BORING MAY BE BEAUTIFUL

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I Figure I Need 10% or More In My Retirement Accounts. You Can Do That, Right?

You've done your best to accumulate funds for the years ahead, but you just can't see working any longer. So, you've committed to hanging it up by a date on the calendar, come what may. And you have a pretty good idea of what you want to do, how much it will cost, and so on. But when you examine the assets you are counting on to carry you for the years ahead, you've determined you'll need significant returns to get along alright. To be able to spend $5,400 per month, after taxes, your $1,000,000 retirement account would need to earn 10% yearly. If the need is $6,000 per month, you'll need even more. So do you begin your retirement planning by pressing your financial advisor candidates about their investment approach and track record with the expectation, "You can do that, right?"

Financial Markets Investing

Investing via the financial markets (listed and over-the-counter stocks; government, municipal, and corporate bonds; bank certificates, money markets, etc.) should not be approached with such "great expectations." Of course, there are the more uncommon examples of the wise investor who invested in a company just prior to a major advance in its share price, thus earning unusably high returns, but this is the exception, not the rule.

Why You Should Be Happy With X%

Investment returns on all instruments change over time, so trying to accurately predict what one will earn in a single investment, many investments, or in the broad financial markets is impossible. So the "X" as it stands for expected return on investment is unknown.

Investing in bonds may be a more convenient way to lend money to a company or governmental entity. Generally, the investment return on a bond, if held to maturity, assuming all interest and principal payments are made in a timely manner) is its stated yield in terms of an annual percentage rate. According to Yahoo Finance as of November 20, 2013, a 30-year government bond should yield 3.88% (and a 20-year "AAA" rated corporate bond should yield 4.99%) for that term – the investor will earn just that over those years (assuming he or she holds the bond until it matures). So, if your investment strategy calls for investing some capital in these bonds, what you'll earn on this part of your portfolio should be fairly obvious.

Stock market returns are usually less predictable. And you might be tempted to seek out the next company with prospects for high returns as part of your investment portfolio for the years ahead. But uncovering such opportunities when most others overlook them is more difficult than one might imagine. Determining a fair value for a business is one thing (as demonstrated when investment bankers negotiate bids for private companies in line with their expectations), but investing in public companies also involves the collective perspectives of millions of other investors who may decide for themselves what is a fair value and will purchase or sell a stock based on their own assessments of many unrelated variables at any given moment. This tends to make successful stock investing much more difficult, even for the seasoned financial manager or analyst.

More often, experienced financial advisors will recommend that investors wishing to invest in stocks do so in broadly diversified portfolios. Such diversification could reduce the risk that any one company may have the potential to significantly lose one's investment capital. But this diversification will also reduce the opportunity for outsized gains (a low probability event). Still, this approach may offer the opportunity to earn reasonable long-term returns in line with historical experience. While the past is not necessarily indicative of the future, according to Ibbotson Associates, from 1970 to 2013, the S&P 500 stock index produced a compounded annual growth rate of 10.4%, with the best single year (1995) producing a gain of 37.6% and the worst single year (2008) producing a loss of 37.0%.

Additionally, financial markets' liquidity, along with reasonably small and standardized investment units of ownership (a share of stock or a bond), also allows investors to spread their investment dollars around to various potential opportunities. While it does not ensure a profit or protect against loss, this spreading, or diversification, can play a key role in reducing the risk of investing a given sum of money. The ability to diversify is a prudent approach to investing, but it will likely mitigate the opportunity for unusably high returns, particularly over long periods of time.

While these are not all the opportunities available in the financial markets, they describe the most common choices, and possible expectations. For the relative safety and liquidity of your capital, you may learn to be happy with X%.

How to Incorporate More Aggressive Opportunities

Once comfortable with the returns likely to be earned in the financial markets, looking for reasonable opportunities for higher returns is not reckless. Some investment assets and strategies can – and have – produced greater long-term returns, but usually come with the risk of greater potential losses. These alternatives include hedge funds, private equity investments, venture capital, futures trading, and many unique securities trading strategies. These investment vehicles may produce higher returns, but none are assured or predictable, and often are less liquid.

If these alternative investment vehicles are of interest to you, work with your financial advisor to create an investment strategy that includes them. You should make sure that your exposure to these investments is properly allocated to a small part of your overall portfolio strategy and be wary of chasing seemingly exciting opportunities that come your way. Any new commitments should come from these dedicated assets or the returns of capital you may have from similar investments previously made.

Boring May Be Beautiful

For the executive who is prepared to leave the business world, prudently investing his or her life savings is critical to being able to do the things he or she would like over the years ahead. The financial markets provide a way to invest those savings to seek to generate reasonable returns for the future. With this understanding, those fortunate enough to be able to move on from the business world are wise to remember that, when investing the sum of your life's work, boring may be beautiful.