Nightingale Conant

RIC EDELMAN'S

No-Nonsense System for Building Wealth

Ric's Straightforward Plan for Creating and Enjoying Financial Success

GUIDEBOOK

IMPORTANT

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RIC EDELMAN'S
"No-Nonsense" System for Building Wealth Guidebook

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Session 1: Making Sense of the Nonsense

THE RULES OF MONEY HAVE CHANGED.

In this guidebook, I'm going to share with you the new rules about money and give you some insight into how to make your money work for you. Instead of simply trading hours for dollars, I'm going to show you how to put your money to work for you because here in America we're really good at making money with our time. Nowhere in the world is anyone as good at making money with their time.

The problem is that the day's going to come when you're going to want to stop making money with your time. You're going to want to stop trading hours for dollars. And you're going to want to start making money with your money. Unfortunately, most of us don't know how to do that because we've been paying attention to our parents and our grandparents. Whatever money habits they have are the ones that we probably have and, unfortunately, the habits that they have might not have been all that good in the first place. But even if they were, they made more sense for them than they do for us now.

This is why I want to share this information with you. We'll cover everything: taxes, investments, insurance, mortgages, real estate, buying cars, debt, college planning, retirement planning, and estate planning. You name it, we're going to cover it because all of these broad subjects in the field of personal finance are making a huge difference in your lifestyle and the financial success of your family. I'm going to give you a lot of very practical, very tangible information to show you specifically what you can do on a day-by-day basis, and it's incredibly simple, incredibly easy, and incredibly effective. These are the types of things you're not likely to learn from most other people in the personal finance press because what they're doing is simply repeating what they've been told. Just as you do what your parents and grandparents told you, they simply do what they have been taught by others.

THE TWO BIGGEST MISTAKES PEOPLE MAKE.

1. Procrastination
2. Getting advice from all the wrong people

The first mistake people make when dealing with personal finance is that they procrastinate. They simply do nothing. You'll make more mistakes by doing nothing than by doing something that doesn't work out. You'll actually hurt yourself more by not investing than by investing in the wrong place. I have never met a successful investor who has been able to tell me that they've never lost money in an investment. If you're going to be a successful investor, you're going to lose money along the way. It's okay to lose money when you're investing. You simply have to make sure you don't lose all of your money when you're investing.

But without question, the single biggest mistake people make is procrastination. They fail to do anything at all. They sit there and they put it off until later. And there are two reasons they don't do it. Number one, this stuff is really boring. Let's face it, the subject of personal finance is really dull and boring. I hate the subject of personal finance. What I'm really interested in are the people behind personal finance. What I'm really interested in are your goals, your aspirations, and your family. The fact that we have to deal with

money along the way, well, that's just one of the evils we have to tolerate in our society, but that's the way it is. The point is, the subject of money for money's sake is really dull and boring.

The other reason you put it off is because there's no deadline. We live with deadlines every day. You've got deadlines at work, projects you've got to get completed by a certain date. You've got obligations at home. You've got to get the kids to soccer practice today. The in-laws are coming into town for the weekend. Thanksgiving is coming up. It's a deadline. You've got to meet the deadline. But personal finance, you can put that off until later. And you end up putting it off forever.

The second mistake people make is that when they do finally decide to take action and they do finally decide that they're going to make an investment, they get all their advice from all the wrong people. They get their advice from the personal finance press, which in many cases I liken to nothing more than financial pornography. What you have to understand is the difference between financial education and financial noise. It is not there for your benefit and welfare, it is there for their benefit and welfare. You've got to learn to separate the noise from the information.

So those are the two big problems you've got to watch out for. Number one is procrastination. You've got to make sure you get started now. Do something now. Taking action today is better than inaction tomorrow. Second, make sure that you are acting on independent, objective, valid information geared to your own personal circumstances. Not something that is written for the masses, not something that is going to be read or seen simultaneously by millions of other people that has no bearing on your personal circumstance. Make sure you're separating the information from the noise so that the actions you are taking are genuinely going to benefit you and your family.

Session 2: Setting Your Financial Goals

IT ALL BEGINS WITH GOALS.

• Step One: Set a Goal
When a brand-new client comes into our office for the first time, the first question we ask is, "What are you doing here? What do you want to accomplish?" And very clearly, very effectively, very consistently people tell us that they have some goals. They have some concerns. They want our advice and recommendations, and we say to them, "Okay. It all begins with goal setting." It all begins with discovering what it is that's important to you. The only reason people are interested in the subject of money is because they have goals. Money is of no value unless it's used. Hoarding cash is pointless. The key is to use the money that you've accumulated. So what is it that you want money for?

You've got to decide what excites you, what motivates you, what fulfills you because you're sitting there, at the moment, on auto-pilot. You're doing the same thing today that you did yesterday and the same thing that you're going to be doing tomorrow. What you're doing right now is acting on the decisions that you've made before, and this is something that people really have to understand because decision making is the key element here. What goal setting is all about is decision making. I'm asking you to make a decision. Tell me what would excite you. Tell me a goal that you would love to accomplish. Let's say that you want to go to Greece for a month. Okay, there's a goal. Let's say that's what excites you. You know what you've just done? You've made a decision. That's a decision in itself. Most of us are pretty bad at making decisions. Most of us haven't made a decision in a very long time.

So, what we have to recognize is that it all comes down to the goals and objectives that we have, and that's why I'm stressing that to you. While you've got to talk about your goals and objectives, in order to make and establish a goal and objective, you've got to make a decision! And until you make a decision, nothing else happens. So that's step number one in goal setting: Set a goal.

• Step Two: Set a Date
After you have set a goal, the next thing you have to do is set a date. A goal is not a goal unless you put a date on it. And by the way, when I say date I don't mean some nonsense such as, I'll do it after I retire or when the kids are grown or when the dog dies. Nothing that's nebulous, vague, or superficial. You've got to give me a specific date. I will go to Greece for a month in the year 2012. That's still not good enough. I want a date. I will go to Greece for a month and I will leave on July 12, the year 2012. That's a goal. A goal is not a goal until you put a date on it. And when you establish dates, remember that they must be reasonable, attainable, and realistic.

• Step Three: Write it Down

A goal is not really a goal until you write it down. It is not real. When I say "write it down," I don't mean you write it down on a piece of paper and shove the paper in a drawer in your desk or on a shelf in your office. I mean that you put it in front of you all the time. You need to slap it on your bathroom mirror. You need to put it on your refrigerator door. You need to stick it on the steering wheel of your car. You need to put it in front of you on your computer monitor at work and home. You've got to write it down and you've got to keep it in front of you.

• Step Four: Stay Focused

The fourth and final step of goal setting is that you must stay focused on it. The reason people often don't stick with their goal that is they never give it any thought. They get preoccupied with other things. You've got to stay focused on your goal all the time. It's as simple as that. How do you do that? If your goal is to go to Greece, you need to get magazines on Greece, travel brochures. You need to go visit travel agents. You need to go to Web sites about Greece. You need to go hunting around your community for people of Greek descent and interview them and talk with them and get immersed in the goal. You've got to figure out what will it cost to go to Greece. Where are places to stay? What are you going to do while you're there? You've got to really live, eat, and breathe your goal.

THE 9 QUESTION FINANCIAL PLANNING PROCESS.

Please answer the following nine questions in order to help make your goal become a reality. Be as honest and realistic as you can possibly be with your answers.

1. How much is it going to cost?

   _____

2. How many times will you need the money?

   _____

3. How many years will it be before you're going to achieve your goal?

   _____

4. Do you have any money already set aside for this goal?

   _____

5. How much money are you going to get from outside sources that you can apply to this goal?

   _____

6. How much money are you saving monthly toward this goal?

   _____

7. What is the inflation rate going to be between now and when you need the money?

   _____

8. What is your tax rate going to be?

   _____

9. What is the rate of return you are going to earn on your savings?

   _____

Session 3: Extraordinary Wealth Secrets 1 and 2

HOW DO RICH PEOPLE GET THAT WAY?

Look around you. Look at the people who work with you, look at the people who live in your neighborhood. Some of them are a lot more financially successful than you. Some of them have a lot more money than you. How do they do it? Why is it that they have greater wealth?

Well, in order to answer that we decided to look no further than my firm's own clients. I have about 5,000 clients all around the country, and these are all middle-class Americans. These are people who work for a living. These are people who were not born into great wealth. They didn't win the lottery, they aren't multimillionaires, but they are in the top 3% of the American population in terms of wealth. They are in the top one-half of one percent of the world's population in terms of wealth.

So, I had simply one question I wanted to ask my clients: How did they do it? How was it that my clients became so financially successful? They didn't become financially successful because they're working with my firm. These people were financially successful before they came to my firm. They would have been financially successful whether they went to my firm or someone else's firm. Why? Because it's in their nature. It's in their make up. Financially successful people are going to be financially successful. It's been my pleasure and privilege to help them and to work with them, but I cannot claim credit for their financial success.

Even though these people are from all walks of life, we discovered that they are basically doing the same things. They are doing almost everything in the same way even though they don't know each other. They have nothing in common really, except for how they handle their money.

HERE ARE THE 8 SECRETS OF EXTRAORDINARY WEALTH FROM ORDINARY AMERICANS.

• **Secret One: They carry a mortgage on their homes even though they can afford to pay it off.** They have a 30-year mortgage. They make the minimum payment and they leave it at that. They put as little money into their house as necessary because they understand that money you give to a bank is dead money. People who fear mortgages have no valid basis for their fears. It's all about how they were raised because Mommy and Daddy taught them that mortgages were scary and, therefore, that's what they believe. It's sort of like believing in the Boogey Man. There is no rational basis for it. And under today's economic environment, under today's tax environment, under today's financial environment, having a mortgage is the smartest, safest way that you can handle your home.

"Paying off a mortgage at a faster rate only benefits the mortgage company. We can invest the additional payments and maintain a tax deduction."

— Edelman client

• Secret Two: They don't diversify the money they contribute to their company retirement plans. Instead, they put all their contributions into one asset class.

What this comes down to is a very simple fact. There are two types of diversification and you're only familiar with one of them. What you're familiar with is called "asset diversification." Asset diversification is as you know it to be, putting 12 eggs into 12 baskets.

If you have $100,000 as a lump sum that you're looking to invest, yes, you should invest all of it at once, but not all of it into one place. You need to invest that $100,000 in a variety of places, into 12 different baskets. This makes perfect sense and I strongly recommend it. This is how our clients handle it as well, but not when it comes to their retirement plans.

When it comes to their retirement plans, they are not engaging in asset diversification. What they're doing is something called "time diversification" and it is, in fact, a very different thing than what you're used to. Let me give you an example. If you were to take a hundred dollars and put it into just one investment choice, does that sound scary to you? It probably does because you say to yourself, "Oh, my goodness, I'm not diversified!" But, in fact, you really are. Why? Because you're buying it today with a hundred dollars and you're buying it in two weeks with another hundred dollars and, two weeks after that, with another hundred dollars. In other words, you're diversifying by time.

"I look at my plan as a long-term investment. The time horizon is way out there. Best returns historically have been from stocks and I figure it will continue that way. I started putting money in the plan when I was 34. In 1986, when the market had a downturn, I was stupid, so I took the money out. I learned my lesson, though. If we could go backwards in time, I wouldn't have touched that money."

— Edelman client

Let me put it this way. IBM, at $100 a share, is a very different investment than IBM at $50 a share. Do you agree with that statement? Doesn't that make sense? In other words, it doesn't matter what you buy. What matters is what you pay for it. If you invest money all at once, you only get one price, whatever the price is you pay. But if you're investing a little bit over long periods of time, you're getting one investment at many prices.

Session 4: Extraordinary Wealth Secrets 3, 4, and 5

• Secret Three: Most of their wealth came from investments that were purchased for less than a $1,000.

If you are poor and you want to be rich, you've got to start doing what rich people do, and rich people do not get rich by investing large amounts of money. Rich people get rich by investing small amounts of money.

"I started investing when I was 29, just a hundred dollars per paycheck. I had to make some sacrifices to do this. I didn't get many of the things other people had, such as cars and furniture, but it's easier than ever now. The smallest amount I ever invested was $25, which I did often and, as my salary increased, so did my savings. I'll probably never stop saving."

— Edelman client

So, where do they get it? Well, more than 95% of them told us that they got their money through their own efforts. They worked hard. They got an education and got a good job. They had kids and they worked even harder and, through it all, they still managed to save money. And the important thing to understand is that they didn't start with $100,000. Ninety-two percent of my clients say that they saved regularly throughout their lives. They added to their savings whenever they could. No matter how much they had, even less than $100, they saved some of it and they saved intelligently. Eighty-one percent of them set money aside in a special account earmarked for savings. They'd accumulate a few hundred dollars and then invest it. Only 4% left money sitting at home in a drawer for any length of time. Ninety-six percent put the money into an interest-bearing account and then transferred the money to stocks, bonds, and mutual funds.

And here is what's so important to understand. They wouldn't let anything stop them from saving.

• Secret Four: They rarely move from one investment to another.

What we discovered in our research is that they are not making investment changes. Sure, there's a lot of news and a lot of things going on all the time, but these people are investing their money and they're leaving it alone. In the past one-year time period, 52% of them said that they did not make a single change to their portfolio, despite wild volatility in the marketplace. Fourty-three percent made only one or two changes, but, in many cases, that was just routine portfolio balancing, not market timing attempts. Only 4% of our clients moved money four to six times in a single year. In other words, they buy investments and they leave them alone.

"Good personal experiences reinforce the wisdom of sticking with one's investments for the long term. My belief is that people who move money from one investment to another are motivated by fear or greed. I take advantage of dollar-cost averaging and compound interest with a sound, diverse portfolio created to meet my needs. I plan to stay the course."

— Edelman client

• Secret Five: They don't measure their success against the Dow or the S&P 500.
I'm astounded how often people focus on issues that are completely irrelevant to their financial success. For example, how are you doing with your money? Well, if you're going to couch your answer by comparing how you're doing to your friend next door or to the S&P 500 or the latest news from Wall Street, you're missing the point. Remember, financial success is all about achieving your own personal goals. If you're en route to achieving those goals, then that's all that matters. And if you're not en route to achieving your goals, then you have a problem and that is what so many people simply don't understand. It astounds me that so many people are so focused on things that simply don't matter.

The message here is simple. Keep your eye on the ball. Stay focused. It doesn't matter what's going on around you. What matters is are you achieving your goals? If you'll stay focused, you'll be less tempted to make bad decisions.

"I don't pay attention to the Dow or the S&P because we own mutual funds. My problem is that I get nervous when dealing with money. I'm from the old school of money where you save your money under a mattress because you're afraid that the money won't be there when the time comes to retire. I don't like risk. And I know I'll drive myself crazy if I look at the Dow and the S&P every day. I'm in it for the long haul, so I only look periodically because I know I'm not going to do anything about it. I measure the progress of my investments by the annual statement I get. It gives me an overall picture of what my portfolio is doing. I take no action if one annual statement doesn't perform well because I'm in it for the long term, not the short term."

— Edelman client

Session 5: Extraordinary Wealth Secrets 6, 7, and 8

• Secret Six: They devote less than three hours per month to their personal finances and that includes the time they spend paying bills.

It doesn't take a lot of time to be able to accumulate a lot of wealth. You don't have to spend a lot of energy and a lot of effort on a regular daily basis to be able to accumulate a lot of money. According to the survey we conducted with our clients around the country, 85% of them spend less than three hours a month paying their bills. More than a third of them do it in less than an hour. A whopping 97% spend less than two hours a month balancing their checkbook and 9% don't even bother to balance it at all. And 82% spend less than three hours a month on their investments

"I pay bills twice a month. I have just one checking account. Some bills are paid automatically. It takes about 45 minutes. We've never bothered with a budget, never needed to. We've always known how much we could spend, but we do track our expenses. I have a ledger of what I pay by category — auto expenses, credit cards, department store, and so on. It helps us stay focused."

— Edelman client

• Secret Seven: They view money management as a family affair.

Have you discussed money with your parents and with your children? Many people have not and that is a big mistake. Money is a terrible place to keep secrets. You should know what your parents are planning to do with their money.

Let me share with you what our own clients do because how they handle this is very, very different than how it's handled for the vast majority of consumers. Of the clients we surveyed, 87% of them have children and, of those 87%, 82% have told their kids about their financial and estate plans. The remaining 18% haven't talked to their kids about it simply because the kids are too young for a detailed conversation. Beyond that, two-thirds of my clients know their parents' financial situation and their parents' estate plans. If you think that you don't want to talk with your parents about money, you're operating under a misguided sense of respect for your parents.

"We have three sons, 38, 35 and 32, two of them are married. They all know about our finances and estate plans. They all have a copy of our documents. It was a casual meeting and they were fine about learning the information and they appreciated our thoughtfulness. We started talking to our kids about money early, when they were in grade school. My dad is 91, my mom is 86. I have a copy of their estate plans and finances. You have to know about their plans because at some point, you will be faced with it."

— Edelman client

• Secret Eight: They differ from most investors in the attention they pay to the media.
Here's what we discovered in our survey of 5,000 wealthy Americans regarding how much they pay attention to the media. Only 19% said they read *The Wall Street Journal*; only 21% watch CNBC or PBS's *Wall Street Week*. Less than 20% attended a financial seminar in the last year; only 15% read a personal finance magazine; only 11% watch *Nightly Business Report*. In fact, depending on the question at hand, anywhere from 80% to 100% do none of the above! they've learned that it does not require a lot of time. It does not require a lot of attention to do well.

But what about you? Where do you find the great investments? You do a lot of research. You do a lot of study. You go through a lot of effort and a lot of hassle, but if you're not going to put any money into them then you're wasting your time. The smart thing to do is to focus your energy on your savings habits and then you won't have to worry about the rest.

"I've learned to stay for the long course and not to let the interim noise from the news interrupt me from sticking with my plan."

— Edelman client

Session 6: Mind Over Money — 10 Mistakes Investors Make

Here are the ten mistakes people make when they are making investment decisions.

• Mistake No. 1 – Fear
Fear is without question the most powerful emotion, the one that causes people to make more investment decisions than any other. Fear is defined as a lack of confidence in the stock market. If you fear the market, if you have no confidence in it, you certainly will sell. What you've got to recognize is that if your emotions are causing you to act, then you are, in fact, making the wrong decision at the wrong time. When it comes to investing, it is very important that you spend your energy and effort on your intellect not on your fear because your fear is almost certain to guide you to do the wrong thing at the wrong time.

• Mistake No. 2 – Greed
Contrasting fear is greed. Let me give you some numbers to help bolster this. If the Dow Jones Industrial Average grows at 7% per year over the next 20 years, the Dow will be at 40,000. If the Dow earns 10% a year, it'll be at 80,000. I don't even want to tell you what it'll be at 15%. You see, what we have to do is recognize that small rates of return over long periods produce dramatically high wealth figures, and that's what most people don't understand.

But that leads to greed, because if I just told you that 20 years from now the Dow is going to be at 80,000, you no longer have any fear, do you? Now you're full of greed. Now you can't wait to get in. You know what you're guilty of? Overconfidence in the market.

• Mistake No. 3 – Optimism
Optimism means that you have overconfidence in yourself. Remember, greed was overconfidence in the market. Well, optimism is overconfidence in yourself. Without question, we are overconfident and we see this routinely. Optimists tend to exaggerate their talents. They think they're better at investing than they really are. They often overestimate their knowledge. They exaggerate their ability to control events and, as a result of all this, they underestimate the risks that they are taking.

• Mistake No. 4 – Pessimism
Pessimism is a lack of confidence in yourself. Is that you? Well, let me ask you this way. Do you have the ability to pick the best mutual fund? No, I bet you don't. I'll bet you agree that you do not have the ability to pick the very best mutual fund and, therefore, you suffer from pessimism. You think you can't do it. And here's what's so fascinating. You think you can't pick the best. But let me ask you this. Do you think you're likely to pick the worst? You're more than likely to think you're going to pick the worst than you are likely to pick the best. That is pessimism. You're no more likely to pick the worst than you are to pick the best, but you think you are and that demonstrates that you are a pessimist.

As Warren Buffett once said, "It's better to be approximately right than precisely wrong." And this is something that most pessimists simply don't understand, and the reason the pessimists are pessimists is because they fear something else, which is number five on our list.

• Mistake No. 5 – Regret
Regret means wishing you had not done something that you have done, and it is an awful feeling. Can you remember any time in your life that you experienced regret? It's a terrible feeling and we'll do almost anything to avoid regret. You must avoid the feeling of regret, and the best way to avoid the feeling of regret is to make the best decision that you can and then never look back on it because regret is based on looking backward. How did it turn out?

• Mistake No. 6 – Hindsight
Hindsight is the tendency to overemphasize the past. The ability to go backward with hindsight is a very damning experience because we overemphasize the past. We tend to minimize the realities that existed at the time. And as a result, we tend to make bad decisions. In the world of investing, the way this comes about is we say, "You know what? I should have seen the collapse of the dot-coms coming. It was so obvious that the NASDAQ was overpriced. It was so clear that there was no way that those stocks could have sustained their high levels. I am amazed that I didn't see it and I'm convinced I'll see it next time. And due to my overconfidence and optimism, I think I'm going to do better in the future than I did in the past." And that sets up the stage for more economic disaster.

• Mistake No. 7 – Quilting
You know humans tend to perceive trends where none exist. Think about it. Did you ever look up in the clouds and see a dragon? In the world of investing, this is called "the hot-hand fallacy." We tend to see patterns that aren't there. If we look at the historical data, mutual funds, that do really well in one period are no more likely to do well in the next period than the ones that didn't do well. There is no correlation between past performance and future results. None, and yet we seem to believe that there is.

• Mistake No. 8 – Loss Aversion
Loss aversion. What does that mean? Well, it simply means this: Most people dislike losses more than they like gains. Does that describe you? I'd rather avoid a loss than get a gain. This describes an awful lot of people. You're so afraid to lose money, you don't give yourself the opportunity to make money and, as a result, you stay poor. Don't fall into that trap. Recognize that if you're going to attempt to achieve wealth, you must be willing to take risk. If you're not willing to take risk, you have no hope of accumulating wealth.

• Mistake No. 9 – Accidental Anchoring
This is the mistake of assigning importance to random points. Let me give you an example of this. How many different investment choices are there in your 401K plan at work? In most people's company retirement plans, they have five or six choices. When people have five choices, they invest in five different things. When they have ten choices, they invest in ten different things. In other words, people make their investment decisions based on the opportunities in front of them. What you should be doing is deciding how you want your money invested. Then manipulating the available choices to meet that goal.

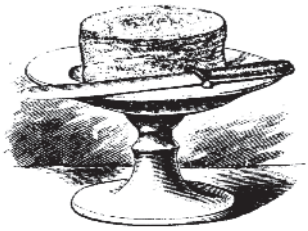
• Mistake No. 10 – Farming vs. Foresting

We know the difference between farmers and foresters. A farmer is a person who takes a seed and plants it in the ground, takes a step, plants another seed, takes another step and plants another seed. They are dealing with individual trees, focusing on them one by one. The forester, of course, is going up into that tower and looking out on the horizon, looking out at the entire landscape of the forest — and that is what you need to do as well.

People who invest based on farming make very bad investment decisions. This is the problem of the entire personal finance press. Think about it. Every issue of every magazine, every broadcast of every radio and TV show is always focused on the very same thing. They are telling you what hot stock to buy now. They are farming. They are talking about individual stocks. Do you know what they never do in any of those publications or on any of those broadcasts? They never tell you how much of your money to place into any one of those stocks at any one moment. They are never giving you the forest, and that is the key. You must look at the forest. It's not a question of what stock you buy. The question is how much of your money did you put into it.

Session 7: The Four Kinds of Financial Cakes You Can Bake

HOW TO BUILD YOUR INVESTMENT PORTFOLIO.



When it comes to the world of investment cakes, you are going to find that there are four different kinds of cakes that you can bake. There's pound cake, marble cake, today's special and cupcakes, and we're going to talk about all four of them.

POUND CAKE.

You know what a pound cake is. A pound cake is a reliable cake. It's consistent. It's also kind of dull. Pound cake has only one flavor, no icing, no decoration. It's pretty darn boring. But you know what? A pound cake is an incredibly common kind of cake.

Let me give you an example of where a pound cake might be appropriate. Let's say that we're talking about Holly, 28 years old. She wants to buy a $200,000 house in two years. She's got $18,000 saved and she's adding $300 a month to her savings. She says to me, "Ric, where should I invest my money so that I can buy my house?" Do you know where she ought to put all of it? Bank CDs. Yes, really. If you do the math, you'll discover that Holly's savings are so aggressive — $300 a month — that over the next two years she's going to accumulate over $7,000. That's assuming she earns no interest. She takes the $7,000, adds it to the $18,000 she already has and she's got a $25,000 down payment — more than enough to get into that house. In other words, she doesn't need anything more exciting. She doesn't need anything more risky than a bank CD for all of her savings. In this example, Holly is perfect with a pound cake, a dull, boring, and incredibly safe and predictable investment.

MARBLE CAKE.

Now, what if Holly wasn't saving enough where her savings alone could do the job? What if the goal was so big or so far away that it wasn't going to work? Well, that takes us to the second type of investment, to the marble cake. A marble cake consists of two different types of ingredients. A marble cake consists of a little bit of those cash assets and, when I say cash assets, I'm referring to cash, money markets, CDs, and bonds. All of those are pretty much lumped together into one type of asset class. And the other one is stocks. A lot of people own a combination of the two, stocks on one hand, bonds on the other. The problem is figuring out exactly how much of your money should be in one versus the other.

TODAY'S SPECIAL.

This is where people go for what's hot. This is where they buy the fad. They say, "I want to get into stocks and out of bonds or out of stocks and into bonds," and this is the whole notion of market timing. And as we've discussed, it is kind of obvious that, at any given period of time, one of them is doing better than the other. The problem is there's no pattern. There's no effective, predictable way to tell which one's going to do better in the future than the other, but people insist on trying to do that anyway.

Clearly, the key to investment success is to leave your money invested for a long period of time. If you try to move it around, chances are you're going to do exactly the wrong thing at exactly the wrong time.

CUPCAKES.

Now, we have to consider a very important question in the field of portfolio management and it's simply this: Should you buy cupcakes or a cake? The question might sound a little silly, but it really is a critical one for investors. Should you have one big cake or should you have lots of little cupcakes?

What I'm talking about is actually known as "sector rotation." This is the notion that the stock market is really not a stock market; the stock market is really a market of stocks. In other words, in the stock market, we really have a wide variety of individual asset sectors. We have aggressive growth, communications, emerging markets, equity income, financial, foreign growth, growth in income, healthcare, natural resources, precious metals, real estate, technology, and utilities.

Clearly, any one of those sectors might be doing better than another one of those sectors at a given moment. So what do we do? Do we have all of our money in all of those all of the time or do we try to own only the one that counts at a given moment? If we look at all the academic data, we find that they are all pretty much ending up in the same place.

You can spend your time buying one and I'll spend my time buying the other and we'll both be okay.

Session 8: Ric's Special Recipe for Financial Success

TWO SIMPLE THINGS — INGREDIENTS AND PROPORTION.

We've already talked about the different asset classes that exist out there and we know that there is cash and government bonds and we know that there's corporate bonds and stocks and international securities and real estate and precious metals and natural resources. The question is how do we put all of these into the proper context? How much of each ingredient do we use? How big of a slice do the stocks get in our cake?

Well, there are two different approaches. One, we could take the market timing and sector rotation approaches that we've already talked about or two, we could simply own everything all of the time.

Let me give you one simple example to illustrate the benefits of owning everything. Let's say that we have two investors. They're each going to invest $25,000 over a 25-year period of time. The first investor takes his $25,000 and puts it into a bank account earning 5%. After 25 years, he's got about $85,000. The second investor takes his $25,000 and he splits it into five piles of $5,000 each.

Pile number one, he buys lottery tickets. What's it worth in 25 years? Zero, same as when you buy lottery tickets. Pile number two, he takes $5,000 and he stuffs it under a mattress. He's so scared of his shadow, he doesn't invest it at all, so the $5,000 never grows in value; it stays $5,000. Pile number three, he puts the money into a savings account earning 2% interest. Five thousand grows to $8,200 after 25 years. Pile number four, he puts it into a U.S. government treasury earning 5% a year. The $5,000 grows to about $18,000. And finally, pile number five, he puts it into a diversified basket of stocks earning the average return of the last 75 years, which is about 12% per year. His $5,000 grows to $85,000. All told, between all five of his piles, he has a grand total of $115,000. He's got substantially more than if he had just put it all into a bank CD.

This is the notion of diversification. This says we don't have to pick the best horse in the race. If we just bet on every horse, we will do just fine because compound interest tells us that an investment that makes money will make so much more than an investment that loses money. Therefore our average return will be just fine. Of course, this raises the next question. How exactly do we slice the cake? Do we literally take our money and put it equally into each investment asset class? Or is there a better way?

Well, the answer is right at your fingertips and it is in the financial press. Oh, not the personal finance press, but in the institutional press. Have you ever heard of *Institutional Investor* magazine? How about *Pensions and Investments* magazine? How about *CFO* magazine? You see, there are a variety of magazines and trade journals written for and read by the professional money managers. So, instead of reading a magazine that is written by consumers for consumers, why not read one that is written by professionals for professionals? Doesn't that make more sense? If you want to achieve professional-level results, you should take a look at how the professionals do it.

ASSET REALLOCATION.

I want to talk with you about something that's perhaps even more important than the initial question of asset allocation and that is asset reallocation.

In other words, if we take a cake and we split it into four equal slices: stocks, bonds, cash and government securities, you tell me which of those four slices are going to grow the fastest over a given period of time. Stocks, bonds, cash, or government securities? Well, most of us would agree that over any length of time, stocks would probably grow the fastest. It might not have been true over the first three years of this new millennium, but over any length of time, stocks are going to grow faster than cash.

Today, if we were to slice our cake into four equal slices and turn around and look at it in a few years, it might no longer be equal. We might discover that the cash is still the same size, but the stocks have grown in value. Maybe the bonds and the government securities have grown in value. Maybe one of them has fallen in value. We will discover that the cake that we so carefully baked and we so carefully sliced is no longer in the same shape that it once was because one asset grew in value faster than another. Well, what do we do about that? Obviously we've got to do something about it because our cake is out of whack. It no longer has the shape it originally had. If we originally wanted each of our assets to consist of 25% of our slices, well, what do we do when one of them is too big and another one is too small? It's simple. We reallocate. We re-slice our cake. If one slice has grown more than another, doesn't it make sense that we reduce the size of that slice and we take some of that and put it into the other slice that has fallen in value? That's exactly what it comes down to. In other words, what I'm telling you is that you sell the asset that has grown in value and you buy the asset that has fallen in value. You sell the winner and you buy the loser.

So, when you're looking at your asset allocation decision, it is very, very important that you rebalance your portfolio periodically. And when you do, you will discover that you must sell your winners to buy your losers.

Session 9: The Pros and Cons of Popular Investment Strategies

RISK VS. RETURN.

There are some people who say, "You know what? This whole diversification thing makes sense, but we can take a good thing too far. Why should we put any money at all into bonds when we know bonds don't make as much money as stocks? Why don't we just invest in all the different sectors of stocks? There are 30 or 40 sectors within stocks, why don't we just rotate among them? I'll give you two reasons.

First, stocks fundamentally are stocks. In a declining market, there is no safe place to hide, and a great example of that is, in fact, the market of 2000 to 2002. Second, take a look at 9/11. On 9/11, something horrible happened. Not only to the country and to the victims of the tragedy, but from a financial perspective, something astonishing occurred. Wall Street was closed. If you had money in a brokerage account, if you had money in stocks, they were illiquid. You could not sell for several days, and if that was where all of your money was and you needed the money for some reason, you couldn't get a hold of it. Diversification is designed to lower risk. It is not necessarily designed to lower returns. If you own a stock portfolio it might make you a lot of money, but it also subjects you to massive amounts of risk. A highly diversified portfolio can make just as much money, but it can do so with half the risk that you would otherwise experience, and that is what many people don't understand. When many people invest, they look at return; they forget to look at risk. A proper investment strategy considers both.

FOUR WAYS TO BUY INVESTMENTS.

You have four choices when it comes to buying investments. First, you can put your money into mutual funds and let the funds buy your investments for you. Second, you can put your money into variable annuities and then let the annuities buy your investments for you. Third, you can put your money with a private money manager and let the manager buy your investments. And fourth, you can buy your own investments, either with or without the assistance of a stockbroker or financial advisor.

MUTUAL FUNDS.

Here are the benefits. Number one, a mutual fund is managed by a professional investor, often the very same people who handle all those institutional assets. And I'm sure you would agree, or at least I hope you would, that a professional money manager is probably going to do a better job at picking investments for you than you're going to do on your own.

Second, you get diversification. Instead of having all your eggs in one basket, trying to pick from a bunch of different stocks. Each mutual fund invests in hundreds of stocks. If it's a stock fund, they buy stocks. If it's a bond fund, they buy bonds. If it's a real estate fund, they buy real estate. But in all cases, you get extensive diversification.

Third, mutual funds are remarkably affordable to own. You can open an account, often with as little as $500, and you can add to it whenever you want. You can also withdraw money anytime you want. They're very convenient and easy to afford

Now on the downside, although you can pick a fund that buys whatever asset class you want—for example, if you want a stock fund, you can buy a stock fund—you have absolutely no say over what stocks the fund is going to buy. So, if you have strong opinions over what stocks you want to own, you can't do it with mutual funds. You also have very little control over the timing of tax liabilities.

VARIABLE ANNUITIES.

A variable annuity has all the advantages of mutual funds plus a few more. Number one, some annuities offer a variety of mutual fund families. So, instead of having to work with several families, you can have one annuity and get several families all in it, so it's actually even more convenient. You also get absolutely no annual tax liability. This is the number one complaint of mutual fund owners. If you have an annuity, it works like an IRA. The money you put in there is not subject to annual taxation and as a result of that, you enjoy total control over the timing of your tax liability. You don't pay any taxes until you withdraw money, so you control when you pay the tax because you control when you make the withdrawal. If you don't make any withdrawals for 20 years, you don't pay any taxes for 20 years. You also can rebalance your portfolio inside the annuity without any tax liability.

Here are the cons. If you do make a withdrawal prior to age 59-1/2, you're going to pay a penalty of 10% and you're also going to pay taxes. In other words, the IRS is saying, "We'll let the money grow tax-deferred. You better not touch it, though, until you're 59-1/2." And when you do finally withdraw the money, the profits are taxed at ordinary income tax rates. That could be twice as high as capital gain tax rates. So, the good news is you don't pay taxes for many years, but when you finally do pay the tax, the tax is probably going to be higher. Also, if you die while owning an annuity, your estate or your heirs are going to pay the income taxes that you never paid. With a mutual fund, if you die, your heirs get the mutual fund and they never pay the taxes on the profits; but in an annuity, they will. So clearly, the annuity is at a big disadvantage when it comes to estate planning.

PRIVATE MONEY MANAGER.

There are basically three advantages. First, when you hire a private manager, your money is put into a managed account, sometimes called a "wrap account." And when you hire the money manager—it's often the same folks who handle mutual funds or institutional assets—they invest your money for you. And the theory here is, again, you'll get better results than if you tried to manage the money on your own. Second, your money is invested separately from all of the other clients. As a result, you have some limited ability to tell your manager how to manage the money. And third, you have a lot of influence over the tax effects of your account. You can tell your manager to delay transactions until the next tax year or to speed them up to get them done this year. You do not have any of that kind of control over mutual funds.

Actually, even though those are the three advantages of private money managers, you could argue that each of those three is really a negative. Here's why. If you want to tell your manager what stocks you want to own, what do you need the manager for? The whole point of this is giving them the ability to handle your account. If you think you're better at it than the manager is, then don't hire the manager; and if you don't think you're better, then shut up and let them do their job.

Second, if you do hire a private manager, you can forget about getting simple statements. Instead, you're going to get multipage statements every month with line-by-line listings of every holding in your account and every transaction detailed. You're going to see how many shares you own, when you bought them, what you paid, what they're currently worth. It makes it really difficult to resist the temptation to micro-manage the account.

And finally, private accounts are also usually more expensive than mutual funds and annuities. Unlike mutual funds and annuities where the fees are hidden, fees for private accounts are not hidden. You will see the debit right on your statement, and it's going to be reflected there every month.

BUYING INVESTMENTS ON YOUR OWN.

There are really only two advantages to this strategy. Number one, by picking your own investment you have total control. If you want a truly customized portfolio, this is how you get it. And as a result of that, you have total control over the timing of your tax liabilities.

The two disadvantages are pretty obvious. By picking your own investments, it's the most complex way to manage your money. The burden is entirely on you. You're going to do your own research, which takes a lot of time and knowledge and attention and energy. And, you can expect to spend more on commissions, transaction fees, and taxes than you would if you went any of the other routes.

Session 10: The Truth about Morningstar Ratings

PAST PERFORMANCE IS NEVER AN INDICATION OF FUTURE RESULTS.

Of all the money invested in mutual funds in this country, about 90% of the money is in mutual funds that are four star and five star rated funds. Now, that can not be a coincidence. Obviously, everybody is relying on Morningstar, the star rating system.

Well, that raises a question, doesn't it? Do the ratings work? If you are relying on the ratings to buy your funds, does it work? Does buying a five star fund make more money than buying a one star fund? And this is where it gets fascinating. Based on the data available from all the academic studies, all the research, including Morningstar's own research, we discovered that if you buy a mutual fund simply based on the rating, then you might as well flip a coin. And the reason is quite simple: Past performance is no indication of future results. The reason that we stress the fact that past performance is no indication of future results in the mutual fund world is because they are not predictable products. And the reason they aren't predictable products is because the environment is always changing.

Here is the truth about Morningstar ratings. Morningstar ratings are not predictive tools. The Morningstar rating is an historical tool. Morningstar is not trying to tell you what's going to do well in the future; Morningstar is simply telling you what did well in the past. Morningstar itself says they make no claims about the future. That is not the intent of the star ratings. In fact, here is what Morningstar's literature actually says, quote, "Our system does not lay claim to some magical methodology for predicting future returns. As we see it, our job is to offer an objective measure of each fund's historical performance and risk." Historical performance and risk, not predicting future returns.

Session 11: Six Steps to Choosing the Right Mutual Funds

Six questions you need to answer when selecting mutual funds.

• QUESTION ONE: IS IT ME OR IS IT HOT IN HERE?

Did you ever say that to somebody? And they say to you, "Oh, it is hot in here." And you instantly feel better because you were thinking, "Oh my goodness, am I getting sick? Am I coming down with something?" And then you think, "You're hot, too? Oh, good, it's not me, everything's okay." What I'm talking about here is something that is called relative performance. You see, a lot of investors focus on absolute performance, and that is a very dangerous thing to do. A lot of people say, "How much money did that fund make last year?" That's not relevant. What is relevant is how did that fund do last year relative to its peers?

• QUESTION TWO: ARE YOU ALWAYS THIS WACKY?

I'm going to put this in the context of two different investments. They both earn a 10% annual return. So, which one's better? Let's say that you've got an investment that two years in a row earns 10%. It earns 10% in year one and 10% in year two. What's its average return? Well, 10%. That's easy, right? Let's take a look at a second investment. It earns 20% in year one and nothing in year two. It's average return is also 10%. Which one would you rather own? Interestingly, the fund that goes 10 and 10 makes more money than the fund that's 20 and zero. Let's do the math. Say you've got $100 and you have an investment that earns 20%. How much money do you have? $120. And the following year it earns nothing. So, you still have $120 after two years. But, let's take a look at the investment that grew by 10%. You start with $100, it grows 10%, how much do you have? $110. And then the second year it grows another 10%. What's 10% of $110? $11. Now you have $121.

So, what you really want to have is an investment that generates consistent returns as opposed to occasionally big returns. Consistency is extremely important in mutual fund investing.

• QUESTION THREE: WHY DOES B COME AFTER A IN THE ALPHABET?

We know what the letter A is in the Greek alphabet. It's alpha. And the letter B is beta. That's the second letter in the Greek alphabet. Why is beta important? It's important because beta is a statistical tool that investors deal with in the world of mutual fund analysis. Now, there is also an alpha in mutual fund analysis, but it isn't used nearly as much. Beta is the key. Beta gives you a sense of how volatile a mutual fund is relative to the stock market as a whole. If you look at mutual fund statistics, a beta of 1 is assigned to the S&P 500 stock index. If you're looking at a mutual fund that is a beta of 1, that means it is equal in volatility to the S&P 500. If you're looking at a mutual fund that has a beta of 2, that means it's twice as volatile as the S&P 500. And if the beta is .50, that means it's half as volatile as the S&P 500.
So, if you're trying to find a mutual fund that is relatively low in risk, you want a beta that is a low number, that is a number below 1. And if you want something really aggressive, something that is really volatile, something that has the potential for making a huge amount of money, you want something that has a beta above 1.

• QUESTION FOUR: AM I GOOD OR JUST LUCKY?

This is a question a lot of folks have to ask about the manager of their mutual fund. Is your manager good or is he just lucky? Let's say that you've got Joe, he manages a mutual fund and he's really good at it, and he knows he's really good at it. Suddenly, Joe gets hired away by a competing firm. Now, Joe's at a new mutual fund. I want to ask you a question, can Joe brag about the track record he produced at his old fund?

Well, there are two regulatory agencies that weigh in on this question. First is the SEC, the Securities and Exchange Commission. The SEC says he can. He can talk about his track record. Therefore, in the prospectus for the mutual fund, you will see data that reflects Joe's performance record at his old mutual fund. But, the NASD says no. The National Association of Securities Dealers, the ones that regulate mutual fund advertising, they say no, no. Not so fast. There's more to a track record than great pitching. There's also great fielding. And this pitcher, without the great team behind him, might not have had as good a record. And therefore, the NASD says Joe may not brag about his track record in his mutual fund advertising and literature. So, the regulators themselves disagree on this topic.

The reason I raise this to you is because it's critical that you look at the manager of your fund. You could have a fund with a tremendous 10-year track record, but if all of a sudden it has a brand new manager, is that 10-year track record of any value? You've got to make that decision. How are you going to make that decision until you drill down into the fund and find out who's managing the fund, how long have they been managing it, and what were they doing before they got there. The manager is key in the mutual fund selection process.

• QUESTION FIVE: IS THAT A DIAMOND RING OR CUBIC ZIRCONIUM?

They say diamonds are a girl's best friend. But, how many of them are wearing cubic zirconium without knowing it? Appearances, in fact, can be deceiving. That's the fifth question on our list in the mutual fund selection process. You need to take a real close look at what a mutual fund actually holds in its portfolio. This is why you've got to go beyond the prospectus and look at the annual report. The prospectus tells you what the fund can do. What the annual report tells you is what the fund <u>does</u> <u>do</u>. You've got to see what the actual holdings of the fund are because it's the holdings that are going to determine the return.

• QUESTION SIX: DO YOU ALWAYS GET WHAT YOU PAY FOR?

We're talking about fees, of course. This is the last thing we're going to be talking about in the mutual fund selection process, and that's where it belongs on the scale of importance. And I stress this because too often investors pick mutual funds and the very first thing they say is, "I want a no load fund. I want a fund with low expenses." That is a very foolish thing to do. Why? Because all of the academic data shows that there is no correlation between performance and fees. No correlation at all!

Session 12: More about Mutual Funds and the Truth about Index Funds

SECTOR-SPECIFIC FUNDS VS. HYBRIDS.

When it comes to mutual fund selection, should you buy sector-specific funds or should you buy hybrids? This is a really important question because a lot of people get this wrong when they buy mutual funds. You have a choice. You're either going to buy a growth or a value fund or you're going to buy a diversified stock fund. A diversified fund is a blend fund. A fund that's going to buy both growth and value. A fund that's going to buy both small cap and large cap. So, it's your choice. But it would be redundant to have two growth funds. And it would be redundant, potentially, to have two diversified stock funds. Are you going to have bonds in your portfolio?

Well, sure you are, because if you don't have bonds in the portfolio, the only thing you've got left are stocks. So, yes, you're going to buy a bond fund. And yes, you're going to buy a stock fund. And another option would be to buy a balanced fund. A balanced fund contains stocks and bonds. So, it's your choice as to whether you're going to buy sector-specific funds or hybrids. It's entirely up to you. My only concern is that people don't understand that there is a difference between them and they haphazardly buy one without knowing its impact on the other. Remember, pay close attention to the nature of the fund you're buying so that the other funds you buy are truly different and not redundant.

HOW MANY FUNDS DO YOU NEED?

I'm going to give you an incredibly diversified portfolio using six funds. Are you ready? One money market fund, one government bond fund, one corporate bond fund, one U.S. value stock, one U.S. growth stock, and one international stock fund. That's it. Six mutual funds and you will have a portfolio that is more diversified than 99% of all U.S. investors. It's simple, manageable, and inexpensive.

SHOULD YOU BUY AN INDEX FUND?

The people who argue that investing in S&P 500 stock index funds is the superior way to go are simply, flatly, and completely wrong. You should not invest in index funds. After I'm through sharing this information with you, you will never own an index fund again.

Let me share with you the truth. It is true that from 1994 to 1998 the S&P 500 stock index beat the vast majority of stock mutual funds. That is true. For that four-year period of time, it is true that the vast majority of stock mutual funds were unable to make as much money as the S&P 500 stock index. But you know what? Somebody came along and said, "Hey, take a look at that fact." Then somebody else came along and said, "Oh, that fact must be a truth." What's the difference between a fact and a truth? A fact is something focused on the situation at hand. A truth is a universal timeless statement.

In other words, yes, it was a fact that in that four-year period the S&P 500 stock index beat most actively managed funds. However, it is not a truth. Take a look at the period 1977 through 1979. During that period of time the S&P 500 beat only 25% of actively managed funds. Take a look at the period 1980 to 1982. It beat only half of actively managed funds. Take a look at the five-year rolling intervals ever since 1981 and you'll see that the S&P 500 beat large cap stock funds less than half the time. And, it beat small cap stock funds only once in the five-year interval of 1986 to 1990. In fact, for much of the middle '90s, indexes won most of the time, but that streak ended in 1998. In 1999, in 2000 and in 2001, the vast majority of actively managed funds beat the index. According to the data for the year ended June 30th, 2001, 67% of stock funds beat the S&P 500. For the 18 month period ending at the same time, 73% of stock funds beat the S&P 500. And, for the last two years, 83% of all stock funds beat the index. It is simply not true that index funds make more money than actively managed funds. It is simply a false claim.

Session 13: A Serious Consideration — Long Term Care

SOMETHING YOU MAY HAVE NEVER THOUGHT ABOUT.

Let me ask you a question. Are you going to live to a nice old age? If you answered yes, do you know what that means? It means you are likely to incur the need for long-term care services. The need for long-term care services is almost certain. In fact, the odds are one in two. That's right. One in two Americans over the age of 65 is going to require long-term care services at some point in their lifetime. It is the single biggest cause of financial poverty among retirees, and you probably have given it little or no thought.

The current cost of long-term care in this country is over $45,000 a year, according to the American Council of Life Insurance. According to the Health Insurance Association of America, 72% of all Americans already have faced the cost of long-term care or eventually will. Odds are long-term care is in your future. The big problem is that the annual cost is not covered by your health insurance and it is not covered by Medicare. It is paid entirely by you. So, how are you going to pay for it?

Well, I'm going to give you a choice. You can pay $4,000 a month for the care or you can pay a few hundred dollars a year for the care. What I'm talking about is that necessary evil called insurance. In this case, it's long-term care insurance. Long-term care insurance, without question, is the most cost-effective way to protect yourself and your family from the financial devastation associated with long-term care. And here's the good thing. The younger you are when you buy it, the cheaper it is and the more likely it is you'll get it.

EIGHT FEATURES TO LOOK FOR WHEN BUYING A LONG-TERM CARE POLICY.

1. You should have a policy that provides you $150 per day in coverage.
2. Make sure your policy provides at least three years worth of benefits, and I strongly prefer five or six years.
3. You want a policy with a 100-day waiting period.
4. Inflation protection. You need to make sure that your benefits rise over time.
5. Make sure that your policy will pay you benefits even though you do not go into a hospital first.
6. Make sure the coverage is not limited to skilled nursing homes.
7. The policy should offer a waiver of premium.
8. Most importantly, make sure your policy offers home healthcare benefits. And make sure that it pays those benefits at 100% of the daily rate.

Session 14: The New Rules for Your Income, Expenses, and Debt

NEVER ACCEPT A NEW JOB JUST TO GET A HIGHER SALARY.

The average American worker changes jobs every five years. That means one out of five U.S. workers changes his or her job every single year. Think about it. How long have you been at the job you're at right now? How much longer do you think you'll stay there? The whole notion of womb to tomb employment is pretty much gone. And the most common reason people site for changing jobs is career growth. But, I want to ask you a question: Is career success the same thing as financial success? Not necessarily, and in many cases people are changing jobs for the wrong reasons. Here's why. When you change jobs you have to stop participating in your company retirement plan. When you join a new job, in many companies they don't let you start the new plan until you've been there for six months or a year. Now, if you change jobs every five years, you effectively throw yourself out of the plan one year out of every five. That is going to cost you a huge amount of money by the time you retire.

Compare two workers. One of them is a job changer. Every five years he or she gets a new job. The other one stays at the same company forever and therefore always participates in the company retirement plan. Even though the job changer might end up with a higher salary, they don't necessarily wind up with more money in their retirement plan. So when you change jobs, make sure that you are allowed to join your new retirement plan immediately. And if you're not allowed to join immediately, ask your new boss to pay you a bonus equivalent to what you're losing in retirement plan benefits. Otherwise, if they're not willing to do that, you need to rethink the validity of changing that job.

CASH ON HAND.

When dealing with a possibility of a downsizing or an interruption of income, there's no substitute for cash. It's as simple as that. Cash is king. We learned that lesson all to harshly as a result of September 11th. Wall Street was closed for a week! If all of your money was tied up in stocks and bonds, you didn't have access to it. Forget about its market value. Wall Street was closed. You couldn't get your money out. Cash is king. It is therefore critical that you maintain sufficient cash reserves to maintain the safety and stability of your family, to make sure that you can put food on the table, put gas in the car, and buy medicine for your kids. What it comes down to is very simple. You need to have cash on hand, somewhere between 2 months and 12 months worth of spending money.

THE FOUR-STEP PROCESS TO MONEY MANAGEMENT.

• Number One

The very first thing you should do is participate in a company retirement plan. Yes, a lot of people tell you that the first thing you should do is pay off your debts. I don't agree. The reason I don't agree is that if you stop investing, if you delay your investing until after you pay off your debts, you'll never invest. And the reason is simple, you will never pay off all your debts. Paying off your debts is a wonderful goal and it's a lofty goal. It's also for most of us an unrealistic and unattainable goal. Remember, I talked earlier about the need to set realistic goals. Setting a goal to be debt-free is fine, but if it takes you 10 years to be debt-free, that's 10 years of retirement savings you'll miss out on. Participate in your company retirement

plan first, to the maximum that you are allowed to participate. Your retirement is inevitable and you need to have money at that time. Start saving for it now.

• Number Two
Second, get rid of all your debt. Yes, now is where you focus on getting rid of all the debt — with the exception of a mortgage, that's okay. Credit card debt, student loan debt, car loans and personal loans, get rid of those other debts as quickly as you possibly can.

• Number Three
After you get rid of the credit card debt and all the personal debt, then you build cash reserves.

• Number Four
After you've built sufficient cash reserves, now you're ready to start investing in stocks, bonds, mutual funds, real estate, and any other investments you like.

GETTING RID OF DEBT — TRACKING YOUR EXPENSES.

The purpose of this exercise is to help you get a grip on where your money is really being spent. Until you know where your money is going, you won't be able to fix the problem. Feel free to expand this list or do it on a spreadsheet program on your home computer. Good luck!

WHO	AMOUNT	WHAT
Example: Grocery store	*$200.00*	*Food*

Session 15: The New Rules for Family Finances, Money, and College Planning

SOME ADVICE ON INHERITANCES.

It goes without saying that people are living longer than ever before. Back in 1900, life expectancy in this country was 47. Today, life expectancy is 76. If you are 76 you're going to live into your 80's. If you're in your 80's you're going to live into your 90's, according to actuarial data. The fastest growing age group in America is those over age 85. What this means is that people are not receiving their inheritances until they are much older. You see, back in the old days when people died in their 40's, their children got their inheritances when they were in their 20's. That doesn't happen anymore. Today, people live into their 80's and 90's and their children get their inheritances when they are in their 60's and 70's. Does your 65-year-old son or daughter really need an inheritance?

What it comes down to is this: Are you going to leave an inheritance to your kids and to your grandkids? You probably are and you might even be very deliberately planning on doing so. After all, your parents may have left you an inheritance. And chances are you're going to leave assets of some form or fashion to your kids and grandkids.

Here's something to consider. Don't wait until you've died to give your kids their inheritance. The reason I say that is chances are you're going to live so long that your kids are not going to get their inheritance until they are senior citizens. Meaning, they don't really need your money when they're 65 or 75 years of age. They will have long since past the time of financial need. Wouldn't it make more sense to give money to your kids when they're busy raising a family, buying homes, and sending their own kids to college? That's when they are in financial need. That's when $10,000 or $100,000 would make a huge difference in their life.

FINANCIAL COMPATIBILITY QUESTIONS.

I've got 28 questions for you. These are questions that you need to answer, ideally, before the wedding takes place. If that's not possible, don't worry, please proceed on with them. These are 28 questions that you need to answer by yourself. Sit down at the kitchen table and carefully go through this exercise. Answer the questions below and then have your spouse/partner do the same. After you've both finished, compare papers to see what the other person's answers were. I think you'll find it very interesting.

1.) I want you to make a list of all of the debts that you owe. How much do you owe and what kind of debts do you have?

2.) Are you behind on any payments? Have you ever missed a payment? Have you ever been turned down for credit? If so, explain.

3.) Has a creditor ever called you? If yes, provide details.

4.) What is your annual income?

5.) Do you plan to work full time until retirement age? You need to write down specific details.

6.) Do you expect your partner to work full time until retirement?

7.) What percentage of the family's total income do you expect to contribute?

8.) Which of the two of you will be responsible for paying the bills each month?

9.) How much of your income are you willing to devote to the household's monthly bills? Write down an answer that's both in dollars and as a percentage of your income.

10.) How much of your partner's income should he or she contribute to the household's monthly bills?

11.) How much of your income are you willing to place into savings and investments? Again, write down dollar amounts and percentages.

12.) How much of your partner's income should he or she devote to savings and investments?

13.) How much credit card debt do you believe is acceptable?

14.) Would you be willing to use your income and assets to pay off the debts that your partner accumulated prior to the marriage? And if so, what percentage of your partner's debts are you willing to pay?

15.) Should your partner be willing to use his or her income and assets to pay off the debts that you accumulated prior to the marriage? And if so, what percentage of your debts should your partner be willing to pay?

16.) Do you plan to maintain a bank account in your name only?

17.) Does it matter to you if your partner maintains a bank account in his or her name only?

18.) Should the two of you maintain a joint checking account? And if yes, A) should money be contributed to it by both of you or just one of you? And if so, which one? B) What percentage of your income should you or your partner contribute? Be specific.

19.) Do you plan to have credit cards in your name only? And if so, how many cards?

20.) Does it matter to you if your partner maintains credit cards in his or her name only?

21.) Should the two of you maintain joint credit card accounts? And if yes, which of you will use these accounts?

22.) How many children do you want to have?

23.) How soon do you want to have your first child?

24.) When your first child is born, will you or your partner leave the workforce to become a full-time parent? And if so, for how long and which one of you will do this?

25.) Are you willing to relocate to another city?

26.) Is it your intention to relocate to another city?

27.) If you received a windfall of a significant amount of money, how much would that be?

28.) What would you do with that windfall? Be specific.

PREPARING TO PAY FOR COLLEGE — ONE GOOD IDEA.

Here's a great option. It is called a Section 529 plan. It's available in all 50 states and it works in a really nifty way. First, you can join any state plan. You don't have to be limited to the state where you live. Anybody can join any plan. You can put in as little money as you want or as much as you want. As little as $25, depending on the state you live in, or as much as $250,000. The money you put into the plan for the child grows on a tax-free basis. The money gets invested into mutual funds and you can pick the mutual funds by picking the specific plan you wish to buy. When you make a withdrawal, the money is withdrawn tax free, provided that it's used for college.

The money can be used for any college in the country and it can be used for just about any college expense. And here's the best part: If the child ends up not needing the money because they don't go to college or because they get grants or scholarships, you can take the unused portion of the money and give it to another person in the family. And I don't mean just a brother or sister, you can give it to cousins, you can give it to parents, you can give it to aunts and uncles. You can give this money to virtually any other member of your family. So, what is really exciting to me is that parents now have an affordable, effective way to save for college.

Session 16: The New Rules of Retirement Planning

RETIREMENT IS BEING REDEFINED.

Are you looking forward to your retirement? Well, knock it off. You're probably not going to retire, not now and not ever. Oh, by the way, this is not a problem. This is actually really exciting. You see, retirement was the social innovation of the 20th century. It never existed prior to the 20th century and we're no longer in the 20th century. Indeed, retirement will not exist in the 21st century. You need to get used to that fact. You need to plan accordingly.

It's really interesting. When you're 21 years old and you're getting out of college, you can't wait to get into the profession of your choice. You can't wait to get that first job. You are two things, number one, totally immersed in your job, and number two, immortal. Heck, there isn't a 21 year old in this country who thinks they're going to die any day. So between loving their new-found profession and never wanting to die, never intending to die, never thinking it's ever going to happen to them, their attitude is, "Why would I ever want to quit work? I love this, I can't wait to do it, I can't wait to go to work in the morning." It's new, it's fresh, and it's exciting. And that's just what they continue to do.

But something happens around their mid-40's. By the time they're in their mid-40's they've been working at that career for 20-plus years. It's not so new, it's not so fresh and it's not so exciting anymore. And they begin to wonder, "Is there something else I might want to do?" And, something else happens by the time you're in your mid-40's, people around you start dying. You begin to realize that you're not immortal. So, those two facts begin to build up and you begin to wonder, "Is there something else I might want to go do?" And, as a result, many people begin to realize that playing golf isn't necessarily something they want to do from age 65 to age 90.

What this means in a nutshell is that you have to redefine retirement. You have to redefine what your lifestyle is going to look like. Are you really going to work until you're 60 or 65? And then spend the next 30 years not working? And what are you going to do if you're not working? What you've got to really understand is that beyond all else, how you're going to spend your retirement future is really not about a retirement future, but simply a core factor of your life.

THREE KEY THINGS TO REMEMBER.

- It all begins with your goals and objectives.
- Average savers with great investments don't make nearly as much money as great savers with average investments.
- Think long term, buy and hold, using extensive diversification of high quality mutual funds.

Finally, let me share with you just a few of the things that my clients have told me over the years. I hope it will give you some inspiration and some motivation. I hope it will help you understand that just like them, you can do it, too. Best of luck!

"I put money into my investments each month before I pay the bills. It's smarter than investing what's left over."

"At a relatively young age, I invested in my employer's retirement plan. As a result, I will retire and never have to alter my lifestyle."

"I started at 35 and didn't wait any longer. I think everyone should do some planning. Most people don't. People should look at everything in the long term."

— Edelman clients

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