Suze Orman Can Woo A Crowd, But Can She Invest?

Written by Cheryl Curran -May 21, 2009 10:00 AM

When Suze Orman gained popularity several years ago, it was very refreshing to me to see a new face and hear an unconventional voice coming from the financial services industry.

In the still heavily male-dominated financial industry, I have been especially pleased to see a woman's advice accepted and taken seriously by people of all ages and in all stages of life, regardless of whether they have a lot of wealth or only a little.

I admire Suze's wonderful ability to break down complicated products and cut through industry jargon.

However, I think investors need to be wary of the information and advice she dispenses—and the example she sets.

What's To Like About Suze

While Suze is a licensed insurance salesperson, she has been openly critical of complicated, expensive insurance products. She has warned consumers about the high commissions and high costs built into variable universal life insurance products. She has advocated substituting low-cost term insurance and has reminded her readers and listeners that "insurance is not an investment."

This unusually candid commentary is especially welcome coming from somebody who could profit from selling expensive products but who chooses not to do so because she believes those products are seldom in the best interests of consumers. (I share that belief, by the way.)

When markets are down, Suze encourages people to continue adding to their retirement funds, even when it doesn't feel comfortable.

In easy-to-follow language, she shows how to make a written plan to pay off debts. As virtually everybody in the financial services business knows, people who follow written plans are much more likely to be successful than those who don't.

For all this and more, I encourage my clients to read Suze. But I advise them to avoid acting on her investment advice.

What's Not To Like About Suze

Suze has made some bad investment calls, especially in the past 18 months, and I don't know why. Perhaps she is under pressure to become a guru. Or it's possible that, like many people, she isn't always able to muster the wisdom, courage and discipline to stick to her own stated beliefs.

Here's an example: Suze used to advocate buying and holding only index funds, although not with the same degree of diversification that we recommend. Then in June 2008, she was interviewed by Eric Schurenberg, who was then a "Money" magazine editor.

Introducing the interview, Schurenberg said of Suze: "She possesses an encyclopedic command of financial planning and her advice is always clear and generally unimpeachable."

Despite that glowing description, I think many people who took her advice last summer would find it very impeachable.

In the interview, Suze told Schurenberg that even though all the evidence indicated index funds outperform 80 percent of managed funds, "Today I think you have to be more active." She recommended exchange-traded funds specializing in emerging markets, U.S. oil and metals & mining.

And what happened to investors who took those recommendations? From the time of her interview in June 2008, these sectors went down 44 percent, 71 percent and 71 percent, respectively, through the end of the year. Certainly this was not a favorable period for investing, but her previously recommended funds, the Vanguard 500 Index and Total Stock Market Index, dropped 28 percent and 29 percent, respectively, in that same time frame.

Of course anyone who recommends specific investments will be wrong from time to time. But abandoning a pair of relatively conservative index funds in order to chase volatile sectors with recent hot performance is not remotely close to what I would call prudent advice.

Suze On Bonds

Here's a second example: In the same interview, Suze said: "You should invest in bonds only when interest rates are going down."

Now that is a very interesting piece of advice, on a par with "Invest only in stocks that are making money."

I am surprised that a journalist as supposedly savvy as Schurenberg let that comment slip by without any follow-up, as if it were the most natural point of view in the world.

If Suze understands bond investing (which I have to assume she does), then she must mean that the only valid reason to own bonds is to buy them at a low price and sell them at a higher price. (As you probably know, bond prices generally rise when interest rates fall.)

Investing this way is legitimate if that's what you are after and if (this is a very big if) you have some system for knowing when to buy and when to sell. Suze of course was not offering any such system.

Millions of investors own bonds with an entirely different objective: to stabilize a portfolio that also contains equities. This is what we recommend. If those investors took Suze's advice, they would be defeating their own purpose.

By allocating a portion of your portfolio to short- and intermediate-term bonds, you have a built-in brake system designed to offset some of the losses experienced in a typical bear market. The only way to do this is to continue to own bonds even when their prices go down.

In fact, with periodic rebalancing (which we also recommend), investors should buy more bonds when their prices are relatively low.

Unfortunately, Suze does not seem to appreciate this very important reason for owning bond funds.

Suze On Asset Allocation

Here's a third example. I think Suze is way off the mark in her recommended allocations between equities and fixed income (including bonds). Her recommendations are so conservative that I fear they could lead many investors to fall far short of their goals or even run out of money after they retire.

Suze has stated publicly that less than 4 percent of her liquid net worth is in the stock market. Why is this? It cannot be that she's totally risk-averse, since last year she was chasing oil and mining sectors.

I think it is obvious that Suze has a huge income from being a successful author and entertainer. Her liquid net worth has been estimated at more than $25 million. She can easily obtain plenty of spending money for the rest of her life by investing heavily in zero-coupon municipal bonds.

That's fortunate for her. But I have to wonder how closely she is in touch with the needs of real-world investors who have limited resources.

Keeping Up With Inflation

There are very important reasons that investors need equities in a portfolio even after they are retired. Unless you have acquired or saved more money than you can ever imagine spending, one of the biggest risks you face is eventually running out of money. A portfolio that's exclusively or very heavily weighted to cash and bonds magnifies this risk.

Suze's advice ignores a couple of the obvious facts of life of investing. Over the long run, cash and cash equivalents tend to approximately keep up with inflation, but not to exceed it. This is fine if all you want is a low-risk way to store a given amount of value. But if you are taking more than token withdrawals out of a cash portfolio, the value will inevitably dwindle.

Yet that, in essence, is what Suze seems to be recommending.

For somebody with only a few years left to live, this may work out perfectly. But people typically need to plan for retirement periods of 20 to 40 years. For that, a heavily cash-weighted portfolio doesn't cut it.

From my point of view, Suze's investment advice has not been good. It does not seem to be based on a good grasp of some important and fundamental concepts. Furthermore, Suze may be out of touch with the needs of most people who are entering retirement.

My advice to her viewers, listeners and readers is twofold: Appreciate and learn from her "plain English" explanations of financial products and subjects. But don't follow her investment recommendations and advice. And don't follow her example.