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It's Your Turn

Financial Information For Playing Life's Game

CFP Board eNewsletter | October 2006

Move Ahead

What I Learned from Ebenezer Scrooge

'It's not about the money' are words most people would not expect to hear from their financial planner. But if you were sitting across from Rick Kahler, a CERTIFIED FINANCIAL PLANNER™ professional based in Rapid City, South Dakota, chances are that those are exactly the words he would say at some point during the conversation. That's not because Kahler thinks money is irrelevant. Far from it. It's because he's convinced that many financial problems have more to do with our unconscious beliefs and attitudes about money than with our bank accounts or credit card companies. "It's the relationship you have with money that is the key," he says.

Kahler puts this idea into his financial planning practice. Together with co-authors Ted and Brad Klontz, he's written a book that takes one of the most notorious misers in literary history, Ebenezer Scrooge, as a model for how to uncover and change problematic beliefs about money: *The Financial Wisdom of Ebenezer Scrooge: 5 Principles to Transform Your Relationship with Money*. The **Klontz-Kahler**

approach mixes financial planning basics and insights from psychology (both Ted and Brad Klontz have backgrounds in psychotherapy) with a close reading of Charles Dickens' classic tale *A Christmas Carol*. The authors start from the premise that, as Kahler puts it, "Dysfunctional behaviors around money come from the same place as any other dysfunctional behaviors: a deep wound from the past that you're running from or trying to medicate. The way forward often starts with a look back."

Kahler learned this lesson the hard way. As a small businessman—Kahler had a real estate firm in addition to his financial planning practice—he struggled for years to pay the bills and build his company. But in the mid-1980s, his business hit the wall as the economy slid into recession. "My daily mood was controlled by my check book," he recalls. "When money was coming in, I was happy; when money was going out, I was not." As his firm dropped into the red, Kahler put his nose to the grindstone. That was a smart survival strategy to get out of the immediate crisis, but he remained stuck in workaholic mode for the next 15 years. His marriage and peace of mind were just two of the casualties. Then, about five years ago, Kahler summoned the courage to look at his balance sheet and was shocked to discover that he was doing just fine. "I always believed you had to work hard for your money," he says. "But I was tired of the struggle and began to realize that maybe things weren't the same as they were 20 years ago."

Kahler and his co-authors call these kinds of hidden financial beliefs "money scripts." "Money scripts are internalized messages about money that are often formed by some financial trauma in the past," Kahler says. "They can still control behavior, even though they've long outlived their usefulness." The book relates the story of "Brenda" as a case in point. As a child, Brenda scrupulously saved her money in a piggy bank. But when family members needed cash, they raided her piggy bank. As an adult, Brenda earned several hundred thousand dollars a year. But she spent everything she earned so she always ended up broke, just like the rest of her family. Why? Because, Brenda realized, she was driven by an unconscious fear that her money would be taken away. When her family called looking for cash she wanted to be able to honestly say, 'I don't have any.' Other money scripts might include statements such as 'I can't earn money doing something I love' (a rationalization for staying in a job you hate) or 'I don't earn enough to save' (a justification for impulsive spending). The aim of *The Financial Wisdom of Ebenezer Scrooge* is to help people identify and overcome the money scripts that may lurk behind their financial predicaments.

The authors use *A Christmas Carol* as a kind of instruction manual for rewriting dysfunctional money scripts. They plant their five principles like signposts along the route of Scrooge's journey from miserly misanthrope to merry emotional millionaire. Scrooge's first encounter on Christmas Eve is with Jacob Marley, his old business partner, who warns him of his fate unless he changes his ways. This corresponds to principle 1, 'Denial inhibits change.' "Before people can decide to change," Kahler says, "they have to be in enough pain to admit there is a problem in the first place." In other words: no pain, no change.

Scrooge then receives a visit from the Ghost of Christmas Past, who takes him back to the events of his youth that formed his beliefs about money and relationships—the negligence of his father, which taught him not to trust anyone, and the pain of losing his fiancée when she realized his only true love was cold hard cash. This corresponds to principle 2, 'To heal you must feel.' Kahler writes in the book how he first had to experience the pain caused by his workaholism before he could get beyond it: "Like Scrooge, I learned how to feel. I began to see how my unconscious money scripts were keeping me from seeing, hearing and living in the present."

Scrooge's next visitor is the Ghost of Christmas Present, who shows him some of the joyful alternatives to his lonely, miserable existence. This corresponds to principle 3, 'It pays to be present.' "Sometimes, we need new information about what money is and what it can and cannot do for us," Kahler says. "When Scrooge sees the Cratchit family enjoying their meager Christmas dinner, he understands that money does not necessarily equal happiness."

Scrooge's last visitation is from the Ghost of Christmas Future, who shows him the grim results if he persists in his current path. This corresponds to principle 4, 'Awareness of consequences creates motivation.' But Scrooge does change, dramatically: He splurges on a turkey for the Cratchit family, gives long-suffering Bob Cratchit a generous raise, promises money to the charities he had previously spurned, and even turns up at his nephew's Christmas party. This corresponds to principle 5, 'Transformation requires action.'

The book suggests a number of exercises—like writing down your first thoughts about money and things like budgets, college, love and retirement—that can help expose hidden financial beliefs. "Becoming aware of your money scripts is the first step toward changing them," Kahler says. "But change can only happen when a person is ready for it. To do that, each person must make their own money journey." With a little help from Ebenezer Scrooge, that journey can be a rewarding one.

— **James Geary**

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Caution

Don't Gamble With Your Future: How Monte Carlo Simulations Can Help in Retirement Planning

Here's a pop quiz. Imagine you walk into a financial planner's office and the planner says she would like to run a Monte Carlo simulation on your money—say, the savings and investments you plan to retire on. Do you: A) Suggest the planner contact Gamblers Anonymous? B) Call the police to report a robbery in progress? C) Exit the office as quickly as possible? Or D) Tell her exactly what your assets are and let her spin the big wheel? Strange as it may seem, the correct answer is D. Monte Carlo simulations are one of the best tools financial planners have to help people determine whether their retirement nest eggs are likely to last for the duration of their retirement.

A Monte Carlo simulation is not a roulette wheel stashed in the back of the financial planner's office, though it is named after the famous Monaco casino. The name has more to do with the sense of humor of one of Monte Carlo's inventors—the Polish scientist Stanislaw Ulam, who worked on the Manhattan Project to develop the atomic bomb—than with any resemblance between it and gambling. Used properly, in fact, a Monte Carlo simulation can decrease rather than increase your financial uncertainty.

A Monte Carlo simulation is a computer program that juggles thousands of different variables to determine the performance of a portfolio over a period of time. It's a much more sophisticated way of retirement planning than, say, simply looking at historical rates of return. An historical analysis assumes that what happened in the past is likely to happen again in the future; if average returns were 8% over a given period in the past, then they are likely to be 8% in the future, too. A Monte Carlo simulation takes many other factors into account, including the variability of returns (high in some years and low or negative in others), fluctuating inflation, interest and unemployment rates, as well as bullish and bearish markets. The computer crunches all these numbers and more to project how your portfolio would perform under different scenarios. It then cranks out a percentage—the odds that your savings and investments will be enough to see you through retirement.

"A Monte Carlo allows you to stress test your portfolio before any of the events in the simulation actually happen," says Christopher Jones, chief investment officer with **Financial Engines**, a Web-based financial-planning service that uses the simulations. "You can see the peaks and troughs of possible events and get a real sense of the potential impact on your retirement income."

In short, Monte Carlo simulations allow you and your financial planner to better account for risk. If you're close to retirement, you obviously want the risk of missing your income goals to be very, very low. If you're further away, a higher risk might be acceptable, since you would have more time to make any necessary corrections. The calculation can show, for example, how conservative investments with low rates of return might leave you with a shortfall, or how more volatile stocks could expose you to big gains or losses. By charting a range of potential outcomes, the simulation can help you achieve the right balance between risk and return for your portfolio.

As an illustration, let's assume that you're 60 years old. You intend to retire at 65 and plan to live off the income from your savings and 401 (k) investments. If the market behaves, you should be o.k. But a Monte Carlo simulation can tell you how some big and unexpected dive (maybe because of a terrorist attack or an oil shock) or a change in your financial priorities (maybe because you want to travel more or need to support a relative) could affect your income.

Let's say that under the best-case scenarios your chances of having enough money for retirement are 95%, a range you're pretty comfortable with. If your chances suddenly drop to 85% under the worst-case scenarios, though, you might want to do something about it. The simulation can tell you exactly how much more you'll need to feather the nest to get back into your comfort zone. "To get the probability of success back up," says Jones, "you could decide to save more, or to work an extra year or two, or to increase your risk by investing more, which could leave you even worse off. Or, you could decide to live on a bit less money." Of course, none of the worst-case scenarios might ever happen. The beauty of a Monte Carlo, though, is that it enables you to be ready if they ever do.

Dan Candura, CFP®, a member of CFP Board's Board of Governors and president of the Massachusetts investment advisory firm PennyTree Advisors, compares Monte Carlo simulations to predicting the paths of hurricanes. Weather forecasters can easily show where they think a hurricane will go. Close to the storm's present location, there is a pretty narrow band of possibilities. But further away in time, that band becomes much wider because the greater number of variables makes the path of the storm more unpredictable. "It's the same with investment portfolios," Candura says. "You have to pay attention to what's close, but you also have to keep an eye on what's further away to make sure your investments are on course, that the band of income possibilities remains within a comfortable range."

Candura cautions that Monte Carlo simulations need to be properly applied and interpreted if they're not to end up as what he calls "black box gobbledygook from someone wearing a fancy tie." If you're seeing an adviser who uses the technology, Candura suggests making sure that he or she is not just punching numbers and that as your priorities change, so do the simulations. "Monte Carlos are not cast in concrete but in oatmeal," he says. "You should be able to see the effects of moving or changing a goal. They're tools for driving decision-making, not ratifying decision-making."

Monte Carlo simulations are complex mathematical computations. But then again, Candura says, "People's lives are complex, too, sometimes so complex that they think things like their retirement are too difficult to plan. Doing a Monte Carlo simulation once a year or so enables you to plan, and to continually ask yourself: Is the plan going to work?" Which is sort of like predicting the path of a hurricane. You don't need a weatherman to know which way the wind blows, but a Monte Carlo can provide some shelter in case a storm heads your way.

ONLINE RESOURCE: There are a number of sample Monte Carlo simulations that you can try out on the Web. Should you decide to have a complete Monte Carlo simulation done, you should first talk to a financial professional. The **Retirement Income Calculator** on the Web site of T. Rowe Price, an investment management firm based in Baltimore, Maryland, employs the technology and is simple and straightforward to use.

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Extra Points

Resources on CFP.net

There are many resources on the Internet with helpful and interesting information that can help you improve your financial situation. From the Web sites of government agencies that regulate financial planners and financial service providers to the Web sites of consumer protection groups and financial educators – there is an abundance of material available for people who want to increase their financial literacy.

CFP Board has updated its list of online resources to provide you with more detailed information about the organizations and Web sites that may have resources of interest to you. **Check out the updated resource information**.

If you come across a Web site not on our list that you believe would be helpful to others looking for financial education resources, we hope you'll **drop us a line** and provide us your suggestion.

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Free Space

ADMIT ONE

Reader Survey

CFP Board published the first "It's Your Turn" eNewsletter in October 2003 in an effort to provide information to people interested in learning more about financial planning. Subscribing to the eNewsletter is simple — all we ask for is an e-mail address.

As the eNewsletter has reached its third anniversary, we'd like to learn more about you. Who are you? What are your interests? What ideas do you have about how we can improve the eNewsletter? To answer those questions, we've put together a reader survey so you can let us know how we're doing and what we can do to make the eNewsletter better. We thank those who have already completed the survey and hope that those of you who haven't will take the opportunity to share your opinions.

The survey is available **here** and should take no more than 5 minutes to complete.

We hope CFP Board's eNewsletter is something you look forward to reading, and your responses to our survey will help us make it just that.

Take Our Survey

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Alert!

NAIC Consumer Alert: Annuities and Senior Citizens

The National Association of Insurance Commissioners (NAIC) recently issued a new consumer alert related to the recent increase in the sale of annuity products to senior citizens. Annuities can be complicated, and many senior citizens find themselves with annuities they don't adequately understand. NAIC provides an overview of different types of annuities, things to consider when deciding if an annuity is right for you, and tips to help you avoid becoming the victim of deceptive sales practices.

Read more about this and other financial alerts.

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The Finish

Play Again?

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