

BEHAVIORAL & FINANCIAL INSIGHTS

Emotional Investing, Like Emotional Eating, Can Be Hazardous to Your Health

Buy Low, Sell High

Every investor wants to buy low and sell high, yet it is so much easier to sell low and buy high; it just feels right at the time – to simply do what everyone else is doing. Very few investors have the discipline to buy low or sell high because it is contrary to how we feel.

Would you rather purchase a basket of stocks with an average P/E (price to earnings) of 13 or 30? Well, if you want to buy low, then 13 would be your answer. Yet, 10 years ago, in March of 2009 when the market had a P/E of 13, no one wanted to touch stocks. Why would they? The expectation was that what had gone down significantly during the financial crisis was sure to continue going down a lot more.

Yet when the P/E has been at 30 (remember dot com mania at the turn of the century?) investors couldn't seem to get enough of stocks¹. We often allow feelings, which can be both fleeting and unstable, to drive our investment decisions.

Keeping it Cognitive

One of the best ways to keep emotions at bay is to ask reflective questions. An honest assessment can often rein in and stabilize emotions (less giddy during good times, less fearful during bad times), and empower you to make more level-headed and thoughtful decisions.

Questioning valuation, investors sentiment, earnings, etc... can engage the thinking brain (which forces emotions out) and can give us a chance to analyze the situation. We are then better prepared to calculate the actual risk, rather than rely on our emotionally skewed *perception of risk*.

The Takeaway – Know Thyself..., Beware of Emotional Investing

Our perception of risk is highly fluid – it's based on our mood, frame of reference and expectations, and influenced by the constant onslaught of the media and their headlines designed specifically to elicit emotion. As a result, we tend to perceive less risk when times are good and overestimate risk when times are bad.

We are all influenced by emotions, especially with respect to our own money. That's just part of being human. As your advisor, one of my primary roles is to help you remain disciplined – to keep you on track with your plan, focused on your goals and objectives. Together, we will think things through and ensure decisions are based on sound judgement, not on how we feel.

¹ P/E calculations based on the S&P 500 Index. The Standard & Poor's 500 index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. All indices are unmanaged and may not be invested in directly.