Week Six

Your Investments: Money Working You or Money Working For You?

After Week Six, you will understand the basics of investing and be empowered to make wiser investment choices. More importantly, you no longer will need to gauge your personal well-being on the fickle movement of the stock markets. Your investments will show you a great deal about yourself and the natural human gravitation toward desire, aversion, and denial. By acknowledging these "poisons," you are able to convert them to "medicine" that help you on your journey of Authenticity. Finally, you have a tool that allows you to examine all the other pieces of your financial life that are as important, or in most cases more important, than investment return. Your Authentic Money Guide provides the framework to integrate this new approach to your investments into your actual experience.

A Call from Wally

"Integrated Financial Planning—this is Paul."

"Paul, this is Wally."

I was shocked to hear Wally's voice. In the two years I had known him, Wally had never called me at work.

"Is everything, alright?"

"Before we go any further I want you to promise me that you'll send me a bill for any time and expenses you incur on my behalf."

"I'll keep track of a few charges if it will make you feel more comfortable," I offered. "I know that you haven't made any profit on my account, especially when you count all the hours I spend chewing the fat with you once you've fixed whatever I bring to your shop."

"I just want this business relationship to be fair to you," said Wally. "What I need is some investment advice. I guess I thought that if I just 'hung in there' with my portfolio that it would eventually start to regain some of what I've lost. I'm embarrassed to admit that I've lost 30 percent of the value of my portfolio in the last three years. I should have done something long before now.

"To make matters worse, I've sat idly by and watched Jane and John's life insurance money dwindle by nearly the same amount. I feel like I've really let them down by not suggesting they come talk to you and get a second opinion from what their broker has been saying."

"I know it's no consolation, Wally," I said, "but I've had new clients who have lost almost 50 percent in that same time period before they finally determined they had to talk to someone. Don't be too hard on yourself. What's important is that you've decided to deal with these losses and make some informed decisions."

"The main thing I need to know is whether or not what is left will be enough to allow us to sustain our lifestyle," said Wally, adding, "I sure would prefer not having to return to the jungle of Engineer World."

"All of those questions can be explored as they relate to your investment decisions," I said. "Why not gather up your latest investment statements and last set of Quicken® reports and come on over to the office tomorrow morning?"

"That sounds great, Paul. Thanks for being willing to help us out with this mess." Wally paused and then continued, "I think at the root of all of my reluctance to face our investments is my greed. I just wanted to hold on to those profits that I once saw in the accounts. I know now that they were just paper gains generated by a host of falsehoods. Somehow I feel better just admitting this."

"It's tough facing these realities, Wally." I said. "I think you've gotten a lot further than most folks in looking below the surface of investment performance. I look forward to continuing our conversation tomorrow."

"Wealth is like a viper, which is harmless if a man knows how to take hold of it; but if he does not it will twine round his hand and bite him."

—St. Clement

After I hung up, I looked out my office window across our little valley to the Smith's cabin. It struck me how they, like everyone, encountered difficulties even though they had settled comfortably in so many aspects of their lives. Even Wally, as aware as anyone I had ever met, struggled with money issues. What a step to admit that he needed help. I was grateful that I might be able to return a favor to this family that Katherine and I had grown to respect and love.

Investment Insanity

LIFE IS JUST A BOWL OF CHERRIES

Life is just a bowl of cherries.
Don't take it serious.
Life's too mysterious.

You work, you save,
You worry so
But you can't take the
Dough when you
Go, Go, Go…

—*Fosse*

No other area of personal finance seems to take us to the emotional extremes as the performance of our investment portfolio. When annual stock market returns were 10–20 percent everyone lived in euphoria. The recent years of negative returns has caused no small amount of anger, depression, and even fear. Like Wally, we wonder if we'll run out of money at a time in our lives when we're helpless to do anything about it.

(Please see the summary for MAP 6-10 later on in this section for an explanation of the difference between stock [equity] and bond [debt] investing, if you have trouble with those distinctions.)

A sampling of recent investment news can illustrate why we are feeling so helpless:

- The Standard and Poors 500 Index outperformed 75 percent of professional money managers from 1973–1992. (*Intelligent Asset Allocator*)

This statistic supports the argument that passive investing, which uses index funds that mimic stock and bond indexes, is a

superior long-term strategy to active investment management. Actively managed mutual funds are run by individual managers or a management team that believe they can identify investments that will enhance performance of a portfolio over the stock indices.

Given that computer-driven index investing is more effective than active management—and at a much lower cost—why would millions not feel a sense of betrayal?

"He that trusteth in his riches shall fall."

—Proverbs

- "In an effort to exceed analysts' projected operating earnings of .73/share (10-15-02), Citigroup conveniently included gain from the sale of its headquarters on Park Avenue of $323 million. This accounted for .06/share and landed them at .74/share." (*MS Money,* Jubak's Journal)

  This is a perfect example of an earnings distortion—as sales of assets are one-time gain items—not to be included in operating income. Investors have become increasingly wary of financial reporting practices in light of these developments.

  There seems to be corruption at every level. Earnings reports seem to be manipulated to "prop up" stock prices, only to collapse when the distortions are discovered.

- "Every sector of the U.S. Equity market sustained damage in the third quarter of 2002. Not since the fourth quarter of 1987 has the market taken such a plunge." (First Affirmative Financial Network,1-800-422-7284, Market Commentary)

  Three years of stock market losses resulted in the following annualized performance and standard deviation (risk) results as of December 31, 2002:

Index*	3 Yr. Return/Risk	10 Yr. Return/Risk
S&P 500(1)	-14.55%/15.1	9.34%/17
Wilshire 5000(2)	-14.37%/16.4	8.74%/17.1
Dow Jones Ind. Avg.(3)	-8.55%/16.9	12.01%17.9
NASDAQ Compos.(4)	-30.83%/28.4	7.62%/32
Wilshire Real Estate(5)	14.01%/15.1	9.97%/14
MSCI Eafe—Ndtr D(6)	-16.67%/12.8	6.26%/15.9
Lehman Bros. Aggr.(7)	10.10%/3.65	7.51%/3.95
1 Year Treasury Note	5.94%	5.31%

* Please Refer to MAP 6-3 for additional information about the indices.

1—500 Widely held U.S. stocks

2—5000 U.S. publicly traded common stocks

3—30 Industrial U.S. stocks

4—All issues of NASDAQ stock market

5—Comprised of companies whose charter is the equity ownership of commercial real estate.

6—Benchmark for international stock performance. An aggregate of 21 individual major country indexes.

7—Composed of the Lehman Brothers Govt./Credit Index, the Mortgage-Backed Securities Index, and the Asset-Backed Securities Index. Common benchmark for diversified bond portfolios.

This chart reveals the frustration that investors have felt. To translate the statistics into reality: an investor who purchased an S&P 500 Index Fund on January 1, 2000 would have lost three times the 14.55 percent annualized return listed, or 43.65 percent. The 15.1 volatility indicates that the 14.55 percent annual loss could have varied between + .55 percent and -29.65 percent!

We have to ask the question, “Is all that risk worth achieving the possibility of a .55 percent return?”

We have become a nation of investors over the past 20 years. The introduction of the IRA in the early ’70s, along with the popularity of mutual funds, made investing an option for anyone with $25/month to save toward retirement. No longer was it necessary to have $5,000–$10,000 in order to see a stock broker and invest in stocks and bonds. Double-digit annual stock market returns made bank certificate of deposits and savings accounts as antiquated as a Model T. In 2001, it was estimated that half of all U.S. households owned mutual fund shares, up from 6 percent in 1980.

At the end of 2001, there were 8,321 mutual funds (triple from 1990) with almost $7 trillion dollars invested—a seven-fold increase from 1990.

This dramatic growth in stock market investing over the past 13 years has also inundated investors with investment information. Unfortunately, more information is not always what people need.

LOAVES AND FISHES

This is not
the age of information.

This is not
the age of information.

Forget the news,
and the radio,
and the blurred screen.

This is the time
of loaves
and fishes.

People are hungry,
and one good word is bread
for a thousand.

—David Whyte, from The House of Belonging

The one good word that begins to address our longing for an escape from having our *money working us* vs. our *money working for us* is "ground."

Before we jump in to fix our investment portfolios, we need to pause and notice what is really going on beneath the surface. Only then will we be able to honor the longing that is asking for our attention and to find some degree of peace and well-being. Only then can we begin to make wise investment decisions.

"Do not despise the world, for the world too is God."

—Muhammad

Hooked!

Wally had grounded around his investment dilemma by the time he called me to set up an appointment. The next day, as we continued our discussion, there were several matters about which I was curious.

"Wally," I began, "you said it was your greed that got you into what you perceive as a mess with your investments. I don't see you as a greedy type!"

"After hanging up yesterday," Wally responded, "I thought more about what I had said. Greed, to me, is wanting more than I need. It's grabbing for more, thinking that getting it will somehow make my life better. At the root of it seems to be a fear that I'll somehow suffer without that extra "cushion." As I finally took an honest look at why I was avoiding our investment losses, it became obvious that I didn't want to admit that the money I thought would ensure our comfort in retirement had been reduced 30 percent. I also realized that I didn't know what we needed to retire and that the broad spectrum of "comfort" carries with it a lot of trade-offs. I do know one thing: My denial and desire to recapture my losses sure hasn't resulted in much comfort!"

"Some of God's noblest sons, I think, will be selected from those that know how to take wealth, with all its temptations, and maintain godliness therewith. It is hard to be a saint standing in a golden niche."

—Henry Ward Beecher

Wally reminded me that illusion of our ability to obtain safety and security brings with it a lot of suffering. His confession also resonated my own experience of easily getting hooked by my emotional reactions.

> *"In the Buddhist teachings, the messy emotional stuff is called klesha, which means poison. There are three main poisons: passion, aggression, and ignorance. We could talk about these in different ways—for example, we could also call them craving, aversion, and couldn't care less. Addictions of all kinds come under the category of craving, which is wanting, wanting, wanting—feeling that we have to have some kind of resolution. Aversion encompasses violence, rage, hatred, and negativity of all kinds, as well as garden-variety irritation. And ignorance? Nowadays, it's usually called denial… The pith instruction is, whatever you do, don't try and make the poisons go away. When you're trying to make them go away, you're losing your wealth along with your neurosis… These juicy emotional spots are where a warrior gains wisdom and compassion."*
>
> *—Pema Chödrön,* Comfortable with Uncertainty

Before we can shift into a relationship with money that serves our Authentic Self and helps us offer our gift to the world, we have

to practice grounding with our human tendency toward desire, aversion, and denial. Each of these poisons provide a critical entry into feeling compassion for every other human who, at one time or another, suffers in these ways as well. As I refuse to identify with the emotion as the essence of my identity, I am able to drop down into the depth of my Authentic Self where I am capable of contentment even in the midst of uncertainty. This process actually transforms the poison into medicine.

Investments and portfolio decisions easily hook us. Let's examine a few specific ways.

"The larger the income, the harder it is to live within it."

—Richard Whately

Desire

The "More Money to Spend = Better Life" Hook

There is no doubt that poverty is not fun. When there's not enough money to pay for food, shelter, health care, and basic transportation, then it is an insult to state that more money will not help improve life.

Remember in Week Five Appendix B—all those *Other Debts*?

> *"The shocking thing is that the majority of American workers, about 60 percent, earn less than $14/hour."*
>
> *—Barbara Ehrenreich,* Nickel and Dimed

We all have to ask ourselves what we can do to narrow, rather than widen, this ever-expanding gap between the *have's* and *have not's.*

A first step in that process can be to take an honest, yet gentle, look at this first poison—desire.

When we receive a raise at work or some other increase in cash flow, our automatic response is to upgrade to a nicer car, take a more expensive trip, or buy a nicer piece of furniture for the living room. We are programmed to expand our consumption to match, even exceed, our incomes. Consider a few troubling statistics and quotes compiled from the book *Affluenza,* by John De Graaf, David Wann, and Thomas H. Naylor:

- The size of our homes; 1945—750 sq. ft., 1950s—950 sq. ft., 1960s 1,100 sq. ft., 1970s—1,350 sq. ft., Today—2,300 sq. ft.
- We spend more money on restaurant food than on food we cook ourselves.

- We drive twice as much per capita as we did half a century ago and fly 25 times as much.
- The savings rate in America in the eighties was 4 percent; half of the German rate and a quarter of Japan. Now it hovers at or below 0 percent.
- "Greed is good."—Ivan Boesky
- "Advertising's most important social function is to integrate the individual into our present-day American high speed consumption economy." (quote by Pierre Martineau, *Chicago Tribune,* 1957)
- The average American will spend nearly two years of his or her life watching TV commercials. A child may see a million of them before he or she reaches the age of 20.

"No wealth can satisfy the covetous desire of wealth."

—Jeremy Taylor

"We've mutated from citizens to consumers in the last 60 years. The trouble with being consumers is that consumers have no duties or responsibilities or obligations to their fellow consumers. Citizens do. They have the obligation to care about their fellow citizens, and about the integrity of the town's environment and history."

—James Howard Kunstler, The Geography of Nowhere

"I make myself rich by making my wants few."

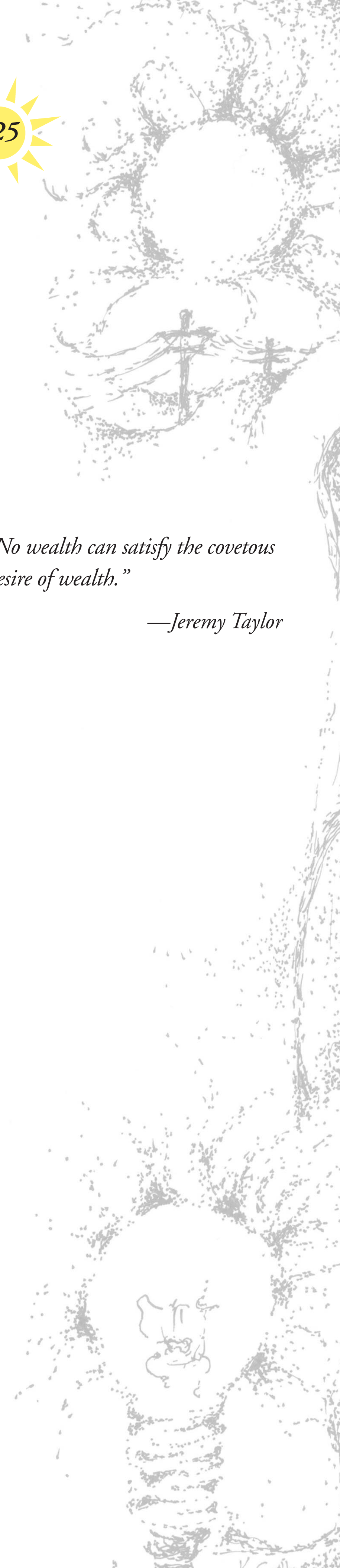
—Henry David Thoreau

It's apparent. Desire for more is deeply ingrained in us—we come by it honestly. To sustain the "good life" we must expect high returns from our investments.

Say you have $500,000 in your IRA when you reach 60. If you want that money to last for 25 years and are given the following three options, which one would you choose?

- Spend $55,084 per year by earning 10 percent with a 100 percent stock allocation.
- Spend $46,839 per year by earning 8 percent with a 60 percent stock allocation.
- Spend $39,113 per year by earning 6 percent with a 10 percent stock allocation.

Why would anyone turn down almost $16,000 per year by choosing the 10 percent stock portfolio rather than the one with 100 percent stocks?



Traditional investing wisdom says that accepting more risk is necessary if we want to achieve “the good life.” Of course “the good life” is dependent upon all the things that more money can buy. Unless you already have loads of money, there is really no better way to get from here to there than by taking more risk and making the money work harder.

“Make money your God
and it will plague you like the devil.”

—Henry Fielding

The following chart provides an example of the trade-off we take with possible return and loss of principal as the equity (stock) portion of our portfolio is adjusted.

Potential for Return and Associated Loss

Table #1

Long-term Average Return*	% Stocks	Downside Loss Probability**
9.6%	80%	-35%
9.1%	60%	-25%
8.7%	50%	-20%
7.5% (estimate.)	40%	-15%
6.9%	20%	-5%

*per AAII, “Portfolio Building,” Table 3

** per “The Intelligent Asset Allocator,” page 144

We know that the 80 percent stock portfolio is much riskier than the one with 20 percent stocks. Is the fear that we have seven times the chance of losing our investment strong enough to overcome our desire to have more money to spend? The answer may be *Yes* when the stock market is losing money, but what about when it starts to generate those double-digit annual returns? How firm will our resolve be then to stick with the lower-risk portfolio?

Desire—from Poison to Medicine

In order to free ourselves from the bondage of desire, we first have to admit the bondage exists. To pretend that we don't want more simply doubles the poison by coupling desire with denial. As we sit with our desire for more, we notice the tension in our bodies. We feel the agony of being chained to a treadmill that is constantly increasing in velocity. We admit, possibly for the first time, how very tired we are of chasing more money. In that moment we catch a glimpse of our deeper self. We know that our well-being no longer has to be linked to getting everything we want. We see that greed enslaves us by causing us to forget what is important and what it is we already possess. We begin to feel our sufficiency and temper our desires accordingly.

Author Wayne Muller was a guest on my radio show. In his book, *Sabbath: Restoring the Sacred Rhythm of Rest,* he addressed this tension between a desire for abundance and contentment with that which is sufficient:

> *"Lynn Twist is a friend who has dedicated her life to eliminating world hunger. She has traveled around the world, working on behalf of starving children. She tells me that our search for 'abundance'…is actually fed by a lingering belief in scarcity. If we are afraid there is not enough for us, we will grab for abundance—which is actually more than we need. Thus, even in abundance, there is great fear.…*
>
> *"Lynn makes a crucial distinction between abundance—a fearful response to scarcity—and sufficiency—which invokes an experience of satisfaction and well-being. Sufficiency is that moment when we have enough…The instant we have enough, dissatisfaction and desire melt away."*
>
> —*Wayne Muller,* Sabbath: Restoring the Sacred Rhythm of Rest

What is "enough"? Remember the example of Charles Gray in Week Three, how he decided to live on the World Equity Budget, consuming no more than his fair share of the world's resources? Though very few have chosen to follow Mr. Gray's courageous example of living on $99/month, thousands have taken the "road less traveled" toward a simpler lifestyle.

David Heitmiller and Jacqueline Blix, co-authors of *Getting a Life,* were living the good life back in 1990. They both had corporate jobs with great salaries and benefits and plenty of things that money could buy. One day shortly after his 45th birthday, David asked himself the question, "Is there something else I might want to do with the rest of my life?" rather than stay in a job that had become less and less fulfilling and meaningful.

"A man is rich in proportion to the number of things which he can afford to let alone."

—Henry David Thoreau

Jacqueline had also discovered that "what I was doing didn't really have much relevance in the larger scheme of things." Those questions led them to ask themselves what was really enough.

> *"You start evaluating things and becoming aware of what you're doing. What we immediately realized was that the house we were living in was too big, and we were paying way too large of a percentage of our income to support this house. Eventually. we were able to sell it. We moved into a one-bedroom apartment and lived there for a couple of years, and that gave us time to evaluate living in a smaller space, as well as how much stuff we had. Finally, we ended up with a medium solution, in about a 1,300-square-foot townhome. In this process, we decided what our needs really were."*
>
> —*Jacqueline Blix,* Money Matters Radio Show

Pause to evaluate what underlies your current investment choices as it relates to your natural desire for more money. This next worksheet will help you.

Week Six
Worksheet A
Investment Circuit Inspection

My Investments and the "More Money to Spend" Hook

Refer to the TEN WEEKS CD—"Week Six: Portfolio Analyzer" and follow the screen-by-screen instructions. Record the results of your analysis below:

Your portfolio's performance;

Year to Date __________%

Last Year __________%

Last Three Years __________%

Last Five Years __________%

? What kind of performance were you expecting? ___________%

? What was the basis for your expectation?

____

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____

? What kind of performance do you need to reach your goals?___________%

? Do you think you may have chosen different investments had you been clear about the last question before you invested?

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Your Portfolio's Risk:

From the Risk Profile section of your Portfolio Analyzer report:

? What is the Standard Deviation of your Portfolio? ____________%

Calculate the volatility (range of returns) for your portfolio:

Step 1—Your portfolio's five-year average annual return ____________%

Step 2—Add 1 times the standard deviation percentage ____________%

Step 3—Upper level of Return Range—67 percent of time ____________%

Step 4—Your portfolio's five-year average annual return ____________%

Step 5—Subtract 1 times the standard deviation percentage ____________%

Step 6—Bottom level of Return Range—67 percent of time ____________%

I would expect my portfolio's return to fall between Step 6 ____________% and Step 3 ____________% 67 percent of the time.

I *was/was not* (circle one) aware that my portfolio had the potential to vary this much in return. I understand that the negative value means that I could lose more than that percentage of my principal, or original amount invested, once every six years.

Don't worry if this is confusing right now, we'll discuss standard deviation in more detail a bit later on in this section.

? What changes, if any, would you have made in selecting your investments after completing this analysis?

____

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____

Your Portfolio's Revised Risk/Return:

? What percentage of your portfolio would you be willing to lose, referring back to Chart #1 in this section? ____________%

? What percentage of return could you expect given your willingness to risk that portion of your investment? ____________%

Please insert the TEN WEEKS CD, complete the Revised Return Analysis section, and then answer the following questions:

? What impact did this change of return have on your Authentic Money Guide scenario?

____

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____

Now, let's determine what level of spending will result in a sustainable plan. Please complete the "New Spending" Analysis Section in the Week Six TEN WEEKS CD.

? Did you have to reduce expenses to offset your projected investment return? __________ If so, how much? $____________/year.

? Knowing the impact on your spending, what feelings come up about your decision to take less risk?

____

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____

? Do you want to change your allocation to stocks, knowing what you know now?

____

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____

? What specific accounts would you adjust in order to facilitate this expense reduction should you select it as part of your final Authentic Money Guide?

____

____

____

____

If you choose to adopt these changes, please checkmark (✔) the Budget Updated column to verify that the reductions have been included in your actual budget.

Category	Expense Reduction Amount	Budget Updated

? How does it feel to adjust your spending levels rather than your rate-of-return assumptions in an effort to create a realistic and sustainable Authentic Money Guide?

____

____

____

____

? Do you feel a sense of relief or freedom in knowing how much you can really afford to spend?

____

____

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____

Aversion
The "It's All Their Fault" Hook

Investment Irritations

Investments, especially in the last three years, provide plenty of ammunition for "violence, rage, hatred, and negativity of all kinds, as well as garden-variety irritation." (Pema Chödrön) Another *klesha,* or emotional poison, is our tendency to avoid the painful, unpleasant parts of life. There is plenty of news about our investments that we would rather avoid!

"The saddest thing I can imagine is to get used to luxury."

—Charlie Chaplin

It seems like the floundering economy is the least of our worries when it comes to investment performance. Financial reporting of company earnings has fallen into disrepute amidst allegations of massive conflict of interest between auditors and their corporate clients—many of whom paid millions of dollars in consulting fees to the same accounting firms performing their "independent audit." When the basis of all investment decisions relates to company profitability and no one really has any confidence in financial reports, it is easy to get angry and upset. Consider a few headlines:

WorldCom accounting scandal.
"WorldCom, the once high-flying telecom giant, appears to be headed for more trouble, according to an exclusive report by CNBC's David Faber. The Company appears to have greatly inflated its operating earnings over the past five quarters…" (CNBC Market Dispatches)

Roots of accounting scandals lie in incentive structure, not ethics.
"Andersen's senior management seems to have revised its partners' compensation and performance evaluation to encourage them to behave more like salesmen and less like auditors, resulting in a lot of sloppy audits." (Professor Ronald A Dye, Kellogg World Alumni Magazine, *Winter 2002)*

Coupled with questionable financial statements came one news story after another about an epidemic of CEO compensation abuse schemes.

We're all paying for CEOs' greed.
*"Spring proxy statements have investors seeing red. They show that greedy CEOs took home tens of millions last year while the stocks of the companies they ran tanked. This isn't the case of a few bad apples, either—it's a fundamental reason the stock market is struggling." (*MSN Money, *Jubak's Journal)*

And if that weren't enough, May 2003 brought news of widespread conflicts of interests among the largest brokerage firms.

> **Your broker misled you.**
> *"There wasn't a wet eye in any boardroom after the news that 10 large brokerage houses will pay, collectively, $1.4 billion in fines for dishonest, double-dealing, fraudulent, counterfeit, sham, yes sham, research reports that bilked investors of billions…The fines were insignificant enough that the day following the news, Standard and Poor's reported that it was not likely to change its ratings on any of the companies charged. (www.motleyfool.com—Jeff Fischer, May 1, 2003)*

These headlines contribute to our general irritability regarding our investments. A common response these days from new clients whom I ask to gather recent investment statements is, "I haven't opened those for months. I got tired of feeling depressed for days after seeing the account value drop even further."

Beneath all these headlines lies a fundamental dilemma. It is you and I, as individual shareholders, who own these companies. It is up to us to take the responsibility to either change how the company conducts itself or sell our shares.

> *"Shareholders should start acting like the owners they are. They must make the most of the voting power that they have today while they mobilize to strengthen their rights to have a meaningful say in the companies they own."*
>
> —The Power of the Purse: How Investors Can Restore Integrity to our Financial Markets *(White Paper State of California Treasurer's Office, 2002)*

The anger and frustration we feel with our investments lies in part with our natural tendency to ignore our responsibilities. We want to participate in the benefits of corporate profitability, but we turn a deaf ear to the abhorrent corporate ethical void and the social cost many of our investments ignore. All of those decisions end up coming back to haunt us—not only economically, but also emotionally.

To ground thoroughly involves taking an honest look at what we actively support with our investment portfolio. Once this inventory is conducted, we can evaluate which investments are consistent with our Authentic Core and which are not. After an honest assessment, our decision may be to radically shift the process by which we select investments. Maybe there really is a way we can turn this poison into medicine.

Aversion: Poison to Medicine
Investing with Heart

As we take notice of our judgment, irritability, and anger, we begin to realize how much energy we lose each day to our investments. The negative energy does nothing to improve matters. Rather, it clouds our ability to see our own failure to invest responsibly. Only when we finally face ourselves can we begin to tap into the healing power of changing our old patterns of avoiding personal responsibility.

FACE YOURSELF

Now or never
Face yourself
No one else will do.
Face your weakness
Face your past
Let your scars show through.

—Michael Hedges, excerpted from the song *"Face Yourself"* from the album *"Watching My Life Go By"*

Socially responsible investing seeks to integrate our values with our need for investment return. A specialist of "socially responsible investing" (SRI), Jack Brill, co-author of *Investing with Your Values,* appeared on "Money Matters" in 2001 to talk about SRI, or what he also refers to as "natural investing." Jack shared his belief that most people want to be philanthropic and kind and to leave the world a better place for their children and future generations. These "natural" longings, he said, can be honored in each aspect of human life, including investment decision-making.

Jack reminded me that each major faith tradition emphasizes the importance of cultivating behavior that aligns with our value to "do no harm." The Golden Rule is truly a universal teaching, as illustrated in faith teachings around the world:

Christianity—*As you wish that men would do to you, do so unto them.*

Islam—*No one of you is a believer until he desires for his brother that which he desires for himself.*

Buddhism—*Hurt not others in ways that you yourself would find hurtful.*

Judaism—*What is hateful to you, do not do to your neighbor; That is the whole Torah; the rest is commentary; go, study.*

Hinduism—*Do naught unto others which would cause you pain if done to you.*

Given these spiritual directives and our "natural" tendency to want to do good rather than harm, the growth of SRI has been phenomenal. Consider these statistics from *Socially Responsible Investing*, by Amy Domini:

- In 1995, $165 billion of investments were socially screened. By 2001, that had grown to $2.343 trillion (an increase of 1,153 percent in six years).
- The growth in professionally managed assets from 1995–2001 was 184 percent—SRI managed growth for that same period was 266 percent.
- In 1999, there were 168 mutual funds for socially aware investors. By late 2001, that had grown to 230.

But what does *Socially Responsible Investing* really mean?

According to *Investing With Your Values*, by Hal Brill, Jack A. Brill, and Cliff Feigenbaum, there are four spokes on the Socially Responsible Investing Wheel:

1. *Affirmative Screening—Identify companies whose products and business policies are important to you and good for their employees, consumers, and the environment.*
2. *Avoidance Screening—Identify companies whose behaviors and products are inconsistent with your values. If you own them, sell them—if you don't own them, don't buy them.*
3. *Shareholder Activism—Encourage shareholders to take an active role as owners of their companies and actively influence corporate behavior for the good.*
4. *Community Investing—Provide financial capital to people in low-income communities at either a market or below-market rate of return. A current initiative within the SRI community has as its goal that 2 percent of all funds invested in socially screened investments be invested in Community Development Financial Institutions.*

Many advocates of SRI agree with the following comment that Jack Brill made in a reference to a "double bottom line":

> *"Screening actually eliminates potential economic disasters…the companies that are good to their employees and environmentally sensitive are actually more profitable. By taking this extra step of screening your investments, you are actually enhancing your possibilities of profit and attaining your goals—the first part of the double bottom line is economic—the second is social."*
>
> —*Jack Brill,* "Money Matters" Radio Show Interview

A mature industry has developed to honor this deep longing to integrate our values with our need for a reasonable investment return. The questions we all have about evaluating the values of our existing portfolio, as well as how to begin the process of evaluating socially screened investments, are addressed in our next Circuit Inspection worksheet. Before you begin Worksheet B, take a moment to review the following Appendix material for Week Six:

MAP 6-1, The Natural Investment Services, Inc. (NIS) Social Rating. This is the perfect place to begin to see which of the mutual funds you already own apply social screens to their stock and bond selection process. NIS, the financial consulting firm of Jack and Hal Brill, updates this analysis of current mutual funds and the extent of their screening process periodically through their webpage *www.naturalinvesting.com*. This webpage is a tremendous resource for locating specific socially responsible issues that may interest you. With over 200 web links, carefully organized under broad categories, you can use this as "home base" in learning more about SRI.

To research a specific company in which you own stock, go to *www.corpwatch.org* and enter that company's name in the "Search Corpwatch" dialog box on the home page. You can also see if your company is listed as passing the social screens of both the Calvert and Domini Socially Responsible Indexes found at *www.naturalinvesting.com.*

MAP 6-2, Socially Responsible Investing Resources provides links to SRI resources that can facilitate the implementation of a socially screened portfolio, as well as help evaluate the social impact of your current investments.

WEEK SIX
WORKSHEET B

INVESTMENT CIRCUIT INSPECTION
My Investments and the Aversion—"It's All Their Fault" Hook

? What phrase best describes your attitude about investing right now?

? Do you sense a need for any kind of change in the way you relate to your investments? If so, what kind of change?

? Are any of the mutual funds you currently own listed in MAP 6-1?
If so, which ones:

Consider the following quotation:

"We seem to have surrendered community excellence and community values in the mere accumulation of material things. The Gross National Product (GNP) counts air pollution, and ambulances to clear our highways of carnage, the destruction of the redwoods, and the death of Lake Superior. It grows with the production of napalm and missiles with nuclear warheads. Yet the GNP does not allow for the health of our children, the quality of their education, or the joy of their play. It measures neither our wit nor our courage; neither our wisdom nor our learning; neither our compassion nor our devotion to our country; it measures everything, in short, except that which makes life worthwhile; and it can tell us everything about America—except whether we are proud to be Americans."

—*Robert F. Kennedy, as quoted in* Investing With Your Values

? Do you sense that your current investment choices put more emphasis on GNP than other, less quantifiable, measures of wealth?

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Insert the TEN WEEKS CD, "Investment Research" and complete the following:

Click on your web browser and type in *www.corpwatch.org.*

? In the "Search Corpwatch" dialog box, enter the name of one of the corporations your mutual fund owns. Did anything come up in the search? If so, what did you discover?

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Select one of the funds you currently own.

Follow the screen-by-screen instructions for Week Six "Morningstar Profile" from the TEN WEEKS CD and complete the following:

Print out all four reports and answer the following questions:

Return vs. Risk—

? What does the Sharpe Ratio tell you about its risk-adjusted return?

? What does Beta tell you about its volatility given the return it earned?

Fund Holdings—

? How expensive is the stock compared to the earnings it is producing (see "Price/Earnings" ratio)?

Cost of Ownership—

? Is the annual expense ratio for this fund higher or lower than its category average?

? What is the three-, five-, or 10-year expense projection for your fund compared to the category average?

Summary

? What are the fund's two biggest strengths?

? What are the fund's two biggest weaknesses?

? Overall, how did this fund compare to its category?

Take a minute to visit *www.calvertgroup.com* and run their "Know What You Own" analyzer on this mutual fund. Refer to Week Six/Appendix B/Section 2 for detailed instructions.

Print out your analysis and place it in your My Financial Education binder under Week Six—Investment Resources.

After completing this analysis, answer the following questions:

? Have you ever analyzed a mutual fund in this detail?

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? What did you discover about your investment and yourself in the process?

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? Based on the companies and investments you own, what causes are you supporting?

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? Have you ever received a voting proxy from a company or mutual fund you own? ______________ If yes, did you vote?

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? Do you feel any differently about investing after having completed this analysis?

? Are you interested in considering Socially Responsible Investing options after what you have read and experienced?

Three-hole punch your mutual fund analysis and place it in the Week Six—Investment Resources section of your My Financial Education binder.

Ignorance and Denial

"I Don't Understand Investing" Hook

I cannot remember a client ever saying, "I love investing—it's something I understand and find very satisfying." When the topic of investing comes up, it's usually more like, "I haven't a clue as to what I'm doing. I'm happy when my investments grow and depressed when they lose value. It's an emotional roller-coaster ride that I'd just as soon live without."

If ignorance is a poison that threatens our ability to experience our Authenticity and Awaken, then we must first admit that we have taken this poison, thinking it to be medicine. We have interpreted the investing mantras, "Buy and Hold" and "Invest for the Long-term" as reasons for our denial and refusal to face what is really going on with our portfolios. Such wisdom has its place when coupled with awareness but when married to denial it can be devastating. Millions of investors routinely leave their investment statements unopened, thinking:

"Why bother opening the statements, anyway? I don't understand anything on the statement other than the 'Current Account Value' line. It seems to always be less than the prior month's balance. To be reminded of my ignorance and poor investment choices just feeds my sense of inferiority as it pertains to the investing world. To spend any more time with these statements than is absolutely necessary is like rubbing salt in my wound."

"Portion of U.S. Stock owned by the wealthiest 10 percent of Americans—90 percent."

—Harper's Index Book

Pema Chödrön reminded us at the beginning of this section, "Whatever you do, don't try to make the poisons go away." Underneath the denial and ignorance is something powerful. It takes a lot of courage—a warrior's heart—to notice when we are pretending life isn't scary and volatile. It's difficult to admit that things do not always go our way, especially when it comes to accumulating the money we anticipated would ensure our happiness.

When we access the disappointment and fear beneath the denial, we allow ourselves to feel genuine compassion for millions of others who suffer in the same way. We also find the freedom to wake up and pay attention to the issues at hand. Rather than create another form of suffering that accompanies our compulsion to fix our portfolios once and for all, we accept the reality that no perfect solution exists. Ignorance and denial begin to fade into awareness and surrender—poison to medicine once again.

"Those who have not found their true wealth, which is the radiant joy of Being and the deep, unshakable peace that comes with it, are beggars, even if they have great material wealth. They are looking outside for scraps of pleasure or fulfillment, for validation, security, or love, while they have a treasure within that not only includes all those things but is infinitely greater than anything the world can offer."

—Eckhart Tolle, "The Greatest Obstacle To Enlightenment", The Sun, *July 2002.*

If we remove all equity or stock risk from our investment portfolios by investing only in U.S. Treasury Bills and Notes, we end up with negative returns after the effect of inflation and taxes are considered. We just traded a potential risk for a certain risk!

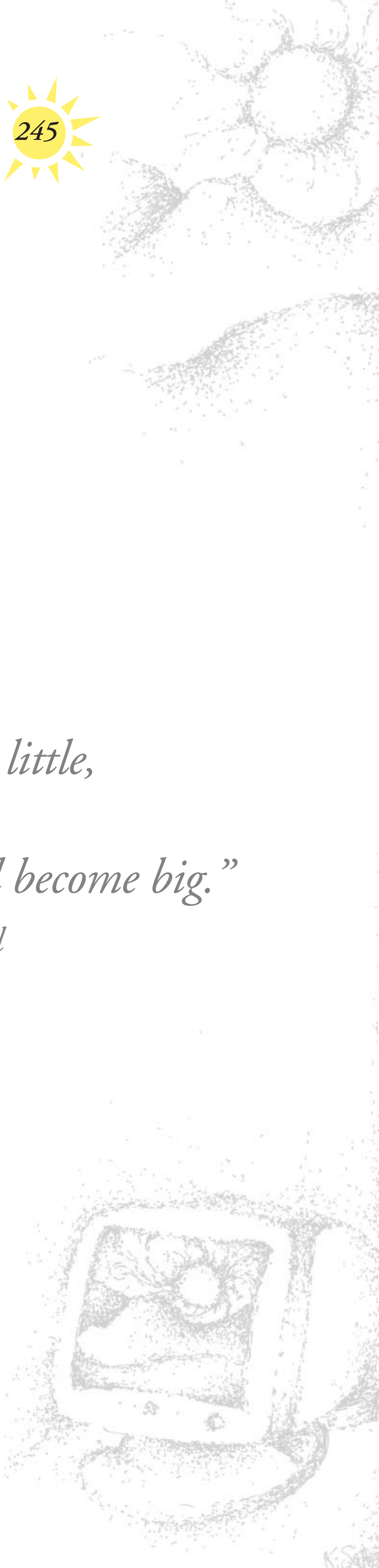
On the other hand, if we invest 80 percent in a diversified stock portfolio, we could lose 35 percent of our original investment in an effort to obtain an investment return sufficient to pay for the lifestyle we want.

Paying close attention to our investments helps us accept this normal tension in our human experience—this give and take between our need for safety as well as sufficient provision. We experience more peace and happiness in life when we're not constantly insisting there be equilibrium.

Investing—Just Use the Map!

"Learning how to invest successfully on your own is much like getting from one city to another..."

—Bill Bernstein, Intelligent Asset Allocator



Some studies suggest that most drivers, especially women, find it much easier to buy a road map when traveling in unfamiliar territory. Of course, there are many of us who think that is way too much work—it is easier to head off in the general direction and trust our instincts. When we do stop to ask directions, oftentimes we discover the person didn't really understand where we were trying to go.

Contrary to popular belief, investing is not impossible to understand. If we started with some basic principles in junior high, by the time our children graduated from high school they would know more about investing than many stockbrokers and investment professionals. I believe that, equipped with a few basic principles, you can make wise, confident investment decisions that respect your core values and personal propensity for, or aversion to, risk. The financial marketplace has a vested interest in keeping the average investor confused. In this state of affairs, you are more likely to purchase products or services that may not be in your best interest. A couple of examples illustrate the impact education of investors can have on the status quo.

"If you should put even a little on a little,
and should do this often,
soon this too would become big."

—Hesiod

During the Quicken® setup process, we encountered a screen that asked about investment fees. There were questions about "front- and back-end loads," as well as asset-based fees. If you were aware of the different fees that can be imposed by a mutual fund, you might be more inclined to research low-cost "no load" alternatives rather than purchase a fund from a commission-based broker. The investment industry wants you to be informed—just not too informed.

As an example, consider two U.S. Mid-cap Mutual Funds, Calvert Capital Accumulation Fund (CCAFX) and Vanguard Extended Market Index (VEXMX). The TEN WEEKS CD will walk you through how to perform an analysis of two funds in the Week Six—"Comparing Two Funds" section.

The Calvert Fund A shares have a front-end load of 4.75 percent of the purchase price. Thereafter, its annual expense ratio is 1.67 percent. These two expense categories result in an estimated three-

year expense of $1,003 for a $10,000 investment. Compare that with Vanguard's three-year expense projection of $80 and $701 for the category (Mid-cap Growth) average. If all other comparisons were equal, knowing this dramatic difference in fees would influence an investor's decision.

Let's consider another situation wherein your investment knowledge could make a difference in what investment options are presented to you.

What about your 401(k) investment options? Let's assume you have three domestic large-cap funds, a domestic mid-cap fund, a domestic small-cap fund, two international funds, a corporate bond fund, a government bond fund, and a high-yield bond fund as your investment options. If you chose to split your money into four equal baskets between U.S. large companies, small companies, international companies, and the high-yield bond fund, selecting the fund in each category that had generated the highest 10-year annualized return, you might feel that you had a pretty well-diversified portfolio.

If you take a closer look at your portfolio, however, you may realize that the combination of your funds leaves you with a large concentration of U.S. large-cap stocks, a smaller than expected allocation to overseas companies, and a higher than anticipated level of risk due to the risky high-yield bond choice. By paying proper attention, you discovered weaknesses that could have increased your overall risk and lessened your potential for return.

Your awareness could also serve as a platform to request suggested portfolio allocations from your 401(k) provider—for investors with varying degrees of risk tolerance. The fund sponsor is finally expected to assume a higher level of responsibility than they had prior to your informed discovery. Your "squeaky wheel" could result in a change that will make it much easier for you to keep your investment 401(k) accounts properly allocated, as well as protect your co-workers who have yet to learn the importance of proper asset allocation.

So, how does an individual investor navigate the maze of investment decisions and restore some awareness and sanity to this aspect of their financial lives? The acronym *SANE* helps me remember the essentials of investing:

S **Slow** Down and Understand Investing

A **Appreciate** the Risk/Reward Relationship

N **Notice** the Whole Is Greater than the Sum of Its Parts

E **Examine** the Cash Flow Needs of your Authentic Money Guide and Invest Accordingly

SANE Investing—There Is a Different Way!

Life is Just a Bowl of Cherries

…so keep repeating

It's the berries,

The strongest folk must fall

The sweet things in life

To you were just loaned.

So how can you lose

What you never owned...

—Fosse

I was honored to have Dr. William "Bill" Bernstein as a guest on my radio show. Dr. Bernstein wrote, *The Intelligent Asset Allocator—How to Build Your Portfolio to Maximize Returns and Minimize Risk* as well as *The Four Pillars of Investing.* The essence of Dr. Bernstein's investment wisdom can be captured in those two words: "Sane Investing." Let's examine each of the four components to his investment approach.

SLOW DOWN *and Understand Investing*

"The very first thing that you want to do, the very first signpost on the road that you want to pass, is simply to do nothing. You want to take a deep breath and don't do anything because the worse thing that you could possibly do is to radically alter your finances without doing a proper amount of study and work…the time you take to learn and plan is going to be well spent."

—Dr. Bill Bernstein, "Money Matters" Radio Show Interview

We get better at things when we practice. So far in TEN WEEKS, you have set up your investment accounts for online updates so you will know where you stand every day. You have done some preliminary analysis of your existing portfolio, as well as practiced some mutual fund analysis skills. These hands-on exercises, coupled with some basic understanding, will prepare you for specific action with your investments—but first it is critical to take the time to understand the basics of investing.

When you feel a compulsion to leave before you stay and bypass the wisdom that can only come through "grounding," remember Dr. Bernstein's wise words: "take a deep breath." You work hard for the money you invest. Until you understand investing, it is better to leave your money under the mattress. So slow down and give some attention to investing. Ask questions.

One question immediately comes to mind: What makes investing so different from saving?

Saving might be illustrated by the purchase of a Certificate of Deposit (C.D.) from a bank. You enter into a contract with the bank that says you provide $10,000, and in five years the bank will pay you $11,593, assuming a 3 percent reinvested interest rate.

If the bank gets into trouble, most likely you will get your $10,000 back, since the Federal Deposit Insurance Corporation promises to return your money. The essence of saving is that there is very little risk that you won't get back your original investment.

It is important to notice that saving involves taking risk. In an inflationary environment, your $10,000 will be worth less in three years than it was when you gave it to the banker. After paying tax on the interest earned, you'll have even that much less to offset the effects of inflation.

Investing, on the other hand, makes no guarantee that your original investment will be returned to you. In simple terms, it's like your friend Joe asking you to become an investor in Joe's Bar and Grill, his new enterprise. He pulls out some grease-stained financial projections that indicate your share of the profits should amount to $2,500 per year—all on an original investment of $10,000. There's no guarantee, however, of getting back your money, much less the 25 percent projected return.

But you believe in Joe and his idea. Sure enough, the restaurant is a hit. Five years later, you want to evaluate your investment. Joe has a little extra cash and is willing to buy back your shares.

Investing, you realize, means that you have to be able to evaluate what happened both financially and emotionally with you and your money.

Going back through your records, you write down the checks you received the first of each March. You make note of what emotions you experienced when the checks arrived (or failed to arrive) each year:

Joe's Bar and Grill $10,000 Investment Ledger

Year	$ Received <Invested>	What I Felt
1998	<$10,000>	This is great—where else can I get a 25 percent return!
1998	$1,200	What about the $2500?
1999	$0	Oh no, it's all gone!
2000	$1,800	Now I'm only $4,500 behind where I was supposed to be!
2001	$3,000	Finally, a bit more than I was promised but still $4,000 behind
2002	$2,000	Not out of the hole yet!
2002	$10,000	If I decide to 'cash out'
Total	**$8,000**	A lot of worry and lost energy!

You can see that life got quite a bit more complicated with Joe than with the bank C.D.—but you also made more money. Was the extra money worth "investing" rather than just "saving"? That leads us into the next phase of SANE investing.

APPRECIATE the Risk/Reward Relationship

"The second thing you do is you have to acquire an appreciation of the fundamental relationship between risk and return in the capital markets…if you want high returns you're going to have to take a lot of risks."

—*Dr. Bill Bernstein,* "Money Matters" Radio Show Interview

If the second aspect of restoring some sanity to our investment responsibilities is to understand the interplay between risk and reward, another question immediately pops up: How do we calculate *return*?

Investment Return

Going back to Joe and the cash flow stream from his business, your average return would be 16 percent, calculated by taking the total cash payments divided by the number of years the money was invested. This average annual return would then be divided by the original investment to arrive at the average return percentage.

As you can see, *average annual return* can be misleading. You didn't receive $1,600 per year ($10,000 x the average annual return of 16 percent)—it was paid to you in differing amounts and times, thus affecting the true annualized rate of return.

To calculate the more accurate *annualized rate of return*, which is the return rate you earned considering the timing of your dividends and final payback of your loan, you would need a financial calculator, like the Texas Instruments BA-35. Look up the annuity calculation instructions, and within no time you will know how your investments are really performing. If you decided to take your $10,000 back in 2002, the overall annualized rate of return would amount to 14.75 percent. That's a far cry from the 25 percent that Joe promised initially—but a lot better than losing your whole $10,000!

Investment Risk

Now you have a clear picture of the "return" side of your investment with Joe. But what about the other side—"risk"? The variability of returns can be analyzed and a statistic, referred to as "standard deviation," can be calculated. Standard deviation comes from the concept of "scatter." The more scattered or varied the returns are for a particular investment, the higher the standard deviation and the greater the risk. Using the same financial calculator, we entered each annual cash flow's return as follows:

Year	% Return for that Year
1998	12%
1999	0%
2000	18%
2001	30%
2002	20%

The average of those returns (added up and divided by 5) = 16 percent.

The calculator tells us that the standard deviation for this investment was 11 percent.

In his book, *The Intelligent Asset Allocator,* Dr. Bernstein illustrates this rather difficult concept:

> *"What does the standard deviation number really mean? It means that two-thirds of the time the annual return of the asset will lie between one standard deviation above and one standard deviation below the mean (average) value…Let's assume you are considering a Latin American stock fund with an expected return of 15 percent and a very high standard deviation of 35 percent. This tells you to expect a loss of 20 percent (15 percent–35 percent) or worse every six years(*), a loss of worse than 55 percent (15 percent-70 percent) every 44 years(**), and a loss of 90 percent(15 percent–105 percent) every 740 years(***). (Reprinted with permission of The McGraw-Hill Companies. William J. Bernstein,* The Intelligent Asset Allocator*, © 2001 The McGraw-Hill Companies, Inc.)*

* Out of a six-year period, one year we might achieve more than a 50 percent return and one year more than a 20 percent loss. The remaining four out of six yearly returns (66 percent of the time) should fall between those two extremes.

** Out of a 44-year period, one year we might achieve more than an 85 percent return and one year a loss of 55 percent or more. The remaining 42 out of 44 yearly returns (95 percent of the time) should fall between those extremes.

*** Out of a 740-year period, one year we might achieve more than a 120 percent return and one year a loss of 90 percent or more. The remaining 738 out of 740 yearly returns (99 percent of the time) should fall between those extremes.

Can you begin to see how critical it is to evaluate investments in light of their volatility and not just their performance?

Now, with these two performance numbers—Return of 14.75 percent and Standard Deviation of 11 percent—you have what you need to shop around and see if you want to leave your money with Joe or take it and invest it elsewhere. Take a minute to compare your investment with alternatives listed below. These returns are reflective of performance from 1926–1998 (*The Intelligent Asset Allocator*).

Table 2

Investment	Return	Risk = Std. Deviation
30-day T Bills	3.77%	3.22%
Five-Year Treasuries	5.31%	5.71%
20-Year Treasuries	5.34%	9.21%
Large Stocks	11.22%	20.26%
Small Stocks	12.18%	38.09%

After comparing your investment with Table 2, it seems like you did pretty well. You achieved a higher return than had you invested

in small stocks at less than one-third of the risk for that asset class. Before you get too excited and run out and invest another $10,000 with Joe, consider two more issues: liquidity and stability/reliability of long-term returns.

Investment History

How were the payments you received from Joe determined? Did he take a large salary or draw from the business that prevented him from paying you the 25 percent he originally promised. Privately held companies, like Joe's Bar and Grill, that do not sell their shares to the general public over a stock exchange, are different than publicly traded ones. Publicly traded companies are supposed to abide by a host of security laws that help protect the individual investor. This helps you and me make informed decisions about companies in which we might invest. Had you been the shareholder of a publicly held company, you could have determined what management decisions affected your dividend. You could also analyze audited financial statements (or run a *Morningstar* analysis) to see how the company's financial position has changed over a longer period of time. It's doubtful that Joe has a set of audited financial statements that allows you to see how secure your investment is, and the fact that he has been in business only five years adds another level of risk as well.

Investment Liquidity

The other feature of owning a publicly traded security is your ability to liquidate, or sell it, in a very short period of time. Even though you may get only a portion of your money back, you still have the freedom to cash it in. We all know, however, that even publicly traded companies can go bankrupt and then your ability to sell your shares in the open market is of no help. When you think about it, Joe's willingness to pay you back now may not be replicated anytime soon. Your investment is liquid only to the extent that you act now.

As compared to investing in a stock of a publicly traded company, how much extra return should you expect for assuming these extra risks? A conservative estimate would be at least 20–40 percent. All of a sudden the 14.7 percent annualized return looks pretty marginal considering what risks are involved.

Given all this information, you decide it's time to take your $10,000 and find an investment that has a better risk/return balance.

Let's take a minute to return to Quicken® and evaluate the risk/return mix of your existing portfolio.

Week Six
Worksheet C
Investment Circuit Inspection

Appreciating My Own Risk/Return Mix

Please insert your Week Six TEN WEEKS CD, "Asset Allocation Guide" and complete the following information:

Return _________%

Std. Deviation _________%

Write down one of your investment accounts ("Ginger's Investment AC"), or a category of investments ("Ginger's Retirement Accounts"):

____

Find the model portfolio which best fits your time horizon* for the above account or category. _________ yrs.

*Time horizon simply asks the question: How long will it be before you need some or all of this money?

Refer to Table 3 below and complete the following:

The largest loss I can tolerate for this account is _________%

The portfolio associated with this loss has _________% invested in stocks.

The time horizon associated with this loss, per Table 3, is ___________years, which is/is not (circle one) consistent with the time horizon noted above.

If the time horizon is not consistent, then I choose to select a portfolio with a __________% loss potential and a ___________% stock allocation.

(Use your historical experience with the 2000–2003 bear "loss" market to honestly evaluate your tolerance for loss. If you weren't comfortable losing 37 percent in actuality, don't select the 83 percent stock allocation portfolio now, even though you have more than nine years to invest.)

Table 3 is derived from Quicken®'s 2003 Deluxe's model portfolio ranges (available at press time). My professional recommendation is to ratchet down the expected return by 1 percent for each line and adjust the time horizon years. I have adjusted the chart accordingly.

Table 3

Exp. Return	Time Horizon	Std. Dev.	Stock/bond	% Portfolio	Loss *
6%-1%=5%	3 yrs.	2.5%	16%–84%	A	5%
7%-1%=6%	3 yrs. +1=4	4.7%	32%–68%	B	10%
8%-1%=7%	3 yrs. +2=5	6.9%	47%–53%	C	20%
9%-1%=8%	5 yrs.+2=7	9.4%	64%–36%	D	27%
10%-1%=9%	7 yrs.+2=9	11.8%	83%–17%	E	37%

*Estimated loss exposure for stock allocation per Table 1.

Consider Dr. Bernstein's recommendations in selecting the portion of your portfolio invested in stocks (*Intelligent Asset Allocator*):

1. Start by referring to Table 1. Select the largest annual portfolio loss you are willing to tolerate. The above table includes similar percentages in the last column.
2. Adjust your stock allocation downward from the first step if your time horizon multiplied by 10 is lower. For example, if you need the money under consideration in five years, your maximum stock allocation should be no greater than 50 percent (five years x 10 percent/year stock allocation).
3. **Circle the portfolio from Table 3 that satisfies both your tolerance for loss as well as your investment time horizon.**

Return to Week Six, **Worksheet A—My Investments and the *More Money to Spend Hook.***

? What was your Revised Rate of Return? ______________%

? How did that affect your lifestyle expenses?

____

____

? Does your rate of return answer in Worksheet A differ from the portfolio you circled above?_______________

? If there is a difference, what do you feel changed in your decision-making process?

____

____

____

Before you finalize how much you'll invest in stocks and bonds, let's discuss Asset Allocation.

NOTICE the Whole Is Greater Than the Sum of Its Parts

> *"The fourth thing you have to do is to appreciate that a diversified portfolio of many different asset classes (many different kinds of stocks, many different kinds of bonds) behaves in a way that is very counter-intuitive (i.e., sometimes adding a volatile investment class can actually lower the risk of the entire portfolio).*
>
> *"It's as if you make a cake with shortening, flour, butter, and sugar—none of those things taste very good at all on their own—but together they taste quite wonderful. So the behavior of the whole is very, very different than that of the ingredients. And this is called Portfolio Theory, and it's absolutely critical to your success as an investor."*
>
> —*Dr. Bill Bernstein,* "Money Matters" Radio Show Interview

Not only do we like cake a lot better than any of its separate ingredients alone, we like what happens when we invest using the principles of asset allocation.

Lack of Correlation is the Key

The magic of asset allocation lies not only in the principle of diversification—"Don't put all your eggs in one basket"—but especially in the power of "negative correlation," or what I refer to as "chicks and calves."

If I were a farmer, I'd just as soon not have my entire livelihood depend on the power staying on all winter and the warming lights hatching my new chicks. It would be nice if I also had a few cows that were ready to calve naturally. These two birthing processes are unrelated, or negatively correlated. A diversified farmer might raise cows and sheep because the birthing processes are similar, or related. An uncorrelated farmer then would raise cows and chickens. It may not have been until the power went out that the "chicks and calves" farmer appreciated the benefits of linking negative correlation with diversification.

When one of my asset class investments behave differently from another of my asset classes (when one is profitable, the other is not) it actually helps to increase my overall return and reduce my overall

risk. A particular investment's correlation to the Standard and Poors' 500 stock index is quantified by a statistic, R2 (R squared), the correlation coefficient. A value of 1 means that this particular investment vehicle behaves exactly like the S&P 500—perfectly correlated. A value of –1 indicates the opposite—they move in exact opposition. (We know when a number is squared, its result is always positive, so the correlation coefficient is always a positive number between 0 and 1.) It makes sense to combine asset classes that have a low correlation coefficient.

Asset Allocation and Investment Attention

Studies have shown that asset allocation accounts for the majority of an investment portfolio's return. Once you have chosen a portfolio that honors your investment time horizon, tolerance for loss, and social parameters, you don't have to worry about finding the perfect mix of asset classes. What is most important is sticking to the allocations, with minor adjustments, over time.

There are several benefits of using asset allocation as a vehicle for giving your investments your attention rather than your energy.

- First, you don't have to worry about picking the right stocks and then buying and selling them at the right time. That would be as absurd as pulling the cake out of the oven every five minutes and adding something to the mix. Once you combine the ingredients, the best thing you can do is let the cake bake. We have learned that the financial markets are much smarter than even the most adept money managers. It's a lot of wasted effort to pretend differently.
- Second, you don't need to agonize over how to invest new money or keep your portfolio balanced. It's as easy as following the instructions in the cookbook for that cake. There are even cake mixes for those of us who have trouble measuring ingredients.

You can also use a "box mix" for your portfolio by following predetermined asset allocations, or "model portfolios," suggested by Quicken®, *The Four Pillars of Investing*—the book by William J. Bernstein, and various Socially Responsible Investment companies.

At least once each year, the portfolio is rebalanced by adjusting the holdings in each asset class to its targeted allocation. We will illustrate this in the next Worksheet and TEN WEEKS CD lesson.

It's a Rebalancing Act

> *"To get back to equal weighting, what you've got to do is sell the best ones, sell the best performing ones, and use the proceeds from those sales, to buy the ones that have performed the worst. It's a way of forcing yourself to sell high and buy low."*
>
> —*Dr. Bill Bernstein,* "Money Matters" Radio Show Interview

The reason rebalancing works is it keeps our overall allocation percentages in line, rather than letting our emotions dictate our investment decisions. If I have set my international stock percentage at 10 percent and it now only occupies 5 percent of my portfolio, then I am forced to buy more of it when its price is lower than when I would normally buy it.

Index Funds—You Only Need a Few

Investment choices are simplified dramatically through the use of index funds that track each chosen asset class. Consider the following chart that lists Vanguard Index funds that cover the major asset classes:

Table 4

Vanguard Fund	Index	Asset Class	Expense Ratio	Taxable or Retirement
500 Index	S&P 500	U.S. Large Co.	.18%	Both
Value Index	Barra Value	Lg.-cap Value	.22%	Retirement
Growth Index	Barra Growth	Lg.-cap Growth	.22%	Both
Extended Mkt.	Wilshire 4500	U.S. Mid/Small Co.	.25%	Retirement
Small-cap Value	S&P600SC	Small-cap Val.	.27%	Retirement
Small-cap Growth	SP 600 SC	Small-cap Grth	.27%	Retirement
REIT Index	Morg. St. REIT	Real Estate	.33%	Retirement
Emerging Mkts.	MSCI-EAFE Emg. Mkt.	Em Mkt. Intl.	.58%	Both
Developed Mkts.	MSCI-EAFE	Europe/Pacific	.32%	Taxable
Infl. Prot. Secur.	NA	Govt. Bonds	.25%	Retirement
GNMA	NA	Govt. Mortgage	.27%	Retirement
Total Bond	Lehman Agg.	Total Bond	.22%	Retirement

"Consider the little mouse, how wise an animal it is which never entrusts its life to one hole only."

—Plautus

Narrowing the field from almost 9,000 funds to 12 makes it easier to tackle this task of choosing funds to build your portfolio.

Expenses and Taxes—More Important Than You Think!

Last, reduction of annual expense fees and unnecessary income tax consequences can be easily accomplished through index funds.

The annual expense ratio for the majority of the index funds just listed is .25 percent. (On a $10,000 investment account, $250 would be paid annually for investment fees. The typical mutual fund averages between 1–1.5 percent annual expenses. The difference in fees alone can account for a 10-15 percent increase in annualized return on a 7 percent portfolio.

The chart on the previous page indicates which funds are best suited for "taxable accounts." All funds are candidates for retirement accounts since there are no immediate tax consequences for such transactions as dividends and purchases and sales of stocks within the fund (turnover). On the other hand, when one of the listed funds is held in a "taxable" or nonretirement account, these transactions trigger a tax bill. Let me explain:

All current tax consequences are tax-sheltered in a retirement account—no taxes are due on any income or gains until monies are withdrawn from the account. At the time of withdrawal, all distributions are taxable.

The unwary investor has most likely been "bitten" by the mutual fund "tax snake." It is not uncommon for a mutual fund shareholder to feel ill when he/she receives a 1099 at the end of the year from his/her mutual fund company that results in thousands of dollars of income tax—all in a year in which the value of their mutual fund dropped! It is important that mutual funds with high turnover (lots of purchases and sales) be placed in retirement accounts, as well as those that pay out larger dividends. Table 4 indicates how to avoid this problem by selecting which funds go in taxable and retirement accounts.

Now it is time to go take some of this theory and apply it to your investments! Insert your TEN WEEKS CD and complete the next Worksheet.

Week Six Worksheet D
Investment Circuit Inspection

Asset Allocation—Giving My Portfolio My Attention

Insert the TEN WEEKS CD, find the section entitled Week Six—"Be Smart About Your Target," open up each of the dialogue boxes, and then print the list as well as the Helpful Hints listed on the TEN WEEKS CD. File these reports in your My Financial Education binder under the Week Six Investment Tab.

EXAMINE The Cash Flow Needs of Your Authentic Money Guide and Invest Accordingly

Cash Flow—The Key to a Cohesive Portfolio and Financial Plan

The last step from darkness (or at least dusk) into some light with our investments is to test some of the initial asset allocations we have selected in Quicken®. We will do that by making sure the investment time horizon, or period of time we can leave the money alone before beginning distributions, is consistent with our most recent Authentic Money scenario.

This process of linking the myriad financial details together in one cohesive plan lies at the core of the power of comprehensive financial planning. A certain portfolio composition may seem very reasonable when it is considered separate from other important financial considerations and yet quite unsuitable when looked at as just one "room" in the financial "house."

Even though the focus of our attention will now turn to how the cash flows of your investments align with your Authentic Money Guide, remember that the real challenge is to integrate and honor your core Authenticity with the choices that we have outlined thus far in Week Six:

- Spending (and the level of return you need)
- Shareholder participation (and the types of investments you support)
- Informed decision-making (and the ability to know why you invest as you do)

Week Six
Worksheet E
Investment Circuit Inspection

Investments Integrated with the Rest of My Life

Please insert the TEN WEEKS CD and learn how to integrate your portfolio with your Authentic Money Guide. Start with Week Six, "Plan Cash Flow."

In the Portfolio Value Section, circle the withdrawals from either the Taxable or Tax-deferred accounts and make a note of it. This is the first year that the investments will be relied upon to meet the cash flow requirements of your Authentic Money Guide.

Plan Scenario #	Year	Account Withdrawals	Retirement or Taxable

? What is the length of time between your current plan date and this first year of withdrawals? __________ years.

For Greg and Ginger, the length of time is 12 years (2015–2003).

Since the 12-year investment time horizon is much greater than the seven years that we used to design their investment portfolio, we know that the portfolio is consistent with the needs of their Authentic Money Guide.

IT IS CRITICALLY IMPORTANT THAT THIS TEST BE RUN EACH TIME THERE IS A SIGNIFICANT CHANGE IN EITHER THE PLAN ASSUMPTIONS OR THE DESIGN OF THE INVESTMENT PORTFOLIO.

FAILURE TO TIE THE INVESTMENT PORTFOLIO TO CASH FLOW NEEDS CAN RESULT IN EXPERIENCING SEVERE LOSSES AND PENALTIES FROM HAVING TO LIQUIDATE OR SELL INVESTMENTS TO MEET LIFESTYLE CASH FLOW REQUIREMENTS.

Now, pause to think a few minutes about what you have done.

? What changed in your Authentic Money Guide as you completed this section?

Investment Return: From_______% to_______%.

Living Expenses: From $_____________ per year to $____________ per year.

Income: From $_____________ per year to $____________ per year.

Other:

____

____

____

____

? Do you notice any patterns in your choices?

____

____

____

____

? Are those patterns leading you closer to or further away from your Authenticity? How?

____

____

____

____

Now is a good time to go back and make any changes to your most recent Authentic Money Guide scenario that honor what you just paused to notice.

Investment Implementation

I recommend you wait to finalize the selection of actual investments and finish the rebalancing of each of your individual investment accounts.

Until you finish the TEN WEEKS program, you will have gaps in your Authentic Money Guide that can distort your cash flows. For example, in Week Seven, you will analyze your insurance needs and may discover your cash flow needs change. This change may affect which investment portfolio is suitable for you.

At this point, our discussion will help prepare you for the time when your Authentic Money Guide accurately reflects the cash flow ramifications of all the decisions you have made and you are ready to choose the actual investments to be held in your new portfolios.

Before beginning this Week's final worksheet on Investment Implementation, consider the MAP materials outlined below.

As an alternative to these resources, set aside one hour to read "Investing Basics" at *www.Quicken.com*. To get to this section:

- Go to *www.Quicken.com*
- Select "Quicken® Brokerage"
- Click on the "Planning and Tax" Tab
- Select "Investing Basics" from the "Investing Education" section.
- Print out the "Introduction to Investing" report. After reading it, file this report in your "My Financial Education" binder under your "Investment Resources" Tab.

Take a moment to review the following MAP (Money Attention Pages) documents:

MAP 6-3—Index of the Indexes explains five common stock indexes and which companies are represented. A basic understanding of these common standards of comparison (benchmarks) for different asset classes (large, medium-sized, and small) of U.S. stocks is essential in purchasing suitable index funds for a diversified portfolio of investments. Please see Week Six Table 4 for other index categories.

MAP 6-4—Many Faces of Risk outlines nine different kinds of risk an investor must consider when selecting investments. One measure of risk is how variable an asset class' returns are over different period of times. The Compound Annual Rates of Return by Decade chart reflects the greater risk in Small Company stocks (<4.5 percent> to 20.7 percent) as compared to Large Company stocks (<.1 percent> to 19.4 percent) as well as Treasury Bills (.4 percent to 8.9 percent).

MAP 6-5—Mutual Fund Investing. This document explains the various categories of mutual funds available to investors. "Share price appreciation" refers to an increase in the value of the fund's stock investments over time, whereas "income and price stability" refers to a fund's bond holdings.

Please read carefully the "Factors to Consider Before Investing" section. The TEN WEEKS CD provides instruction as to how to evaluate a fund using these criteria.

Note also the warning about purchasing a mutual fund before it makes its annual capital gains distribution in November/December of each year. The negative tax consequences would only apply to investment accounts that are not tax sheltered (nonretirement accounts.)

MAP 6-6—Types of Bonds. Bonds are essentially an IOU. The issuer owes the money to the holder of the bond and promises to pay the money borrowed in addition to a certain rate of interest. Bonds vary dramatically in terms of safety, with Treasury Notes and Bonds being the safest and unsecured, high-yield Corporate bonds being the most risky. Refer to MAP 6-4 for an explanation of risk. Also read the following explanation of the difference in risk to an investor in purchasing bonds directly or through a mutual fund.

The value of a mutual fund will vary every business day. For all funds except the most liquid, such as money market funds, there will be a potential for some gain or loss depending on market conditions.

Consider the U.S. Savings Bond Considerations section of MAP 6-6. If you hold U.S. Savings Bonds, I strongly recommend you order an analysis of those bonds from the Savings Bond Informer (800-927-1901). If you own fewer than 10 U.S. Savings Bonds, the report will cost only $15 and will tell you when to sell the bonds you own as interest rates fluctuate.

If you want to avoid any analysis fees, you can go to *www.app.ny.frb.org/sbr*, type in the face value and issue date of your bond, and the current redemption value will be computed. This will not provide, however, an analysis of when interest rates may change on your bond, as does the Savings Bond Informer report.

MAP 6-7—Treasury Inflation Protection Securities (TIPS). TIPS provide an valuable addition to portfolios because of their inflation-protection feature. If an investor purchases a TIPS with a 2 percent real return, and inflation is 3 percent, the nominal return is 5 percent. Should inflation rise to 5 percent, the nominal return increases to 7 percent. Since the underlying bond is issued by the U.S. Treasury, and they have the authority to print more money, technically there is no safer investment.

TIPS can be purchased either directly or through a mutual fund. The Vanguard TIPS fund (VIPSX) offers investors the option of being paid both the interest and inflation-adjusted principal amount as a cash distribution. Direct TIPS purchases have restrictions about cash payouts.

MAP 6-8—Bonds 101. Read this material for a concise explanation of how bonds can change in value. Also consider the following example;

Say Greg wants to buy $10,000 of five-year U.S. Treasury Notes, and he is able to purchase them at that face value. As long as he holds those bills until they mature five years later, he can be reasonably certain he will get his $10,000 back, as well as the stated interest rate for that period of time.

Alternatively, Greg could have taken the $10,000 and purchased a mutual fund that invests in short–intermediate-term Treasuries. If Greg sells all the shares of this fund five years from now, he may get more or less than his $10,000 and accumulated interest, depending on the market price for the shares of the fund on the day he sold. In general, Greg takes the risk that increasing interest rates will cause the value of his shares to drop. The shorter the duration (average maturities of the bonds held in the fund) of the bond fund, the less risk he takes that the value of his shares will fall significantly.

On the other hand, a bond fund is able to buy in quantities that result in higher yields for their shareholders. Certain bond funds can reduce risk by investing in hundreds of issues, whereas an individual bond holder takes greater risk of default. For this reason, it is important to understand that a bond mutual fund purchase and an individual bond purchase each have unique risks that must be considered.

MAP 6-9—Bond Maturity and Duration. How can two bonds that mature on the same day (and issued on the same day) have a different duration? Read this resource to find out and prevent yourself from making common mistakes with bond purchases.

MAP 6-10—Categories of Equity Investments Helps to Differentiate Between Stocks. Remember, a stock represents your ownership interest in a company, whereas a bond indicates that the company has simply borrowed money from you. Stocks historically have rewarded investors for the extra risk they have taken with higher returns than bonds, but the excess earnings over bonds, referred to as the equity risk premium is shrinking. Just keep in mind that common-stock shareholders in a company are the last to get paid when financial difficulties beset a company.

MAP 6-11—Advantages and Disadvantages of Investing in Real Estate. Many clients ask about investing in real estate instead of the stock market. Recent real-estate returns have enticed many investors to direct their investments into this asset-class.

This Money Attention Page reminds us that there are definite advantages and disadvantages to real estate investing. The comment about "opportunities for investments highly leverged with nonrecourse debt because of real estate's value as security for loans" simply means that you can purchase real estate with 20–30 percent cash downpayment and use the value of the property to borrow the rest of the money—hopefully without having to pledge your personal assets. Over a 15–30 year period, income from the real estate investment pays off the bank loan and you end up with an asset that pays you a nice monthly income.

When evaluating a real estate investment opportunity, I have found a "1 percent of purchase price per month" rule of thumb to be useful. This rule is applied as follows:

A residential rental property is for sale in my hometown for $95,000. It is currently rented for $950/month and is in excellent condition. The vacancy history for this property is excellent (it has always stayed rented) and a property manager charges only 5 percent of gross rents as a management fee. My rule of thumb test is met in that the $950/month rent is 1 percent of the purchase price.

Even though I would be responsible for property taxes, insurance, repairs, and management fees, the net cash flows result in a 9 percent return. If the property appreciates at 2–3 percent per year, the overall return of 11–12 percent is attractive, despite some of the disadvantages of investing in real estate outlined in MAP 6-10.

MAP 6-12—Real Estate Investment Trust. An excellent way to invest in real estate without all of the hassles and risks of direct ownership is to purchase shares in a Real Estate Investment Trust. Read this Money Attention Page for additional information and consider the Vanguard REIT Index outlined in Week Six

MAP 6-13—The Key to Investing—Invest! We all know how powerful compounding is in accumulating money. This page illustrates this truth.

The last chart illustrates the growth of various levels of monthly savings for a seventh grader. What other advantages are there to a seventh grader of saving $50/month besides accumulating $509,157 by the time he/she is 65? What a wonderful gift to help our youth turn investment poison into medicine early in life by sharing the "rest of the story" (Paul Harvey) about Authentic Investing!

MAP 6-14—What Are Mutual Fund Sales Charges and Loads? The Ten Weeks CD covers some of this material. When a mutual fund name is followed by an A, B, or C, it indicates that there is a sales fee imposed on the purchase of the fund.

Exercise caution when a broker tells you that a B-Share fund has no up-front sales charge. Technically this is true, but ask the broker to explain the difference in the annual expense ratio between an A-Share and the B-share. Also ask how long you have to own the fund before you are no longer obligated to pay a "deferred sales charge"?

MAP 6-15—What Are Mutual Fund Annual Operating Expenses? Even mutual funds that invest according to a specific index without trying to select specific stocks or bonds have small annual expenses. For example, most Vanguard index funds have annual expense ratios of approximately .25 percent. Be aware that a mutual fund with a 1.5 percent annual expense ratio consumes 21 percent of an investors return, assuming an annual return of 7 percent. The index fund would consume only 3.5 percent of that same return.

MAP 6-16—Comparing Index Funds and Actively Managed Funds. For a concise explanation of passive vs. active investing, read this Money Attention Page. You will remember earlier in the chapter that the S&P 500 Index outperformed 75 percent of professional money managers from 1973–1992.

MAP 6-17—Comparing Variable Annuities and Mutual Funds. Annuities are a popular investment vehicle with much of the investment community because they pay hefty commissions. These commissions result in higher annual expenses, however, and lower returns for the same level of risk with a mutual fund investment. Review Bill Bernstein's comments about Variable

Annuities earlier in this chapter. I recommend you seriously consider consulting a TEN WEEKS financial advisor if you own annuities.

MAP 6-18—Dollar-Cost Averaging and Dividend Reinvestment Plans. Since it is impossible to time the stock and bond markets (i.e., purchase when values are low and sell when values are high on a consistent basis), it makes sense to invest on a regular time-schedule. This page illustrates the power of this discipline in enhancing returns without increasing risk.

Dividend Reinvestment Plans work not only with direct stock ownership but also with mutual fund shares. Take a few minutes to verify with your mutual fund company that you have chosen to reinvest all dividends and capital gains distributions.

MAP 6-19—Glossary of Investment Terms. This is an excellent resource to help you demystify investing. Take back your ability to understand investing by referring to these definitions when you are confused by the terminology.

WEEK SIX
WORKSHEET F

Investment Circuit Inspection

Investments—Intent to Action

Insert the TEN WEEKS CD and follow the Investment Implementation Steps.

Use this outline to summarize your implementation decisions.

STEP 1

Check to See that Actual Spending Aligns with Current Authentic Money Guide Assumptions.

- Compare actual income and expenses to those budgeted. Is there significant excess in actual expenses over the budget? If so, please calculate the following estimated annual adjustment as follows:
- Total expenses over budget* $______________

**Overall Total at bottom of page 2 "Difference" column.*

- Annual variance = Total variance divided by the # months reported on the budget report = monthly variance x 12 months = annualized variance $_______________

In order to reconcile this difference in budget to actual cash flows, specifically how do you plan to adjust one, or both, of the following?

Adjustment to Plan Expense Assumptions_________________________________

and/or

Adjustment to Budget_____________________________________

STEP 2:

Calculate targeted emergency cash funds and required monthly savings.

A. Determine Your "Rainy Day" or Emergency Cash Reserve Fund:

Total Expenses per *Plan Summary*	$ ________________
Subtract Taxes	________________
Add: RE Taxes	________________
Less: Investment Proceeds included in Both income and expense section	________________

Less: College expenses covered by
Sources listed in Income Section ________________

Adjusted Annual Expenses* $ ________________

Divide above result by 12

Average Monthly Expenses $ ________________

Low Range: three times Avg. Mo. Exp. $ ________________

➤ Appropriate for couples or singles with less possibility for extra expenses than for families.

High Range: five–seven (choose)____ times

Avg. Mo. Expense = $ ________________

➤ Appropriate for families.

Step A Total: $ ________________

B. Determine Anticipated Special Purchases:

Special Expense Item	Planned Expense Date	Amount

➤ In Quicken®, review *Planning Assumptions—Special Expenses* for special purchases over the next three to five years. List those items, starting with next year:

➤ Total liquid cash required for these expenses:

One-time purchases after current year: $________________

Annual purchases after current year: $________________

Total future years' purchases for ____# of years

Step B Total: $________________

C. Compare Liquid Investments with Short-Term Cash Reserve Need

Step A total $ ________________

+ Add: Step B total $ ________________

- Subtract: Short Term Cash* $________________
= Equals: Additional Needed $________________
- Subtract: Investments** $________________
= Equals: Cash Reserve Shortfall $________________

*From most recent Quicken® *Net Worth Report*—Total Cash and Bank Accounts"

**Review Investments section of *Net Worth Report*. Include only nonretirement accounts that hold cash or other investments that could be liquidated in an emergency without incurring a significant loss.

D. Calculate Monthly Savings Needed to Save Emergency Funds.

Monthly savings required to cover shortfall within *_____months.

*If future cash expenses are significant, the period of time you take to build your emergency fund balance can be longer than if most of the reserves are needed to cover living expenses over the next three–eight months.

To calculate the monthly savings required to meet this objective, follow the directions provided on your TEN WEEKS CD in the Week Six "Savings Calculator."

Greg and Ginger determined they needed to set aside an additional $23,180 to current savings. This addition would leave them with five months of living expenses, as well as provide for special cash needs for five years.

Using the Savings Calculator, they determined they would need to set aside $700/month into a savings account earning 2.5 percent to reach this goal. They realize as soon as they accumulate $64,720, they can stop funding this monthly transfer to savings.

STEP THREE:

Honestly Evaluate Your Current Investment Complexity

Over the years, it is easy to accumulate a multitude of investment accounts. Not only does the volume of accounts become overwhelming, but other issues can develop that may make obtaining outside advice the smartest thing you can do. The following questions will help you decide if such a course of action makes sense because of your investment complexity.

Please refer to your most recent *Net Worth Report*, found in your Authentic Money Guide notebook. Check the box if your answer is "yes"—

- ❑ Do you have more than five separate investment accounts?
- ❑ Do you participate in a 401(k) or other retirement plan that limits your investment choices to offerings within that plan?
- ❑ Do you own individual stocks and bonds and not just mutual funds?

- [ ] Do you have taxable investment accounts for which you don't know your "tax cost" for?
- [ ] Do you have a portfolio in excess of $250,000?
- [ ] Do you have the option of converting IRAs, 403(b)s, or 401(k)s into a public pension through the purchase of service credits?
- [ ] Do you own any fixed or variable annuities?

If you checked at least two of the above boxes, then consider the following options:

➤ Consider retaining a TEN WEEKS Advisor™ listed on the *www.tenweeks.com* website. These qualified advisors will assist you in the construction of a portfolio that matches your Authentic Money Guide. Each advisor is trained in the use of the TEN WEEKS TO FINANCIAL AWAKENING program and will be able to pick up where you left off with helping you implement your investment plan, as well as any other questions you have about your experience. Visit that website for more information about this option.

➤ Consider *www.financialengines.com* This web-based investment service offers unbiased investment recommendations for an annual fee. The fee for retirement accounts only is $149.95/year and for all investment accounts $300/year. Please consider the following items when considering this Internet advisory service:

1. Couples need to be aware that investment recommendations do not result in each individual having an independently balanced portfolio. I recommend both individuals submit his/her investment accounts separately.
2. The service does not provide detailed investment advice for variable annuities. If you own annuities, I recommend that you consult a fee-only financial advisor for advice on how to create your portfolio.

➤ Choose one of the following options for creating your investment portfolio and then have it reviewed by a TEN WEEKS Advisor™ or another advisor recommended in the Section Four Appendix D materials.

STEP FOUR
Create Your Own Portfolios

Option One: Bill Bernstein's Model Portfolios as Outlined Below:

In his book *The Four Pillars of Investing*, Dr. Bernstein describes four investor profiles. Take a few minutes to read the following information to see which profile best matches your own.

Taxable Ted:

Ted finally sold his business last year and has a pile of cash. He never had the time or inclination to set up an IRA or retirement plan, even though it would have saved him a fortune in taxes.

Investments Ted can use will need to fit into the "Taxable" or "Both" column of Table 4 that lists suitable Vanguard Index Funds.

In *The Four Pillars of Investing,* Dr. Bernstein makes one exception to this rule:

"There is one other option available to him, and that's to open a variable annuity (VA) so that he can invest in REITs. I didn't have many nice things to say about these vehicles a few chapters ago, but here I'd make an exception. Vanguard does make available a relatively low-cost VA…this will enable him to hold REITs in his portfolio without being punished by the taxes on their hefty dividend distributions since they would be sheltered inside the annuity account. The disadvantages are an extra .37 percent in insurance expense and not being able to withdraw funds before age 59½ without a penalty."

(Reprinted with permission of The McGraw-Hill Companies. William J. Bernstein, *The Four Pillars of Investing,* © 2002 The McGraw-Hill Companies, Inc.)

If your situation resembles Ted's, use the following table to choose the Vanguard Funds, based on the stock/bond allocation you used in Week Six Worksheet C.

"Taxable Ted's" Portfolios

Stock/Bond	100/0	90/10	80/20	70/30	60/40	50/50	40/60	30/70	20/80	10/90	0/100
Vanguard Total Stock Market Index	40%	36%	32%	28%	24%	20%	16%	12%	8%	4%	---
Vanguard Tax-Managed Small Cap	20%	18%	16%	14%	12%	10%	8%	6%	4%	2%	---
Vanguard Tax-Managed International	25%	22.5%	20%	17.5%	15%	12.5%	10%	7.5%	5%	2.5%	---
Vanguard REIT Index	15%	13.5%	12%	10.5%	9%	7.5%	6%	4.5%	3%	1.5%	---
Treasury Ladder	---	2.5%	5%	7.5%	10%	12.5%	15%	17.5%	20%	22.5%	25%
Vanguard Short-Term Corporate Bond	---	2.5%	5%	7.5%	10%	12.5%	15%	17.5%	20%	22.5%	25%
Vanguard Limited-Term Tax-Exempt	---	2.5%	5%	7.5%	10%	12.5%	15%	17.5%	20%	22.5%	25%
Vanguard California Intermediate-Term Tax-Exempt	---	2.5%	5%	7.5%	10%	12.5%	15%	17.5%	20%	22.5%	25%

Reprinted from *The Four Pillars of Investing* by William J. Bernstein, Published by McGraw Hill, 2002

Sheltered Sam:

Sam's investment portfolio is almost all in IRAs and other retirement accounts since, as a CPA, he knew how valuable tax-deferred compounding could be in meeting his retirement goals.

Since Sam is over 59½ and ready to retire, he doesn't have to worry about penalties for withdrawing his money too early. He does have to consider, however, the cash flow distributions he will need to live after retiring.

Sam's retirement accounts shelter any income tax until he chooses to take the money out, so he can utilize the entire range of investment options outlined in Table 4. He, unlike Ted, would not benefit by opening a variable annuity since his accounts are already tax-deferred (or tax-sheltered).

Use Sheltered Sam's investment options if most of your investments are in retirement accounts. Select the stock/bond mix that most closely resembles that on your Rebalancing Worksheets.

Sheltered Sam's Stock/Bond Mixes

Stock/Bond	100/0	90/10	80/20	70/30	60/40	50/50	40/60	30/70	20/80	10/90	0/100
Vanguard 500 Index	20%	18%	16%	14%	12%	10%	8%	6%	4%	2%	—
Vanguard Value Index	25%	22.5%	20%	17.5%	15%	12.5%	10%	7.5%	5%	2.5%	—
Vanguard Small-Cap Index	5%	4.5%	4%	3.5%	3%	2.5%	2%	1.5%	1%	0.5%	—
Vanguard Small-Cap Value Index	15%	13.5%	12%	10.5%	9%	7.5%	6%	4.5%	3%	1.5%	—
Vanguard REIT Index	10%	9%	8%	7%	6%	5%	4%	3%	2%	1%	—
Vanguard Precious Metals	3%	2.7%	2.4%	2.1%	1.8%	1.5%	1.2%	0.9%	0.6%	0.3%	—
Vanguard European Stock Index	5%	4.5%	4%	3.5%	3%	2.5%	2%	1.5%	1%	0.5%	—
Vanguard Pacific Stock Index	5%	4.5%	4%	3.5%	3%	2.5%	2%	1.5%	1%	0.5%	—
Vanguard Emerging Stock Markets Index	5%	4.5%	4%	3.5%	3%	2.5%	2%	1.5%	1%	0.5%	—
Vanguard International Value	7%	6.3%	5.6%	4.9%	4.2%	3.5%	2.8%	2.1%	1.4%	0.7%	—
Vanguard Short-Term Corporate		6%	12%	18%	24%	30%	36%	42%	48%	54%	60%
TIPS (3.375% of 2032)		4%	8%	12%	16%	20%	24%	28%	32%	36%	40%

Reprinted from *The Four Pillars of Investing* by William J. Bernstein, Published by McGraw Hill, 2002

In-Between Ida:

Ida, 57, just lost her husband and received some life insurance and her husband's $100,000 pension plan, which she rolled over into her IRA. Her total portfolio is $1 million, of which $900,000 is in taxable accounts.

Since Ida's portfolio is very similar to Ted's we can use that Table for selecting her investments. The only item that is different is to allocate 12.5 percent to an Ohio state bond fund rather than to a California fund. Since both Ted and Ida end up in a 31 percent federal tax bracket, it makes some sense to invest in these state bond funds that will be exempt from state and federal taxes.

Consider the following chart to determine if selecting a tax-exempt municipal bond fund really makes sense:

TE Yield	Tax Bracket Percentage (Federal Only) and Taxable Yield Equivalent				
	15%	**27%**	**30%**	**35%**	**38.6%**
4%	4.71%	5.48%	5.71%	6.15%	6.51%
5.5%	6.47%	7.53%	7.86%	8.46%	8.96%

A state income tax rate of 8 percent would enhance the taxable equivalent yield on the 5.5 percent tax exempt bond, assuming the owner was in the 27 percent tax bracket, from 7.53 percent to 8.19 percent. As you can see, in many instances the tax-free yields are so low that it makes sense to purchase taxable bond funds and just pay the tax.

Young Yvonne:

Yvonne, 26, has just finished law school and finally has a job that allows her to save about $5,000/year. She has no current investment accounts and wants to save for retirement with an IRA since her employer won't offer a retirement plan for several years.

The portfolio Dr. Bernstein recommends for a person in Yvonne's shoes deals with the following problems for small investors:

- Some of the $5,000 will need to be directed to the creation of a liquid Emergency Fund. Since Yvonne is entitled to contribute $3,000 to an IRA in 2003, she'll open up a good money market account with the other $2,000.
- To avoid small IRA account charges with Vanguard, $10 per fund with a balance of less than $5,000 in each fund, she will take a laddered approach in purchasing her investments. This means that she will buy one piece of her desired portfolio at a time. Though she will lack the diversification early on, as her money grows, she will be able to add the funds she needs, while avoiding unnecessary expenses.

"Young Yvonne's" Investment Path: Vanguard Funds.
Note: Funds are added from left to right, in $5,000 increments.

Total Amount	Money Market (Taxable)	500 Index	Total Int'l Index	REIT Index	Small Value Index	Value Index	Small Cap Index	Short Term Corporate	Prec. Met Fund	European Index	Pacific Index	Emg Mkt Index	Int'l Value Funds	Inflation Prot. Sec. (TIPS)
$5,000	$3,000	$2,000												
$10,000	$4,000	$4,500	$1,500											
$15,000	$6,000	$6,000	$2,000	$1,000										
$20,000	$8,000	$6,500	$2,500	$1,500	$1,500									
$25,000	$10,000	$3,500 **	$3,000	$2,000	$2,000	$4,500								
$30,000	$10,000	$4,000	$3,500	$2,000	$2,500	$5,000	$1,000	$2,000						
$35,000	$10,000	$4,100	$4,600	$2,100	$3,100	$5,100	$1,000	$4,000	$1,000					
$40,000	$10,000	$4,800	$5,000	$2,400	$3,600	$6,000	$1,200	$6,000	$1,000					
$45,000	$10,000	$5,400	$5,800	$2,700	$4,000	$6,750	$1,350	$8,000	$1,000					
$50,000	$10,000	$6,000	***	$3,000	$4,400	$7,500	$1,500	$10,000	$1,000	$1,500	$1,500	$1,500	$2,100	
$55,000	$10,000	$6,600	***	$3,300	$4,950	$8,240	$1,650	$12,000	$1,000	$1,650	$1,650	$1,650	$2,310	
$60,000	$10,000	$7,200	***	$3,600	$5,400	$9,000	$1,800	$12,000	$1,080	$1,800	$1,800	$1,800	$2,520	$2,000
$65,000	$10,000	$7,800	***	$3,900	$5,850	$9,750	$1,950	$14,000	$1,170	$1,950	$1,950	$1,950	$2,730	$2,000
$70,000	$10,000	$8,400	***	$4,200	$6,300	$10,500	$2,100	$14,000	$1,260	$2,100	$2,100	$2,100	$2,940	$4,000
$75,000	$10,000	$9,000	***	$4,500	$6,750	$11,250	$2,250	$15,000	$1,350	$2,250	$2,250	$2,250	$3,150	$5,000
$80,000	$10,000	$9,600	***	$4,800	$7,200	$12,000	$2,400	$16,000	$1,440	$2,400	$2,400	$2,400	$3,360	$6,000
$85,000	$10,000	$10,200	***	$5,100	$7,650	$12,750	$2,550	$17,000	$1,530	$2,550	$2,550	$2,550	$3,570	$7,000
$90,000	$10,000	$10,800	***	$5,400	$8,100	$13,500	$2,700	$18,000	$1,620	$2,700	$2,700	$2,700	$3,780	$8,000
$95,000	$10,000	$11,400	***	$5,700	$8,550	$14,250	$2,850	$19,000	$1,710	$2,850	$2,850	$2,850	$3,990	$9,000
$100,000	$10,000	$12,000	***	$6,000	$9,000	$15,000	$3,000	$20,000	$1,800	$3,000	$3,000	$3,000	$4,200	$10,000

** When portfolio reaches $25,000 in size, approximately $3,000 is exchanged from the 500 Index Fund into the Value Index Fund.
*** When portfolio reaches $50,000 in size, the Total International Index Fund is exchanged into the International Value, European, Pacific, and Emerging Markets Index funds.

Reprinted from "The Four Pillars of Investing" by William J. Bernstein, Published by McGraw Hill, 2002.

Option Two—Use Quicken® to select a portfolio of mutual funds.

See the TEN WEEKS CD with Greg and Ginger using this approach. Guidance can be found in the Quicken® "Portfolio Implementation" section of the CD.

Option Three—Construct a socially-screened portfolio, using resources outlined earlier in this chapter.

- First, choose a Bernstein model portfolio and then pick socially-screened investments from those asset classes as follows.
  - Consider the Asset Allocator at *www.calvertgroup.com* with specific recommendations of Calvert Funds. Please note that these funds do carry front-end and back-end loads unless purchased through a load-waived program such as that offered by *www.naturalinvesting.com*
  - Another option for getting started with Socially Responsible Investing is the Vanguard Calvert Social Index that can be purchased at *www.vanguard.com.*

Option Four—No stock market approach

If you have problems accepting any risk associated with equity (stock) investing, or you philosophically don't feel that you can support the system it represents, then consider discussing these concerns with a TEN WEEKS Advisor™. These advisors assist

other clients with the purchase of direct bond and alternative investments. They may also assist in the evaluation of a rental property in your geographical area that may meet your investment criteria.

To locate such a trained advisor, visit *www.tenweeks.com.*

STEP FIVE:

Monitor Your Investment Contributions and Rebalance Your Investments Once Each Year

Set up each of your investment accounts in Quicken® for online downloads. This will enhance the accuracy of your monthly financial reports and make tax preparation much less "taxing."

The most important aspect of investing is to invest. (See MAP 6-13.) If you spend your energy worrying about performance and fail to contribute regularly to your portfolio, you will find your investment balance falling short of your targets.

"Anyone who can live on welfare should be courted by Wall Street. He is a financial genius."

—Joanna Clark

Since you have taken the risk involved in investing very seriously, you can contribute new money to your accounts with the confidence that your concern about losses has been factored into the creation of your portfolio of investments.

The power of asset allocation can only be accessed if you follow the disciplines of rebalancing on an annual basis. By selling a portion of the funds that have performed well and purchasing those that have not, you increase the chances of enhancing your returns while lowering your risks over time.

The Solar Panels and My Investment Choices

We started this section on investing with a discussion about the three *kleshas,* or poisons, we humans deal with on a daily basis: desire, aversion, and denial. Rather than attempting to distance ourselves from these poisons, we have tried to cultivate our warrior's heart and begin to access their medicinal qualities as they relate to our money and how we seek to have it work for us, rather than have it work us into a frenzy. With each opportunity to "stay" before we "leave," we have used money to help us align our behavior with the power of our Authenticity.

"Adversity is something hard upon a man; but for one man who can stand prosperity, there are a hundred that will stand adversity."

—Thomas Carlyle

By facing our greed and desire, we saw how we could be less controlled by investment returns when we took the initiative to limit our lifestyle. There is such a thing as "enough." We can experience "sufficiency." There is more to life than squeezing the last ounce of performance from our investment portfolio and having it poison this precious life journey. Aligned living is much simpler than that of one excess after another.

There is a numbing dread and disillusionment that accompanies our taking of little or no responsibility for our investment choices. We did feel some relief from the numbness when we began to take our role of Citizen as seriously as that of Consumer. There is a way, with the development of the Socially Responsible Investment industry, to invest with our values rather than in opposition to our Authenticity.

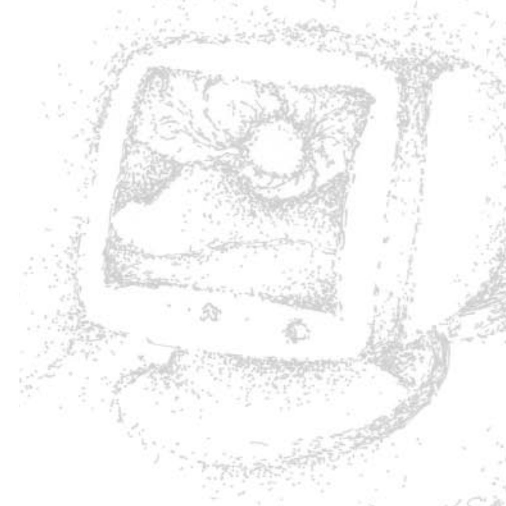
Wally mentioned the importance of alignment when he explained his electrical diagram several years ago:

*Conversion Method—The Solar Panels (Diagram Component #2) ** a flashback ***

"Since I've chosen the sun as our source of energy, we have to figure out a way to harness that energy. We'd be in the same predicament if we had chosen coal, oil, natural gas, or wind as the power source. If I had drawn the Hoover Dam, the conversion method would be turbine-driven generators. In my diagram I've used a photovoltaic cell, or solar panel, to illustrate this conversion. We now have electrical energy ready to move to the next step in our system, the transmission lines.

"The critical thing in the conversion of energy is proper alignment.

"The solar panels here in my diagram are useless if they aren't positioned properly to capture the sun's rays. In the same way, the



Hoover Dam wouldn't generate any power if Lake Powell suddenly dried up. Those generators have to be placed where the fall of water will turn the turbines."

Wally and the Path of "No Ecstasy"

"In some ways I think I just wanted you to tell me how to invest my money," recalled Wally. "I had no idea what was in store for me when I asked you for some investment advice. I didn't think you would actually make me understand investing as it related to comprehensive financial planning!"

That was three months after Wally had come to my office for our first meeting. Since that time, he and Jane had agonized over the creation of an investment portfolio that honored the life they valued.

"Did you really think that I was going to let you off that easily," I said, "after what you put me through with that electrical diagram?!"

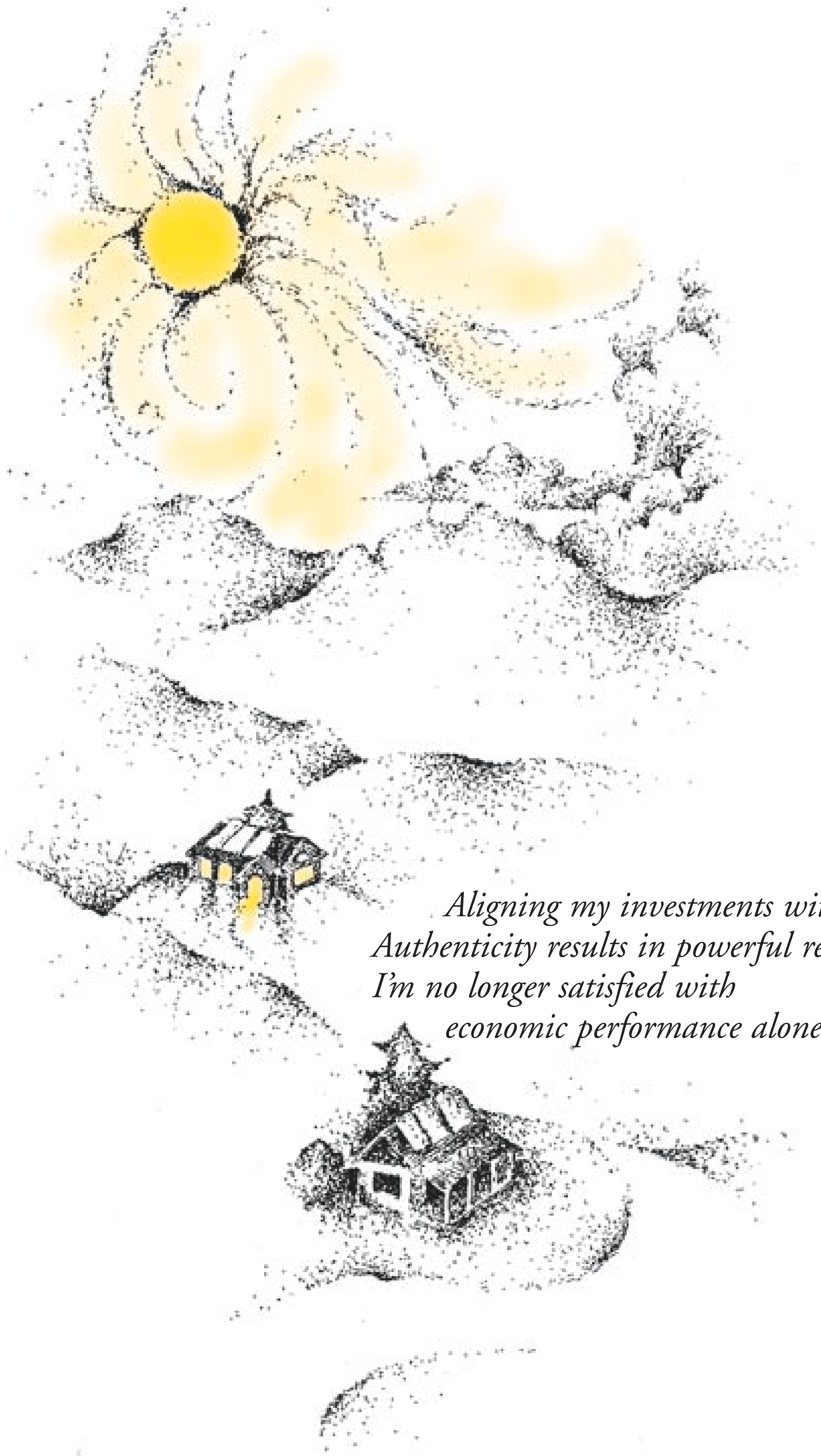
"I sure should have seen that one coming," was Wally's lighthearted reply.

Just like Wally, you eventually tackled your reluctance to understand investing. Rather than blindly following advice, you experienced some freedom from the insanity of being blown every direction by the fierce winds of opinion and "expertise."

By Slowing down, Appreciating the risk/reward relationship, Noticing the whole as greater than the sum of its parts, and Examining the cash flow needs of your life and investing accordingly, you accessed SANE investing. This process of finally giving your investments your attention was by no means a walk in the park; it involved some serious realignment.

"With money in your pocket, you are wise and you are handsome and you sing well, too."

—Yiddish saying



Aligning my investments with my
Authenticity results in powerful returns.
I'm no longer satisfied with
economic performance alone.

The following poem by T. S. Eliot summarizes this process of realignment, full of its struggle and mystery:

Shall I say it again? In order to arrive there,

To arrive where you are, to get from where you are not,

You must go by a way wherein there is no ecstasy.

In order to arrive at what you do not know

You must go by a way which is the way of ignorance.

In order to possess what you do not possess

You must go by the way of dispossession.

In order to arrive at what you are not

You must go through the way in which you are not.

And what you do not know is the only thing you know

And what you own is what you do not own

And where you are is where you are not.

—T. S. Eliot, excerpted from the poem "East Coker"
from Four Quartets

Come to think of it, I bet T.S. Elliot, Hermes, and maybe even Wally have been hanging around one another. I can hardly wait to see what else money has to show us about how to cultivate our comfort with all this uncertainty.