ALASKA HIGHWAY NEWS

Brad Brain: Check your reasoning

Brad Brain / Alaska Highway News

JUNE 24, 2020 01:22 PM

Brad Brain: "When decisions are made based on the cycle of market emotions you end up with the opposite of buy low, sell high. When fear and greed kick in, and you make decisions based on past performance, you are far more likely to buy high and sell low. So lets step back and look at things rationally."

You can tell that people are feeling better about making an investment. My phone is starting to ring. Now that the markets are up about 35% from March, my phone is starting to ring.

This was totally predictable. Don't get me wrong. I am not saying that this is a bad time to work on your finances. Its never a bad time to work on your finances. It's just that working on your finances is not usually the type of phone call I get after the markets go up 35%. The types of calls I get after the markets go up by 35% are often determined by the cycle of market emotions.

To understand the cycle of market emotions you need to understand that money decisions are often not rational, but emotional. And the two dominant emotions are fear and greed.

Here is how it works: As an investment goes up in value people will feel better and better about it. They will start out as being optimistic. As the investment rises they will be pleased. As it rises further they will get excited, then thrilled, and then euphoric.

This is the point when the money rolls in. People extrapolate the recent good performance as continuing uninterrupted, they feel great about the prospects for the future, and they want a piece of the action.

Conversely, if an investment slumps people will feel progressively worse about it. At first they might dismiss a decline as being inconsequential. They might be in a state of denial, but that's going to turn to frustration, then a feeling of helplessness, then anger. Often when things seem the worst people will just get so fed up they capitulate, and sell off the investment to try something new.

This is where the money rushes out. People extrapolate the recent lousy performance as continuing uninterrupted, they feel terrible about the prospects for the future, and they want out at any cost.

The problem is, when decisions are made based on the cycle of market emotions you end up with the opposite of "buy low, sell high." When fear and greed kick in, and you make decisions based on past performance, you are far more likely to buy high and sell low.

So let's step back and look at things rationally.

If you are thinking about making an investment because you think there is no time like the present, I agree with you. I don't try to time the markets, and if you have a long-term outlook there is little empirical reason to try. Investing when you have the money to do so is a sound strategy.

If you want to invest because there are important things that you want to do with your life, and these things will cost money, I agree with you. The calendar shows no mercy. The sooner you start, the better.

But if you want to make an investment because you think the recent exceptional performance will continue unabated, you need to check your reasoning. Trees don't grow to the sky.

If you want to make an investment because you are fearful that you are missing out, check your reasoning. FOMO is a powerful motivator, but that does not make it a good reason to invest.

If you want to make an investment because you think you can make a quick buck, check your reasoning. Past performance is no assurance of future performance, and applying a short timeframe to a long-term investment is speculation.

People will often make money decisions based on fear and greed. But these are usually lousy reasons to invest. So if you feel an urgent need to get in on the markets right now, ask yourself, is this a rational decision based on my financial objectives, or is this me getting swept away in the excitement?

If it is the latter, maybe sleep on it, see if you still feel the same tomorrow. If it's the former, give me a call, we are open for business.

Brad Brain, CFP, R.F.P., CIM, TEP is a Certified Financial Planner in Fort St John, BC. This material is prepared for general circulation and may not reflect your individual financial circumstances. Brad can be reached at www.bradbrainfinancial.com.