

## Keep It Simple!

Investing can be overwhelming. You have to do research, read articles, listen for tips, review your existing investments, maintain diversification, and so on. In reality, investing is only as difficult as you make it. The basics of investing are easy:

Step 1: Pick a stock/bond mix.

Step 2: Select diversified investments to achieve that mix.

Step 3: Monitor the portfolio.

Of those steps, the one that captivates many investors is step 2. Though it is far more important to focus energy on proper asset allocation, stock picking is, unfortunately, the part that delivers the most excitement. People enjoy stories, and the stories lie in the investment selection.

The draw of stock picking creates a problem because investors are often overconfident in their ability to achieve success. Sure, someone can get lucky and pick out a hot stock before a price jump, but what isn't acknowledged is that he or she is just as likely to pick a stock that is a dog. Often, investors arrogantly believe they can identify investments that will outperform, either through quick research on the Internet, an overheard stock tip, or some new product release that is identified as a “sure thing.”

If our expectations for stock picking are so high for ourselves, then our expectations of mutual fund managers must be even higher. They are professionals who spend their days doing research. Surely a manager with a research staff and high-powered analytical tools can identify winners.

The scary part is that even these well informed professionals have the odds stacked up against them. These smart people are competing with other smart people like themselves that collectively form the market—the very thing they are trying to outperform. Over the long term most active managers do not out performed the indexes; you could have outperformed, avoided the higher management fee, and most likely paid less in taxes due to the efficiency of index funds.

## Simple = Boring = Effective

That strategy may seem too simple...but what's wrong with simple? The problem for most of us is that it's a boring strategy. My response is this: Sure, active management may deliver a better story, but getting good stories to tell should not be your goal in investing.

By investing in index funds that capture large, small, and foreign companies, you work to own the market. You don't have the ability to beat it. Your aim is to have a different kind of story to tell, one that involves a happy ending and attainment of your financial goals. With index investing, not only do you give yourself a better chance of reaching your investment goals over the long run, but you will spend less time worrying about your investments and more time with your family enjoying the wealth you have worked to create.

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## Ask the CFP®

### Q. Does 1% make really make a difference when investing?

A. Yes, a big difference when compounded over time. Take the case of Joe and Sarah both are age 25; they contribute \$5,000 to their employer 401k plans. If Sarah invests in a portfolio of stock and bonds which earns 6% annually, and Joe likes low risk; he chooses the stable value fund that returns 5%. By the time they retire at age 65, Sarah will have \$829,788. Joe will have \$635,842. A difference of \$193,946, or 23.4% greater amount for retirement.

Two things contribute to Sarah's success. First, she makes her contributions every month for 40 years. The power of compounding had a significant impact over her time frame. Secondly, she stayed with her portfolio through the ups and downs of the market over her entire working life.



**Charles Buck CFP®**