RBC Dominion Securities Inc.

Wade Wealth Report

FOR THE CLIENTS AND FRIENDS OF PORTFOLIO MANAGER FRANK WADE | SPRING 2015

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Seven Psychological Pitfalls of Investing – And How to Avoid Them

Do you get anxious when the stock markets are volatile? Or do you feel optimistic that everything will turn out fine? Both reactions – natural parts of your psychological makeup – can actually impede your progress towards your investment goals.

The good news is that you can gain some control over your psychological responses – unlike the financial markets. The following are seven psychological pitfalls of investing – and how you can avoid them.

1. **Optimism**

People have a natural tendency to overestimate the likelihood of positive results on everything from the weather to investing. This largely explains why people are so often disappointed by their investment performance – they simply felt they would do better based on this psychological bias.

Avoiding the feeling of disappointment is only one good reason why you should consciously compensate for this natural optimism. If you base your financial goals on unrealistically positive

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expectations, you will almost certainly fall short of these goals. This can affect your anticipated retirement date, amount of retirement income, or the value of your estate.

How much should you compensate for this bias? Some people are better calibrated than others, but studies indicate that in general if you feel there is a 99% chance of something happening, the actual odds are closer to 85%.

2. **Overconfidence**
Another powerful psychological bias is overconfidence. Just as people tend to be overly optimistic about the probability of positive results, they also tend to be overconfident about their own talents. Some investors think that they can "outsmart the market" – and even control largely unpredictable events such as stock market volatility.

This leads to one of the most common pitfalls of investing – market timing. Confident in their own abilities, many investors try to time the market so that they always buy low and sell high – despite the fact that not even the most accomplished professional investors can do this consistently.

Recognizing this tendency towards overconfidence is the first step towards dealing with it. Try to be honest about your abilities, and if you find yourself falling into traps such as market timing, take a step back and rethink your approach.

3. **Hindsight**
Hindsight is the tendency to believe that after something has happened, you knew all along that it would – even though you didn't. This tendency can lead you to believe that events are far more predictable than they really are, raising unrealistic expectations about how well your investments will perform and your advisor's ability to foretell the future, among other things. If you find yourself confidently declaring that you "knew it all along" ask yourself whether you really did. As with optimism and overconfidence, you may have to consciously compensate for hindsight.

4. **Obsession**
Do you follow the performance of your investments minute-by-minute on TV or the Internet? Do you dwell on short-term changes in the market value of your investments? Do you fixate on the negative performance of a single investment, even when your overall portfolio is doing well? These can all be signs of obsessive behaviour commonly displayed by investors.

Take a step back and look at the big picture. Are you on track to achieving your longer-term goals? Are you comfortable with the level of investment risk in your portfolio? If not, you may have to make adjustments to stop obsessing about short-term events.

5. **Denial**
When stock markets go down, investors can sometimes panic and sell what is still fundamentally a good investment. The flipside of this is denial – when investors continue to hold an investment that has gone bad, thinking it will eventually come back. It can be hard, but when an investment has fundamentally deteriorated, it may be time to sell. Having an investment discipline in place with specific, rational criteria for buying and selling can help you overcome this tendency.

6. **Greed**
The desire to "get rich quick" compels many investors to take bigger risks than they should, such as investing too much in a single investment. When the risk doesn't pay off, it can jeopardize their financial security. That doesn't mean you should never take a risk – it's a normal part of investing. The key is to take well-calculated risks within a properly diversified investment portfolio, which is designed with your personal risk tolerance in mind. That way, when the occasional risk doesn't pay off, the impact is mitigated by the other investments in your portfolio.

7. **Herd instinct**
When we see other people doing something, we have a natural tendency to think that it must be a good thing and we should do it too. This "herd instinct" is often behind sharp ups and downs in the financial markets. When other people are buying, propelling the market upwards, we buy too, sending the market even higher. Similarly, when other people sell in a panic, sending the market downwards, we sell too, fueling the decline. Unfortunately, this often results in buying at the height of the market euphoria, or selling close to the depths of the panic. Instead of following the herd, follow a disciplined investment strategy based on logic and reason.

Successful investing over the long term is less about how the markets are doing than how we react to what the markets are doing. Unfortunately, many of our natural psychological reactions – like denial, panic or greed – can impede our long-term success.

We can show you how a disciplined approach that removes the emotions and guesswork from investing can help you avoid these psychological pitfalls of investing. Please contact us for more information.

U.S. Debt Burden

The debt situation in the U.S. and the associated issues of unfunded liabilities continue to attract significant commentary. And while not yet urgent, we believe the sooner the issues are faced and action taken, the easier it will be for the economy. Click here to read more about the cold hard facts.

An Easier Way to Move Money to RBC Dominion Securities

Did you recently experience that last minute panic of needing to get a cheque over to RBC Dominion Securities before the March 2 RRSP deadline?

If your bank accounts are with RBC, did you know that you can easily contribute to your RRSP, TFSA or transfer funds to other DS accounts from the convenience of your personal computer using DS Online?

To learn more about this and other benefits of DS Online, or to sign up, please contact our office or click here.

Keeping You Informed

Insights & Research

For views on the global financial markets and insights on managing your wealth, don't forget to visit the Insights and Research section of our website at www.frankgwade.com. Once on the Insights & Research page, click on the ⊞ symbols to find publications like our Global Insight 2015 Outlook Edition which provides a look ahead at the global economy.

You'll also find the following topical reports:

- Building Tax-Free Wealth – TFSA Quick Tips 2015
- Portfolio Advisor RRSP Edition – Twelve Strategies to Maximize Your RRSP
- Over a Barrel – Special Report on Oil

Commentary

If you are interested in receiving daily or weekly updates about what is happening in the markets, please contact Chris Cherepuschak at 204-982-3468 to be added to our email distribution lists. Alternatively, you can visit the Commentary section of our website where this daily, weekly and monthly information is available to download.

Introducing Our New Team Member

Associate Melanie Potter

Melanie joined Wade Wealth Management of RBC Dominion Securities in December of 2014 and has been with RBC Dominion Securities since 2006. She was born and raised in Manitoba, and graduated from the University of Manitoba with a Bachelor of Human Ecology degree. Melanie is responsible for supporting wealth management processes, annual client reviews, and administrative activities for the team.

Melanie is married to Colin and they have a son, Liam, who keeps them very busy.