

You're Biased Towards Your Own Money: What to Do About It

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Each of us has a complex relationship with our own money and, accordingly, it can be difficult to be consistently rational with regard to our wealth. Where do our behavioral biases come from, and what can we do to counteract those biases? We explore these questions this month's blog.

What Are Behavioral Biases?

Many of us set budgets, monitor our investments, and spend conservatively. By doing so, we like to think we're acting rationally with our money. But the truth is, people are emotional when it comes to their finances and this can affect decision-making in myriad ways.

Common emotions that influence how we spend and invest include:

- Fear
- Guilt
- Shame
- Envy
- Hope
- Excitement

Acting on these feelings can lead to investment decisions that impact your portfolio in the long run. For example, you may choose to "follow the crowd" and make a risky investment in "fear of missing out (FOMO)" or impulsively sell shares of a quality company when its stock price starts trending lower.

Emotional spending (sometimes nicknamed "retail therapy") is another common practice influenced by behavioral biases. When you're unhappy or upset, buying something new can make you feel better (at least for a little while).

What to Avoid

Although tempting, avoid making rash investment decisions based on what you see in the news or hear from friends and family.

For example, you may hear that the CEO of a major corporation is stepping down because of a fraud allegation against him or her. In turn, your first reaction may be to sell your stock in that company. In reality, the CEO's departure may not have any significant impact on the company's performance - especially in the long run. Instead of considering that company's stock price over the span of years or decades, you made an in-the-moment decision based on short-term changes. Your gut reaction was to immediately protect your assets, when you may have actually hurt your chances for greater returns down the line. Hiring an investment manager with discretionary investment authority (i.e., handing over trading to a professional) may help mitigate this risk area.

Challenge Your Mindset

Talk to a Professional

If you know that your emotions will impact planning for future spending or managing your investments, consider working with a Certified Financial Planner® who can act as an educated, unbiased third party to guide you through investment decisions and other aspects of your financial life. Together, we can reframe the discussion so your investment portfolio becomes the engine for your

financial plan. The appropriate risk/return profile, in line with your specific goals and objectives, can help steer you in times of trial.

Think Long-term

It's vital to take a long-term perspective when making decisions, rather than following short-term trends that may not be beneficial in the long run.

Know Yourself

Being self-aware is an important step towards avoiding behavioral biases when investing. Know your level of risk tolerance and allow that information to help determine your asset allocation strategy. Doing this should help alleviate some worry regarding your investments and reduce the urge to make impulsive choices.

Acknowledging and controlling your behavioral biases can help you feel confident in your investment decisions and everyday spending choices. Working with a trusted financial advisor allows an objective third-party to offer educated guidance and direction - without emotional bias.

Final Thoughts

Independently navigating a lifetime of twists and turns in the market can be challenging at best. Setting and staying the course are key components to reaching your financial goals. Let us help you chart a path for success.

If you have any questions or would like to talk further about your specific financial situation, please reach out to me anytime.

All the best to you and yours.

CONTACT US

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