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Key to Investing? Look Inside.

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What's the greatest sin an investor can commit? Picking the wrong stocks? Buying too late? Selling too soon? No: the greatest sin is failing to anchor your investments to your goals.

I witness this problem from a valuable perspective as an adviser. I'll ask a client what they're trying to accomplish with their portfolio. Response: I'm trying to make as much money as I can. Then I ask: How will you know when you've succeeded?

That's when I get the blank stare. Then, I think about the steps we all must take as investors to move past this reaction.

Financial Authenticity: the Cure for the Blank Stare

The essence of authenticity is aligning your behavior with your deepest goals and values. This virtue is essential in personal finance and investing. These goals might be assembling a down payment for a house, funding your children's education, taking a sabbatical to volunteer in underprivileged communities, generating a retirement income that will last your lifetime, charitable contributions, or leaving a meaningful legacy.

As investors, we must identify honest goals for ourselves. Then we can determine when they will need funding, how much they will cost and what percentage return we need on our portfolios to achieve them. These are the first steps to creating a true plan.

Summary: Key to Investing? Look Inside.

Market-focused rather than goals-focused investing distracts us from our financial aspirations in significant ways

Money is a terrible master, but an excellent servant.

—PT Barnum



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Your Way to Prosperity

The cornerstone of a sound financial plan, goal-driven investing also leads to a disciplined investment strategy, which itself requires diversification, asset allocation consistent with your risk tolerance and periodic rebalancing. Then patience—which, somewhere it is written is a virtue—allows the miracle of compounding to do its work.

Wrath of Human Nature

For many of us, human nature—the emotions of fear and greed—unbearably infect our investment management. Market gyrations cause us to bail out when the market falls. Overconfidence compels us to think we can outsmart the market and somehow “outperform.” We are bombarded by “financial pornography” from Wall Street, hedge fund managers and the financial media.

These temptations cause us to become speculators rather than investors. When that happens, we burden our portfolios with high turnover and increased transaction costs and virtually guarantee that we will—ironically—under-perform.

For example, some local professional athletes and other wealthy investors chased performance with the now defunct International Management Associates hedge fund. Most likely, by pursuing unrealistic returns rather than their commitment to their goals and values, these investors were vulnerable to market-driven thinking.

Disastrous Distractions

Market-focused rather than goals-focused investing distracts us from our financial aspirations in significant ways:

- It lulls us into a false sense of financial security resulting in insufficient saving.

- We shift blame to our fund managers or advisers when we are disappointed with the results.
- It inhibits us from the most important—and difficult—work of consciously establishing meaningful goals.

Goals-focused portfolio strategies change when our personal circumstances change—not in reaction to the markets. Moreover, it fosters the extremely beneficial practice of focusing on the whole and less on the component parts

Practicing Conscious Finance

Goal setting offers significant psychological benefits as well, by

- Providing a framework for making good decisions,
- Giving us a positive outlook and the motivation to succeed, and
- Allowing us to bounce back from disappointment.

Setting money goals, of course, may require us to confront our financial demons. Despite the enormous benefits, we may be reluctant to establish concrete financial goals. Stated goals often conflict with one another and we have to prioritize and make agonizing choices. Frequently our spouses or other financial partners are in disagreement with us.

Nevertheless, this challenging practice is well worthwhile and the key to being a successful investor.