Beyond the Mortgage: The Next Step to Creating Wealth

by Ric Edelman

With the guidance of your professional mortgage broker, you've just been granted a new mortgage. Perhaps you obtained a cash-out refi. Or maybe you now realize you have money that's not invested ideally. Now what?

Don't get me wrong; I agree completely that getting a new, big, long mortgage is a great idea. I've been saying this for more than 20 years, and every academic study that's examined the issue agrees: Mortgages can help create wealth.

But obtaining a mortgage is just your first step. By having a big mortgage, you get to invest money you otherwise wouldn't have. The key, then, is to invest that money correctly.

Unfortunately, most consumers don't know how to invest that cash. Many are confused, while others fear the stock market's daily ups and downs. The ongoing scandal in the retail mutual fund industry has not helped. (Virtually every major mutual fund company and brokerage firm has been embroiled in one way or another — some people are in jail while dozens more have been ousted from the industry. At last count, regulators have assessed more than $5 billion in fines.) At the same time, some unscrupulous agents tout life insurance policies as "investments."

Thus it's understandable that consumer faith in the investment industry has been shaken. But you still need to invest the money you now have. How can you lower your investment risks and reduce your costs while generating competitive returns?

Like much of the public, my colleagues and I at Edelman Financial have grown disturbed over the state of the retail mutual fund industry in recent years. That's why we created the Edelman Managed Asset Program (EMAP), now one of the largest and most popular investment management services in the country. EMAP is a revolutionary, state-of-the-art investment solution that meets the needs of today's investors, and consumers around the country have already invested more than $2 billion through it.

EMAP allows ordinary Americans to invest alongside the nation's biggest institutional investors, such as pension funds, endowments, and ultra-high net worth investors. EMAP uses the same time-tested, proven investment approach they use, based on the latest academic research. This approach is based on three simple common-sense principles:

1. Invest for the Long-Term.

Many people think the stock market is risky. They're right — if you're trying to generate profits in just a week, a month, or a year. But if you look at the performance of the overall stock market over periods of 10 years or more, you'll see that stock prices are actually surprisingly stable. In fact, the stock market, as measured by the S&P 500 Stock

Index*, has been profitable in every 15-year or longer period since 1926. Thus, the first secret to successful investing is to remain invested for very long periods.

2. Be Diversified.

Too many people think investing consists of being either "in" or "out" of the stock market. But investing means much more than just U.S. stocks. Through EMAP, our clients invest in as many as 19 major asset classes and market sectors. Stocks, yes, but also bonds, government securities, international securities, oil and gas, commodities, and precious metals such as gold.

Each year, some asset classes and market sectors will perform better than others. Since it's impossible to know which those will be, the only way to be sure you'll capture all the profits is by owning *all* of these asset classes and market sectors. Thus, our clients own all the markets, all the time. This is called diversification — and it's the second secret to successful investing.

You achieve proper diversification through something called "asset allocation." Through this process, a portion of your money is placed into each of those 19 asset classes and market sectors — carefully distributing the money in conformance with your risk tolerance, need for liquidity, and desire for current income.

To further reduce risks, institutional investors invest very broadly in each asset class and market sector, using a market-based rather than manager-based approach; EMAP does the same. This means we don't hire fund managers who try to pick "hot stocks." Instead, our clients own thousands of securities within each asset class, allowing their asset allocation to serve as the primary investment consideration. This approach is supported by important academic studies showing that investment results are almost exclusively determined by asset allocation, not security selection.

Many people have heard of diversification, but most don't truly know how to do it properly. We've met consumers who own five or six mutual funds, and they're smug because they are "diversified." But when we examine their funds more closely, we often discover that each of their funds owns the same investments — meaning their portfolio is redundant, not diversified like they think. That's a big — and potentially costly — mistake. True diversification, by contrast, lowers your investment risks while providing you the competitive returns you seek.

3. Strategically rebalance.

The final secret is to rebalance your portfolio. If you don't, your carefully constructed asset allocation will drift over time due to varying returns of each of your investments. To correct this, you need to rebalance the portfolio; if you don't, you will not sustain your properly diversified portfolio — creating potentially big risks that could cause you to lose lots of money during a market downturn.

Shockingly, few investors ever rebalance their portfolios. Even those who do rebalance tend to do it inefficiently (simply based on the calendar, such as quarterly rebalancing). But EMAP is much more sophisticated, again following the pattern used by many of the nation's biggest institutional investors: We rebalance *when needed.* This means we review each of our clients' portfolios every single day. By examining the portfolio on a continuous, ongoing basis, we can rebalance your portfolio whenever it's necessary, while avoiding pointless transactions that can occur when you rebalance by the calendar. (It's silly to rebalance merely because it's June 30!)

Strategic rebalancing is a vital part of investment management. It is how institutional investors manage their money, and it's a primary advantage of EMAP.

Use Institutional Mutual Funds, not Retail Funds

Thanks to EMAP, you can obtain the very investments used by some of the nation's largest institutional investors. Normally, these investments require $2 million each — meaning a properly diversified portfolio would require you to invest $25 million or more. But through EMAP, these same investments are available to you — and you don't need millions of dollars. Instead, EMAP's minimum is just $75,000 per household, and we can open individual accounts for you with as little as $3,000. And these investments, which are not available through retail brokerage firms or ordinary stock brokers, are incredibly inexpensive — typically a fraction of the cost of ordinary retail mutual funds.

Avoiding high investment costs is just one more advantage of EMAP. More importantly, you can now leave behind the retail mutual fund industry and their deceptive business practices. Since 2003, federal and state regulators have been uncovering hidden costs, undisclosed risks, unfair trade practices, conflicts of interest, fundamental violations of trust and outright crimes. I reveal all of this — including naming names — in my new book, *The Lies About Money* (Simon & Schuster, available October 2007) and show that people who own retail mutual funds are suffering lower returns, and incurring higher costs and higher risks than they realize. EMAP provides consumers with the solution to these problems.

You were smart enough to obtain a big long mortgage. You've taken the first step toward long-term financial security. Now, you must take that next step.

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* An Index is a portfolio of specific securities (common examples are the S&P, DJIA, NASDAQ), the performance of which is often used as a benchmark in judging the relative performance of certain asset classes. Indexes are unmanaged portfolios and investors cannot invest directly in an index. Past performance is not indicative of future results.

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Best-selling author Ric Edelman's sixth book, *The Lies About Money*, will be published in October 2007 by Simon & Schuster. Ric also writes a nationally syndicated newspaper column and hosts a weekly personal finance advice show broadcast by ABC Radio Networks. For more of his financial planning advice, visit www.RicEdelman.com. Information about the Edelman Managed Asset Program (EMAP) is at www.emapadvisor.com.