

If you're following the herd, you're going in the wrong direction

BY ANDREW MENACHEM

If you want to make money in today's markets and perhaps more importantly, preserve wealth, don't follow the herd. Taking a contrary approach to the market — selling stocks or real estate when everyone else is buying for instance — should be part of an investment strategy which will help by reducing investment risk and ensuring that your portfolio of assets remains diversified.

After boom and bust cycles in dot-com stocks, real estate condos, and oil and gas companies, you would think investors would have learned this lesson. But the hot asset today is gold, which seems to be the topic of every cocktail party conversation. Just remember that every boom in the past 25 years has been followed by a bust. So, it doesn't make sense to pay top dollar for trendy assets that have nowhere to go but down once the frenzy subsides.

In fact, the biggest winners this year are likely to be investors who bought stocks at bargain prices last year at a time when the "herd" was selling. It is no easy task to ignore the noise and take the opposite approach of the majority but it can be important in being a successful investor.

So, how can investors avoid the classic mistake of following the herd?

In my experience as a financial advisor and educator, it's essential to make sure your investment decisions are being driven by intellect, rather than emotion. That objectivity helps ensure that you maintain a diversified portfolio of assets rather than

betting your financial future on any one investment.

Building a well-balanced portfolio is highly complex in today's environment. It's not enough to own only stocks and bonds, even if those stocks are mixed between small and large, growth and value, and U.S. and international. That kind of diversification may have worked before the millennium, but now even domestic and international stocks move in lockstep with one another.

While diversified holdings of stocks and bonds may still form the core part of your portfolio, effective asset allocation now includes all or some of the following asset classes: private equity, real estate, oil, timber, gold, TIPS, hedge funds, high-yield bonds, international bonds, global currency and managed futures.

This is extremely important in reducing the risk to your overall portfolio. That's because historically these alternative assets move independently of one another.

Unfortunately, most investors aren't allocating their assets properly or building portfolios that match their risk tolerance. Most investors don't even know how much risk they are taking and a good financial advisor should quantify that for you. Buying a variety of mutual funds, for instance, won't diversify your holdings if all those funds invest in the same stocks and bonds — as many investors sadly found out in 2008.

But a proper asset allocation strategy actually worked in 2008. Despite the huge drops in stocks, managed futures rose 14.4

percent, gold was up 5.8 percent and investment grade bonds climbed 5.2 percent.

Since no one can foresee the future, investors will always face political, economic and financial surprises that change market conditions. When this happens, try not to react emotionally, but stick with your plan and use your intellect. Remember that crisis creates opportunities. A properly diversified investment portfolio that includes rebalancing remains the best way to reduce your overall risk, as well as increase potential returns. Real wealth is made and lost during times like these. It takes courage and fortitude to ignore "group think" and take a step back and recognize when an asset class has become an imploding bubble or an incredible opportunity.



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