Issue 3 | Financial Journeys

RETIREMENT PLANNING

Some behaviours can make us less wealthy

We have evolved over 3 million years and only lived the way we do today for a fraction of that time. Our behaviour is often at odds with how we make financial decisions.

When investing, we aren't wired for graphs, facts and figures. In fact, they are designed to make us feel they are important and the person behind them understands them. Often, we are told the stories of star fund managers – famous people who run large investment funds and who have the foresight into the markets others do not possess.

In reality, these star fund managers are akin to football managers – they burn brightly for a while and then fizzle out, sometimes with disastrous results. Clever marketing companies know our brains are wired for stories, especially where there is a central character that is the hero. Fighting the temptation to follow the herd blindly by investing in the funds of these people is a fool's errand.

Let performance do the talking

Instead, follow this principle – chose straightforward, strong investment teams. They let the fund performance speak for itself over the long term and make no claims or foresight. They know that a well-diversified portfolio will deliver.

Here is another behavioural flaw – we worry about normal investment market volatility. Simply put, volatility is the entrance fee to gain long-term wealth. However, when markets crash, we panic. We are wired to react. Imagine being alive 20,000 years ago and war, pestilence, famine and a wandering band of terrible singers arrive at your cave doorstep – you are likely to get your family out of that place quickly.

With investing, we do the opposite – that is, nothing. Markets will recover and to quote the world's most famous investor, Warren Buffett: "Be fearful when others are greedy and greedy when others are fearful." Within reason (and this is the reason that we ask you to complete a risk-profiling questionnaire), the greater the volatility of a fund, the far greater the potential returns. Risk only comes into it when you need to access the money and this is where a professional financial planner, on your side of the decision-making table, enables you to navigate things effectively.

Focus on the long term

One of our favourite behavioural biases relates to present value. Experiments show that refusing a reward now for a larger one later is a wealth-building hack. For example, consider someone who wants to save to buy a house. It's a difficult process that takes time and involves short-term financial sacrifices.

It's easy to get mission drift, give up and spend the money on a car with bucket seats and a loud exhaust or an exotic holiday and be back at square one. A useful tool to overcome this challenge is having a strict budgeting plan, a financial plan and building in progress rewards that don't detract from the end goal.

Lastly, another dangerous behavioural trait is succession bias. For example, "My Uncle David smoked Woodbines until he died at the ripe old age of 99." What I have ignored are the thousands who died prematurely and often in great pain. Another is "My friend invested in a star manager's fund and they've made a fortune." Let's have the conversation a few years on and obtain the data for all investors in that fund and assess where they are on their wealth journey.

There are many examples of succession bias. We filter out what we don't want to know and anchor our believes on the one story that we want to believe – usually at the cost of our wealth.

HOW TO OVERCOME BEHAVIOURAL BIASES

Behavioural finance attempts to explain the psychology behind why some people make irrational financial decisions. A financial adviser can keep your plans on track by helping you:

Understand your risk tolerance	Design and implement a robust financial plan	Ignore market noise	Curb your herd instincts	Take the emotion out of investing