# A Dave Ramsey Manifesto

I ‘ve been teaching an investment course at my church for many years. A comment I often get from my students is, “Dave Ramsey only takes us so far. He has helped us get out of debt and get our financial house in order, but we don’t know where to go from there.” They want to go beyond Ramsey’s advice of “buying a good mutual fund,” whatever that means.

I have occasionally listened to Dave’s radio show, read most of his books and even taught his Financial Peace University course. I would have to agree with my students, Dave Ramsey is a great personal money management expert. He is not, however, in any way, shape or form, a qualified investment professional. To be absolutely clear, Dave Ramsey is not licensed or trained to give investment advice.

Bear in mind, this is not a personal attack on Ramsey; he has helped millions of Americans straighten out their finances, for which he should be commended. But he should stick to what he knows and stop giving investment advice. It’s potentially dangerous! Dave’s investment philosophy, which he shares on his website is seriously flawed and represents nothing more than his opinion, which is misguided. Take Jim Cramer for example. He told one of his viewers not to sell his shares in Bear Stearns. Three days later, the stock fell from $159 a share to $2. Cramer expressed his opinion, which turned out to be disastrous. The problem is the viewer had to pay the consequence, not Jim Cramer. I don’t know about you, but I am much more interested in facts than opinions when it comes to investing.

The following are opinions expressed on Dave’s website, DaveRamsey.com: “I always encourage people to choose a good growth stock mutual fund.” I am fascinated by this statement. How does one define a good growth stock mutual fund? Is it the top performer for the past year, three years, five years, ten or 20 years? If you do a search, you won’t find the same fund ranked as a top performer in all of these time periods. In other words, you won’t necessarily find the top-rated mutual funds for three years ranked highly in a list of top funds for ten or 20 years. So, what time frame do you use? Ramsey doesn’t say. Guessing is not a sound investment strategy.

Last year's winner can easily end up next year's loser. According to research from Davis Advisors: “Ninety-five percent of the top-performing managers from 2004 to 2013 fell into the bottom half of their peer groups for at least one three-year period.” Get the point? Most top-performing mutual funds end up under performing sooner or later. Even Morningstar’s top-rated equity funds have lagged the market by a wide margin at some point in time. I'm still scratching my head on exactly what Ramsey means by "good." Perhaps I should contact a financial astrologer.

*One essential truth about investing is that, generally speaking, good results will bring more money to "hot" money managers and strategies, and if allowed to grow unchecked, more money will bring bad performance.*
**— HOWARD MARKS**

How about a reality check? Index funds beat roughly 90 percent of all actively managed stock mutual funds. They have substantially lower fees, lower turnover, thus generating less taxes, and they have no front-end sales charges, unlike what Dave recommends—mutual funds that will cost you 4-5%. Why pay for an upfront commission when you can buy no-load funds and save yourself some serious money? Help me out here, how is paying a 5% upfront sales charge in your best interest? Maybe it has something to do with the radio star aligning himself with brokers who earn commissions selling mutual funds with front end sales charges? Brokers have to pay Dave $549 per month to become an "endorsed local provider." This is an outrageous conflict of interest, wouldn't you say?

"I recommend growth, growth and income, aggressive growth and international funds." —from DaveRamsey.com. Does putting 100% of your investable assets into stock mutual funds make any sense to you? This is Dave's blanket recommendation to everyone who visits his website.

Whether you are an aggressive or conservative investor, age 30 or 70, retired or 40 years away from retirement, everyone gets the same investment advice.

That's not exactly stellar counsel. How anyone can recommend putting 100% of your money into stocks[1] regardless of your goals, risk tolerance and time horizon is beyond my comprehension. In fact, it's malpractice, which is prescribing without proper diagnosis. It shows he has very little mastery of the investment world. His advice is idealistically distorted, lacking intellectual integrity and any kind of critical thinking.

Consider the following:

- In the 1987 crash, the market was down 33.5 percent.

[1] A stock mutual fund is nothing more than a portfolio of individual stocks.

- In the aftermath of 9/11, the market was down 36.8 percent.
- In the aftermath of the 2007-2009 Great Recession, the market was down 57.6%.

If you had followed Ramsey's advice, you would have gotten creamed in those bear markets. Who do you know who would be okay with losing half their money? Anyone in their right mind should avoid putting all of their money in the stock market. Let's do some quick math. If you went with Ramsey's recommendation and lost 50% of your portfolio in 2007-2009, the stock market would have to go up 100% for you to break even.

$100,000 investment
- $50,000 = 50% loss
$50,000 portfolio value X's 100% ($50,000) equals
$100,000

How long might it take for the market to go up 100% for you to break even?

Three years, five years, ten years? Only God knows. Ramsey states in *Total Money Makeover*, "Your financial process and principles must work in good times and in bad times—otherwise, they don't work." Well, if what Mr. Ramsey states is true, then his own investment advice is severely lacking. I wouldn't call losing half my money a successful investment strategy, would you?

Dave's advice on splitting your investment dollars among four stock funds is not biblical! Remember what Solomon said, *Divide your portion to seven even to eight, for you do not know what misfortune may occur on the earth.*[2] I will take the ancient wisdom of Solomon over Ramsey any day.

Dave's advice defies common sense and my grandmother's wisdom of not putting all my eggs in one basket. If you take Ramsey's advice, that's exactly what you're doing—putting 100% of your hard-earned money into the stock market. As a side note, I was a chief compliance officer early in my career. In my professional opinion, Dave's investment tips are not suitable for most of the people on planet Earth.

[2] Ecclesiastes 11:2 (NIV)

Let's dig deeper into his recommendations. Putting your money in four mutual funds as Dave suggests does not give you any degree of real diversification. I went to the mutual fund company's website most people think Ramsey refers to when he cites long term track records. I looked at one of their growth funds and a growth and income fund. Both funds owned 22 (out of the top 45 holdings) of the same stocks. In other words, if you invested in each of these two funds, you owned a lot of the same stocks in both portfolios. This is not diversification, it's duplication.

*Maximum diversification, minimal cost, and maximum tax efficiency, low turnover and low turnover cost, and no sales loads.*
**— JACK BOGLE ON HOW VANGUARD ACHIEVED SUCCESS**

Bogle's advice is just about the opposite of what Ramsey recommends. Dave's advice is indefensible; it will eventually get you into big trouble; it's just plain foolish.

*Focus on long-term returns, 10 years or longer if possible.*
**— DAVERAMSEY.COM.**

Really? According to research done by the *Financial Analyst's Journal*[3], only 6.9 percent of the nearly 3,000 mutual funds that had been around long enough to be included in their study had managers with at least ten years' experience.

Their research resulted in a couple of enlightening conclusions:

1. "In any given year, even the longest surviving solo managers are unlikely to produce significantly more positive style-adjusted monthly returns than negative ones." The point? Managers with ten years' tenure do not necessarily provide enhanced returns.
2. "The key to a long career in the mutual fund industry seems to be related more to avoiding under performance than to achieving superior performance." The point? Mediocre investment returns are the norm.

One last jab: According to Morningstar, as many as one out of three mutual fund managers change jobs in any given year. The point? You find the perfect fund for

[3] 2014 "The career paths of mutual fund managers-the role of merit." By Gary Porter and Jack Trifts

you and your family, only to find out your manager leaves his or her job in a year or two. Now what? Start all over again? —Good luck!

Here is the final nail in the coffin: Dave says, "Focus on long term returns, 10 years or longer if possible." The problem with this advice is, according to the Schwab Center for Financial Research, "It is hard for active managers to repeat success year after year." Not a single actively managed mutual fund manager ended up in the top performing quartile[4] every year when at the helm for at least eight years. Got that? Not a single equity mutual fund manager was able to rank in the top performance quartile for more than seven years in a row.

Under the cost section on how to choose the right mutual funds on DaveRamsey.com, Dave recommends front-end load MFs. He also says, "Pay attention to the fund's expense ratio, a ratio higher than 1% is considered expensive."

What about the rest of the fees mutual funds charge? Transaction or trading costs (approximately 1.44% per year), cash drag, and taxes can also be expensive. According to Forbes magazine, the real cost of owning a mutual fund is 3.17% a year in a tax deferred account like a 401(k) or IRA, and a staggering 4.17% per year in a taxable account (including sales charges and commissions). Plus, Ramsey wants you to pay a 4-5% up-front sales charge, which means only 95-96% of your money actually gets invested.

Fees, charges, commissions and lack of diversification can destroy your nest egg. Why not invest in an index fund that charges only 0.09% per annum? By doing so, you would save about 3% per year. That would give you an extra $109K in a $100,000 portfolio over a 25-year period of time. Dave Ramsey's advice is very costly and not very well thought out.

And now, the coup de grace:

> *Dave does not recommend exchange traded funds (ETFs), single stocks, certificates of deposits (CDs), bonds, fixed annuities, variable annuities (VAs), real estate investment trusts (REITs), cash value or whole life insurance.*
> — **DAVERAMSEY.COM**

[4] 25%

I agree with Dave on the last item. For the most part, life insurance is a terrible place to put your investment dollars. In most policies, the insurance company keeps the cash value or savings/investment portion when the insured passes away. Anyone who thinks that's a good deal needs to have their head examined. I also agree with Dave on CDs; they are savings vehicles, not investments. CDs are ideal for short-term safe dollars and for an emergency fund. On the other hand, if I agreed with Dave on the rest of what he "does not recommend," we would both be wrong.

Let's briefly examine the remaining asset classes Dave does *not* recommend. First, exchange traded funds, or ETFs. ETFs, for the most part, track indexes like the S&P 500. Since the S&P 500 has outperformed about 90% of all actively managed mutual funds, and since ETFs do not have a front-end sales charge, and since the internal fees ETFs charge vs. a mutual fund are minuscule, with lower turnover and taxes than mutual funds, Ramsey's prohibition of ETFs makes no sense at all.

For whatever reason, single stocks are also forbidden. Hmm, what about Berkshire Hathaway, a single stock run by Warren Buffett and Charlie Munger? These two guys are arguably the greatest investors of all time. They manage assets of around 700 billion dollars. Compare that with the average mutual fund with about 20 billion in assets.

Buffett and Munger have a 20% average annual return[5] since 1965 versus 9.9% for the S&P 500 index. I challenge Dave to find a mutual fund with a better track record. There aren't any that come close. I can think of numerous other individual stocks besides Berkshire Hathaway that would make suitable investments for a lot of people seeking growth and/or income. Once again, Dave's advice is baffling. And just when you thought his judgment could not get any worse, he surprises us.

Next on Ramsey's forbidden list is bonds. I took the time to listen to Dave's explanation on why he doesn't recommend bonds on YouTube. Parenthetically, after watching the video, I would say Dave Ramsey and I have the perfect face for radio. He said, "They[6] don't perform as well as stocks over time." That's neither true, factual or correct. Reality check: According to Jason Zweig, writer of the Intelligent Investor column in the *Wall Street Journal,* "As recently as 2011, bonds

[5] Source: Berkshire Hathaway Annual Report 2017
[6] Bonds

had earned higher returns than stocks over the prior 30 years."[7] According to ABC News, from 2002 to 2012, bonds outperformed stocks by five percent. Avoiding the facts does not change them, Mr. Ramsey. You cannot ignore the truth for the sake of convenience; sometimes bonds do outperform stocks. Period.

What fantasy land does Dave live in? What about the risk mitigation, quarterly income and diversification bonds provide?

Here's some food for thought; I don't like broccoli. That doesn't mean you shouldn't eat it, if you like it and it is good for you. Just because Mr. Ramsey doesn't like bonds, doesn't mean they are not suitable for a lot of folks.

Take 2002, for example: Bonds[8] were up 10.26% for the year, while the stock market[9] was down 22.1%. A 32.36% difference! In 2008, bonds were up 5.24%, while the market was down 37%, a 42.24% difference! Bonds can look pretty attractive when the stock market is getting pummeled, don't you think? What about the steady, reliable income stream that bonds offer? I'd rather rely on my bond income when the market is down than be forced to sell shares of my "good growth stock mutual funds" at a substantial discount to supplement my income.

I was puzzled when Dave said it was alright to invest in a balance fund if you want to take on less risk. The reason I am baffled is because a typical balanced fund will generally have 30-50% of its portfolio invested in bonds. So, why is it not ok to invest in bonds, but permissible to invest in a mutual fund that has as much as 50% of its holdings in bonds? What kind of double talk nonsense is that? Sadly, some people avoid reason until they have tried everything else.

The next asset class not allowed in Ramsey Land is fixed annuities. Dave says fixed annuities are "designed to deliver a guaranteed income for a certain number of years in retirement." Sounds good to me. As a retiree living off my investment and annuity income, I don't see anything wrong with a guaranteed lifetime income stream; it actually comes in pretty handy.

I love the next line from DaveRamsey.com: "Dave doesn't recommend annuities because they are often expensive and charge penalties if you need to access your

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[7] Source: The Bank Credit Analyst, March 2003
[8] Barclay's Aggregate Bond Index
[9] The S&P 500

money during a defined surrender period." Okay, Dave, why not buy a no-load annuity with no surrender charges? Problem solved.

Variable annuities (VAs) are next on Dave's no-no list. DaveRamsey.com says, "VAs are insurance products that can provide a guaranteed income stream and death benefit." So, if you don't need either one of those benefits, don't buy a VA.

On the flip side, however, many retirees find these benefits attractive. Dave goes on to say, "Fees can be expensive, and VAs also carry surrender charges." Yes, indeed, VAs can be expensive, but so are many mutual funds. Why buy a costly VA when you can buy a no-load, no surrender charge variable annuity? I think I already solved that problem above.

Real Estate Investment Trusts (REITs) are also banned in Ramsey Land, yet, Dave says they are "similar to mutual funds." So, apparently, it's okay to own mutual funds but not REITs, even though they are similar to mutual funds. I'm not quite sure that makes sense. Here's the best part: "Dave prefers to invest in paid for real estate bought with cash and does not own any REITs." I'm happy for Dave. He has a net worth of 60 million, so he can pretty much afford to pay cash for his real estate investments, or anything else for that matter. But what about the rest of us homo sapiens who don't have millions laying around?

For the average investor, REITs can make a lot of sense. With a single small investment (like a MF) you can buy a portion of dozens of different properties in various geographical locations and industries.

Oh, one minor detail Ramsey seems to have overlooked: Equity REITs have historically outperformed direct real estate investing,[10] not to mention providing a diversified pool of liquid real estate assets that pay a quarterly dividend and the potential for price appreciation. Even better, REITs are passive investments. You don't have to fix broken stuff.

I'm sitting here pondering Ramsey's logic, or lack thereof. It's okay to buy stock mutual funds, but it's not okay to buy REITs which are indeed stock mutual funds? Is it permissible or prohibited to buy a stock mutual fund that owns nothing but real estate? While you ponder the question, let me point out that REITs are one of the top performing asset classes with a double digit average annual return over the

[10] Source: *Forbes* magazine July 19, 2017

past 40 years.[11] Why wouldn't you want a top performing asset class in your portfolio? Why no REITs, Mr. Ramsey? Based on the facts, I'm stumped. Farewell to reason and logic.

Okay, that's enough. I am done wandering amongst innumerable absurdities.

Here's the bottom line in my, not so humble, professional opinion: Dave Ramsey provides less than brilliant advice. Period! Follow it at your own peril. As I said earlier, prescribing without proper diagnosis is malpractice. Anyone who advocates for the entire American population to put 100% of their investable assets in the stock market is lacking common sense. Obviously, giving sound investment advice is beyond Dave Ramsey's realm of competency. If he was so smart, he'd know he was wrong.

Finally, Dave completely ignores investor behavior, the tendency most folks have to overreact to both positive and negative developments in the markets. Investors are rarely objective and rational, especially if the stock market is getting trashed. So many sell at precisely the wrong time and lock in permanent losses. He also ignores the impact of having to withdraw money to live on when the stock market is down over a protracted period of time.

Remember, if you follow Dave's investment philosophy, you're taking advice from someone who filed for bankruptcy. He may be entertaining, but his investment advice can lead to disastrous results. I could go on and on, but I will spare you. My recommendation to you is to follow Dave's financial advice and completely ignore his investment philosophy. He is, by his own admission, not an investment professional. It is unlikely you will ever become a great investor by listening to Dave Ramsey.

I would say to Mr. Ramsey, "Don't try to be something you are not, an investment professional." Take the advice of Dirty Harry Callahan, "A man's got to know his limitations."

One last thought on Mr. Dave Ramsey: There are certain things I will not do, like skydive, swim with sharks and take investment advice from an unlicensed talking head. His methods are unsound.

[11] Source: NAREIT

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Want to know more about Dave Ramsey's investment advice?

Order a copy of my latest book, *How to Be a Great Investor, Investment Techniques for Christians* on Amazon.

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