Money Matters: Investors, don’t be your own worst enemy

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As financial professionals, we find ourselves quite often thinking “Help us, Help you!” a la Jerry Maguire.

I sometimes joke that, as a financial professional, a psychology degree might be better suited over a masters in business. Having worked with great clients over the years, I’ve become increasingly aware of investor behavior and its impact on their financial decisions. The Dot-com Bubble of the late ‘90s and the Financial Crisis in 2008-9 are just a few events that have strengthened innate human behaviors and biases. It is important that you understand the impact they will have on the decisions you make with your investments.

Many investors have biases, which can trigger emotional reactions to market movements and misinformation; resulting in potentially, self-defeating, and counter-productive behaviors. Without a disciplined methodology to counter-balance these biases and emotional reactions, the investment performance will reflect this through lower returns, missed opportunities and potentially a complete loss. Investors, despite their clear motivation to make wise investment choices, can unknowingly be their own worst enemies.

Investors routinely make a series of fundamental mistakes without seeking the help of a finance professional. I have seen mistakes such as investing too simply, fear of losses compelling investors to get out of the market and move to cash, not seeing the big picture, and being excessively confident in their own abilities in trying to “beat” the market.

A common oversight is what is called “Home Bias.” This is simply a bias towards investing in the country in which you reside. The things that are familiar to us are more likely to be a natural part of our comfort zone. US based investors tend to be limited by this bias more than the European

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It is beneficial for client's to stay off the proverbial emotional bandwagon or roller coaster. Warren Buffett says that the key to investment success is to "be "greedy when others are fearful and fearful when other are greedy."

I have seen first hand that adhering to this mindset isn't intuitive for clients, and in all actuality investor's natural reaction is quite the opposite. Most investors buy high, lured in by the emotional sentiment tied to an investment that is increasing, and sell at a loss, when the market is down. As a result further declines ensue; adding to the emotional panic that accompanies such circumstances. Scientific studies have shown people perceive gains and losses differently. These studies have shown and emotional pain of a loss is 2X longer-lasting than a gain. This tendency is constantly running in the background and may cause people to make different decisions than what they might otherwise make.

I'm sure you have heard the adage "patience is a virtue." The two most ignored virtues in investing are patience and discipline. I have witnessed people trying "to make up for lost ground" with investments, because the investment discipline was broken. I've also observed people behaving in a similar fashion and making the same mistakes repeatedly, because of the belief that "this time" will be different. This does not allow for investments to have time to work for you and allowing the effect of compounding to happen. Remember Albert Einstein's quote: "Compound interest is the eighth wonder of the world. He who understands it, earns it ... he who doesn't ... pays it." This becomes a vicious cycle of self-destructive behavior.

It is key to be aware of these tendencies and their impact. When making potentially life-altering decisions, a certain level of emotion can undermine, or blur our decision making process. Working with a neutral unemotional third party, an advisor, may help aid in making better financial decisions, not to mention providing a reality check in "Helping us, Help you."

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