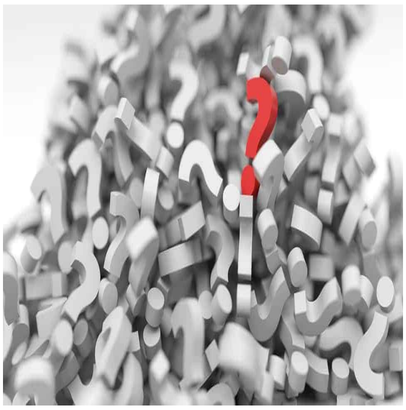

Is Financial Independence A Myth?

Description

Financial independence is a goal to which many people aspire. The idea that it is possible to be independent of the wider economy and for a portfolio to deliver rising returns no matter how the macro outlook appears is clearly highly attractive. After all, to generate a high and consistent return is the fundamental goal of most investors.

However, is this a realistic aim? Or, is it impossible for an investor to generate high returns without being reliant on one or more factors?

Financial independence

By its very nature, being financially independent means an individual's financial affairs are not dependent upon anything or anyone else. For example, someone seeking financial independence may no longer rely on a salary from an employer, or financial aid from a relative or family member. They may have a portfolio of assets which they believe makes them financially independent, thereby reducing their overall risk profile.

Furthermore, diversifying a portfolio may also provide a greater feeling of independence for an investor. This is because diversifying among a range of companies causes company-specific risk to fall. Similarly, buying shares in companies which report in different currencies causes currency risk to fall, while countering geographic risk by having a spread of companies across the globe means an investor may develop an even greater feeling of independence.

The reality

However, no matter how much capital an individual has in their portfolio, nor how well diversified they are, they are still dependent upon the performance of the global economy. Should the global macroeconomic outlook decline, their capital growth and income returns from risky assets such as shares may fall. Similarly, if the world inflation rate increased, they may see their spending power decline in real terms, for example.

As such, all investors depend on stable growth being present in the long run when it comes to risky assets. Even if they are invested in assets which are less reliant upon the performance of the global economy and may even rise during a global recession, such as gold, the reality is that in the long run those assets are dependent upon investor sentiment to a large extent. There is no guarantee that gold would become popular in a global recession, for instance, which means an investor buying gold in order to seek financial independence may in fact be reliant upon a rise in market sentiment in response to changing trading conditions.

Limited financial dependence

Therefore, it may be prudent for investors to seek a state of limited financial dependence, rather than financial independence. Given the globalised nature of the world economy, it seems improbable that any investor could create a situation where they have high returns which are not dependent upon someone or something else in the long run.

As such, while reducing risk, increasing diversification and seeking to become less reliant on other individuals or factors are noble aims, all investors must accept that to at least some extent their financial future is simply out of their hands. That’s why obtaining a wide margin of safety and seeking the best risk/reward opportunities could prove to be the best strategy for Foolish investors.

CATEGORY

1. Investing

PARTNER-FEEDS

1. Msn
2. Newscred
3. Yahoo CA

Category

1. Investing

Date
2025/08/27
Date Created
2017/07/29
Author
peterstephens