If you're over the age of 30, you probably remember the USDA's Food Pyramid. It represented the best thinking (at that time) as to how Americans should structure their diets for optimum health.

I'm not sure what the correct diet is, but consuming most of your calories from muffins, pasta, bagels, and cereal is probably not it.

Is the correct diet Paleo? If so, this old Food Pyramid is exactly upside down. Or is it the Mediterranean diet? In that case, it is more sideways. Perhaps the right answer is simply caloric restriction and intermittent fasting, in which case any food allocation is likely too big by a third.
Whatever the ultimate “right answer” is, we know one thing for sure: We’re closer to it today than we were 30 years ago. The more we learn about nutrition, human metabolism, and genetics, the better we get at creating a healthy diet. This is not to suggest there aren’t discrepancies in the literature; but food research and nutrition science paint a more nuanced picture of the body, and with that, create more informed conversations about what constitutes a healthy diet…of course, having the discipline to implement that diet is a separate issue.

The other day, I heard an analogy from Naval Ravikant, who was not talking about food pyramids, but about blockchain technology. In this analogy, he referenced the way that layers of amber compound, each building upon the previous layers. I believe there’s a similar cumulative dynamic when it comes to learning. The Food Pyramid from yesterday – though flawed – was a requisite “layer” from which our nutritionists built, moving us closer to the healthier diets of today. In essence, yesteryear’s mistakes became the foundation for today’s understanding.

What’s this have to do with investing?

Well, similar to the Food Pyramid, the best investment thinking of 50 years ago seems a bit silly and outdated to us now, given the layers of knowledge that have accumulated in the years since.

For instance, 50 years ago, the Investing Pyramid probably looked like this...

You could argue a number of different variants of this pyramid, but I think it’s in the ballpark. Ideas like Modern Portfolio Theory, Buy and Hold, and the Nifty Fifty were all part of the conversation. One could make the case that buying a home should be included, but I believe a home purchase falls more into the personal finance arena. Given that, we’ll come back to housing later. As, for now, I want to focus on blueblood investing concepts.
So, the above pyramid is likely what our parents and/or grandparents considered good investment protocol back in the day. However, we've learned a great deal about investing in the subsequent years – not just through academic papers and books, but practitioner experience as well. So, what should the pyramid look like today? Below is my slightly biased opinion as to what your investment diet should be.

Let’s briefly touch upon each layer...

**Don’t do dumb things:**

The foundation of a long-term, healthy portfolio is, in many ways, simply avoiding a self-inflicted explosion. We’ve all read the studies and are aware that, left to ourselves, we’ll often find a way to vastly underperform the benchmarks. However, many of us still can’t seem to get out of our own way. Whether it’s chasing the latest hot stock, doubling down on a trainwreck investment because it just has to bounce soon, or getting swept up in a herd-mentality-buying-frenzy when fundamentals are screaming the opposite, we still find ways to hurt ourselves.

You begin to avoid these outcomes with the help of two things: awareness and humility. Awareness is no more than the simple recognition that you’re inclined to hurt your portfolio. Humility is what enables you to accept that reality and seek a better way, which leads to our next layer...

**Diversify globally across stocks, bonds, and real assets:**
Self-explanatory and simple, so everyone does it, right? Unfortunately, no. The portfolios of most investors manifest an abundance of home country bias. This isn’t a uniquely-American phenomenon; it happens in every country around the globe. (We talk more about this in our free eBook *Global Asset Allocation.*

The problem is home country bias isn’t patriotic, it’s dangerous, and exposes your wealth to unnecessary risks. Just ask the Chinese and Russian investors who lost everything when their governments turned Communist last century. Or ask Japanese investors who saw their stock market go sideways for decades...

Of course, diversifying by geography isn’t the only challenge. The kind of robust portfolio that will help you sleep at night requires proper asset diversification as well. For instance, many investors are overweight in equities. That’s been great for the last nine years, but what about the next nine?

**Have a rules-based plan, rebalance accordingly:**

What’s going to happen when one of your assets drops 40%? What about when another outperforms and begins to dominate your portfolio-weighting? What if you inherit $500k? How will you put it to work? How will your allocations change as you approach retirement?

For most of us, portfolios aren’t a “set it and forget it” thing. They require a bit of maintenance. Fortunately, this doesn’t have to take up tons of time – a yearly checkup might be all that’s required. But the idea is simply to have an awareness of where you want your portfolio to take you, engineer it for that result, then establish regular diagnostics to make sure it’s accomplishing its purpose.

The question becomes “do you have a written-down plan?” (We covered this topic recently in our article "You Are Not Alone")

**Implement with low-cost funds and a low-cost brokerage:**

This is a wonderful time to be an investor. In the past several decades, we’ve seen investment costs gutted. Broker commissions used to cost hundreds or thousands of dollars per trade, depending on your investment size. Today, it’s a fraction of that. The advent of ETFs and other aggregated investment products gives investors exposure to broad asset classes that weren’t possible even 30 years ago. We have it easy compared to our parents and grandparents. Yet, too many investors are still paying far too much for no good reason. For instance, did you know there’s an S&P index fund that still charges over 2% while you could buy practically the same thing for just 0.05%?

And what about advisors? How much are you paying yours? Don’t misunderstand – many advisors are worth every penny charged. Yet others that do not offer value-added services outside of asset allocation, not so much. Unless right now – in this moment – you know exactly how much you’re paying your advisor, and you’re confident it’s a worthy expense, then there’s a chance you’re overpaying. (Here’s another old article on the topic "Would You Pay Your Advisor $1,000,000 In Fees?")

**Implement tax aware investing:**

One of the great final frontiers of investing is capturing the elusive “tax alpha” (or rather, reducing its injurious effects). Rob Arnott of Research Affiliates recently gave a wonderful presentation on the subject. One of the takeaways was the effect of taxes based on portfolio turnover, and how much alpha was required simply to breakeven due to this turnover. (Here’s another great piece from Morningstar on the subject.)
The Investment Pyramid

How often do we think about this? How often do we implement this reality into our aforementioned investment plans? Are your various investments domiciled in the right accounts – taxable versus tax-exempt? (This is another reason to never hold high yield dividend stocks in taxable accounts.)

Tilt away from market cap weights:

If you’ve followed me for any length of time, you’re likely aware of my preference for practically anything other than a market cap weighting. Why invest purely due to size? In my opinion, and that of many experts out there, tilting toward value, momentum, and trend will likely lead to far better long-term performance.

What’s your Pyramid?

I’m not claiming my Investment Pyramid is the Investment Pyramid. There are obviously a million ways to approach investing – and they’re probably as different from one another as the Paleo Diet is from the Mediterranean Diet. Heck, you could only have one layer of the Pyramid which is "Invest in Bank CDs" and that would be totally fine if it fits your needs.

But as our collective investing knowledge has compounded over the years, it has hopefully made all of us better investors than we’d otherwise be. Given this, whatever investment approach you choose today (and its associated pyramid) is still likely to share most of the same broad elements as mine, differing mostly in the specific weightings of those elements. That’s great, because as long as you get the big muscle movements of investing correct, the rest generally takes care of itself. In other words, thanks to those who have come before us, even the misguided investing pyramids of today hopefully put the broad pieces in place. We’ll check back in 50 more years – you know my allocation is the Trinity Portfolio but who knows – maybe crypto will be the new base...

The Personal Finance Pyramid

Now, to this point, we’ve focused purely on investing. But for many people, the impact of personal finance choices swamps that of investment choices in the short run (I am of the opinion that the vast majority of people should spend near zero time on their investments). In the long run, the power of compounding might take over the heavy lifting.

Indeed, in the average person’s Personal Finance Pyramid, an investment allocation would likely occupy only the highest levels of the Pyramid. On other words, only once you get your house in order do your investments come into play. That doesn’t mean these investing decisions aren’t worth considering, but for most, the basic day-to-day financial decisions make the most difference (and Vanguard agrees).

Below we examine what might be an effective Personal Finance Pyramid for most individuals.
Let’s quickly touch upon these as well.

**Fund an emergency account and pay down or eliminate high interest debt:**

At the bottom, we’re just trying to create a solid foundation – some emergency cash in the bank, and an escape from crippling debt payments. A recent article in Business Insider reported that Americans under age 35 have just $1,580 saved. What happens when someone runs a stop sign and plows into your car? If you break a few bones, that $1,580 (and more) vaporizes. Having enough money to cover emergencies is a critical first step.

With a few bucks in the bank, paying off your high interest debt is the next step. How are you supposed to build up your own reserves when all your money is going to your lenders? I’ve read Dave Ramsey recommend to his listeners that they should pay off smaller debt accounts first (rather than high interest accounts) in order to build momentum. By the numbers, choosing high interest accounts first is the smarter way to go, but if paying off smaller accounts is the behavioral trick needed to get moving, I’m all for it (he calls it the “snowball” approach). The most important takeaway is simply escaping any kind of toxic debt.

**Track expenses, set a budget, and save:**

This topic is personal finance 101 so I won’t spill tons of ink on it. First, know what you’re spending your money on right now. In order to do that, you have to track where your dollars are going. Once you make that decision, set a budget that makes saving money a priority. After all, if you’re spending everything you make on basic day-to-day living, where will the dollars you’ll need come from when it comes time to fund the other layers of the pyramid?
Max out retirement and tax-exempt investment accounts:

A 401k employer match is free money. To the extent you can, fund up to the match limit to take advantage of this great perk. Plus, allocating to your retirement plan maximizes the ability of your investing dollars to compound for you.

This advice might seem obvious, but two-thirds of Americans aren’t saving any money in a 401k. And Vanguard claims that just 4% of people earning below $50k max out their 401k. For people earnings between $50k-$100k, that number climbs to just 11%.

Buy a home if reasonable:

For years, the common belief was purchasing a home was the ultimate investment. It might be the ultimate emotional investment, but the numbers don’t support the first takeaway.

Elroy Dimson (who we just had on our podcast) in conjunction with Paul Marsh, Mike Staunton, and Credit Suisse, recently came out with the Global Investment Yearbook 2018. This edition includes new data on global residential real estate, with some sobering statistics.

First, as many of us remember all too well, in the U.S., house prices fell by more than 36% in real terms between 2005 and 2012. Certainly, a tough drawdown for anyone who had been cash-poor-house-rich during that time.

But what about longer-term appreciation? Isn’t your home a great wealth-generator in the long-term? On average, no. The chart below shows the average long-term yearly returns after inflation from residential real estate between 1900 and 2017 – just 1.3%. And notice where the U.S. comes in...
Now, there are many reasons why investing in a home might make sense. But assuming "great investment decision" is one of them could be sorely misinformed.

**Address investments:**

Finally, and only finally, do your actual investment decisions come into play. Think about that – the entire Pyramid at the onset of this paper only occupies the top level of this new, Personal Finance Pyramid. Yet so many of us spend tons of time languishing over those market decisions. As I’ve said before, I don’t believe this is the best use of your time or mental energies.

**Wrapping up:**

So, how do your Investment and Personal Finance Pyramids look? Do you have one?

Full disclosure, this article has been a camouflaged way of hitting an important point I’ve made many times, yet from a new angle – the critical importance of having a deliberate plan for your money, whether investing money or personal finance money.

It could be a formally written-down investment plan, or a goofy, personal finance pyramid graphic, but the takeaway is the same: Where are your dollars going, in what order, and why? It aligns with the old saying, “show me your calendar and your checkbook, and I’ll show you what you really value.”

So many of us are flying blind out there. But by taking a few extra minutes to write down your own plan of attack, it doesn’t have to be you.