Wisdom From John Montgomery

Lots of people like to read Warren Buffett's annual letter from Berkshire-Hathaway. However, I really enjoy reading what John Montgomery has to say in his annual reports from Bridgeway. I recently read the semi-annual report and he had a nice bit to say about how he invests. The real meat in his writing, however, comes long before he talks about his actual asset allocation (100% stock, mostly very risky, all in Bridgeway funds if you care.) At any rate, there were enough pearls that I thought were worth sharing with you all that I'm going to quote him extensively, and make a few comments.

> *Looking at individual stocks is mildly entertaining but ultimately irrelevant to long-term investment success.*

I agree. There is little sense in taking uncompensated risk.

> *If you've followed my writing in the past, you won't be surprised to hear that my target allocation hasn't changed much over time. Compared to others, I have a very long-term, very static view of asset allocation.*

Music to my ears. Long-term. Static asset allocation. Rare changes.

> *Bear in mind, everybody’s situation is different in terms of goals, risk tolerance, emergency fund cushion, and especially time horizons. I am not recommending your follow my target allocation, because your situation is undoubtedly different than mine. I share it with you simply to show my thought process and also by way of disclosure.*

Asset allocation is as personal as personal finance gets. The key is to find something likely to meet your goals that you can stick with through the long-term. Consider your goals, risk tolerance, and time horizon. Basically, as Swedroe says-your need, willingness, and ability to take risk.

> *Personally, I have a high threshold for pain in a market downturn. I don’t usually look at my account statements beyond updating them in Quicken often enough to ensure accuracy and tax lots and disclosure reporting. My rule of thumb—both professionally and personally—is, “If it doesn’t make a difference in a decision you make, don’t look.”*

Incredible wisdom there. Knowing yourself and how you react in a bear market is key in choosing your asset allocation. If you haven’t yet been through a big bear market or two, err on the side of a conservative portfolio. Don’t look at your account balances frequently. Like choosing individual stocks, it simply isn’t relevant. Obviously, you do need to keep track of some things, but it is far less than most beginning investors think.

> *I realize this is hardly classical wisdom, but I see two big problems with watching one’s investments too closely. First, investors tend to become more nervous, especially in a downturn, which causes unnecessary stress – and studies show that stress causes investors to make costly changes to their investment mix. Second, investors tend to chase “hot” returns, buying more of an investment after a big run-up and selling after a downturn. That’s a formula for financial disaster.*

If anything matters more to investment returns than asset allocation, it’s investor behavior.

> *So what’s the antidote to obsessing about returns? Here’s my philosophy:*
>
> *a) Structure an asset allocation plan that matches your goals, investing time horizon, and risk tolerance. Generally, this means diversified, short-term investments for near-term needs and more stocks for long-term needs.*
>
> *b) Write it down*
>
> *c) Implement it*
>
> *d) Rebalance it about once a year, or as lifestyle changes occur.*

I hope that sounds familiar to long-term readers.

> *Increasingly, I support hiring an investment advisor to help you implement this strategy – but only one who charges reasonable fees, does tax-lot level reporting, practices*

> *regular rebalancing, and takes advantage of donating appreciated tax lots. Above all, you need an advisor who understands the dynamics of the behavior gap and has a strong record of helping clients avoid chasing hot returns and panicking in downturns.*

Nothing wrong with that, except the actual task of hiring an investment advisor that meets that description requires you to be sufficiently savvy that you no longer have the need of him. I'm all for competent advisors offering their services at a fair price for most doctors. Unfortunately, most "advisors" aren't competent, and many of the competent ones don't charge a fair price because investors are more than willing to pay their inflated price. More so than almost anything else in life, hiring an advisor is a caveat emptor situation.

What do you think? Do you agree or disagree with Montgomery's advice? Why? Comment below!