramatic changes, to your methodology.

A prudent first step in this process is getting an arms-length second opinion from an independent and fee-only expert.

Bradley R. Newman, CFP® is with Roof Advisory Group, Inc., an independent investment management and financial advisory firm based in Harrisburg. The firm is a fee-only Registered Investment Advisor that provides portfolio management and financial planning services for individual and institutional clientele. The firm's email address is invest@roofadvisory.com./p