Personal finances and investing for the physician: a Boglehead's approach

Vinay Mehta, MD

Allergy, Asthma & Immunology Associates, P.C.

Lincoln, Nebraska

Disclosures

- I have no relevant financial disclosures
- I am not a financial advisor
- The information presented is for educational purposes only

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

Why is this even important?

- Doctors start their first real job relatively late in life
- Little or no financial experience
- High student debt load (average $200,000)
- We assume that financial advisors have our best interests in mind
- NOT ALWAYS THE CASE…

Who is a Boglehead?

- Disciple of John Bogle, founder of The Vanguard Group, the world's largest mutual fund company
- $7.2 trillion in assets under management
- Created the first index fund available to retail investors
- Credited for driving costs down across the mutual fund industry

May 8, 1929 – Jan 16, 2019)

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

10 principles we believe in

- Live below your means
- Invest early and often
- Never bear too much or too little risk
- Diversify your investments
- Never try to time the market
- Use index funds when possible
- Keep costs low
- Minimize taxes
- Invest with simplicity
- Stay the course

#1 Live below your means

- Save at least 15% of your gross income every month
  - Emergency fund (6 months of living expenses) (fully fund first)
  - Retirement fund (10%)
  - Big-ticket items (5%)
- Develop a sensible household budget that accounts for needs & wants
- ☞ Median US family income: $79,900 (2021)

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#1 Live below your means

Needs

- Emergency fund
- Basic groceries, clothing, housing
- Basic transportation
- Health insurance
- Disability insurance
- Life insurance (term)
- Retirement fund

Wants

Everything else!

#1 Live below your means

How much money do you need to retire?

- The Trinity study (1998) suggests a 4% safe withdrawal rate in a 50/50 stock/bond portfolio over a 30-yr period (the authors examined data from 1925-1995)
- Due to low bond yields, recent studies suggest a 3% safe withdrawal rate
- $2M portfolio gives you $60,000 per year (inflation-adjusted) for 30 yrs
- $4M portfolio gives you $120,000 per year (inflation-adjusted) for 30 yrs

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#2 Invest early and often

- Money invested early in life is greatly more valuable than money invested late in life
- "Magic" of compounding

#2 Invest early and often

Ages 22-32

Ages 40-50

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#2 Invest early and often

- Work-around for physicians: live on a fellow's salary for the first 3 years post-fellowship
- Average salary increases from $70,000 to $170,000/year
- Assuming you invest the extra income: $100,000 x 3 yrs x 5% annual rate of return (inflation-adjusted)

=$1.2 M in 30 yrs

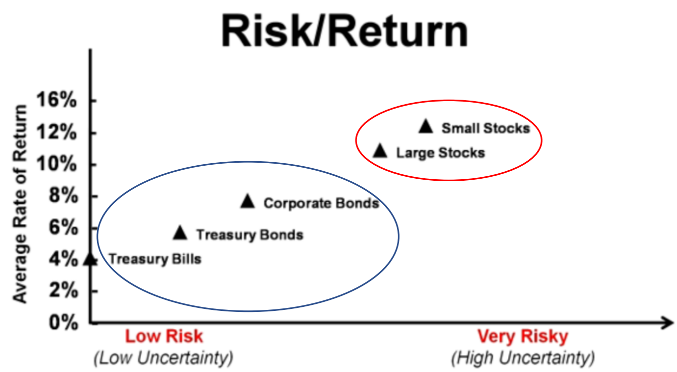
=$1.5 M in 35 yrs

#3 Never bear too much or too little risk

- Investing = earning a return in exchange for shouldering risk
- 2 major classes of assets
  - Stock: ownership in a company
  - Bond: loan made to a company (or government)
- The higher the risk, the higher the expected return

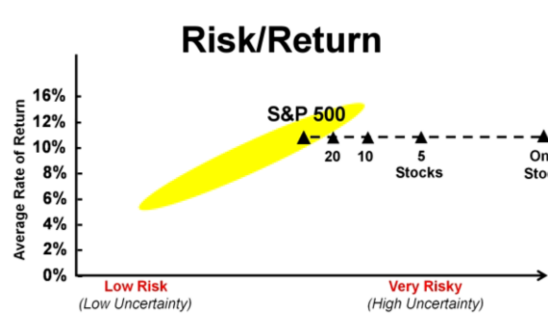
Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#3 Never bear too much or too little risk



#3 Never bear too much or too little risk

- Overall risk of a portfolio is determined by the stock/bond ratio
- Only applies to diversified portfolios – not individual stocks or bonds



#3 Never bear too much or too little risk

How much risk should you bear?

- Ability to take risk
- Willingness to take risk
- Need to take risk

#3 Never bear too much or too little risk

Ability to take risk is determined by your investment horizon

• <5 years	Treasury bills Certificates of deposit Money market
• 5-10 years	Bonds
• >10 years	Stocks

#3 Never bear too much or too little risk

- Willingness to take risk: how much loss can you live with?

	Asset Allocation Percentage Stock/Bond	Exposure to Maximum Loss
	20/80	5%
	30/70	10%
	40/60	15%
	50/50	20%
Sweet spot →	60/40	25%
	70/30	30%
	80/20	35%
	90/10	40%
	100/0	50%

#3 Never bear too much or too little risk

- Need to take risk: determined by your financial goals, time horizon, and the rate of return

US Financial Market Annual Returns and Inflation, 1926–2018

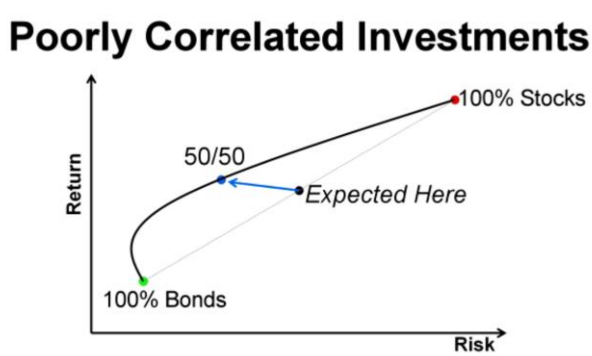
Nominal Returns	Arithmetic Average Return	Average Compounded Return	Standard Deviation
Small-Cap Stocks	16.2%	11.8%	31.6%
Large-Cap Stocks	11.9%	10.0%	19.8%
Long-Term Corporate Bonds	6.3%	5.9%	8.4%
Long-Term Government Bonds	5.9%	5.5%	9.8%
Intermediate-Term Government Bonds	5.2%	5.1%	5.6%
30-Day Treasury Bills	3.4%	3.3%	3.1%
Consumer Price Inflation	3.0%	2.9%	4.0%
Real (Inflation-Adjusted) Returns			
Small-Cap Stocks	13.0%	8.7%	31.0%
Large-Cap Stocks	8.8%	6.9%	19.8%
Long-Term Corporate Bonds	3.4%	3.0%	9.4%
Long-Term Government Bonds	3.1%	2.5%	10.8%
Intermediate-Term Government Bonds	2.3%	2.1%	6.6%
30-Day Treasury Bills	0.5%	0.4%	3.8%

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#4 Diversify

- Buy index funds that hold large segments of the market
- Broad diversification ensures average market returns
- Holding investments whose performance correlates poorly (e.g. stocks vs. bonds) maximizes returns while reducing total risk

#4 Diversify



Efficient frontier (modern portfolio theory)

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

#4 Diversify

How?

Single-fund

- Buy a single fund that is in itself diversified (i.e. target retirement fund)

Multiple funds

- Buy a few index funds that cover the entire market (i.e. Total US Stock, Total International Stock, Total US Bond)

#4 Diversify

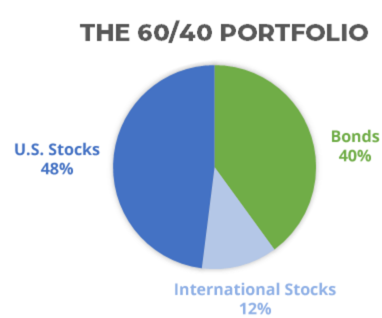
3 fund portfolio

Stocks (60%)

- Total US stock market (60%)
- Total international stock market (40%)

Bonds (40%)

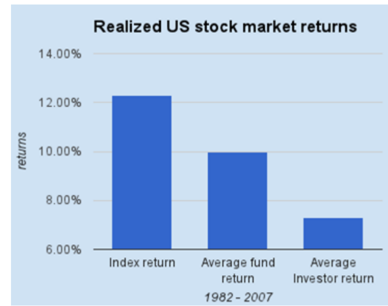
- Total US bond market



Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#5 Never try to time the market

- Between 1982-2007, the US stock market provided an annual return of 12.3%
- The average equity fund earned an annual return of 10.0%
- …but the average investor earned an annual return of only 7.3%



#5 Never try to time the market

Mistake #1

- Attempting to predict the future direction of the market

☞ Fool's errand

Mistake #2

- Investing in yesterday's winners

☞Regression towards the mean

#5 Never try to time the market

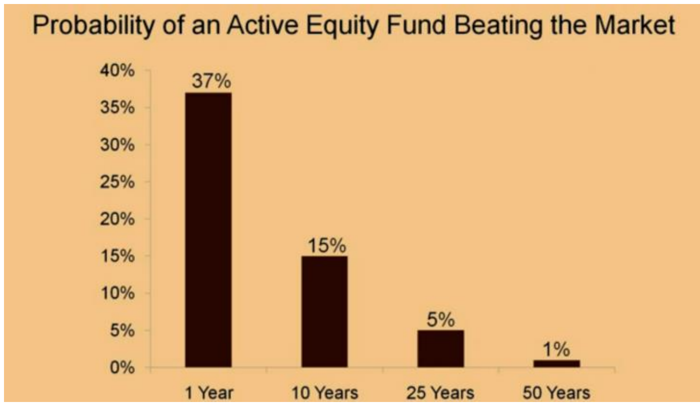
- Asset allocation determines 90% of a diversified portfolio's return
- People who chase after performance ultimately lose money from poor market timing and increased transactional costs
- Rather, periodically rebalancing your portfolio ensures that you are selling "high" and buying "low"

#6 Use index funds when possible

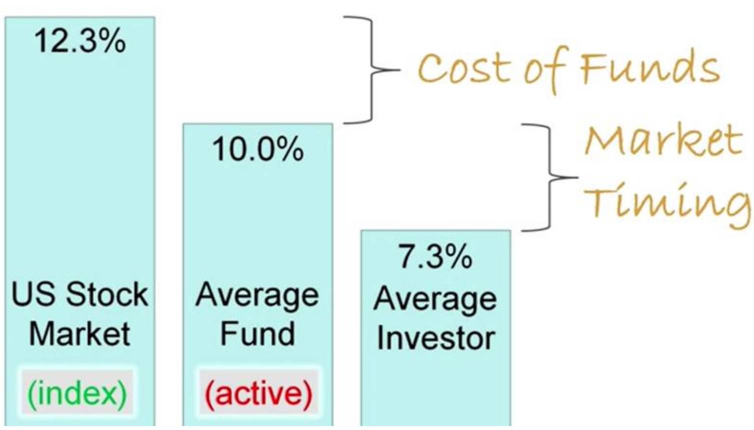
Index funds	Active funds
Match the market benchmark	Try to outperform its benchmark
Buy the entire benchmark	Hand-pick individual stocks/bonds
Extremely diversified	Less diversified
Highly tax efficient (few trades)	Less tax efficient (more trades)
Low expense ratio (<0.2%)	High expense ratio (0.75-1%)

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

#6 Use index funds when possible



#7 Keep costs low



Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

#7 Keep costs low

- An expense ratio of 1% might not seem like much, but if compounded over a lifetime, it is enormous!
- 1% expense ratio over 50 years will reduce your total net return by 40%

#8 Minimize taxes

- Take advantage of tax-deferred plans:

401(k): $19,500/individual + $6500 catch-up if ≥50 yrs

IRA: $6000/individual + $1000 catch-up if ≥50 yrs

HSA: $3600/individual, $7200/family + $1000 catch-up if ≥55 yrs

- Allows immediate tax deductions up to the full amount of your contribution
- Monies in these plans are not taxed as income until withdrawn

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

#8 Minimize taxes

- Take advantage of tax-exempt plans:

ROTH 401(k): $19,500/individual + $6500 catch-up if ≥50 yrs

ROTH IRA: $6000/individual + $1000 catch-up if ≥50 yrs

- No immediate tax deduction but earnings grow tax-free
- Ideal for new physicians because we start out in a low tax bracket but end up in a high tax bracket in the future
- Phase-out if income >$140,000 (single) or >$208,000 (married)

#8 Minimize taxes

Work-around (backdoor ROTH IRA)

- Open a traditional IRA
- Make a nondeductible contribution to the traditional IRA
- Convert the traditional IRA into your Roth IRA (income thresholds do not apply to conversions)
- Repeat this process every year

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

#9 Invest with simplicity

Advantages of a simple portfolio:

- Low costs
- Easy to analyze
- Simple to rebalance
- Simple tax-preparation
- Simple record-keeping

#10 Stay the course

- Once you have set your long-term investment goals, established an asset allocation and invested assets, stick to your plan
- Tune out all the media noise
- Doing nothing is often the best course of action

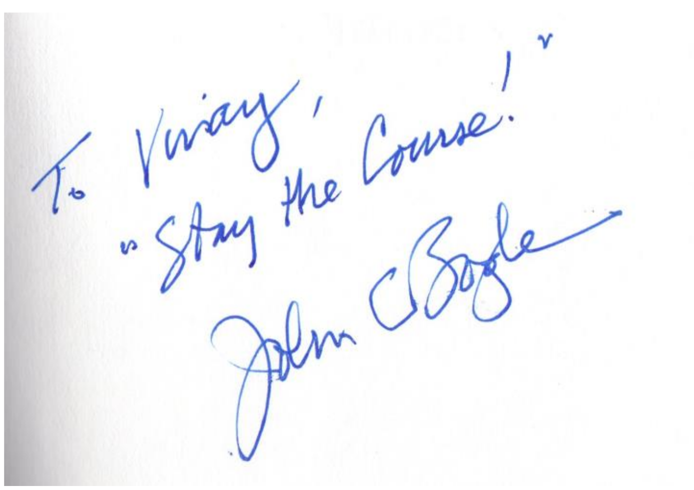
Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

Concluding remarks

- Good financial and investment planning is important for late career starters such as physicians
- Consider implementing the Boglehead philosophy
- Living below your means and investing early practically guarantees a secure retirement
- Consider living on a fellow's salary for the first few years post-training
- Asset allocation determines 90% of a diversified portfolio's return

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

Happy investing



Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
AAAAI American Academy of Allergy Asthma & Immunology

Bibliography

1. www.bogleheads.org
2. www.whitecoatinvestor.com
3. www.vanguard.com
4. The Bogleheads' Guide to Investing, 2nd edition (2014)
5. The Bogleheads' Guide to Retirement Planning (2009)

Practice succession planning

Nick Hernandez, MBA, FACHE

Founder & CEO

ABISA

Virtual Practice Management Workshop
JULY 23-24, 2021
Accessible, affordable, applicable
American Academy of Allergy Asthma & Immunology

Four Myths of Succession Planning

- There is plenty of time
- It's easier to just sell it
- A successor will be ready when I'm ready
- Giving up ownership means losing control and income

Contemplating Succession Planning

- Selling to an outside party
- New patients
- Website
- Cosmetic
- Revenue and procedural volume
- Accounts receivable
- Staff
- Planning your exit strategy