



## THE BAM ALLIANCE

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### My Take: Ask Before You Act

#### Neal Merbaum

Recently, I had a conversation with a few friends about the wisdom — or lack thereof — of using past performance as a guide when considering an investment. I didn't handle it well. I talked about studies that show that past performance isn't a reliable indicator of future performance. I dismissed stock picking and market timing. I didn't persuade anyone.

Pondering how I could have better approached the conversation with my friends got me thinking about how children often ask question after question — sometimes as simple as "Why?" — over and over again. Might it be good for us grown-ups to do more of that when it comes to our investments? Too many of us, it seems, just accept what we see, read and hear from Wall Street, when a simple "Why?" could go a long way toward giving us a better understanding of what's credible and meaningful.

For example:

- When a broker says, "You should buy this stock," we could ask, "Why?" If the broker says it's because it will outperform the S&P, we could ask, "Why do I need to outperform the S&P? Will that give me a better chance of achieving my goals? How much risk would I be adding in return for the supposed benefit? And how do you know this 'hot' stock will continue to be hot?"
- When we see an advertisement for a fund family that touts its past performance, we could ask, "Why is that a reason to buy these funds? What is the evidence that past performance is a good predictor?"
- When someone forecasts the direction of the market, we could ask, "Why should I accept that this person is a good forecaster? How often has he or she been right in the past?"

I should have asked my friends questions. Why do you think past performance is a good indicator of how someone will perform in the future? How long does a fund or a manager have to do well before you consider it sufficient to predict future performance? What evidence do you have that good performance over that particular time period is a good predictor of future results? By asking a few questions like these, it would have quickly become apparent that such beliefs are not based on evidence (because, as far as I know, there isn't any). We then could have talked about the evidence that shows that it's enormously difficult to consistently outperform a low-cost, well-diversified, passively invested portfolio.

The more we ask questions like these, the more we realize how little of what we hear from pundits or read from Wall Street is actually based on solid evidence. We can't, of course, spend all of our time asking "Why?" But a little childlike curiosity can be a very grown-up thing to have when viewing our financial future.

### About Neal Merbaum, President, Rocktree Financial Advisors, Boston

Neal Merbaum is president of Rocktree Financial Advisors LLC. His diverse background includes stints as a commodities trader, trading-desk manager, executive director of a family foundation, and nonprofit consultant. For fourteen years he worked for John W. Henry, the principal owner of the Boston Red Sox, in a variety of roles. Neal is trained as a mediator and has mediated small-claims cases and landlord/tenant disputes in the Boston court system.

Neal holds a bachelor's degree in philosophy from the State University of New York at Stony Brook and an AWMA certification from the College for Financial Planning.

Neal enjoys playing tennis when he's not injured. He and his wife reside in Boston.

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