

FINANCIAL POST



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WEALTHY BOOMER

The Empowered Investor

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In reading the just-published second edition of Keith Matthews' *The Empowered Investor*, I was struck by how much the portfolio approach it espouses would help investors so flummoxed by the turbulent markets of the last nine months.

When I reviewed the first edition in 2005, I wrote that the book "should have a profound impact on Canada's investing landscape," which ended up as back-cover blurb on the new expanded edition. Perhaps that was an overly optimistic assessment since markets were flying high then and – as the old saw goes – everyone is a genius in a bull market. And of course by definition, do-it-yourself investing geniuses don't need any help (or don't think they do).

But as Warren Buffett says, 'It's only when the tide goes out that you find who has been swimming naked.' I dare say many an investor in 2008 is feeling somewhat under clothed.

While my own portfolio has taken its lumps of late, I nevertheless don't feel too exposed to the receding tide. As I read Matthews' new edition on my daily commute, I felt some comfort in the fact that my own portfolio is constructed upon similar lines. Matthews' three investment principles are to invest in asset classes, diversify and to realize that risk and return are related.

But before putting those principles into practice, investors must first beware of eight common pitfalls, many of which are relevant in these troubled markets.

Here are the eight pitfalls:

1. Lack of an investment plan
2. Not aligning your investments with your personal objectives
3. Miscalculating your investment time horizon
4. Trying to profit by timing the market
5. Buying high and selling low
6. Lack of proper diversification
7. Building portfolios based on bold predictions
8. Letting behavioural biases get in the way

I'd be surprised if even one reader of this blog has not fallen into at least one of these pitfalls. If you haven't,

please apply immediately for the position of co-author of this blog!

Matthews doesn't spare the financial industry which has been his bread and butter since he arrived on Bay Street during the Crash of 1987. A chapter entitled "The emperor has no clothes" helps investors recognize the varied conflicts of interest that abound in the financial services industry.

Those who followed Matthews' later career at PWL Capital and now at Tulett, Matthews & Associates Inc. will know that Matthews eventually became an evangelist for passive asset-class investing, chiefly through exchange-traded funds or ETFs. Actively managed mutual funds and "stock-picking investment counselors" are no longer sacred cows, he writes in a chapter outlining the superiority of indexing. This will be familiar ground to anyone who has read the work of John Bogle, Larry Swedroe, Mark Hebner, David Swensen, Ted Cadsby, Brian Noble, Howard Atkinson or Daniel Solin. So too will the following chapter on why investors need to pay attention to investment management costs and taxes.

Two short but useful chapters follow on how to create an IPS or Investment Policy Statement and how to coordinate your investment plan with your life plan.

The above structure was pretty much in place for the first edition but Matthews has added about 60 new pages of material he dubs "Advanced Investing 101." It includes two new chapters on international investing, a survey of alternative investments, the boom in ETFs, the "core and explore" concept and finally the joys of home ownership.

Not all his conclusions are predictable. For example, Matthews is not at all convinced that the explosion of new specialized ETFs is necessarily investor-friendly. As for hedge funds, private equity and venture capital, he dubs all these as "risky business."

And while many financial advisors use the "core and explore" concept to slip in a few "fun" investments, Matthews argues that investors should treat their entire portfolio as a "core" investment. Those that wish to take on more risk for a shot at better returns should merely add more passively managed value or small-cap investments to their mix.

A new chapter on "Future Returns" reminds investors that these are the expected annual returns of the major asset classes:

T-bills = inflation plus 1%

Large-cap equities = T-bills + 3.5 to 4.5%

Value stocks = large-cap equities + 1 to 3%

Small stocks = large-cap equities + 1 to 1.5%.

As for residential real estate, Matthews is cautious: "Long-term real rates of price appreciation may be much lower than you thought If the average Canadian homeowner does get inflation plus 1-2% over the next ten to fifteen years, these will be strong and reasonable returns. After all, the gains will be tax-free." Interested readers may also refer to [this entry](#) on Garth Turner's newest book on the subject, entitled Greater Fool.

All in all, I'd put *The Empowered Investor* on my top ten list of must-read books for Canadian investors. The subtitle is *A Guide to Building Better Portfolios*, which pretty well sums it all up.

(Photo: Keith Matthews. Source: Tulett, Matthews & Associates Web site)

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