Protection First!

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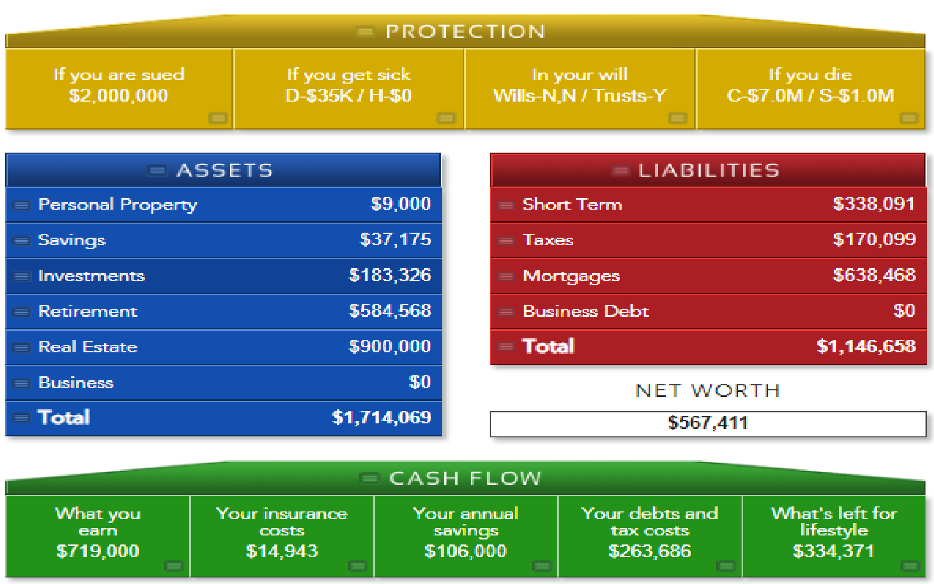
When engineering a sustainable wealth building financial strategy, there are many factors that one must consider, but for simplicity let's break it down into two areas I identify as "Phase 1" and "Phase 2". In Phase 1, the focus should be on building solid Protection, building liquidity, becoming a world class saver, and reducing debt. Notice the order…Protection first! That's right, I said it, PROTECTION FIRST! In Phase 2, we focus on Exit Strategy. Let's save Exit Strategy for another article. For now, let us zoom in on how to build an efficient Phase 1.

You can focus all you want on reducing debt, building wealth, investing in the stock market, buying houses, etc. However, if you have not given attention to maximizing your protection component first, it's like driving a car without a seatbelt. Everyone wants to get to the destination of "retirement", however the most common mistake I see in Phase 1 of anyone's so called financial plan, is lack of proper protection.

In my strategy meetings with clients, we work with a financial model. This model helps in making financial decisions much easier as it coordinates all the components of one's financial world. This allows for holistic financial choices based on fact, not opinion. As I have said many times before, most people make financial decision based on the opinions of others. The model allows for clarity as we can stress test how one micro financial decision affects other areas of your model. This is because when you work with a model you quickly learn that no financial decision stands alone, but rather our many micro-financial choices are all part of a much bigger macro-economic plan. If you have read some of my previous articles, you know by now that this financial model consists of 4 domains. These domains are Protection, Assets, Liabilities and Cash flow.

If you take notice to the image below, this is a good example of a well-balanced financial model. Try not to focus on the dollar amounts, (everyone's model is different because we all make different incomes, have different levels of assets, debt, etc) but rather take notice to the protection component. It is what I like to call "maxed out".



What is very common in most clients I coach towards optimal Financial Balance®, is that they are grossly under insured. Mainly due to lack of education about proper protection amounts by their advisors, but partly because of cost. Most have a preconceived notion that the higher the protection, the higher the cost. Let me ask a question, if cost was not an issue, how much protection would you want? Most people would say “As much as I can get”. Now let me ask another question…If you knew you were going to have a fire in your house tomorrow, get into a car accident, or even worse pass away, how much insurance would you want? When asked that way, you might now think “to replace the value of loss”. That is exactly the correct answer. You see, you cannot insure a $50k automobile for $100k. You cannot insure a $15k diamond engagement ring for $25k and you cannot insure your $500k house for $1,000,000. The definition of insurance is full replacement value. However, over 95% of the time, when I gather information from clients to build their personal financial model, we discover major lack of protection. Specifically, in liability insurance, disability insurance, wills, trusts and life insurance.

If you really take notice to that model image I referenced earlier in this article, you will see some correlation between income (bottom left green box) and death benefit for example (top right yellow box). Most people have never thought about there being a correlation between these areas. Let’s dive deeper with an easier example first. If you had a fire in your house, and the entire house burnt down, you would hope you would receive a check from your insurance company equal to the “replacement value” of that house. In other words, what would it cost to build the same “like” quality house in today’s dollars? Most likely it would cost more than when you purchased it because building materials, and construction labor costs to rebuild tend to rise over time. So, it is important to make sure that area of your protection component is always up to date. Be mindful of your “replacement costs” on your homeowner’s policy.

Now let’s relate this concept to death benefit. As I stated earlier, there is a direct correlation on that referenced model between income and death benefit. This is an area that is a major flaw in most people’s planning. Remember, insurance is “full replacement value”. If you are 40 years old, making $100k a year, perhaps married with two children, your “expected” to work another 25 years. If god forbid death occurred unexpectedly at age 40, what would be the Human Life Value of that person’s earnings potential? I can tell you its much more than $500k. Its more than $1,00,000. You see, we all have a economic value, and most often that value is not even close to being properly protected. Have you guessed the answer yet? This persons Human Life Value (the amount of death benefit on a life insurance policy that an insurance company would be willing to insure) is over $2,500,000, and arguably higher if you consider that income might rise over time. This is no different than ensuring a ring, or art, or a house, a boat or a car for its replacement value. The difference here is that boats and cars are not human beings. They cannot work, produce, be a father, a mother, a brother or a sister. Material items are replaceable. Its so much harder to replace what a human contributes to a family, or to friendships. Its hard to replace a father or mother. However, putting the proper amount of protection in place can ensure that life goes on uninterrupted. That no financial stress will exist and that future weddings can be paid, or education costs. This can ensure that a widow who might not work because she is a stay at home mom can continue to be home to support her children financially.

What if you could approach this without the word “cost” as the issue. You see, cost is only an issue in the absence of value. Once value is understood, cost is never an issue. By thinking holistically, and planning with a model, you can accomplish maximum protection in all areas of your life. This is because when you focus on strategy first, you find the dollars to make this work. I often find that people make financial decisions backwards. This might be because they are listening to so called financial gurus on tv or the radio who don’t even hold the proper licenses to warrant giving financial advice. Or maybe because they are to focused on paying down debt, when there exists major holes in their model that need to be addressed first. You don’t put your underwear on before your pants, right? Of course not! There is a proper order in the way we get dressed!

It is no different in engineering a well-designed and balanced financial life. I encourage you to think Protection first!

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I am the president and founder of *Statera Wealth Solutions, Inc*. We focus on sustainable wealth building solutions for those who want to grow and protect their wealth. Our modern perspective challenges outdated conventional financial wisdom, awarding our clients improved financial wellness and less financial stress.