**The Balancing Act: Are You Truly Diversified?**

*Everything in life… has to have balance.”*

*—Donna Karan*

****Have you taken a “30,000 foot view” of your finances lately? Is it positioned for the growth, strength, stability and cash flow you desire? To help you answer that, let’s examine asset allocation and diversification through the lens of Prosperity Economics.

First off, let’s define a couple of key terms. Asset allocation and diversification are not the same thing, although they both help with the problem of excessive risk that is created when you “have all your eggs in one basket.” Next, we’ll look at what those terms typically mean in “common financial advice,” which will let us notice what may be missing. Lastly, we’ll present a NEW model for achieving greater balance—*and better results*—with YOUR money!

**Asset Allocation Vs. Diversification**

**Asset allocation** refers to investing in different asset classes. Typical financial advice tells us that the common asset classes (where you should put your money) are: 1) stocks, 2) bonds, and 3) cash. Typical advice tells us that stocks are best for long-term growth and that is where most people should have most of their money. We are told that bonds provide adequate balance to the risk of stocks, and that the older you are, the more you may want to have in bonds verses stocks. Lastly, typical advice tells us that cash vehicles such as savings accounts, money market funds and bank CDs should make up the remaining (very small) balance of your assets.

Of course, there are big problems with this limited asset class model. Bonds are no longer the safe haven they once were. Stocks aren’t the only valid or the safest growth strategy. Most cash options haven’t been performing well, and represent too small a portion of most portfolios to provide any real safety. And the options are simply too few and narrow.

Typical advice does little to actually help you achieve balance and stability! Those following this model ten years ago suffered huge losses in the Financial Crisis and spent years recovering. Even the age-based or target-date funds supposedly designed to SOLVE asset allocation problems for investors—completely failed, so beware popular financial “wisdom.”

**Diversification** refers to how to diversify the options WITHIN a particular class, especially stocks. *Without* diversification, asset allocation could look like this:

* a million dollars of stock in a growing, forward thinking company. (Enron, anyone?)
* some “safe” municipal bonds, perhaps in a classic US city (like Detroit).
* cash in a bank account that’s depleted through inflation or even threatened by an [asset forfeiture scandal](https://www.prosperitypeaks.com/stolen-savings-civil-forfeiture-banks-unsafe/).
* a million dollar property (perhaps in an area subject to hurricanes or forest fires).
* a cryptocurrency, such as PayCoin (which hit bottom after a promising start).

Diversification in the stock market spreads risk among different funds, stocks, industries, and companies of different sizes and locations. But stocks aren’t the only asset you may wish to diversify. Consider diversifying:

* real estate, such as we describe in [“Is Your Real Estate Portfolio Diversified?”](https://www.prosperitypeaks.com/diversify-real-estate-portfolio/)
* cash equivalents, using more than one savings institution for short-term cash and multiple insurance companies for long-term cash.
* Non-correlated growth and cash flow strategies [apart from the stock market](https://www.prosperitypeaks.com/alternative-investments-non-correlated-assets-better-portfolio/).

**The Problem with Typical Models of Risk Reduction**

Typical asset allocation models try to focus you only on the limited assets that banks or brokerages *sell.* The pervasive debate about “how much should you have in stocks vs bonds?” is designed to get you to forget about other alternatives, such as real estate, life insurance, investing in a business or alternative cash flow vehicles. This is a problem because it increases your risk!

Additionally, as described in this article on [why 401(k) can be risky](https://www.prosperitypeaks.com/401k-risk-assessment/), the popular investment vehicles subject you to MANY risks, including *systemic* stock market risk. Market crashes and corrections can bring sweeping losses to virtually every type of stock, yet typical financial advice tells you to subject MOST of your assets to the whims of the market. You’ve been trained to put your assets in stocks where a “diversified” portfolio won’t save you from a crash, correction, or bear market. (And note how the word “correction” minimizes this loss. We tend to think of a “correction” as a good thing—“a change made to something in order to correct or improve it,” says the Cambridge English Dictionary, as if losing 10% or 15% of an investment’s worth is somehow *supposed* to happen!)

**The Balanced Prosperity Model**

If your investment model was a chair, you’d want it to sit on a stable foundation, have several sturdy legs, and a seat that would support you. Let’s start from the ground up:

**The Foundation:** Your chair needs to sit on something! What should your foundation be? Virtually all advisors will tell you that you should have an emergency fund (even before investing), and savvy investors won’t neglect the need for protect their assets and their loved ones.

Unfortunately, typical savings solutions are lacking, often producing only a fraction of a percentage point in interest. And when it comes to protection, often financial professionals recommend cheap term life insurance that’s designed to expire before you need it 99% of the time—like a product warranty that never gets used! (But you’ll have more to invest on “their” products with systemic risk.)

We recommend (and use!) whole life insurance as our financial foundation because it provides

* long-term cash growth that outpaces bank rates and inflation
* exceptional security (banks use it as part of their Tier One assets)
* excellent financial flexibility (including the ability to withdraw or leverage against your cash for emergencies and opportunities)
* an incentive to save consistently
* opportunities for long-term care riders and other benefits that can supplement when medical needs arise,
* plus a guaranteed, permanent, death benefit that transfers (usually) tax-free to heirs.

**The Investment Legs:** A stable chair or stool has four legs. (Three to six will also work, as you’ll start with fewer and build towards more.) Our favorite four legs that many of our clients have include:

**1. Steady Growth Vehicles.** While many people look to stocks for growth, the big problem with stocks is the roller coaster ride of the stock market. We want our clients to invest in a growth vehicle that will grow steadily regardless of the economy, the market, or other changing factors.

Life Settlements are an excellent choice for steady growth vehicles. They represent the secondary market for life insurance policies, which can be bought and sold much like a deed of trust to a property. They rely on actuarial math rather than speculation and have proven to be immune to market swings, housing crashes, low interest rates and virtually every kind of economic downturns.

A Life Settlement is the sale of an existing policy from the current policy owner to a third party via a secondary institutional market in exchange for an immediate one-time cash payment that is less than the policy's death benefit, but more than the policy's  cash surrender value. You might have never heard of life settlements because until recently, they were reserved for institutional investors. (Now they are also available to accredited investors.)

Life Settlements create a win-win for both investors and sellers, matching policy owners who no longer need or want their policies (perhaps having outlived heirs, or finding themselves in need of cash to meet their own needs) with investors (or private investment funds) who are willing to pay more than the policy’s surrender value to obtain an asset with a secure future value. (Ask us for more information about life settlements.)

**2. Private Lending.** Many investors make the mistake of focusing on accumulation but ignoring cash flow until they try to retire or cut back at work, only to realize that they don’t know how to turn their assets into income!

The oldest and most reliable investment model for generating cash flow is private lending. This can include real estate bridge loans, fractionalized real estate investments, peer lending strategies such as Prosper.com and LendingClub.com, land leases, and more. Learn about [the advantages of being a private lender.](https://www.prosperitypeaks.com/private-lending-investment/)

**3. Real Estate.** This means a home to start, as it’s virtually impossible to build wealth dumping money down the rent drain. Then it can include investment real estate such as rental homes, apartments, or commercial real estate. Investment real estate can (and should) produce cash flow, while also allowing you to build liquidity or equity, perhaps even enjoy the property yourself seasonally. Real estate can also offer potential tax benefits of such as mortgage interest write-offs, depreciation deductions, and shielding growth from capital gains taxes (in certain circumstances and up to certain limits).

**4. Business Investments.** Putting your own expertise to work creating your own source of income is a fabulous way to diversify! While perhaps not for everyone, many more people have obtained wealth through business ventures than through working a job and making typical investments.

*Many of our clients also have:*

**5. A Stock Portfolio.** Many of our clients come to us with mutual funds and a stock portfolio already. Although we would never recommend the majority of your assets to be in the stock market, there can definitely be a place for equities.

Stocks, mutual funds, indexed funds, and ETFs etc. are also assets that many young investors will get started with due to the ease of investing when you don’t have lump sums required for some other investments. Low-cost options such as Vanguard make it simple to start investing as little as $50/month after you have established your emergency/opportunity fund.

**6. Precious Metals.** Some clients desire precious metals in their portfolio, perhaps as a hedge against the dollar. Even with a traditional investment such as gold, be aware that it will lock up your money in an asset that can’t produce cash flow while you have it.

**7. Digital Hedges.** Some people enjoy speculating with bitcoin and other cryptocurrencies. This requires great caution as this is a volatile and speculative asset! If you enjoy living and investing on the edge, just make sure it’s but a leg of your strategy, and not a big financial gamble.

**The Seat.** A chair is not a chair without a seat! The seat represents *cash flow,* because cash flow is what *supports* you and your life—literally! While private lending is especially focused on cash flow, there are ways to convert every leg as well as the chair’s foundation into cash flow that will support you and your life long-term.

The key to generating maximum cash flow is to sequence how you use or liquidate your assets. You can often enjoy greater cash flow—and fewer taxes—by changing your disbursement strategy. But don’t wait to create cash flow—generating income builds confidence and expands your life options.

**Is it time to balance your financial strategy?** Contact us today; we’re here and happy to help!

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