

# New Year's Investment Resolutions

By Brian Bush

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**The beginning of a New Year is typically the time when we make commitments to reform our habits. Often, we make resolutions that involve a lifestyle change we think to be advantageous to our health and welfare. Soon, you will be bombarded with advertisements on how to lose weight, get out of debt, quit smoking and become more organized. Unfortunately, I am unable to help you change any of those behaviors and will be fighting battles of my own after Jan. 1. However, I would like to suggest a few Investment Resolutions for you to consider in the New Year.**

## **Resolution No. 1: Stop trying to pick individual stocks.**

Holiday parties are a wonderful opportunity to mix and mingle with good friends. They can also be a breeding ground for lucky investors who proudly recount their stock picking prowess. ("I bought Google at \$85!") Unfortunately, they are much like the gambler returning from Las Vegas after a winning weekend that is not quite as vociferous about his previously unsuccessful trips to The Strip. When you pick stocks on your own, you are doing so with the assumption or hope that you will be able to beat the market. Since the advent of the mutual fund industry, the stock market has been transformed into a battlefield dominated by large sophisticated institutions. These companies are staffed with the brightest minds from the country's top business schools. Each day these professionals receive, dissect, and analyze mountains of research and corporate information distributed by thousands of publicly traded companies and the research firms who follow them. Today, these institutions "are" the market. Given the inherent advantage professional investors enjoy over any individual, what are the chances you will pick the next Google? In gambling parlance, The House (Mr. Market) has a distinct advantage every time you roll the dice. A stock picker battles difficult odds. Resolve yourself to building a diversified portfolio that suits your individual goals, time horizon and risk tolerance and that minimizes your costs.

## **Resolution No. 2: Allocate your investment assets properly.**

Asset allocation is the process of determining the right mix of stocks, bonds and other investable assets needed to match your individual investment objectives and risk tolerance. Asset allocation is based on the principle that different asset classes offer returns that are not perfectly correlated. Therefore, having a mixture of asset classes reduces the overall risk and variability of returns in your investment portfolio. Investment research studies conclude that almost 90% of an investment portfolio's performance can be attributed to the asset allocation strategy. The amount of your investments you will allocate to each asset class will largely depend on your personal situation: your return objective, the amount of

risk you are willing to take and what other assets and investments you own. During the market's rollercoaster ride of 2008 and 2009, many investors realized their asset allocation was not appropriate for their circumstances. Determining the appropriate asset allocation for your investments is a very important decision. Make a commitment to sit down with a financial advisor and review your asset allocation in the New Year.

**Resolution No. 3: Don't try to time the markets.**

As the saying goes, "timing is everything", but waiting or trying to time the markets can be a costly decision. History shows that stocks rise over long periods of time; however they can be very volatile in the short-term. Market timing is based on the premise that an investor can divine when stocks will rise and when they will fall. One problem with market timing is it requires you make two correct decisions, when to buy and when to sell. Keep in mind, the market does not know or care when you are in or out of the market, and on average, the market does just as well during both periods of time. The best way for investors to take advantage of short-term swings in the market is through systematic rebalancing. Here's how it works. Once you have decided on the optimal asset allocation for your portfolio, you rebalance the assets regularly by selling the assets with the highest return and buying the assets with the lowest return. The strategy is based on long term probabilities and allows you to maintain your target asset allocation and improve your returns. It is impossible to know when stocks will go up or down, but systematic rebalancing will force you to buy low and sell high.

**Resolution No. 4: Allow the power of compounding to work for you.**

Procrastination may be a habit you would like to break, but it may be costing you lots of money as well. When asked what he considered mankind's most powerful mathematical discovery, Albert Einstein replied, "Compound interest." When you put your money in an investment that delivers a return, and you reinvest those earnings as you receive them, you can achieve amazing results. This is particularly true in retirement accounts where the earnings are allowed to grow tax-free. The following illustrates the value of time and compounding.

Assume investor A begins saving \$2,000 per year but does so eight years earlier than investor B. Investor A ceases making new contributions at the end of his 8th year, just as investor B is beginning to make his first. Both investors earn the same rate of return (10 percent), with no withdrawals or taxes over the next 45 years. Not only will investor A end up with more money, he will enjoy a 64 fold increase in his principal versus 10 fold for investor B.

	Investor A		Investor B	
	Annual Investment	Year-End Value	Annual Investment	Year-End Value
Year 1	\$2,000	\$2,200	\$0	\$0
Year 2	\$2,000	\$4,620	\$0	\$0
Year 3	\$2,000	\$7,282	\$0	\$0
Year 4	\$2,000	\$10,210	\$0	\$0

Year 5	\$2,000	\$13,431	\$0	\$0
Year 6	\$2,000	\$16,974	\$0	\$0
Year 7	\$2,000	\$20,872	\$0	\$0
Year 8	\$2,000	\$25,159	\$0	\$0
Year 9	\$0	\$27,675	\$2,000	\$2,200
Year 10	\$0	\$30,442	\$2,000	\$4,620
Year 11	\$0	\$33,487	\$2,000	\$7,282
Year 12	\$0	\$36,835	\$2,000	\$10,210
Year 13	\$0	\$40,519	\$2,000	\$13,431
Year 14	\$0	\$44,571	\$2,000	\$16,974
Year 15	\$0	\$49,028	\$2,000	\$20,872
Year 16	\$0	\$53,931	\$2,000	\$25,159
Year 17	\$0	\$59,324	\$2,000	\$29,875
Year 18	\$0	\$65,256	\$2,000	\$35,062
Year 19	\$0	\$71,782	\$2,000	\$40,769
Year 20	\$0	\$78,960	\$2,000	\$47,045
Year 21	\$0	\$86,856	\$2,000	\$53,950
Year 22	\$0	\$95,541	\$2,000	\$61,545
Year 23	\$0	\$105,095	\$2,000	\$69,899
Year 24	\$0	\$115,605	\$2,000	\$79,089
Year 25	\$0	\$127,165	\$2,000	\$89,198
Year 26	\$0	\$139,882	\$2,000	\$100,318
Year 27	\$0	\$153,870	\$2,000	\$112,550
Year 28	\$0	\$169,257	\$2,000	\$126,005
Year 29	\$0	\$186,183	\$2,000	\$140,805
Year 30	\$0	\$204,801	\$2,000	\$157,086
Year 31	\$0	\$225,281	\$2,000	\$174,995
Year 32	\$0	\$247,809	\$2,000	\$194,694
Year 33	\$0	\$272,590	\$2,000	\$216,364
Year 34	\$0	\$299,849	\$2,000	\$240,200
Year 35	\$0	\$329,834	\$2,000	\$266,420
Year 36	\$0	\$362,818	\$2,000	\$295,262
Year 37	\$0	\$399,100	\$2,000	\$326,988
Year 38	\$0	\$439,010	\$2,000	\$361,887
Year 39	\$0	\$482,910	\$2,000	\$400,276
Year 40	\$0	\$531,202	\$2,000	\$442,503
Year 41	\$0	\$584,322	\$2,000	\$488,953
Year 42	\$0	\$642,754	\$2,000	\$540,049
Year 43	\$0	\$707,029	\$2,000	\$596,254
Year 44	\$0	\$777,732	\$2,000	\$658,079
Year 45	\$0	\$855,505	\$2,000	\$726,087
Year 46	\$0	\$941,056	\$2,000	\$800,896
Year 47	\$0	<b>\$1,035,161</b>	\$2,000	<b>\$883,185</b>
<b>Less \$ invested</b>		<b>(\$16,000)</b>		<b>(\$78,000)</b>
		\$1,019,161		\$805,185
<b>Money increased</b>		<b>64 fold</b>		<b>10 fold</b>

Source: Stephens Capital Management

Time is an asset money can't buy, but time can buy you money. The longer you have, the greater the potential benefits of compounding. Don't wait. Harness the power of compounding in the New Year.

New Year's has always been a time for looking back to the past, and more importantly, forward to the coming year. It's a time to reflect on the changes we want (or need) to make and resolve to follow through on those changes. Research shows that half the people who make New Year's resolutions have given up on them by June. Here's hoping you stick to these valuable investment resolutions. Now, its back to the Thighmaster.

Wishing you a Happy and Prosperous New Year.

*Brian Bush*

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