Step 7 - Reduce investment expenses and control investment taxation

Category : Financial Planning -- 10 Personal Steps in the Right Direction

Published by The Skilled Investor on Jul/24/2005

Reduce investment expenses and control taxationStep 7 of "10 Financial Planning Steps in the Right Direction"CLICK HERE TO READ *THE SKILLED INVESTOR*'s OTHER ARTICLES ABOUT THESE "10 FINANCIAL PLANNING STEPS IN THE RIGHT DIRECTION Even with optimal investment strategies, there is still substantial room to improve upon net investment performance through continued and vigilant focus on controlling investment costs and tax realization. The fees extracted by the financial securities industry increased substantially during the last two decades of the 20th century on both a total and a percentage of returns basis. At the same time industry deregulation, market innovation, and increased competition provided many new and useful mechanisms for investors to manage their assets in a much more cost- and tax-efficient manner. This important step focuses on investors’ net or realized investment returns – the returns that investors could actually spend. Adopting investment strategies based on scientific finance is the first part of investment cost reduction. Many such strategies are inherently more cost-efficient, which contributes to improved risk-adjusted returns. This is not surprising, because a fundamental goal of investment science is to discover strategies to maximize personal economic welfare on a risk-adjusted returns basis. Skilled investors must carefully control known and hidden investment costs and taxation to ensure that they obtain maximum net returns from their hard-earned investment assets. This step again also investors’ attention to the potentially negative personal financial impacts of biased and sub-optimal advice. The conflicts of interest between individual investors and the financial services industry continually threaten individual investors’ returns. The financial services industry offers products and services for investors to buy at prices that include the market value of the investment securities plus the costs and profits related to the sale and transaction. Often the true cost of the industry’s markup is obscured or hidden. Investors need to understand that their interactions with the financial markets through these industry intermediaries are a “zero-sum game.” In and of itself the industry does not create value, but it can siphon away a significant portion of investors’ potential returns through visible fees and hidden costs. Particularly with the abnormally high market returns for equities-based securities during the last two decades of the 20th century, many investors became very lax about managing investment costs and tax realization. The fees extracted by the financial securities industry increased substantially during this period on both a total and a percentage of returns basis. At the same time industry deregulation, market innovation, and increased competition provided many new and useful mechanisms for investors to manage their assets in a much more cost- and tax-efficient manner. Many investors need to give this topic a far higher priority. (See: Excessive investment costs are a huge problem for individual investors and Passive individual investors are “free riders” who benefit from the higher costs of active traders)