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Have You Weeded Your Financial Garden?

By Donna Skeels Cygan

Guest Commentary

FROM THE EXECUTIVE'S DESK: Everyone knows that gardens need to be weeded. Cleaning out the weeds and the old growth clears the way for new, healthy flowers and vegetables. The same strategy applies to your investment accounts. By getting rid of the clutter — the assets that have dropped significantly in value, or that are not appropriate for your goals and tolerance for risk, you can eliminate the weeds and let the flowers bloom.

I am amazed at how many new clients we see who have the same portfolio they had in 1999. Unfortunately, now the total in the account is often one half of the 1999 total, due to the stock market being so brutal during the past three years. Many people never weed their investment accounts, and just hope they will recover their lost dollars. Another problem is that many of the investment accounts were far too aggressive in the first place, which has caused the decline to be even greater.

From the Executive's Desk
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First, I recommend you analyze your goals and your tolerance for risk. In the late 1990s many people thought that bonds and other fixed income assets were unnecessary, and having 80 to 100 percent of a person's investments in the stock market was appropriate. We have statistics that show that even young people with a high tolerance for risk should not have 80 percent in the stock market, because the risk in down years (such as years 2000-2002) is too great. Anyone who has had a significant amount of bonds in their portfolios during years 2000-2002 has been amazed at how the bonds protected them from the turbulent stock market.

In order to determine the appropriate asset allocation for you, I recommend you use financial tools such as www.vanguard.com. You can go to the Planning and Advice section and then select "Create Your Own Plan."

You can also order or download their Plaintalk brochures. One of the best is called Investment Basics.

Once you have determined what you would like your asset allocation to be, you can compare that to your current investment accounts. A good place to analyze your current investments is at www.morningstar.com. Other good financial Web sites include www.troweprice.com, www.kiplinger.com, and www.bloomberg.com.

Because I am a fee-only financial planner, I do not recommend paying a commission to buy mutual funds. If you have commissioned funds in your investment accounts, you may want to look at www.personalfund.com. This is a Web site created by Andrew Tobias, who has written several excellent financial books. The Web site allows you to input a mutual fund that you own, and the Web site will then compare your fund to a comparable fund that has no commission and a lower annual expense ratio. It will estimate the growth of your money over a 10-year period if you keep the fund or replace it with a no-commission (no-load) fund with a low expense ratio. The difference in the growth over 10 years can be staggering.

I do not recommend individual stocks for investment, because I believe a diversified mutual fund with no commission and a low annual expense ratio significantly reduces the volatility within a portfolio. A white paper was published in 2001 by David Loeper of Financeware that reviewed 6,698 individual stocks over 1998-2000 and determined that the individual stocks on average were 3.2 times as volatile as their index benchmark. Some people may argue that volatility and risk can affect the upside or the downside of performance. However, we all know that during the past few years the volatility has primarily been on the downside, leading to greater losses.

So how do you weed your financial garden?

Doing the research mentioned above will likely lead to conclusions about whether the investments within your current accounts are appropriate for you. If you determine that a stock or mutual fund is appropriate for you for the long term, maybe you should keep it. If you determine some investments you own are not appropriate, definitely weed out those investments and replace them with better choices.

Many people have a hard time selling a stock or mutual fund that has lost a large amount of money. Human nature tells us to leave it alone so it can recover.

I encourage you to think of the "opportunity cost when deciding if you want to sell a stock or mutual fund. You must acknowledge that the fair market value of the stock is the value today. It is currently not worth what it was 2 or 3 years ago. The opportunity cost is simply defined as the cost of passing up an opportunity.

Most portfolios from 1999 are not appropriate for 2003. Devote some time to your investment accounts, and then reward yourself with a beautiful bouquet of flowers. Or better yet, plant some sunflower seeds in your garden, and you will be reminded all summer long about the benefits of weeding your financial garden.