

WHAT IS THE REAL REASON YOU SHOULD INVEST?

Most people think they know the answer to the question of why should they invest. Yet many all too often invest for the wrong reasons—and that can lead to financial difficulties.

Most investors assume that the goal of investing is to simply earn the highest return possible without losing money. If they're investing in common stocks, they assume they should earn at least 10 to 11 percent every year because that's roughly the long-term average for stocks. But often they're not satisfied unless they exceed that by earning 20 or 30 percent or, heck, doubling the return on their investment.

But wise financial planners will tell you that earning the highest possible return should not be the real goal of investing. Rather, the main purpose of investing is—in conjunction with other components of your financial life—to help you realize major life goals: a comfortable retirement, a dream job or business, a college education for your children, funding for your favorite charities, or accumulating assets to pass on to your heirs.

What's the difference between these two approaches to investing, you may wonder. What's wrong with double-digit returns? Won't they accomplish those life goals? Nothing's wrong with consistently earning double-digit returns. It's nice work if you can get it.

The problem with shooting for the highest return possible as the main goal in investing is that it can create unnecessary risks and erratic investing patterns that ultimately undermine efforts to achieve those life goals that truly matter to you.

Most financial planners have war stories about clients, or more often, prospective clients, who come to their office expecting that the planner's primary job is to earn them fat returns on their investments—to beat the market. When these planners respond that they can't design a sound investment strategy until they understand the person's goals and the other aspects of their financial circumstances, these prospective clients often leave and head for the next financial advisor, until they find one who promises them glorious returns.

How can investing solely for the highest returns create unnecessary investment risk and erratic investing patterns?

Holding unrealistic return expectations. A California CERTIFIED FINANCIAL PLANNER™ practitioner recalls being fired by a client during the height of the booming late 1990s stock market because though the client's portfolio was doing very well, and was more than accomplishing the client's goals, it wasn't earning the 100 percent annual return the client thought it should be earning. The ensuing bear market harshly demonstrated to that former client and many other exuberant investors that high double-digit returns of the 1990s were not a given.

Taking unnecessary risks. Much of the riskiest investing, overbuying, and panic selling during the late 1990s and early 2000s would have been avoided if individual investors had created their own investment plan for achieving *long-term* specific goals such as retirement or a college education. For example, investors who can reach an investment goal by earning a modest average annual return are less apt to jump into higher-risk investments than those with no plan except to always “go for the highest return.”

Investors shooting for the highest returns also are more vulnerable to investment scams offering returns that “are too good to be true.”

Not taking enough risk. After risking all for the highest returns during the good times, many investors who got burned bailed out of the stock market and are now afraid to invest at all. Some have even stopped contributing to their company-sponsored retirement plans.

Again, they've lost sight of the real purpose of investing. The result is that they not only panicked and cashed in their losses, they shifted their entire portfolios to low-yielding savings accounts and money markets. While these vehicles can serve useful financial purposes, holding an entire portfolio in them hinders efforts to achieve long-term financial goals.

Failing to diversify. Shooting solely for the highest returns tempts investors to chase and overload in the current hot part of the market, and ignore underperforming sections. When large-cap and high-tech stocks stumbled in 2000–2002, stock-heavy investors weren't situated to take advantage of the previously ignored real estate investment trusts (REITs), bonds, commodities, and even gold, all of which had banner-return years.