The Common Yardstick of Financial Success Has Its Flaws

There's a one-size-fits-all mentality to much of the news coverage of investing, which typically defines successful investment strategies and successful investment managers as those that "beat the market." Active management fails, maintains the media, because the majority of active managers have not outperformed their benchmarks over the last 10 years (although there is a significant number who have done so).

In reality, the success of an investment strategy is determined by how well it meets the investor's goals.

While most investors would prefer higher versus lower returns over a given period, they also have a wide range of objectives that don't necessarily include beating the market, particularly when it comes with the risk of market downturns.

Capital Preservation

For those individuals who have reached the status of high-net-worth investors, keeping what you have achieved and avoiding major market downturns becomes more important than maximizing return. Their performance goal may be to offset the impact of inflation and taxes, but manage the risk of losing money. Retirees also tend to focus on capital preservation versus return, particularly when chasing higher returns comes with the risk

Growth

Most investors don't have the luxury of knowing they are adequately funded to make it through retirement and need their invested capital to grow in value. But these investors often find it hard to buy and hold through market volatility and the emotional impact of bear market losses or ongoing negative media coverage. A low-cost index fund with its market volatility may not be an appropriate investment. Adding a layer of financial management can mean the difference between growing assets and failing.

Income

Many individuals invest with the objective of generating income. Appreciation or losses in the current value of the underlying investment are not as important as the income stream it provides.

Tax exemption

There are investments that offer the ability to reduce current tax liability through depreciation or expenses that can be recovered later, typically through a sale of the asset. Other investments may offer the potential to convert short-term gains to long-term capital gains, resulting in more favorable tax treatment.

Liquidity

When an investor anticipates a near-term need for cash, liquidity may dominate his or her investment objective. A successful investment becomes one that provides a modest return, but is available when needed and less vulnerable to declines in value.

In each of these objectives, it is unlikely the investor will equal or outperform the S&P 500 index. But that doesn't make the investment unsuccessful. Passive one-size-fits-all investment approaches may well be one of the most dangerous bandwagons the financial media has ever jumped on. There is very much a place for investment advice shaped to the needs of the investor. We would argue good investment advice is well worth the fee it costs when it allows investors to meet their objectives. Risk must always be a consideration in the investment decision.

Brian R. Carruthers, CFP®, CMT

Brian R. Carruthers & Associates
Your Conservative Advisory Firm Since 1990
301 Forest Avenue
Laguna Beach, California 92651-2115 USA

Telephone: 1-949-464-1900
www.gobcafunds.com
brian@gobcafunds.com