

Financial Literacy: Stress Test Your Investment Portfolio

Last month we discussed stress testing our family finances in two specific categories:

1. **Cash flow adequacy** during extended periods of income disruption - the *savings program*.
2. **Loss of an income stream** when a family member dies and their government and/or private annuity income stream stops - the *survivor assistance program*.

This month we're going to cover the third category: **Retirement income adequacy** - the *investing program*. Having enough money to maintain our standard of living in retirement requires a sound investment program.

For the (too small) portion of American households that do have an investment program in place they need to stress test their investment portfolio. Coincidentally, here too are two categories of stressors:

1. An **extended cash flow disruption** or **emergency expense** that forces an unplanned redemption from long term investments to meet short term living expenses, or
2. **Manic market "adjustments"** that trigger either an unwise stop loss sell off of holdings at a realized loss or forces an emotional decision to stop the hemorrhaging and "get out of the market" while we still have some money left.

Stress testing the first situation is our normal portfolio asset allocation assessment. That assessment requires us to set aside a portion of our investment money in secure, liquid, albeit low growth investments. This is money that we'll tap for longer term living expenses in emergencies. It's not going to grow much, if at all, after inflation. But setting that money aside protects the rest of the money we've earmarked for our future use that are in our investments. With that cash-like account we won't be forced to make an unplanned redemption, particularly from a tax deferred retirement account, to meet our current needs. *Tip: be thinking of covering at least 6 months of non-deferrable expenses.*

The best stress test for the second situation is having high confidence in the quality of our investment portfolio holdings. Having current, complete, and well researched stock studies for each company in our portfolio builds the confidence we need to not just stay the course when the market drops but to actually buy more shares while our watchlist companies are on sale.

Stress testing our portfolio requires dispassionate quarterly fundamental metric reviews to spot the early warning signs of troubling months ahead. Slowing sales and declining profit margins often presage earnings drops that, once noticed, invariably result in alarming price drops. Armed with a watchlist of companies that are not showing these early warning flags gives us the confidence to do what most investors won't do -- buy low while the companies are on sale.

If you would like to know more about how to do a stress test for your own personal investment portfolio or to find out how to learn more about financial literacy so you can contribute to our chapter's financial literacy program please contact Bob Houle at bob.houle@gmail.com.

It's time for all of us to take action and help others become financially secure and independence. ***Never Stop Serving!***