



Investment Strategy Guide

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Personal Money Planning Investment Strategy Guide

Personal Money Planning is more than an investment management firm. Of course, much of what we do is help clients invest their hard-earned money. We take this very seriously. As we see it, our clients trust us with the money that will educate their children, allow them to retire in comfort, and leave a legacy. This isn't just about money; it's about dreams, lifestyle, and family.

This investment policy outlines the way Personal Money Planning will be investing your money. Obviously, that makes this an important document. It is not, however, a contract. Nor is it a prospectus. It is a booklet of generalities, as the specifics of our investing necessarily change to meet the daily variations of the markets. Building an optimal portfolio requires that, essentially, we predict the future, which at best is an iffy endeavor. Therefore, you should understand that we will do our best to meet your goals and objectives, but there is no guarantee.

Please feel welcome to contact us if any of this gets a bit confusing. Clearing up any misconceptions you might have now will go a long way to our having a good long-term relationship.

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WE BEGIN WITH YOU

It may seem strange, but when we build an investment portfolio for a client we are not going after the best returns (though we certainly aren't trying for low ones either). Rather, we are trying to provide investment advice that will give you a reasonable return, at a reasonable risk, and provide for your goals. To do this, our investment advice has certain characteristics that this booklet outlines.

It answers the question, "What do we do with your money?"

"Money is not the most important thing in the world. Love is. Fortunately, I love money."

– Jackie Mason, comedian

We don't begin with a list of top stocks. We don't start the process by pulling up the latest Morningstar mutual fund ratings or by predicting the direction of interest rates.

We begin with you.

We learn about you, your needs, your tax situation, your tolerance to the ups and downs of the market, and much more. Your objectives become ours.

The Asset Allocation Spreadsheet

Portfolios are usually managed using the output from a proprietary Asset Allocation Spreadsheet (AAS). There is no requirement to strictly follow the output of the AAS. There is, after all, a reason we were given brains. But the AAS is the guide from which your advisor's portfolio recommendations begin.

The AAS produces a target band for specific asset holdings. The target percentage, breadth of the band (high and low), and the asset classes analyzed are carefully constructed by Personal Money Planning based on long-term studies of asset allocation, rebalancing techniques, and long-term investment trends.

In other words, it is our best guess as to how to get the greatest long-term return with the least amount of downside portfolio volatility. As such, it is an ever changing spreadsheet as new research and interpretations are incorporated.

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Asset Allocation

So why do we have the AAS? To understand that, we need to look at what asset allocation is and how it works.

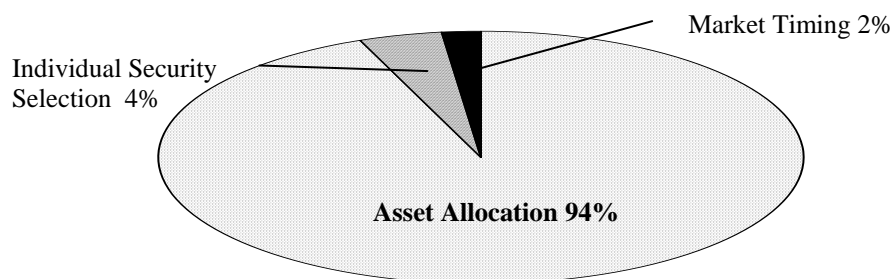
History shows that all asset classes have given positive total returns across time. They haven't, however, done this at the same time. Different markets and asset classes do not always move in tandem.

Studying the volatility and returns of the different asset classes across time shows that, in combination, they can reduce long-term volatility without decreasing returns. In some cases, such mixes may even increase returns while decreasing risk. It's like having your cake and eating it, too.

The process we have been describing is known as *asset allocation*. Part of the process involves rebalancing the portfolio. This is a critical part of the asset allocation process and is responsible for much of its benefit.

The importance of asset allocation in determining performance is well established. A 10-year study, which ended in 1983, set out to examine how the investment results of 91 large pension funds were determined and why they differed. The results, published in 1986, surprised the entire investment community.¹

The study demonstrated that 94% of the portfolio's performance could be attributed to asset allocation; only 4% was attributed to individual security selection, while market timing contributed a mere 2%. Even more surprising--attempts at market timing and individual security selection usually resulted in *reduced* returns.



That doesn't mean properly blended asset classes will keep you from losing money. In horrific economic conditions you can have a broad sell-off across most all asset types (think 2008). Yet over the longer haul, asset diversification will dampen quite a bit of your portfolio's volatility.

¹ Source: Brinson, Hood, and Beebower: "Determinants of Portfolio Performance," *Financial Analysts Journal*, 1986, 1991. Though many parts of the study are not relatable to individual investors, it did show that the mix of assets greatly affects the return of a portfolio.

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Individual security selection and market timing still have their proper places, but it's clear from the available research that the asset allocation decision has the primary impact on investment success.

Developing an effective asset allocation strategy can become complicated. There are dozens of asset classes within the basic categories of stocks, bonds, and cash; each with different risk/reward tradeoffs. Nevertheless, proper asset allocation is critical to meeting your financial goals.

Risk Management

The target allocations are modified for each client based on a number of factors. One of the prime modifiers is your risk tolerance. "Risk" means different things to different people.

Statistically, investment risk is "the variance of period returns about the long-term mean of those returns." Practically, it is rare for clients to mind when their portfolio goes up "too much." Rather, it is the risk a portfolio will go down and the magnitude of that loss which matters most to us normal folk.

People react differently to risk. Some run away from it, others accept it as a necessary evil to gain a reward. And a few actually enjoy the ride. Risk tolerance is a psychological trait that has been studied for a century.

Personal Money Planning first measures client risk tolerance using a survey produced by FinaMetrica. Their risk profiling system has been developed using the disciplines that apply to psychological testing; the test itself exceeds international psychometric standards.

Our own research has shown this instrument by FinaMetrica to be reasonably reliable when applied to clients whose risk tolerance has been observed first-hand over many years.

This risk survey produces a standardized curve of scores from 1 to 100; the higher the number, the higher the client's risk tolerance. A score of 50 would indicate a person of average risk tolerance.

The second method used to determine client risk tolerance is what can be called a "gut feeling" by the advisor based on interviews with the client and an examination of their previous investment experience and actions.

The more conservative measure of the two is initially used unless overridden by the client. As the advisor gains experience with the client and sees their reactions to market volatility, the risk tolerance measure is adjusted upward or downward. After all, neither gut nor psychometric measure beats direct knowledge of our clients' reactions to market volatility.

“The essence of investment management is the management of risks, not the management of returns.”

–Benjamin Graham

Bond Additions

Once we know your risk tolerance, we compare it to the risk we anticipate from our base portfolio. If we do not think you can stand that amount of risk, corporate or government investment grade bonds are added to the portfolio to reduce the down-side volatility.

As you might expect, by lowering the risk of a portfolio, we also lower the anticipated long-term returns. This is a good trade-off. Why? Because in time of market turmoil, investors will do stupid things if their portfolios drop too far or too long.

In both the tech-bubble burst at the turn of the century and the credit crisis that followed, markets crashed. In both instances investors could stand only so much and many sold *after* the massive declines. If, instead, they had been able to hold on they would have seen their portfolios eventually recover. But fear overrode sense and their temporary losses were made permanent.

By limiting a portfolio's risk in line with your ability to tolerate it, we can reduce or eliminate the chance that you will “freak” and sell out during a market bottom. Preventing that possibility is well worth a slight reduction in expected returns.

Cash Flow

Cash flow needs are taken into consideration in modifying the AAS. In fact, this may be the most critical part of the allocation process.

Depending on client circumstances, the portfolio's recent performance, and the judgment of the portfolio manager, between six-months and five-years of cash-equivalent and other lower-risk securities are kept in the portfolio.

The reason for this is simple: Murphy's Law. This law humorously (though in my experience, accurately) states that whatever can go wrong, will. Applied to

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cash flow, this means that the markets will be stellar until right before you need to make a withdrawal to buy something; then they crash.²

This then leaves you in a hard place. If you don't cash out some of the investments, you can't buy what you were planning. If this was a piece of art for the living room, it might not be a big deal. But, if this was to pay for your groceries next week, it *is* a big deal. If you do cash out your investments in the doldrums of a bear market, temporary losses become permanent.

Either choice you make is a bad one.

By keeping enough money out of the way of a crash, we can be sure that you can draw out the money you said you'd need when you need it without harming the rest of the portfolio.

Client Restrictions

Clients will sometimes place restrictions on the management of their accounts. There may be a particular security that you do not want sold (or at least you want to discuss it prior to sale) or a class of securities in which you do not want to invest.

If this applies to you, make sure your portfolio manager knows these restrictions. We'll abide by any reasonable (and legal) guidelines you give.

Tax Management

It is after-tax returns that a client gets to spend; therefore we are always concerned about the taxes we generate in your account. This is done in a number of ways. First, we encourage clients to use tax qualified accounts when they fit their circumstances.

We also try to put asset classes into specific types of accounts depending on what type of income is generated. For instance, we avoid, if practical, using high income investments in taxable accounts.

If we can delay the sale of an investment and capture a long-term gain instead of a short-term one, we'll do it. But this is done only if we feel it is prudent. After all, it is better to have a highly taxed short-term gain than a tax-deductible long-term loss.

² A more scientific way of discussing devastating events like these is the statistical concept of "fat tails." This is where seemingly improbable events occur more often than anticipated. If you've heard discussion of the term "Black Swans" (popularized in the Nassim Taleb book), it is the same concept. Having the cash flow cushion discussed in this section will keep Black Swans, Fat Tails, or Murphy from devastating your standard of living.

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Investment Objectives

Most people don't invest just for the joy of investing...they have a goal. Life's goals become investment objectives. And while we list this last, it is actually the essence of what drives the rest of our work. Objectives need to be carefully considered, mulled over, and studied. Doing so allows us to mine the information concerning the amount of risk a client is willing to take, cash flow that is expected, the restrictions they want to place, and their tax situation.

WE DIVERSIFY

Most people know that diversification is a good investment strategy for their portfolio. In this post-Enron, post-Internet bubble, post financial-crisis world, it has become pretty obvious: It is a bad idea to concentrate your investments in a single company or a single sector. Yet we see these narrow tactics quite regularly.

It might be a former manager who has 80% of her assets in her previous employer's stock. She's frozen by the fear of taxes as well as being seen as disloyal by selling any of it.

Or it could be the packing line worker who knows the importance of diversified investing, so he places his 401(k) contributions in four different mutual funds. Unfortunately, if those funds invest in the same types of stocks, he has, in essence, purchased one type of investment-- four times.

**"Let every man divide his
money into three parts, and
invest a third in land, a third in
business, and a third let him
keep in reserve."**

*– Talmud,
circa 1200 B.C.-500 A.D.*

While we don't use the Talmud as our investment bible, however, this quote does illustrate an important lesson about diversifying investments.

Diversification takes on many forms. First, we want to make sure that a disaster befalling a single company will not undermine your portfolio. That is why we never put too much money in any single stock, bond, or other individual investment, and why we use mutual funds and exchange-traded funds so extensively.

Next, we don't want to have too much of your money in a single investment sector. In the year 2000, the sharp drop in the technology sector demonstrated the value of this approach. More recently, the performance of real estate and financial stocks made this wisdom very obvious.

One step up from sectors are asset classes. The main ones are stocks, bonds, real estate, and commodities. We use a wide variety of asset classes and sub-classes so that you are better protected during bear markets that might significantly damage your portfolio.

Another area of diversification is global. The United States generates less than one-third of the global gross domestic product. Some of the strongest investing opportunities exist in international markets. And while U.S. and foreign markets act similarly to global events, they do not react identically.

We take this one step further and apply diversification to your portfolio's asset allocation. While we *think* that our model portfolio is just perfect when it comes to how to mix the different asset classes, we are not so delusional to think that it actually is perfect.

Many different asset allocation models will make you money over time. Through the use of mixed-asset funds, we compare our ideas side-by-side with other professional portfolio allocation opinions. We like calling this segment of the portfolio WIGGIW, or What-If-Gary-Gets-It-Wrong. In other words, we diversify your portfolio against us making an allocation mistake.

“Diversification is an established tenet of conservative investment.” – Benjamin Graham

Proper diversification can increase returns *and* lower portfolio risk.³

Stocks

When we build a portfolio for a conservative retiree, we buy stocks. When we build a portfolio for an 80-year-old widow, we buy stocks (just not as many). Compared to bonds or cash, stocks have given investors superior returns and are particularly important in growing assets faster than inflation and tax costs.

Over long time periods, stocks reflect the growth of business profit: profit that every business person strives for. Because of this, stocks are the asset class best suited to produce growth over the long-term. And since the retiree and the widow have a good chance of living another 10 years, we need to make sure that *part* of their portfolio will grow fast enough to keep their purchasing power intact.

It is natural to be hesitant to invest in the stock market. This is a cautious reaction to the fact that the stock market can go down (and often does so in a spectacular manner). That is why the percentage of a portfolio invested in stocks is as varied as

³ Diversification works wonderfully in a “normal” market. But when you get massive disruptions like we did in 2008 and early 2009, diversification alone will not help your portfolio. After all, no matter how diversified you are, if pretty much everything goes down, you'll lose money. That's where our cash-flow cushion (discussed earlier) comes to play.

the number of portfolios we manage. For some people it's a clear majority; for others a minority.

**“The real key to making money
in stocks is not to get scared
out of them.”**

—Peter Lynch

Diversification Means Not Making a Killing

While diversification is done to raise returns and lower risk, it does have its drawbacks. When stocks are going down, clients wonder why we had so much money in them. When stocks are going up, they wonder why we had so little.

If you allow Personal Money Planning to help with your investments know that our trying to minimize market volatility and losses does not mean we will eliminate them. In every market downturn someone you know will have gotten out early. In every bull market many will make more money than you. No matter what benchmark you want to compare us to, there will be times, sometimes measured in years, in which we will disappoint.

Our goal is not to design the best investment mix for today. Our goal is to design a portfolio that is best for you across time.

**“Some days you're the dog,
some days you're the hydrant.”**

—unknown

Being Perfect vs. Being Less Wrong

This is not a technique or a product, rather it is a philosophy. There is a lot of information out there to learn and understand. To put all of the information together and achieve investment perfection--buying at the lows and selling at the highs--is the Holy Grail of Finance.

We don't do this.

We don't know how.

You see, market movements depend on little things like supply and demand and how humans, their companies, and their governments interact with it. While the concepts don't change, the specifics of what happens in the real world changes every second of every day. There are trillions of interactions that occur

between billions of people on this planet. Each one affects the world's economy.

So we use the plethora of available information to come up with good theories that lead to sound practices we can use. To do this we integrate new facts as they come along. This allows us to make better forecasts of what investments or combination of investments will work best for your needs. In other words, it allows us to be less wrong.

“Money is of a prolific generating nature. Money can beget money, and its offspring can beget more.”
– Benjamin Franklin

There's a saying in investing that Bulls make money and Bears make money, but Pigs get slaughtered. When the NASDAQ market and tech stocks had an amazing year in 1998, we rebalanced portfolios by selling off some of those positions. When they had the meteoric rise in 1999, we did so again.

Not only did we not keep riding the market up, we certainly didn't shift our clients' accounts heavily into the technology sector. Subsequently some clients fired us. They wanted all of their eggs in the “sure thing” basket of the tech sector. They wanted to find the next Microsoft. Reaching for those ultra-high returns in the late '90s resulted in portfolios that dropped off the cliff of the early '00s.

Buying high and selling low is not the road to riches.

Don't read into this that we avoid losses. Hardly. 2002 was a miserable year for us and 2008 was dreadful. Diversification can help, but even it has its limits.

Weather Changes

The stock market is like the weather. It fluctuates. Good weather doesn't last forever. Fortunately neither does the lousy weather. Over the seasons there tends to be more fair weather than foul. And in the markets, we have more good years than bad.

We tend to recall horrendous weather more than the normal weather days. Which do you remember better, a sunny day with a gentle breeze blowing, or the day a hurricane, tornado, or blizzard blew into town? Just the same, folks remember the sharp market corrections better than the smaller, more normal moves that increase their assets over time.

The market usually bottoms when rains of despairing headlines drop around us and the winds of scandals are blowing their fiercest. The market tends to peak when skies are sunny with strong company earnings. Beautiful fall colors and

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an easing of scorching summer temperatures lead to ice storms and snow shoveling. Frigid temperatures lead to blooming spring flowers. Temperatures and markets both fluctuate good and bad, up and down.

On a practical basis, being out of the market at its bottom is dangerous. After dropping 43% in the 1973-74 bear market, small stocks gained 140% over the next two years. A good part of those gains were concentrated in two months. If your money had been sitting in treasury bills instead of the stock market for those two months, your return would have been reduced by 90%.

There is no problem preparing for the bad times. But nailing shut your storm shutters and hiding in a closet it is not the way to enjoy the majority of your life.

A study by Dalbar shows that while the average equity mutual fund returned an average annual return of 9.3% per year from 1984 to 2000, the average mutual fund investor in those same funds earned only 2.6%. This 6.7% difference was due to investors chasing hot funds and hot sectors. They tended to move in to top performing funds *after* a period of great performance and sounded the retreat *after* the fund had dropped. They were trying to time the market for better gains. Yet the evidence—a 2.6% return in a 9.3% market—shows otherwise.

**“To buy when others are
despondently selling and to
sell when others are avidly
buying requires the greatest
fortitude and pays the greatest
reward.”**

– Sir John Templeton

WE TRY TO HIT SINGLES, NOT HOME RUNS

Never expect a stock, bond, or mutual fund that we recommend to go up quickly. It may, but don't expect it. We will often get into an investment well before it begins moving up. This is not because we want your investment to stagnate (or go down). Rather, it is because we don't know how to figure out exactly when a stock or the market as a whole will go up.

We don't think anyone does.

Instead, we look for those stocks, bonds, and mutual funds that will, on average, give a good return over the time period we are shooting for. That may be five, ten, or thirty years. This is why we do not seem rattled when an investment has gone down. It is not that we like taking losses. Rather it is because we realize that investing takes time and patience.

**"If you hear that everyone is
buying a certain stock, ask
who is selling."**

–unknown

We are not alone in this sentiment. Peter Lynch of Fidelity Magellan fund fame has said that most of his holdings saw their best returns in the *third year* of ownership by the fund.

In fact, the Magellan fund is an excellent example. Do you realize that under Lynch's reign, the Magellan fund once lost over 50% of its value? Let's say you had \$100,000 invested in Magellan on January 1, 1973. Just two years later on December 31, 1974, you would've been down to only \$43,000. What would most people do if this happened to their mutual fund? That's right—they would sell, sell, sell! Hindsight lets us know that even with this crushing drop, Magellan ended up being one of the best performing funds during Lynch's time.

**"He who wishes to be rich in a
day will be hanged in a year."**

– Leonardo da Vinci

The year-to-year variations in the market (and in your account) are not what interest us. What we concentrate on is creating a portfolio that has a high

probability of you achieving your goals. This includes keeping its volatility to a level that you can live with, so that you don't abandon the course due to bumps in the road.

**“Nobody who plants corn digs
up the kernels in a day or two
to see if the corn has sprouted,
but in stocks most people want
to open an account at noon
and get their profit before
night.”**

*– Charles Henry Dow
(founder of The Wall
Street Journal)*

That's why we don't see "beating the market" as our goal. We do not measure ourselves against a market benchmark. What we concern ourselves with are your goals...both short-term and long-term. Our first consideration in portfolio design is to produce the return over time that you need, keeping the risk below what you can stand. Whether we beat the market or it beats us is immaterial.

WE IGNORE WHAT IS HOT AND WHAT IS NOT

We won't invest in an area just because it is doing well. First, it must make sense as an investment. Next, it has to fit your needs. Finally, it should work in concert with the rest of your portfolio.

For instance, beginning in 1996 if you had purchased the top mutual fund from the previous year, over the next five years your average portfolio return would have been negative 2%. That's not to say that every winner turns into a loser—but it does show that trying to pick your funds by looking backward can be fraught with error.

**“Sometimes your best
investments are the ones you
don't make.”**
—Donald Trump

Just as we are not running toward the hot asset classes, we are not running away from the ones that were cold last year. If a particular investment type makes sense for your portfolio, that shouldn't preclude you from adding it just because it's recently had a rough time.

Much of this is due to a concept known as “reversion to the mean.” If there is a mean reversion behavior for securities, then a period of great returns will most probably be balanced by a period of low returns.

No trend lasts forever. Cycles are a fact.

“It will fluctuate.”
*—J.P. Morgan,
when asked what the market was
going to do*

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Here's a story to help pull this together:

Imagine that you had to drive from New York to Los Angeles. You are in downtown Manhattan hopelessly stuck in traffic. Bicycle messengers have been whizzing past you for the last hour. Inspired, you sell your car at a loss and buy a bicycle. Now you are whizzing by all those idiots still in their cars.

Sound absurd? Investors do it everyday when they make short-term decisions for long-term journeys.⁴

We also don't like newer investments that we don't understand. If a prospectus or a product presentation leaves us scratching our heads, we won't recommend it to our clients. This kind of philosophy would have saved many people grief in the limited partnership fiascoes of the '80s as well as the more recent problems with derivatives.⁵

"The early bird may get the worm, but the second mouse gets the cheese."
– *unknown*

⁴ Thanks to the American Century Investment Services group for providing this illustration.

⁵ This is not to say that limited partnerships and derivatives are never appropriate. It is using them without understanding the risks that go along with them that is problematic. What seems like a "good deal" can get you in trouble.

WE KEEP EMOTIONS OUT OF INVESTING

In the current Internet-Information age you'd think that all investors should do better. After all, you can find out almost everything there is to know about any stock. Why, then, have so many lost miserably during market corrections? A big reason is that information is useless when we let emotions interpret it for us.

Amateur investors base what should be long-term decisions on short-term information. They look at last year's mutual fund return or a recent earnings estimate on a stock and assume the trend will continue forever. At the end of 1999 investors could look back at the previous five years and see that growth stocks had grown much quicker than value stocks. You can guess what happened—value stocks completely dominated growth stocks in 2000 and for many years hence.

Taking emotions out of investing should be a major difference between amateur and professional investors. Yet sadly, many "professionals" react emotionally to the ups and downs of the market.

Economic uncertainty is certain.

Making a long-term commitment to investing in stocks is easy to say but hard to live through. During a bull market people want me to concentrate their investments and ignore allocation principles. During a bear market people want me to dump their stocks and put everything into fixed income securities. Rationally speaking, "buying low" and "selling high" is a self-evident formula for making money on investments. But rationality goes out the window when prices fly up or plummet down. Because of this, investors have the tendency to "buy high" and "sell low."

This departure from rational behavior occurs because investing is an emotional experience. Prices go up—people feel confident—they invest more money. Prices go down—they feel scared—they sell. This is a normal emotional response. There is no problem with feeling this way. My gut goes through the same feelings whether I'm riding a roller coaster at Six Flags or the roller coaster of the markets. The difference is that I have trained myself to listen to my mind and not my gut.⁶ One of my jobs is to help my clients do the same thing.

⁶ This works for the market. I still get queasy on the newer roller coasters.

“The one thing that unites all human beings, regardless of age, gender, religion, economic status, or ethnic background, is that deep down inside, we ALL believe that we are above average drivers.”

– *Dave Barry*

In August 1979, *Business Week's* front cover declared “The Death of Equities.” It was a bleak time in the nation’s economic history. Inflation, interest rates and energy prices were at an all-time high, and 7 million shareholders had abandoned the stock market since 1970. “Only the elderly who have not understood the changes in the nation’s financial markets, or who are unable to adjust to them, are sticking with stocks,” concluded *Business Week*. Those that read and followed the teachings of that article missed out on a great bull market that lasted until 1987.

That bull market ended spectacularly on October 19, 1987. That day, Warren Buffet lost \$342 million of his own private shareholdings in Berkshire Hathaway. Actually that’s not true. What is true is that his portfolio’s value went down \$342 million. He didn’t lose anything. He didn’t lose because he didn’t sell. If he had sold, he would have missed an even greater bull market that was yet to come.

Therein lies the secret to all investing: markets don’t create losses—real, permanent capital losses. Real losses are created by people making irrational and counterintuitive (stupid) judgments.

The key is to keep your focus on where you are going.

WE AVOID TAXES

We avoid taxes, but we don't get ridiculous about it. We never let the "tax tail" wag the "investment dog."



Taxes are important...important to reduce. For the average American, taxes reduce their stock mutual fund returns by over 2%. We help our clients determine how to do their investing to save taxes. That is why we periodically sell some investments that we still believe in. If they have lost money by December and are in a taxable account we usually sell in order to provide some tax losses for our clients. We stay in the market though, replacing these with investments that are similar in nature.

**"The wages of sin are death.
But by the time taxes are taken
out, it's just sort of a tired
feeling."**

– Paula Poundstone

We also look at whether to use IRAs (Roth or Traditional), 401(k)s, SIMPLE plans, etc. Should we invest in tax-free municipal bonds or taxable ones that pay better? These are the decisions that must be made in light of your particular tax circumstances.

But as we mentioned at the top, we don't let the tax tail wag the investment dog. It's okay to pay taxes. I know that few enjoy the prospect, but it is part of the game of making money. Some gains need to be taken now, regardless of the tax consequence. Enjoy the gain, pay the taxes. It's better that than having the tax savings of taking a loss.

**"The income tax has made
more liars out of the American
people than golf has."**

– Will Rogers

WE CARE ABOUT THE NEXT DECADE, NOT NEXT YEAR

“Calling someone who trades actively in the market an investor is like calling someone who repeatedly engages in one-night stands a romantic.”

–Warren Buffett

Could the Dow go up 30% next year? Sure it could. Could it drop 30% next year? Sure it could. Both are improbable, but both are possible. So how do we at Personal Money Planning handle this? We don't. It's not easy; we have opinions like everyone else does, but acting on those opinions would not fit our overall investment philosophy.

Imagine an investment in which you have a 30% chance of losing money this year. Would you want a part of it? Probably not. Yet if I told you that it would average 10% a year for the next 20 years it sounds quite a bit better. Both describe stocks.

If you are concerned with what your money will be worth in the next year or two, then you shouldn't be in the stock market to begin with.⁷ You should keep that money in the bank or a money market fund. If, on the other hand, you want to ensure enough money is there 10 years from now—when your child enters college, or when you finally retire, or when you reach your '90s—in that case stocks can help.

All of this comes from our fixation on goals—what you are planning to do with your money. Financial success begins with understanding the core values and goals of our clients. I often get questions that concentrate on investment returns:

Why didn't my portfolio beat the S&P 500 last month?

My neighbor said the return on his investments with the broker across the street from you was three percent higher than yours last quarter. What about that?!

A friend of mine doubled her money in the futures market in one month. Why can't we do that?

⁷ Nor should it be in the long-term bond market, the real estate market, the commodities markets, and a lot of other places.

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These types of questions show that the client is looking at a short-term fix to their problems. Many people get caught up in trying to time the market; to find the next Microsoft, or some fool-proof way to double their money in a year. Instead, we try to steer them to a long-term solution to their goals.

Getting irrationally exuberant on market gains, or panicking after a holding gets hammered, is not a healthy way to react to the market.

We use asset allocation to reduce risk and maximize return in a way that matches a client's specific situation. In this we use both equities and other types of securities...no one type of investment is the answer to every problem. Using this investment process we build wealth, so that our clients can realize their dreams.

"Although the market may not always be rational in the short-run, it always is over the long haul."

*–Burton Malkiel, in
A Random Walk Down Wall Street*

None of this is to mean that we ignore what is happening around us. When Treasury Bond prices soared to the point that they were, effectively, giving a negative return, that got our attention. In our more aggressive accounts we shorted these bonds.⁸ While for the first many weeks this tactic lost money, we closed our position quite successfully.

That's not to suggest we'll get it right all the time, just that we do keep our eyes open.

⁸ Shorting is a method that is essentially a bet that the price of a security will go down in the near future.

WE KEEP WORKING AND LEARNING

Every month we go through over a thousand pages of financial books and periodicals.⁹ Countless hours are spent perusing even more information on the Internet. Add to that meetings, seminars, workshops, and conference calls and you get a picture of what it takes to stay up on the latest in the financial world.

**“The difference between
genius and stupidity is that
genius has its limits.”**

–unknown

We are constantly monitoring thousands of stocks and mutual funds to determine which will fit our clients' allocation needs. We look at factors such as expenses (brokerage fees, 12-b-1 fees, etc.); and we keep apprised of legal, compliance, shareholder service, transfer agent, and custodian issues.

We check on mutual funds our clients own to see if there have been any changes in managers, investment style, or expenses. We check bonds to see if there have been any rating changes and how they have been affected by the current interest rates. We check on stocks to monitor changes in earnings, accumulation of debt, and any problems that their management might be getting into.

We determine how your portfolio matches our target asset allocations and how those allocations match your goals. We meet with you to determine any changes in your life that merit changes in your investments.

We examine the asset allocation and style categories we use to determine if our previous research is still valid. We then adjust our investment strategies accordingly. In other words, by the time you read this, some of our strategies will have changed.

We don't get confused or distracted by the various rating services that seem to imply they know what your mutual fund will do in the future. We also don't believe there is a list of the “6 stocks you must have in your portfolio.” To us, one size does not fit all.

We don't recommend or buy investments for a client because we get a bigger commission.¹⁰ We don't give preference to a fund because they sent us a gift

⁹ It doesn't hurt that Gary is a book reviewer for the Journal of Financial Planning.

¹⁰ We're Fee-Only and do not accept commissions of any kind from mutual funds, brokers, insurance companies, or anyone.

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(but we love getting them). We don't try to sell you anything; rather we try to work with you to be your trusted advisor.

We ensure that the investments integrate seamlessly with your overall plan if you have used us for financial planning services.

We keep the worry about investing out of your life.

We stay awake at night so you don't have to.

We strive to do things a little better every day.

"Good enough never is."
– *Debbie Fields,*
founder of Mrs. Fields Cookies

FOR THE INQUIRERS

Not all of you reading this are clients—some are investigating whether we are the right advisors for you. We'd be remiss if we didn't share some thoughts on that.

One question we get asked is: What does Personal Money Planning have that others don't? It's difficult to pinpoint. After all, there are hundreds of financial advisory firms in the country that serve their clients well, are honest, build a great investment portfolio, follow the tenets of financial planning, and put their clients first. We are among those hundreds.

However I can say, when it comes to investing, there are three traits that serve us well:

Emotional Neutrality: I can be opinionated. I can be emotional. I get excited about many topics (ask me about curling sometime). But when it comes to investing I get rather robotic. Maybe it's because I'm an introvert, but the crowds stampeding around affect me little. If my spreadsheet says sell, I sell. If it says buy, I buy. A company that has done great does not impress me. One that does poorly does not disappoint. I may be wrong a lot in the short-term. But that's better than being wrong in the long-term.

Discipline: Even when I get a good "gut" feeling on a client's tolerance for risk, we still run a risk analysis on them. While I may get an idea that an asset class will continue descending into the abyss, if it exceeds our tolerance bands, we begin to build the position back up. While I may want to invest more in an area of the market, if cash flow needs dictate we leave the cash alone, we leave the cash alone. It's our discipline that enforces our emotional neutrality.

Flexibility: Being able to change is critical for long term survival. Success can breed complacency. We continue learning, challenging our notions, asking what could go wrong from here and what could go right. Our target bands have changed over the years. The asset classes we use in our portfolios and their target weights have also changed. Discipline keeps us from doing this in response to current conditions, but rather due to long-term trends. Flexibility can be a great investment virtue, while stubbornness can drastically shorten an investment career.

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Still, there are hundreds of firms across the country and thousands of advisors that do the same. So what's different? We love what we do, we're rarely bored, and we have a great sense of humor. But what makes us and everyone else different is how we connect to you. Come in, sit a spell, ask your questions, and see if you like what we say and how we say it. Can you be free and open with us when it comes to your finances? Does it seem like we can be open with you as well? Do we connect? That's the difference. That's what makes us a good fit or a bad one.

A LAST WORD

Investments in and of themselves serve no purpose. Investments are just part of what should be an overall plan to get you where you want to go.

We are a financial planning firm. And planning always starts with goals. After all, you need to know where you are going if you are to ever get there. But where do these goals come from? Professed atheist Bertrand Russell stated a very important truth:

Unless you assume a God, the question of life's purpose is meaningless.

A few of our clients do not believe in a God and even more are undecided. For those of you who believe in God, start your financial journey there. If not, then you will have to determine your own path in life. Either way, a message of Proverbs is a good place to begin:

*He who trusts in his riches will fall,
but the righteous will flourish like the green leaf.¹¹*

Even better is a longer passage from the New Testament. Whether you are a believer or not, I think you'll see the wisdom in it:

But godliness is a means of great gain, when accompanied by contentment. For we have brought nothing into the world, so we cannot take anything out of it either. And if we have food and covering, with these we shall be content. But those who want to get rich fall into temptation and a snare and many foolish and harmful desires which plunge men into ruin and destruction.¹²

This next part of the same passage is of less significance to those who are not Christians, yet I think there's some relevance to all:

For the love of money is a root of all sorts of evil, and some by longing for it have wandered away from the faith, and pierced themselves with many a pang. But flee from these things, you man of God; and pursue righteousness, godliness, faith, love, perseverance, gentleness.¹³

¹¹ Bible, Proverbs 11:28, New American Standard Version.

¹² Bible, 1 Timothy 6:6-9, New American Standard Version.

¹³ Bible, 1 Timothy 6:10-11, New American Standard Version.

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All of these passages point to the fact that money itself is not a goal. It is not the prize you should seek. To some it is a gift, and to all it is a tool. We see our job as one that helps you be the best steward of the money that you have.

“It is not the man who has little, but he who desires more, that is poor.”

- Seneca the younger, (3BC-65AD)

No matter what is the foundation of your life, we look forward to helping you on your journey. We hope that this introduction to how we view the investment process will aid you in determining if we are your best resource for managing your investments. Whether you are looking at us for the first time or are already a client, know this: we take our responsibility to you very seriously.

As stated at the start of this booklet:

As we see it, our clients trust us with the money that will educate their children, allow them to retire in comfort, and leave a legacy. This isn't just about money; it's about dreams, lifestyle, and family.