MARIA SHRIVER

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Is the Stock Market Broken?

By Anthony Glomski, Creative Expert

Chances are you have been tuned into the media the past couple weeks, and are aware that the stock market experienced some traumatic swings. In fact, it was nearly impossible to tune out the barrage of information. It is often times difficult to determine:

- What is going on?
- Does it matter to me personally?
- What actions, if any, do I need to take?

The world of finance is loaded with information overload. I constantly seek the voice of reason. When the Standard and Poor's downgraded the U.S. debt, many people were in a panic, and I understand why. If you tuned in to any station, you would see a world of frenzy. My response was to go to the voice of reason. I want to know the opinion of someone with many years of experience who has a personal stake in the market. I immediately searched for Warren Buffett's response to the downgrade. In short, he shrugged off the importance of what Standard and Poor's did. He further went on to say that likely the market would be unchanged. Was he correct? If we followed the market, and the news that following Monday, a casual observer would say, 'no.' If you were entrenched in the tick by tick action, you may be concerned that a repeat of 2008 was about to happen. And how about now, a mere week later? The market is basically unchanged since the downgrade of the U.S. debt.

What is going on?

Find your voice of reason. I read the words of Warren Buffett as a guide. They are calm, reassuring, and rooted in decades of experience. As much as you hear the words "we haven't seen this before", it's likely that he has experienced a similar event or situation and knows how to remain calm. Find your own Warren Buffett, and tune out the other 95% of what you hear. I promise this will lead to a better night's sleep.

Does it matter to me personally?

If your investment horizon is 20+ years, my belief is that you too can shrug off the recent volatility of the market. Over considerable periods of time, the stock market has produced positive returns. Rest assured, history will likely repeat itself. Continue to fund your 401k and other investment accounts, and celebrate that you are buying investments at cheaper prices.

What Actions Do I Need To Take, If Any?

I want to focus here on a concept of balance. This will greatly reduce the roller coaster ride of investing. It is crucial to have a balanced portfolio of stocks and bonds. We strive for balance in all areas of our life. For example, we balance time, our personal and professional lives, our meals, etc. Our investments need balance as well. How do we balance? Choose the right percentage of stocks and bonds, and re-adjust at least once per year. (Changes in the market will cause our investments to go out of balance.)

At this point I could go into a lengthy discussion and define stocks and bonds, but this would likely put many people to sleep. Instead, allow me to offer an analogy using two children. Billy represents stocks, and Herbert represents bonds.

Billy is energetic, active, artistic, and always has new ideas. He moves at 100 miles per hour. Some days you are afraid he will wind up a criminal, and other days you are convinced he is a creative genius. Every day you wake up, you cease to be amazed at what he has done. You are convinced that he is destined for great things, so long as you keep him on the right path.

Herbert, on the other hand, plays only by the rules. His report is due next week, and he finished it yesterday. His stress is limited to whether he got an A or A+ on his report. If you look in his closet, the clothes are perfectly folded and sorted by color. You are amazed by his consistency.

We predict that Herbert will likely be in a safe secure job when he grows up. This is very reassuring for the conservative side of our emotional balance. Hopefully, Billy will be in a position of power and success. Perhaps CEO of a Fortune 500 company, world renowned artist, or Internet entrepreneur. His earning capacity is far greater, and far more uncertain than Herbert. Billy adds some stress to our lives, but also a lot of excitement. Herbert on the surface could be considered boring, but we truly appreciate the calmness and consistency of his nature.

In short, your portfolio needs to be part Billy and part Herbert. So how much Billy (stocks) and how much Herbert (bonds)? This is where your homework comes in. Percentage of stocks versus bonds is a function of age and risk tolerance. Vanguard.com offers many tools and guides for the do-it-yourself investor.

One autopilot investment I mentioned before is a target retirement fund. This will have the right balance of Billy and Herbert based on your age. The re-balancing of stocks and bonds will happen each year. Do an Internet search for target retirement funds to learn more.

Life is all about balance. Your investments are no different. If you get ahead and work to balance your portfolio between stocks and bonds, you will be far less prone to reacting to short-term market volatility. Investing requires a long-term commitment. You can empower yourself by doing some homework and you will likely be headed down the road of success.