AHWATUKEE FOOTHILLS NEWS

Don't Be Seduced By The Lure Of Wall Street Promises

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Wall Street makes money either by commissions on the investments they sell or a percentage of the total assets they manage. The common pitch for most people is "I can make you more money in stocks than anyone else". The research done at the UC Berkeley and Stanford 40-50 years ago found this was incorrect.

We looked at a 10-year period and found that only about 5 money managers could beat the stock market averages for that decade. Warren Buffett and Sir John Templeton were two of those folks. Warren Buffett later became acknowledged as the single greatest stock market investor of the last 50+ years. Sir John Templeton was way ahead of the curve after World War 2 and believed that if one invested overseas, stock market returns would outperform the U.S. market.

Wall Street has told folks that you can average 8-10% annual returns over long periods of time. If one goes to www.moneychimp.com, for 1/1/2000 to 12/31/2018, the average compound annual growth rate (CAGR) in the S&P 500 stock market index has been 2.85%. If one adds the average 1.98% annual dividends, one's total ROI has been 4.83%. When one adjusts for inflation, it's 2.63%. For the last 30 years, the goal of all Wall Street full-service brokerage firms has been to earn at least 3% annual fees from money you deposit with them. If you subtract this, your ROI is negative for this century.

I'm not saying that you should not try to get the highest ROI on your investments, but you also must temper that with the risk you are willing to take. We've had 2 major stock market crashes this century: the 2000-2002 Dot-Com Crash, where the NASDAQ index dropped by about 78%; and the 2008-2009 Financial Meltdown, where the stock market dropped by about half.

Efficient Frontier: In 1990, Harry Max Markowitz received the Nobel Memorial Prize in Economic Sciences by proving that there is an Efficient Frontier, which is the ideal tradeoff of return vs. risk. However, one cannot even approach the efficient frontier without owning at least 3 asset classes that are not closely correlated with traditional stocks, bonds, or cash.

Alternate asset classes could include: commodities, farms, precious metals, foreign currencies, real estate, equipment leasing, and private pensions. I have checked with people in the real estate, banking, and mortgage business over the last 3 decades and the consensus is that only about 2% of the population has even owned 2 rental houses or more. For most, real estate is the alternate asset class that is easiest to understand.

How Much You Save is the Most Important Factor to a Secure Retirement: To make the math easy, suppose that there are 2 families with the same $100,000 of annual household income. Recent statistics show that the average U.S. savings rate is 8% of after-tax disposable income. So if this household saves 8% of $80,000 disposable income, or $6,400. If they do this every year for 25 years and earn an average 6% net-after-fees ROI in the stock market, they will have $372,200 in their retirement account. In contrast, if a different family saves 3 times as much ($19,200 annually) but earns half the ROI (3%), they will have $761,219 in 25 years, or double.

Conclusion: instead of being seduced by Wall Street promising big returns, spend more time and effort figuring out how to up your savings rate. What's more important to you: a financially secure retirement or buying lots of stuff that does not create long-term happiness, joy, and love? It's good health, family, good friends, hobbies, and causes you are passionate about that creates happiness, joy and love.

Contact Dr. Harold Wong at (480) 706-0177 or harold_wong@hotmail.com to RSVP.

Dr. Harold Wong earned his Ph.D. in Economics at the University of California/Berkeley and has appeared on over 400 TV/Radio programs.