



The guaranteed return fantasy

Investors need to understand the real world and the structure of their investment holdings

BY DANIEL COHEN

My kids love shows about mermaids, those delightful ocean creatures of fantasy and dreams. It got me thinking about some of the talk in the business press about unicorns – a new term in the investment community that refers to a startup whose valuation exceeds \$1 billion. There is a great deal of money being used to buy investment products that provide “guaranteed returns.”

From a young age, most of us are fascinated with fictitious characters, and that fascination seems to be present throughout our lives. In the storybooks and movies, there are always heroes that can rescue us from danger and make us safe. In the case of “safe” guaranteed returns from investment products, the buyers of these products would probably be better off by forgoing the guarantee and simply investing their money in the markets without the promise of a guaranteed return.

My formula for success is simple. Clients are primarily invested in portfolios of stocks or bonds depending on their goals and the investment climate. Low-cost index funds supplement this strategy when an account cannot be properly diversified in individual stocks and bonds. A fee is charged to clients for the ongoing management of client portfolios and for the comprehensive financial planning we provide.

Clients know exactly what they are paying. The fee is clearly reported on their quarterly statements. Unfortunately, much of the financial services industry avoids this kind of transparency to the point where individuals may think they are paying nothing for the services they’re getting.

Recently, I was competing for business, and as I always do with new clients, I explained the risks of investing. I explained that some years the stock and bonds markets lose value. Over time, investing in the

markets has been very rewarding. This prospect decided to go elsewhere because the other advisor was offering a 20 percent bonus on the funds invested, and this prospect told me that the product had no cost associated with it.

I offered to review the fine print of the product with this large “up-front bonus and no cost,” but the prospect did not respond to my offer.

Too many people are sold on something that sounds great at the beginning without fully understanding the long term cost. No insurance company would give a 20 percent bonus to their policyholders just to be nice. That money must somehow be covered and accounted for.

Wouldn't it be great to quit your job, develop an app to change the world, and overnight be the owner of a \$1 billion dollar company?

Uber, Airbnb, Snapchat, SpaceX, Pinterest, Dropbox and Square are just some of those unicorns that have achieved this. The founders have become wealthy in a short period of time. These stories are a new version of the American dream where the success we dream of happens overnight rather than through years of hard work with gradual increases in income and eventual retirement.

Most enduring success is achieved gradually over time as we build our businesses or careers and save a portion of our earnings for the future. My success was never guaranteed and the performance of my clients’ savings have no artificial guarantees. But they do have a track record. We follow time-tested strategies and my clients have profited and are achieving their life goals.

It is fine that children believe in Santa and the Easter Bunny. Let them enjoy the shows about mermaids and dragons, and yes, unicorns. At some point, children understand what’s real and what’s not. Investors need to understand the real world and the structure

Too many people are sold on something that sounds great at the beginning without fully understanding the long term cost

of their investment holdings. Even the lowest-cost investment products like the Vanguard index funds are not free, as they have an expense ratio.

A lot of money is being tied up in investment products that will lock in today’s low interest rates for the rest of people’s lives. The long-term benefits of investing often gets overshadowed by the comfort of having a guaranteed return starting today. The costs of these guarantees often come in the form of low returns to the investor while the issuing company profits handsomely.

Remember, there is no “free lunch.” No large company is willing to give away its profits because they just want to help people.

My advice is to thoroughly analyze the long-term impact of your investment decisions. Most investment products with guarantees have little or no liquidity, which means that the decision you make is irrevocable. Get a second opinion before committing to an investment that cannot be surrendered without a large charge. Research what the investment is expected to be worth 10, 20, and 30 years into the future and compare that to other types of investments using realistic potential returns.

The real impact of one’s decisions are often not felt until decades later, when it’s too late to change course. **NHBR**

Daniel Cohen, CEO and chief investment officer at Cohen Investment Advisors, Bedford, can be reached at 603-232-8351 or through investwithcohen.com.