Many struggle to get successful results from their investments. Committing to a sound investment philosophy is key to successful investing yet often, this critical first step is skipped.

Having an investment philosophy and a plan that matches is critical to making sound investment decisions. It provides the filters necessary for processing the large quantity of information we can receive about financial matters. In addition, not having a plan or having a bad plan can cause one to make poor decisions, take on the wrong types of risk in inappropriate quantities, or lose too much of returns to taxes. Often, one does not even realize this is happening.

This month marks the low point of the U.S. stock market after the ’08 financial crisis. We have noticed that the more defined people were regarding their investment philosophy and the better their plans matched that philosophy, the better they fared before, during, and after the crisis.

What is an “investment philosophy”? An investment philosophy is a set of principles that guide one when designing and managing investment assets. The starting point is this question: are you going to be a speculator or an investor? Many people are whipsawed by the markets because they have no plan, a bad plan, or a plan that is not aligned with sound philosophical underpinnings.

We are investors, not speculators. A portfolio should support a family’s goals and should be designed as part of a coordinated financial plan. From a portfolio implementation and management standpoint, there are two broad choices to make.

First, will you be broadly diversified or will you concentrate your holdings to a smaller number of securities, themes, sectors, asset classes, or areas of the world? Common terms for this are “stock picking,” “money management,” and “active management.” Whatever it is called, the more you rely on your best ideas, the less diversified you are and the closer you become to speculating. Second, will you try to move funds in and out of financial markets based on your expectation of whether markets are about to rise or fall? Common labels for this are “market timing” or “tactical allocation.” Regardless of what you call it, the more you try to move ahead of the markets, the closer you are to speculating.

We believe trying to outmaneuver the markets as in the above mentioned ways is folly. We came to this belief from years of experience and the overwhelming evidence that the likely outcome of such an approach is an inferior result. Over time, fewer and fewer people make excess profits and the typical excess gets smaller and smaller.
Here are a few examples of when being committed to a plan based on a sound philosophy can make life simpler:

- **“Story” stocks.** Many people have bought shares of stock because the company’s “story” was so compelling that the stock seemed like a low risk buy. If your plan calls for broad diversification, you will ignore these stories. If you absolutely cannot help yourself, remember there must always be a seller in order for you to buy. The seller thinks you are dead wrong and that their money is better placed elsewhere.

- **“New” products.** Wall Street is in the business of creating and selling products to the public. We analyze many products each year and often the only thing “new” is how the product is packaged and presented. Most products are designed to make money for the brokerage firms, insurance companies, and banks that create them, ahead of any earnings that may filter through to the buyer.

- **“Cutting edge” strategies.** Provocative packaging and presentation is also a common element to selling various strategies. We see this often with creative tax strategies. We are all for saving taxes, but many of the schemes are untested. In the last few years, we have found profound flaws in several arrangements to put real estate or gold in IRAs, fund new franchises with retirement account money, and various investments in life settlements.

- **Market gurus.** If your plan eschews market timing, the market predictions that serve as much of the content the media distributes should not be of interest to you. No one can buy without a seller and no one can sell without a buyer, so differing opinions about the markets’ prospects is the normal state of affairs. If it seems “everyone” thinks the market will go one way or another, it is your perception and cannot be the reality.

- **Economic experts.** The other favored topic of the media is predictions about how the economy will do. “We think X will happen in the economy, so therefore the markets are set to rise/fall/move sideways,” is the basic statement you will see. There are simply too many variables for markets to be that linear. If your plan calls for not moving in and out of markets in anticipation of market movements, you will not care what a pundit thinks the economy is about to do or what market movements will be.

“What to do now” is always a hot topic but during the financial crisis, it was at its most popular. Our investment philosophy allowed us to use tactics such as rebalancing, tax loss harvesting, and Roth IRA conversions and reject costly options, hedging strategies and a slew of “principal protection” and “guaranteed” products that financial service industry firms rushed to create.

There are additional choices to be made in adopting an investment philosophy and having a plan to match. For instance, what risks should be taken or avoided and in what quantity? How will taxation be managed? From where will cash flow be drawn when needed? How might a family’s needs change in the future?

But the heart of the matter comes down to that critical question: are you going to be a speculator or an investor? By choosing how you will view your portfolio and committing to your choice, you can better recognize what matters, tune out that which may be interesting but not applicable to your situation, and better discern the probable from the merely possible.

Markets do not always cooperate, but our choice to be investors, not speculators, and our mantra of “diversification, patience, and discipline” have guided our decision making during booms, busts, and everything in between.

Making sound financial decisions is not just about thinking long term and strategically. Having an investment philosophy and a matching plan makes it easier to identify tactics which can be beneficial and avoid those likely to be harmful. It promotes the behavior and disposition that can lead to better odds of reaching one’s numerical financial goals and of finding financial contentment— a form of success hard to measure yet very real.

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