

Investing: Where to Put Your Money Now

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You make more money than you spend. It's the right problem to have, but it's a problem nonetheless. In fact, every new dollar of savings seems to call for a new investment strategy, but you don't know where to begin. When you ignore the problem, cash piles up in your checking account—first \$40,000, then 6 figures. Then you get nervous. If it was hard to invest a smaller sum, it seems impossible to invest more than \$100,000.

Then one day, you stumble upon the headline that brought you here, hoping to find the answer. And if this were any ordinary article, you might be well on your way to making the same mistake that most of your colleagues have made at least once in their careers: they pile their money into a hot investment touted at the time. First, they buy it. Then, they watch it drop like a rock. And, months later, when the promised results fail to materialize, they sell everything and feel foolish. It gets worse as the cash continues to pile up and your question goes unanswered: "Where do I put my money now?"

The best investment strategies have nothing new about them and they work. Here are 3 investment strategies you can use over and over again, decade after decade, to make your savings last.

Stop Trading Stocks and Start Owning Markets

We are sure that you have heard stories in the doctor's lounge about how your colleagues doubled or tripled their money with their latest stock picks or how they nabbed a tax-free bond paying 5 full percentage points above average. Sounds like they are making a killing, right?

Not exactly. The chances are good that they have gotten killed on plenty of trades, but physician cul-

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Single stocks can go bankrupt and single bonds can go into default, wiping you out completely. Index funds, which represent ownership in

hundreds if not thousands of companies, make it easy to gain instant diversification, diluting the uncompensated or "bad" risk while retaining the "good" risk that leads to rewards over the long haul.

Index funds are cheap. With operating expense ratios as low as 0.05%, you can buy an index fund and gain exposure to bonds or stocks around the world. That insignificant carrying cost also buys you the freedom to stop acting like a stockbroker and allows you to get back to serving as a healthcare provider. Savvy physicians prefer mutual funds for their tax efficiency. Since they follow a buy-and-hold approach to investing, index funds are more likely to realize tax-favored capital gains and tax-qualified dividends than more highly taxed short-term gains. This keeps your tax bill in check.

Stop Timing the Markets and Start Owning Them (All)

If you have heard about index investing, you probably know about the S&P 500, a basket of stocks that represents the 500 biggest companies in the United States. The index was made famous in the 1980s and 1990s as it ran up to the dotcom bubble, then vilified in the ensuing "lost decade" when the 10-year return on that index was close to zero.

What index hecklers fail to realize, even to this day, is that there's more than one index. In fact, you can gain exposure to practically all the stocks and bonds on the planet by owning as few as 4 mutual funds. Had investors done this during the past 10 years, they would have avoided some of the technology crash, found the lost decade, and enjoyed very decent returns after all.

Unfortunately, the average inves-

tor seldom receives average returns. According to a recent study by mutual fund data company Morningstar, “the typical investor gained only 4.8 percent annualized over the ten years ended December 2013 versus 7.3 percent for the typical fund.” That’s a yawning 2.5% gap.

Why did investors miss out on fully one third of the market returns? It’s simple. They did the same thing with their funds that your colleagues did with their stocks: they traded in and out of the market. To garner the returns advertised over the past decade, or even the last 3 decades, you would have to own them through thick and thin, no matter how dramatic or dire the news.

Invest Like a Nobel Prize Winner

The main argument against an index-only strategy is that it generates merely average returns in the best-case scenario. This logic appeals to doctors who have never once settled for things that are merely average (and that’s pretty much all the physicians we’ve met).

Thanks to the research of Nobel laureate Eugene Fama, we now know it’s possible to reliably beat the averages over the long run—but it’s not free. Mr Fama, a financial luminary who founded the first small cap index mutual fund, discovered that the smaller a company is, the more likely it is to outperform a larger one. This is known as the “small cap effect,” and it is robust, having been observed in US market history as well as the

return series of developed foreign stock markets and even emerging markets. Mr Fama and colleague, Kenneth French, both researchers who hail from the renowned University of Chicago Booth School of Business, also found that the stocks of cheap companies, known as “value stocks,” tend to outperform their more expensive “growth stock” peers in what is known as the “value effect.” This effect is also robust in markets domestic and foreign, and is available to investors using index funds.

Remember, the answer to good investing is more than where you put your money now. It’s where you keep it over the long haul.

While a small cap value tilt may add up to 4 percentage points more than the average untilted portfolio over long periods of time, it brings more volatility, too. When equity markets decline, those index funds filled with cheap little stocks take it hard, and you may wish you had never owned them. The only way to reliably garner the higher expected returns from small cap value stocks is to remain fully invested and stay the course, even when times are tough. This, too, is old news. Even

though Mr Fama won the Nobel Prize in economics just last year, his research on the small cap and value effects has been public knowledge since the 1980s.

Summary

These perfectly decent strategies are so mundane—so incredibly boring—that you and your colleagues may never have heard of them. After all, words like “diversified,” “tax-efficient,” and “cost-effective” make lousy headlines. The good news is that you can start using a solid investment strategy and keep using it year after year, decade after decade, secure in the knowledge that you have found a permanent answer to a nagging question. Remember, the answer to good investing is more than where you put your money now. It’s where you keep it over the long haul. ●

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