"Why So Many Investors Fail"

Over the last 30 years, individual equity investors averaged a paltry 3.79% annual return, while the S&P 500 Index* averaged over 11% during the same period (Dalbar, Inc. financial research firm). Such returns for the average investor are woefully short of the 8% -12% most of us plan on . . . if we plan at all. How can this be? *Why is there such* a *huge difference between the investment and the investor?* Why do most of us make such a botch of this?

- **What Goes Up:** Markets *always* go down at some point. When investors believe investments are stable and safe they buy them, the markets go up, and they buy more. As buying continues, investments get expensive, and when they get expensive investors get wary . . . and wary investors are likely to jump ship at the first whiff of uncertainty. And the markets go down. It's a cycle that's been repeated for over 100 years (Hyman Minsky, economist), and smart investors understand this natural cycle.
- **It's in Your Head:** Three primary causes for underperformance are that people don't have the money to invest regularly, they need the money for purposes other than investing, and overwhelmingly they underperform because of psychological reasons/bad decision-making (Lance Roberts, Advisor Perspectives).
- **You Just Raised the Price? Sure, I'll Buy:** According to investment research firm FactSet, there is a powerful correlation between the rise in the stock market and increase in investor buying of equities (since 1996). We buy more when things are most expensive. And the same powerful correlation holds for selling . . . we bail out when things are near the bottom ("on sale").
- **As Ben Says:** In a recent interview, Ben Bernanke stated that the "Fed" was aware that there was a housing bubble in 2007 . . . but what they didn't anticipate was the herd mentality and irrational behavior of investors whose selling drove the markets far lower than could be rationally explained. Investors play follow the leader sending markets higher than they ought to go because it seems everyone is buying and we don't want to be left behind . . . and we sell when everyone seems to be getting scared.
- **What, Me Worry?** Those are the immortal words of Alfred E. Newman of Mad Magazine. For most investors, the answer is "Yes! I do worry". Study after study has shown that the sting of loss is about twice as powerful an emotion as the thrill of winning. And so, many investors are likely to bail out of investments when they can't stomach a "temporary" loss, thereby missing the inevitable (historically speaking) upswing.

- **Did We Already Say It's in Your Head:** Behavioral economists talk about humans being of two minds (Kahneman and Klein). The intuitive mind helps us make rapid judgments common to daily life. It's not the best for making long term financial decisions, however. We're far better at financial choices when we employ the reflective mind, which is more reasoned and methodical. Too often though, when faced with alarming news, our intuitive output can be so powerful as to override our rational tendencies. Investors can get jittery, fearful, and latch onto relatively meaningless or even erroneous information and make poor decisions that cost them.
- **We Forget History:** Good investors know their history. They remember that there have been hard – and harder- times before, and that markets are resilient. Since 1926, there have been 65 up years for the S&P 500 and just 24 down years; only 6 times was the market down 20% or more, but a whopping *33 occasions when the market topped a 20% gain*. There were only 4 occasions when a negative year was followed by another negative year (Lord Abbett). So . . . why worry?

We're not stupid, we investors. Most of us understand the benefits of diversifying, of not trying to time the markets, of sticking to a plan and being disciplined. But somewhere along the path many of us stray, we think the challenges are different now, that our strategies don't work anymore, or we're not getting where we want to go fast enough. And we blow it. Through our own behavior, we give up over 65% of the gains of the market, barely beating inflation. It's hard to get ahead that way.

Maybe having a professional to get you over these humps is the smart choice. Why not give us a call.

We can be reached at 615-777-2125.
Back issues of our Commentary may be found at www.premiercares.net