A reader recommended I read and review a book by Zvi Bodie a few months ago and I recently had the opportunity to read Risk Less and Prosper—Your Guide To Safer Investing, a book he co-wrote with Rachelle Taqqu. Zvi is an academic who in recent years has been writing more and more on the topic of retirement planning for individuals. His contributions to the retirement and investing literature, both aimed at the academic and at the lay reader, are significant and should be understood by every investor.

The book itself has a unique format. Mr. Bodie and Ms. Taqqu enlist a fictional group of friends (although based on real people) who are interested in getting their investing plans into shape and meet (apparently for free) with their friendly neighborhood financial advisor, Paul. (If every one had a Paul, there would be no need for this blog by the way.) Paul walks them through the important aspects of designing their own investing plan, from setting their goals to developing an asset allocation to implementing the asset allocation. Along the way, the authors teach a few important principles.

**Goal-Based Investing**

Mr. Bodie writes a great deal about risk. Rather than defining it as volatility as so many do, he is very clear that the only risk that an investor should care about is the risk that he doesn’t meet his investing goals, whether that is...
because his investments didn’t grow fast enough or because he lost money on his investments. Here is what he says about it:

“With all the noise in the marketplace about performance it’s easy to get distracted from this fundamental fact. The standard of success is not a comparison with a market index or composite. These work well for evaluating professional money managers. But they fluctuate constantly and serve only to weigh your results against various market averages. When it comes to judging your own personal investment performance, it’s your goals that make the most meaningful benchmarks.”

Every time you have an investing decision to make, you should consider that you should be focused on your goal, such as having a certain amount of income each year in retirement or need to have a certain amount of money available for college in X years, rather than what the market is doing or how you’re performing in relationship to the market or other investors. According to Bodie, you want to take the minimum amount of risk necessary to meet your goals. Avoiding failure is far more important than achieving great success.

Stocks Get Riskier With Time

Another idea that you should take away from Risk Less And Prosper is that stocks get more risky with time, rather than less risky as many financial advisors (and even good investing books) seem to imply. They usually say something along the lines of “Stocks have never lost money over any 20 years period” which suggests to the mind that stocks are plenty safe in the long run, you just have to hold on for the long run. Bodie is quick to point out that in the long run we’re all dead and that those who adopt this idea that stocks get safer with time start making bizarre conclusions like the Dow 36,000 guys. In his mind, stocks get riskier with time since the variation in your return gets wider and wider, kind of like the charts you see on TV when a hurricane is zeroing in on the
When the hurricane is still 5 days out in the Caribbean, that cone is awfully wide. The cone narrows up as the storm moves toward shore and by the time it hits, we have a pretty good idea where it is going to hit. The authors say this:

The cone of uncertainty [i.e. a hurricane prediction tool] applies quite well to the way investments will perform over time. Here too the span of possible outcomes widens as the time horizon lengthens....Over the long haul the more you are exposed to danger, the more likely it is to catch up with you.

Those who disagree would do well to remember what happened to the St. Petersburg and Egyptian stock markets in the 20th century.

Inflation is the enemy

The book recommends you divide your retirement assets into two piles- a safe investing pile that will allow you to maintain your bare minimum standard of living (although it allows you to define that however you like) and a risky pile for those extra niceties in retirement. Basically, one for your needs and one for your wants. For the safe investing portfolio, Bodie puts heavy emphasis assets such as TIPS, I-Bonds, and SPIAs, especially inflation-protected SPIAs. In fact, it may be the best primer I’ve yet seen describing how to invest in inflation-protected assets. In the epilogue, he discusses some other options out there (along with their pluses and minuses) for protecting income in retirement, including annuities with guaranteed lifetime withdrawal benefits (GLWBs).

We end up in the same place

To me, the biggest disappointment in the book came at the end. I was expecting that after all this time talking about
goal based investing, minimizing risk, and using these inflation-protected investments that the “clients” would end up with some type of revolutionary portfolio, perhaps somehow split between risky and non-risky assets. But as he went through each client’s thought process with their asset allocation, they all seemed to end up with what would be considered a pretty standard “Boglehead-type” portfolio, with 25-75% of the portfolio invested in stock index funds and the rest in inflation-protected bonds. He was quick to explain:

[The client’s] choices have resulted in an overall allocation of 50 percent to risky assets. That allocation emerged after the fact—it was not based on arbitrary percentages or on a 50-50 product pulled from the shelf.

I agree that his thought process is important, but what’s the difference really if you get to the same place as you would otherwise just pulling a “50/50 product” off the shelf?

Overall, it’s a good book that deserves a place on the White Coat Investor reading list, but I would have to admit I didn’t really learn anything new from the book. I’ve heard all the main themes of the book batted around on the Bogleheads forum for years (although they were probably brought up by others who were influenced by Bodie’s writings). But if any of these ideas are new to you (stocks get riskier with time, your goals matter more than any “bogey”, and inflation-protected bonds are far safer than nominal bonds) then you should spend some time with Risk Less And Prosper.

What do you think of Bodie’s books and ideas? Agree? Disagree? Sound off below!