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Horsetooth Financial Outlook

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7 Psychological Traps That Make You a Worse Investor

Sometimes when it comes to investing, volatile markets aren't your worst enemy. It's actually you. That's because money and logic don't always go hand in hand. Unfortunately, our brain often plays tricks on us, causing even the savviest of investors to make decisions that don't really make a lot of sense, from panic selling to ignoring opportunities.

In fact, the problem of psychological investing traps is so pervasive, there's a whole field dedicated to studying it called behavioral finance. Researchers in this discipline look at the way psychology affects how we make financial decisions, and some of what they've discovered is pretty interesting. Knowing about these traps can help you avoid them and make you a better investor.

Here are seven psychological traps to keep in mind.

Sunk Cost Bias

The sunk cost bias has to do with the all-too-common tendency to stick with something, whether a bad boyfriend or bad investment, long after it's clear that it's not worth it anymore. Still, because you've invested a certain amount of time or money, you're reluctant to give it up. In investing, you might end up hanging on to a stock long after you should sell it in the vain hope that you'll eventually come out ahead. But in these cases, it's better to cut your losses rather than to hang on to a loser.

Familiarity Bias

Most of us are biased toward those things that are familiar to us. We head to restaurants we've been to before and follow the same roads to work, because we know what to expect. With investing, familiarity bias involves favoring investments that are familiar to you. You might

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10 Ways to Boost Savings

By embracing some simple lifestyle changes or taking full advantage of savings incentives, you can easily boost the amount of cash you save. Here are some ideas to get you started.

- **Take advantage of savings perks:** If you contribute pretax earnings to a 401(k) plan or IRA, you're saving money beyond your actual contribution amounts. Another way to save? Make sure you're contributing enough to get your employer match, since this is a great way to increase your savings without actually shrinking your take-home pay.
- **Get your benefits:** Your employer may offer benefits beyond a 401(k) plan that could save you money. Flexible spending accounts are common benefits that allow you to set aside pretax income for out-of-pocket medical expenses. Make sure to review all benefits and take advantage of all that apply to you.
- **Cut recurring expenses:** Monthly subscription boxes, streaming entertainment services, gym memberships you don't use — these regular costs can add up. While some may be worthwhile, trimming the fat in the area of recurring expenses can help you save more.
- **Buy generic:** Do you always buy the name-brand version of a product? If so, you might be wasting money. In many cases, the generic version is just as good — if not

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7 Psychological

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prefer to invest in the company you work for or big-name businesses that are in the news. This could cause you to overlook important opportunities you don't know that much about.

Anchoring

Anchoring is the process of getting attached to a particular reference point — such as the price you paid for a stock — and using that to guide future decisions. Or you might fixate on a stock's previous high, even though that price was an anomaly. Anchoring is why you think you got a great deal when buying a $60,000 car for $50,000, even though the car is really worth closer to $40,000.

Whether you are buying stocks or cars, anchoring involves using a single piece of information to determine what the item should be worth while also discounting more relevant information, such as a company's fundamentals or broader economic trends. Unfortunately, avoiding anchoring is difficult, but considering all available information before choosing an investment can help.

Focusing Too Much on the Recent Past

Recency bias is the tendency to make decisions or judgments based on information that's relatively new or recent. For example, during times when the market is up, people may ignore or discount the possibility of a market decline. Or, if a certain category of stocks has done poorly recently, people may conclude that those stocks *always* have negative returns, even if the dip is an anomaly. As with other psychological investing, you can avoid this one by doing your best to consider the entire universe of information at your fingertips, not just what happened yesterday.

Following the Herd

While following trends might be fine for fashionistas, it's not always a smart investing move. Yet herd investing is an all-too-easy trap to fall into. If everyone is telling you that now's the time to get into a certain hot investment, you may feel you need to act fast so you don't miss out. But just because something is popular doesn't make it a good investment. Blindly following the herd without first consulting your own financial goals and plan doesn't make you a smart investor.

Overconfidence

Most of us like to think we're smarter than the average person, but when it comes to investing, you're probably not. Yet if you hit it big with a certain investment, you may attribute that success to your skill rather than what it really is — luck. That can cause you to repeat the same way of thinking.

Panic

Investing isn't for the faint of heart. When the market takes a sudden dip it's easy to panic, which can lead you to make bad decisions, such as selling at a big loss, rather than riding out the natural hills and valleys of investing. Making these emotionally driven choices can cost you a lot of money. When making investing decisions, make sure they're based on evidence, not your initial gut reaction to the day's events.

Avoiding psychological investing traps on your own can be difficult. Please call if you would like to discuss this in more detail. ❍❍❍

Do You Really Need 70%?

A general retirement planning rule of thumb indicates that you'll need 70% to 80% of your preretirement income. When you realize how much you need to save, it's tempting to question whether you really need 70% of your preretirement income.

First, you should prepare a detailed analysis of your expected expenses after retirement. How much you will need depends in large part on how you plan to spend your retirement years.

How can you help ensure that your expenses will be lower? Consider these tips:

- ❍ **Pay off your mortgage.** Mortgage payments often consume 30% or more of an individual's gross income. Eliminating this expense can drastically reduce income needed for retirement. If you can't pay off your mortgage, consider selling your home and purchasing a smaller one.
- ❍ **Get rid of other debts.** It's not unusual for consumer debt payments to equal 10% to 20% of an individual's take-home pay. Try to enter retirement debt free.
- ❍ **Keep your automobile.** Instead of purchasing a new car every couple of years, keep your current car for as long as it's in good working order.
- ❍ **Look for ways to reduce travel and leisure expenses.** Look for and use senior discounts. Plan activities for nonpeak times, when rates may be lower.
- ❍ **Consider relocating.** The cost of living varies significantly from city to city and state to state. You may be able to reduce your living expenses substantially by moving to another locale. However, you also need to decide whether you want to move away from family, friends, and familiar surroundings.
- ❍ **Work at least part-time.** If you still don't have sufficient funds to support yourself during retirement, consider working at least part-time. Even a small amount of annual earnings can help significantly in funding your retirement. ❍❍❍

10 Ways

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identical to — the pricey, branded version.

- **Make it automatic**: Not sure where your money goes each month? Automate your savings so you don't have to think about setting aside extra cash. Chances are you won't even miss that money.
- **Be generous:** If you itemize your taxes, make sure you're keeping track of all charitable donations — from checks you write to the value of that box of gently used clothes you just dropped off at Goodwill.
- **Cut one habit**: Do you indulge in daily soda or an expensive coffee drink? Cut the habit (or, if that's too hard, limit it to two or three times a week). Set aside the money you would have spent.
- **Repair, don't replace:** It's easy to toss a slightly worn or damaged item and buy a new one to replace it. But many of the items we throw out can actually be repaired. Find a skilled shoe repair person, quality tailor, experienced upholsterer and furniture repair person, and other professionals to spruce up items that need a bit of repair. By purchasing quality items and taking good care of them, you'll likely save yourself money in the end.
- **Use coupons:** Clipping coupons may seem distinctly old-school. Fortunately, you can now take advantage of coupon savings without having to spend an entire Sunday morning sorting through newspaper inserts. When shopping online, always do a quick search for online promo codes and coupons before hitting buy. Or sign up for your favorite grocery store's rewards program.
- **Review your insurance premiums:** Raising deductibles or bundling policies could save you money. Also, make sure you actually need the insurance you have. Finally, make sure you're getting all the discounts you qualify for, like car insurance premium reductions for being a safe driver or homeowners insurance discounts for having an alarm system.

Please call for help analyzing your budget and identifying ways to cut your expenses and save more of what you earn. ❍❍❍

Reevaluate Your Portfolio

Periodically, you should thoroughly review your portfolio. Follow these steps during that review:

Review your current portfolio mix. List the current value of all your investments. Determine what percentage of your portfolio is held in stocks, bonds, cash, and other investments; but don't stop there. Take a closer look at where the stock portion of your portfolio is invested.

Analyze each investment. Determine whether it still makes sense to own each investment. Review why you purchased each investment and whether those reasons are still valid. Emotionally, it is difficult to sell an investment at a loss, but holding on until you get back to breakeven may not be the best strategy. You may want to sell the investment and reinvest in another with better prospects.

Determine if changes are needed to your current allocation. Look to broadly diversify your portfolio. Some points to consider include:

- **Decide how much to allocate to stocks and bonds.** Your stock and bond mix is a major factor in determining your expected portfolio return and how much your portfolio will fluctuate. Make this decision based on your financial goals, risk tolerance, and time horizon for investing. If you are investing for the long term, say 10 years or more, you probably still want a major portion of your investments allocated to stocks.
- **Reassess your stock allocation.** Is your stock portfolio too heavily weighted in technology or blue-chip stocks? Have you selected only growth stocks, ignoring value stocks? The stock market moves in cycles, with varying sectors outperforming other sectors at different times. Since no one can predict when one sector will outperform, it is typically best to broadly diversify your stocks.

Move your allocation closer to your desired allocation. When making changes, first consider the tax ramifications of the transactions. If you can make changes without incurring tax liabilities, you may want to make the changes immediately. But if substantial tax liabilities will be incurred, look for other ways to get your portfolio closer to your desired allocation. For instance, any new investments should be made in areas that are underweighted in your portfolio. Or you may be able to reallocate in your tax-deferred accounts, such as individual retirement accounts and 401(k) plans, where you typically won't incur tax liabilities. However, if you can't get your allocation in line within a year using these approaches, you might want to sell some of the poor performers and reinvest the proceeds. ❍❍❍

Financial Data

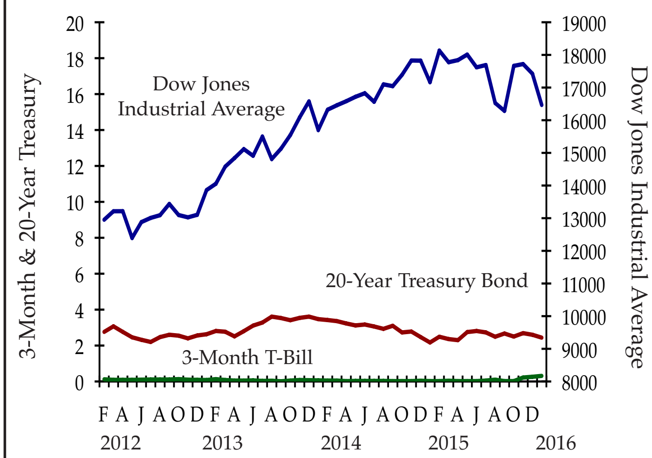
Indicator	Nov-15	Dec-15	Jan-16	Dec-14	Jan-15
	Month-end				
Prime rate	3.25	3.50	3.50	3.25	3.25
Money market rate	0.28	0.27	0.27	0.43	0.42
3-month T-bill yield	0.22	0.26	0.31	0.04	0.02
20-year T-bond yield	2.69	2.60	2.44	2.47	2.17
Dow Jones Corp.	3.37	3.43	3.40	3.08	2.71
30-year fixed mortgage	3.54	3.58	3.25	3.47	3.14
GDP (adj. annual rate)#	+3.90	+2.00	+0.70	+2.20	+2.20

	Month-end			% Change	
Indicator	Nov-15	Dec-15	Jan-16	YTD	12 Mon.
Dow Jones Industrials	17719.92	17425.03	16466.30	-5.5%	-4.1%
Standard & Poor's 500	2080.41	2043.94	1940.24	-5.1%	-2.7%
Nasdaq Composite	5108.67	5007.41	4613.95	-7.9%	-0.5%
Gold	1061.90	1062.25	1111.80	4.7%	-11.8%
Consumer price index@	237.80	237.30	236.50	-0.3%	0.7%
Unemployment rate@	5.00	5.00	5.00	0.0%	-10.7%
Index of leading ind.@	124.10	123.90	123.70	-0.7%	2.4%

— 2nd, 3rd, 4th quarter @ — Oct, Nov, Dec Sources: *Barron's, Wall Street Journal*

4-Year Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

February 2012 to January 2016



Past performance is not a guarantee of future results.

2016 — The Issues and The Election

As we head out of the snowy winter of the West and the East and into the seasons of green this spring, there are many events and variables that will affect the outcome of the economic landscape in 2016.

1. **The Election –** In my lifetime and experience as an investment and estate planning advisor, this is the most unusual and interesting presidential election I have witnessed. It is also one of our most important in history.

Having slowly recovered from the fiscal debacle of 2008 in which our banking system was run to ruin by political folly, we are now in a position to move forward with a plan to stimulate business, job formation, and employment for future generations. We also need to have an immediate financial plan to resolve the obvious shortfalls in Medicare and Social Security, and perhaps most importantly, get the electorate back in control of our country. With financial accountability and attention to our constitutional and personal rights, we are in a great position to continue to dominate in world affairs.

The question is, who will be directing that plan and who will be able to unite Congress in the actions that are necessary to uphold our constitutional rights?

The field of candidates runs from traditional family, independents, lifetime politicos, young, old, and even left-wing socialists. There has never been a larger field of candidates to choose from. This is both good and an indication that the existing policies and direction of the country need to change. One thing is certain, we definitely cannot afford an administration that does not recognize the importance of fiscal responsibility. In the past eight years, the national debt has doubled.

This election will have an immense importance regarding the next four years for client investments and personal rights.

We truly live in the greatest nation of the world, where exercising the right to free speech affects the world in which we live daily.

2. **Currencies –** For almost two years, the developing markets, Europe, Brazil, and China have been in turmoil.

Without financially trained and astute elected officials, the U.S. faces huge challenges in the future in managing currency valuations relating to trade agreements and to ensure that businesses want to come to the U.S. to establish residency. The long- and short-term consequence of managing that currency risk is essential for American businesses to be profitable and incentivized to invest and employ more Americans.

3. **Interest Rates –** The Fed needs to be consistent and hopefully becomes a much less-important ingredient in the daily financial news.

It is hard to believe that any organization or educated person can truly take seriously the incessant worry that raising interest rates by ¼ point makes a difference. As interest rates rise slightly and the Fed finally ceases to intervene, the stock market, real estate market, and competitive financing rates the banks and individuals live by should be a good long-term policy.

4. **China –** Has emerged as the most dynamic growth market in our lifetime, but will continue to be volatile as it battles between the benefits of capitalism and the restrictions of communism.

As China's stock market levels out over the course of this year, they should emerge again with fresh energy, a massive population eager to be a consumer society, and are already the most important business partner of Europe in many ways. They will need to provide more transparency with their debt.

5. **Defense Strategies –** Since the late 1980s, the U.S. economic engine has continued to drive ingenuity for defense products, aircraft, and technologies. We need to remain strong defensively to command a strong negotiating position in all areas, both economic and geopolitically. We are currently failing miserably in this respect.

The rise of radical organizations like ISIS, AI Qaeda, Boko Haram, and the Taliban demonstrate that there is a need to maintain aggressive resistance, educate affected countries in how to defend themselves, and for our military efforts to be successful with every passing day. Most of all, we need a definitive plan with well-communicated policies to succeed.

6. **Oil and Gas –** Not since the 1970s when the oil embargo occurred have we seen a more radical occurrence in energy economics. As the high cost producers slowly disappear, the stability of the oil and gas market should coincide with improving economies around the world.

I'd be lying though, if I didn't tell you that $1.49/gallon for diesel makes me smile.