

Investment Knowledge versus Literacy

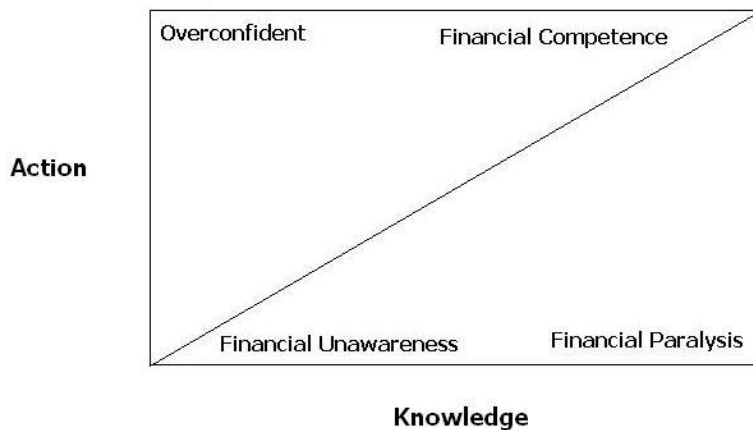
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After all is said and done, a lot more is said than done

Though an investor may be knowledgeable, he might not be able to act like it. This is according to Sandra Huston from Texas Tech University who spoke at the Networks Financial Institute at Indiana State University Conference in Indianapolis, Indiana on May 17, 2009.

Huston and her colleagues at the meeting explained that financial literacy is different than knowledge. It is the ability to use information and skills to manage financial resources effectively rather than just understanding them. This concept of literacy versus knowledge relates to budgeting, saving, and borrowing, as well as investing.



Dr. Huston explained these concepts by using a chart similar to the one above. Knowledge is on the horizontal axis and action on the vertical. Little knowledge (on the left) results in financial unawareness and thereby often leads to lack of action. If action is taken, it is because such a person is overconfident because he doesn't possess understanding.

On the other end of the spectrum (to the right) is someone with high financial knowledge. If he acts, he is able to be financially competent and serve his own best interests almost certainly better than anyone else because he knows what they are. If he doesn't act, he is exhibiting financial paralysis because he has enough understanding to do so, but has internal issues (perhaps fear or a weak self protective instinct) that prevent him from acting.

Knowledge without action is useless because the same, often destructive, habits are continued without improvement. This can work to the detriment of an investor. For example, one who is well-informed, but paralyzed in this depressed economy because he doesn't feel capable of making a change. He knows his portfolio is too risky, but doesn't act to protect himself. This could include adjusting it himself if he is self-directing his investments, or if not, speaking with his advisor about his concerns so that appropriate steps are taken.

Next week: 'No brainer' portfolios even the financially paralyzed can love.

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