



JULY 2011 INVESTMENT UPDATE

Dear Friends and Clients,

Wouldn't be great if we lived in a world where all the investment tips you received came from totally objective and rational sources that had only your interest at heart. Once this happens, if ever, then you probably will no longer need our wealth management services. The purpose of this special investment update is to make you aware that the financial arena has many different types of "financial advisors" who get paid by "commission" versus "fee-only" type of compensation. This update focuses on those advisors who get paid by commission only.

People who work in the financial field often feel a powerful tug to tell you a slanted story: They have got an investment to sell. Stockbrokers, of course, are the poster kids for this kind of behavior, along with some insurance agents, realtors and coin dealers. We're not implying everybody in these businesses is crooked – far from it. In fact, my insurance agent is not only a crackerjack insurance person who has my very best interest, but he has also been a good friend for many years.

However, it's essential to remember that salespeople wrestle with an inherent conflict of interest. To earn their bread, they have to move product. And the stuff they move may, or may not be what's best for you. As most of you already know, we are especially wary of mutual funds that impose a "load" (sales charge), which can be imposed on both ends- upon purchase and/or sale. Loads can put a serious dent in your profits if you decide to exit the investment within the first few years. That is part of the reason why we use only a few select mutual funds that fit our criteria as part of our investment portfolios.

There's also the velvety "free" advice that investment firms hand out to the public. My e-mail box is cluttered, as I'm sure yours is too, with financial advertising disguised as research. Fund families offer to share their latest market insights with you in supposedly exclusive conference calls. Of course, the intent is always to get you to buy something – a product or service the advisor just happens to peddle. The same subtle bias, by the way, still percolates through much of the stock research currently issued by major brokerage firms. True, the outrageous excesses of a decade ago are gone, but analysts are clearly still afraid of angering their firm's investment – banking clients.

Sometimes, outlets that may not appear to have any direct sales motive can deliver tilted advice. Here are three carriers of the bias to handle with particular care:

1) The electronic media. With the advent first of cable news and now the internet in its myriad manifestations, it's easier than ever for shrewd operators to stampede public opinion. Beware of TV shows which focus almost exclusively on fleeting short-term trends. For most investors, the way to make serious money is by riding long-term tidal movements, not by playing this morning's squiggles.

2) Government. Yes, indeed, our own government is a generous source of slanted investment advice, starting with the self-serving, everything is – ok pronouncements of Treasury and Central Bank officials. Federal Reserve Chairman Ben Bernanke seems determined to go down as one of the worst offenders ever in this department. In July 2008, just two months before Fannie Mae and Freddie Mac collapsed, Bernanke told congress the twins were “adequately capitalized” and “in no danger of failing”. In October 2005, as housing was teetering on the brink, Bernanke proclaimed, “there is no housing bubble to burst”.

3) Bloviating billionaires. Before the Sokol Scandal blew up, cyberspace was crackling over Warren Buffett's negative comments about bonds. Sure, we all know Buffett is a genius at investing in stocks. But has anybody bothered to ask why that talent necessarily makes him an expert on bonds? The fact is, Buffett never liked bonds, even though government bonds have logged almost the same return as stocks for the past 30 years. Billionaires don't need bonds. Even if Buffett's stocks dropped 99%, he would still be rich beyond the dreams of avarice. However, this is not so for most of us. For ordinary mortals, bonds or bond-like substitutes play an important role in generating income and stabilizing our portfolios. Don't let a billionaire's prejudice blind you to the importance of a balanced investment strategy.

A final species of bias may seem perfectly innocent. However, it can also hinder your investment returns if you're not careful. I'm talking about your own psychological bias. We all carry around preferences and preconceptions in our heads, built on years of experience (as well as a fair amount of genetic hard wiring). I have these biases, and so do you. When it comes to investing, I'm a skeptic. Because I tend to doubt glowing promises and rosy scenarios, I lean toward growth assets that produce an immediate income or ones that are undervalued but generate significantly increasing free cash flow. Just make sure you understand your own biases and you've got to know yourself, truly and honestly. Only then can you cope with the sometimes crazy and even destructive biases of the financial noisemakers around you.

Sometimes the future can be very difficult to predict but a fee-only financial advisor can help you focus on long-term financial goals than about short-term goals. Our firm is a fee-only investment advisory firm and we encourage you to contact us to review your financial plan along with your investment portfolio for the first six months of this year.