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CLASSIC INVESTMENT MISTAKES

There are several mistakes that most investors make almost intuitively. I am so convinced of this that I am tempted to go so far as to say that successful investors almost always go against their instincts. Thus behavior modification or mistake prevention is 50% of the road one must navigate properly in order to arrive safely at their destination. (The other 50% is having a written plan.) Here are some classic investor mistakes:

Panic and Euphoria. These diametrically opposed concepts are commonly seen in the lives of investors. Current events are almost always the culprit from which these evil investment twins are born. The exacerbation of these events by the news media trying to sell advertising contributes to the problem. Emotion can be a powerful motivator to enable the accomplishment of many great endeavors. However, emotion can also become a detriment to making clear headed decisions that should be made based on data and empirical evidence. We all have made hasty decisions in all aspects of our lives which turned sour because we made them while on an emotional high or low. This same phenomenon can affect our judgment in the investment arena and furthermore cost us a lot of money.

Speculating vs. Investing. There is a difference. Most investors deem speculation the same as investing. The *American Heritage Dictionary* defines *investing* as "acquiring property for future income" and *speculating* as "engaging in risky business transactions on the chance of great profit." Which would you rather stake your retirement claim on? To be more descriptive, picking individual stocks and timing the market are speculating techniques. Buying into the miracle called capitalism via broad and deep asset classes is called investing. Do not be fooled into playing Wall Street's speculation game – because rest assured the "house always wins."

Bonds vs. Stocks. Many investors – especially in turbulent stock markets - head to bonds for "safety." The imminently wise Nick Murray explains that once one understands the relationship between money and purchasing power, then it all falls into place. What does that mean? Most investors that "go to bonds" are trying to be *conserv*ative." In other words, they are trying to *conserve* their money. However, the investment that conserves purchasing power – not just principle, is the truly conservative investment. You see, conserving purchasing power conserves principle *and* future growth. Bonds do not do this (and never will.) Only stocks in the long run will accomplish this mission. Thus, stocks are more *conserv*ative, not bonds. I know this is a paradigm shift for most. But it is an essential one for those that are serious about being successful investors. (I might add that the next 20 to 30% drop in a market is most likely to occur in the bond market – not the stock market.)

Underdiversification. One can get rich by underdiversifying, but one cannot *stay* rich. This is easily exemplified with the tremendous amount of stock options that were issued in the 1990's. We have friends and relatives that have told their horror story of how huge their retirement plans grew only to plummet because so much was tied up in company stock. Individual investors, including those already retired are not immune from this danger. I see quite often investors that have relied on only one or two asset classes to grow their nest egg only to see it dwindle when those markets went through inevitable shifts. There is never a wrong time to diversify properly. Get a properly drafted *Investment Policy Statement* done today and proceed as expeditiously as possible.

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Tax Moves. Another classic. If your accountant is doing her job correctly, she is doing everything within the limits of the tax code to reduce, eliminate, or defer your income taxes. If your advisor is doing his job, he is doing everything within his legal power to convince you to avoid making investment mistakes. Unfortunately, sometimes the twain shall meet – and it costs you money. Many times the proper investment move is not made because of the adverse tax consequences that may be present. Investors inevitably weigh the consequences of paying the tax piper now vs. paying the unforeseen "value reduction tax" later. In recent years many have chosen to ignore the possibility of a stock market reduction and have saved income taxes in the process. However, the cost in lost value has far outweighed those taxes. One silver lining for those in this boat is that now may the perfect time to redeploy your assets into a proper allocation for the long run now that the unrealized tax burden in your portfolio is not as great.

While the bad news is that these mistakes are prevalent and will never be eradicated – the good news is you can correct all of them now. What a great thing to have that kind of empowerment! The key is sitting down with a qualified advisor and creating a plan of action – we call this an *Investment Policy Statement.* Once this plan is finished, then the correcting of these mistakes can take place at once. We are big proponents of using *asset class funds* that provide the broadest and deepest diversification in the universe. They are also generally less expensive than retail funds and are used by institutions such as pension plans and scholarship funds for long term investment success. So avoid those classic mistakes and keep those emotions in check, invest – don't speculate, believe in capitalism and its potential and don't let the tax man dominate your investment decisions. All these will add up to long term investment success!

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