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How to Get Rich -- Safely

Inc.'s finance editor and other financial planners explain why your company should not be your only investment.

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Personal Portfolio

Your company may well be your best bet for building wealth. But don't make it your only one

Would you fly to las Vegas and bet your net worth on a single number? Of course not. Then why keep all or most of your assets tied up in just one investment--especially one as illiquid and risky as an entrepreneurial company? That kind of boom-or-bust mentality can sabotage your long-term financial future. As a business owner, you're better off diversifying into other investments as soon as possible--if you haven't already.

CASH RESERVES: Here's a good place to begin. Every family needs an emergency nest egg. And when you own a business with unpredictable cash needs, that account might just turn into a life--and company--preserver. To make certain that the cash is available when you need it, invest in safe, liquid investments: short-term bank certificates of deposit or a money-market account.

How much do you need in your emergency account? For most people, financial advisers typically recommend including enough to cover three to six months' worth of living expenses. But business owners may need more, especially if they lack the protective cushion that comes from a top-of-the-line disability policy. (That's the kind with a short waiting period, a high reimbursement level, and a favorable definition of qualifying conditions.) Jody Tallal, whose financial-planning firm, Life-Plan, is based in Dallas, argues that business owners need to set aside substantially more than the rest of the population. "Unless your company has many different income streams that seem very safe, I'd set aside enough to cover three to six months' worth of corporate, as well as personal, expenses," Tallal advises. (There's no problem with commingling funds, since all the cash represents personal savings. But it will be there if you need to provide a loan to your company.)

MUTUAL FUNDS: Mutual funds provide another great way for entrepreneurs to start spreading risk, since investors can take small steps, diversify quickly, and rely on the advice of seasoned portfolio managers. With thousands of mutual funds to choose from, there are successful funds aimed at every niche of stock and bond markets. Still, entrepreneurs with an itch to invest should consider other options, too.

BONDS: For a moment, think about your company dispassionately--in pure investment terms. "It's a growth asset," says Harold Evensky, a fee-only financial planner in Coral Gables, Fla. "When you want to diversify, you might want to move into income-producing investments, which will complement your company's growth potential. They'll also protect you by guaranteeing some income if your company experiences a downturn."

To Evensky, the income-producing investments that make the best sense are bonds, especially municipal bonds. His recommendation: buy bonds until your bond portfolio reaches up to 50% of the value of your investment in your company. It's important to diversify your bond holdings, too, through different bond-maturity levels, types of issuers, and geographic regions. Stick to double- or triple-A ratings, Evensky advises.

REAL ESTATE: Let's set home ownership aside. It may no longer be an investment gold mine, but people buy their own homes for plenty of reasons other than future profits. However, other real estate investments may make sense from a strictly financial vantage point.

Often, an entrepreneur purchases a building and leases it to his or her company. There are plenty of risks to that strategy. "If your company runs into financial problems, the first bill it's not going to pay is rent to the owner--so you haven't really diversified your investment risks at all," explains Elaine Bedel, a fee-only financial planner in Indianapolis. She adds that playing landlord to your company may well make sense from a business standpoint, but you shouldn't consider it a form of diversification. To diversify, you need to lease your commercial space to some other company.

Another real estate play that might make sense is to buy a vacation home in an area you may retire to--and rent the house out in the meantime. "That could be a good way of generating income and planning for retirement--while your investment produces tax benefits and, hopefully, grows in value," advises Jean Shamo, a financial planner in Hilton Head, S.C.

INDIVIDUAL STOCKS: What about the business owner who wants to rely on his or her own stock-market instincts rather than those of a mutual-fund manager? "Business owners do not have time in their day to manage a stock portfolio," is Tallal's blunt response.

Unless you're the exception, don't throw yourself whole hog into following stocks while trying to grow your business. However, you might be able to dabble in a handful of well-chosen stock plays. The big question: should you stick to your own industry? "I've seen it work beautifully," says Roy Ballentine, a fee-only financial planner in Wolfeboro, N.H. "You probably don't want to invest in a competitor, but you've probably got very good knowledge of an industry and can target some great investment plays. Maybe you'd even want to invest in one of your suppliers or customers."

But there's plenty of debate about the issue. "I tell business owners to stay away from investments that parallel their own company, and that includes stocks within their own or related industries," says Evensky. "A better strategy is to talk to friends who own businesses in other industries and trade suggestions about good potential investments. That way, you all get a chance to diversify." It's your call.

RETIREMENT SAVINGS: Remember O.J. Simpson, advises D.J. Shah, a financial planner in Weston, Mass. "He's able to protect several million dollars from the court judgment because it's in retirement savings," Shah notes. His suggestion: consider starting a qualified pension or profit-sharing plan at your company. A retirement plan will benefit both you and your employees, and you can design it to accommodate different kinds of investments.

Pitfalls
The Wrong Way to Diversify

If you're trying to diversify your holdings, don't kid yourself. You want to spread your risks, not increase them. So take a pass on any diversification strategies that involve the following:

Art or other collectibles. Indulging your passions can be fun, but don't confuse that with an investment strategy. Besides their risk of losing value, investments like these are much too illiquid for those who might need to raise cash in a hurry if their companies demand it.

High-risk, high-glitz investments in general. They're just too dicey for all but extremely established (and already diversified) company builders. Be wary of things like oil-and-gas partnerships unless you're in the business. "I have watched clients put several million dollars into these and have never seen anyone who's not an oilman make any money," one planner confides.

Jill Andresky Fraser is Inc.*'s finance editor.*

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