THE 5 MISTAKES EVERY INVESTOR MAKES (AND HOW TO AVOID THEM)

BASED ON THE WORK OF **PETER MALLOUK**, #1 FINANCIAL ADVISOR IN AMERICA BY BARRON'S.

MISTAKE #1

MARKET TIMING

"I'll wait for the market to drop before investing"

"Forecasts may tell you a great deal about the forecaster, but they tell you nothing about the future"

WARREN BUFFET

WHAT IS MARKET TIMING?

The attempt to predict the **optimal times** to buy and sell investments based on **market trends** or **external factors**.

WHAT DOES THIS LOOK LIKE? WHY IS IT A PROBLEM?

01 **The Desire for Outsized Returns**. It appeals to our innate desire for growth and reward, making it feel like a **competitive game** rather than a **disciplined**, **long-term process**.

02 **The Illusion of Control**. This belief gives people a **false** sense of control over unpredictable events, which feels empowering.

03 **Media and Success Stories**. Stories of investors who "**timed the market**" and made fortunes are amplified in the media, creating a skewed perception of what's possible.

04 **The Fear of Missing Out** (FOMO). Seeing others profit from market booms creates anxiety about being **left behind**.

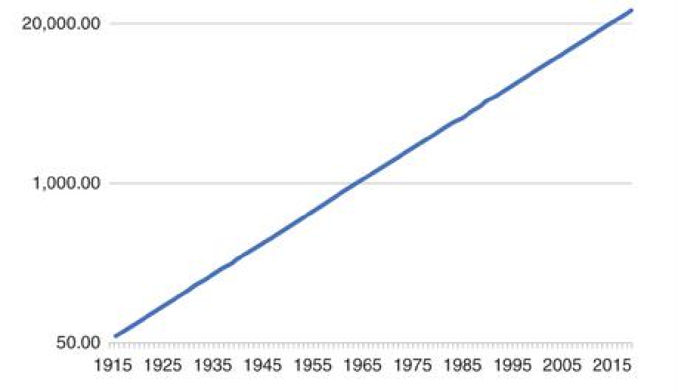
05 **Advisors Need to Sell Something.** Pitches are designed to justify their fees and differentiate their services, even when evidence shows that market timing is rarely effective.

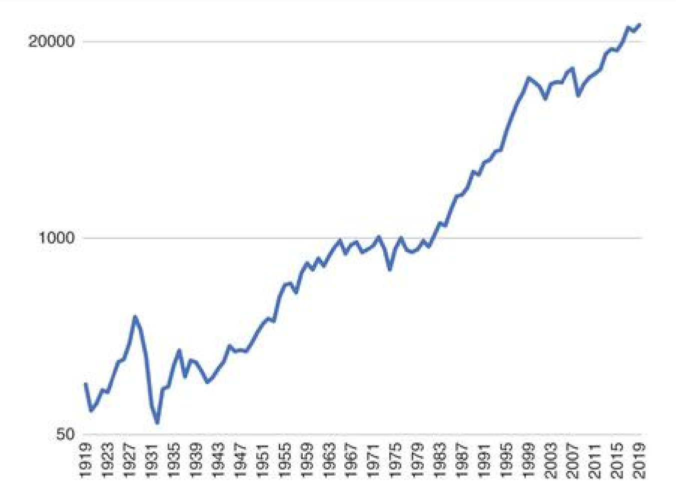
06 **Complexity Sells.** Investors might assume that a strategy involving market timing or intricate analysis must be better because it **feels sophisticated**.

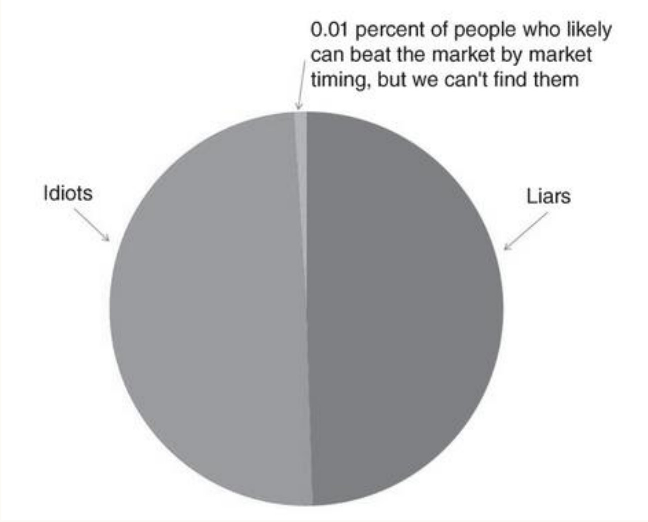
THE CORE PROBLEM WITH MARKET TIMING:

Historical Data sourced from S&P Dow Jones Indices 2014.

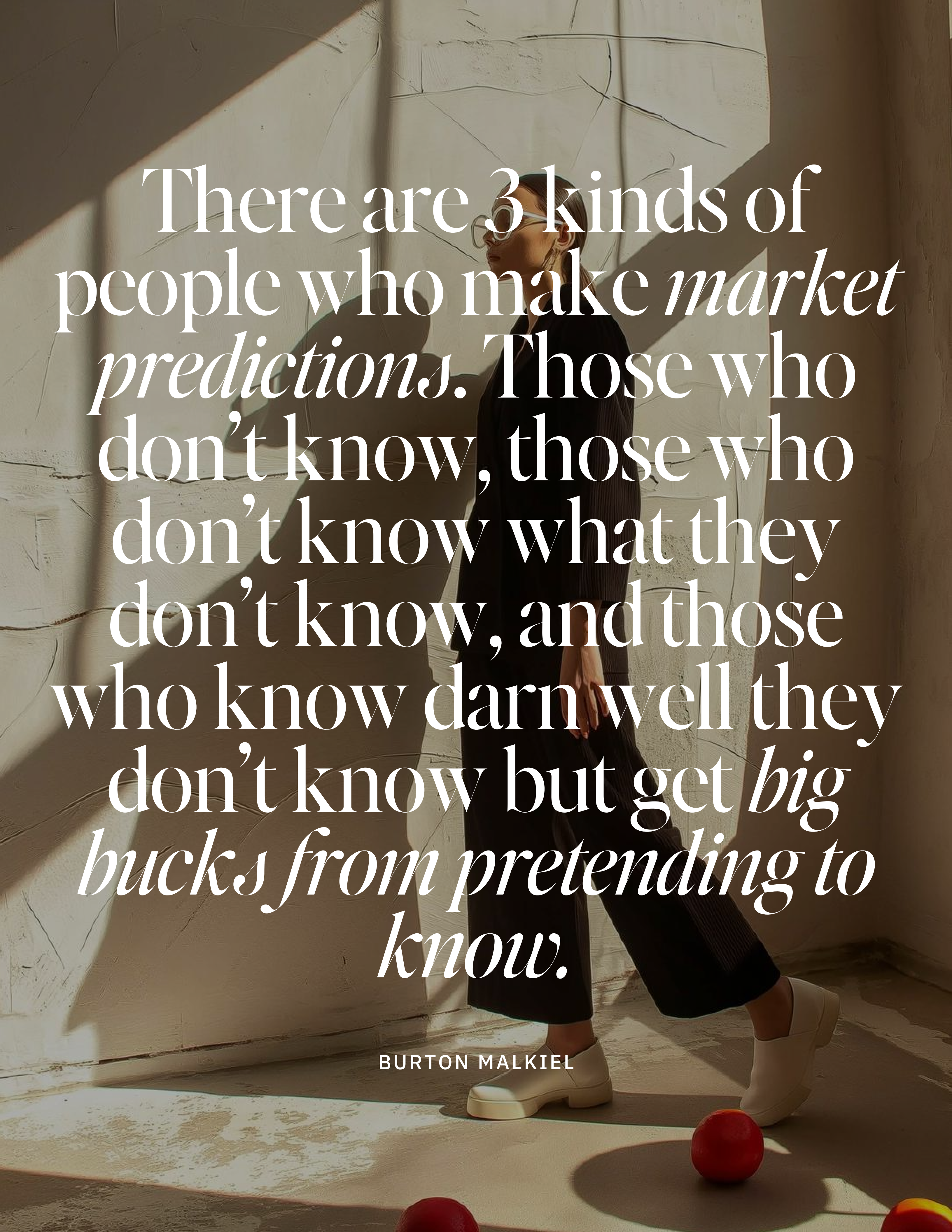
Imagine this investment - about **10%** every year over the last 88 years! Well, this return is real. It's a *magical* investment called the **stock market**. Why do almost all investors lag behind the stock market return? **Market timing.**







Graph by Creative Planning LLC.



There are 3 kinds of people who make *market predictions.* Those who don't know, those who don't know what they don't know, and those who know darn well they don't know but get *big bucks from pretending to know.*

BURTON MALKIEL

THE EFFICIENT MARKET HYPOTHESIS

WHAT IS THE EFFICIENT MARKET HYPOTHESIS?

The **Efficient Market Hypothesis** (*EMH*) is a financial theory proposed by Nobel Laureate Eugene Fama. It suggests that at any given moment, **the prices of securities (stocks, bonds, etc.) fully reflect all available information about them.** In other words:

- Prices are always "correct" because they incorporate and respond to **all known data** and **events**.
- Markets are efficient because information is **quickly** and **accurately absorbed** into **asset prices**.

THE EVIDENCE

ECONOMISTS

Famous Failures: Renowned economists like Irving Fisher declared in 1929 that "stock prices have reached a permanently high plateau," just before the market crash leading to the Great Depression.
Reason for Failure: Economists grapple with too many variables (known and unknown), making accurate market forecasting nearly impossible.

FINANCIAL ADVISORS AND INVESTMENT MANAGERS

Ken Fisher: Prominent for bold predictions and actively managed funds, but his fund consistently underperformed compared to the S&P 500, with returns lagging by significant margins (e.g., -52.86% over 15 years).
Harry Dent: Author of bold economic predictions like a "depression in 2009" and the Dow dropping to 3,800. His strategies and associated funds lost money for investors.
Peter Schiff: Correctly predicted the 2008 crash but failed in subsequent predictions and investment strategies, which often led to significant losses.

MEDIA

Exaggerated Headlines: Media outlets often sensationalize news to attract readers, using dire predictions like "The Death of Equities" (Businessweek, 1979) or "Buy Stocks. No Way!" (Time, 1988), which were proven wrong shortly afterward.
Eyeball Strategy: The goal of financial media is not accuracy but engagement, often leading to fear-based reporting that misguides investors.

THE MASSES

Retail Investors (The Masses)

March 2020 Example: During the COVID-19 panic, retail investors withdrew $326 billion from equities at market lows, missing the recovery that followed.

BehavioUral Flaw: Emotion-driven decisions (fear and greed) lead to poor market timing, resulting in buying high and selling low.

> FAR MORE MONEY *has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in* CORRECTIONS THEMSELVES.
>
> PETER LYNCH

How to AVOID MISTAKE #1

01

MARKET TIMING DOES NOT WORK

Overwhelming evidence from academic research and real-world studies shows market timing **consistently fails**.

Everyone gets it wrong: the masses, media, economists, advisors, and investment managers.

02

WHAT MARKET TIMING LOOKS LIKE

It can be direct (e.g., moving to cash and waiting for the "right" time) or indirect through coded strategies such as: Asset-Class Rotation, Sector Rotation, Downside Protection, Tactical Asset Allocation.

03

CORRECTIONS ARE NORMAL

Market corrections and bear markets will occur repeatedly over a lifetime. Trying to predict or trade through these events usually harms portfolios more than it helps. Remember: The bear will always give way to the bull.

04

BEWARE OF ADVISORS PROMOTING MARKET TIMING

If an advisor offers market-timing strategies, they are likely **increasing** the odds of underperformance in your portfolio.

The research is clear: professionals, friends, or anyone else are **unlikely** to succeed in market timing.

MISTAKE #2

ACTIVE TRADING

WHAT IS ACTIVE TRADING?

Active trading involves **frequent buying** and **selling** of securities to outperform the market.

Tens of thousands of professionals and millions of retail investors are all trading a limited number (around 4,400) of publicly listed stocks in the U.S., creating intense competition.

THE REALITY OF MARKET RETURNS

THE COMBINED PERFORMANCE OF ALL ACTIVELY TRADED STOCKS IS THE MARKET RETURN. FOR SOMEONE TO "WIN" IN ACTIVE TRADING, SOMEONE ELSE MUST "LOSE."

ACTIVE TRADING INCURS ADDITIONAL COSTS LIKE TRANSACTION FEES, TAXES, AND MANAGEMENT EXPENSES, REDUCING NET RETURNS FOR MOST PARTICIPANTS.

FINANCIAL INSTITUTIONS (THE "HOUSE") PROFIT FROM TRADING ACTIVITIES REGARDLESS OF WHETHER INDIVIDUAL TRADERS WIN OR LOSE. THIS SETUP ENSURES THAT THE AVERAGE ACTIVE TRADER UNDERPERFORMS AFTER ACCOUNTING FOR COSTS

"On average, it's a *simple fact* that *passive indexing* always has and *always will outperform active fund management*—it's as certain as night follows day in this uncertain business."

— John Bogle

Why Index Funds Win

LOWER COSTS: NO EXCESSIVE TRANSACTION OR MANAGEMENT FEES.

FEWER TAXES: INDEX FUNDS TRADE LESS FREQUENTLY, MINIMIZING TAX LIABILITIES.

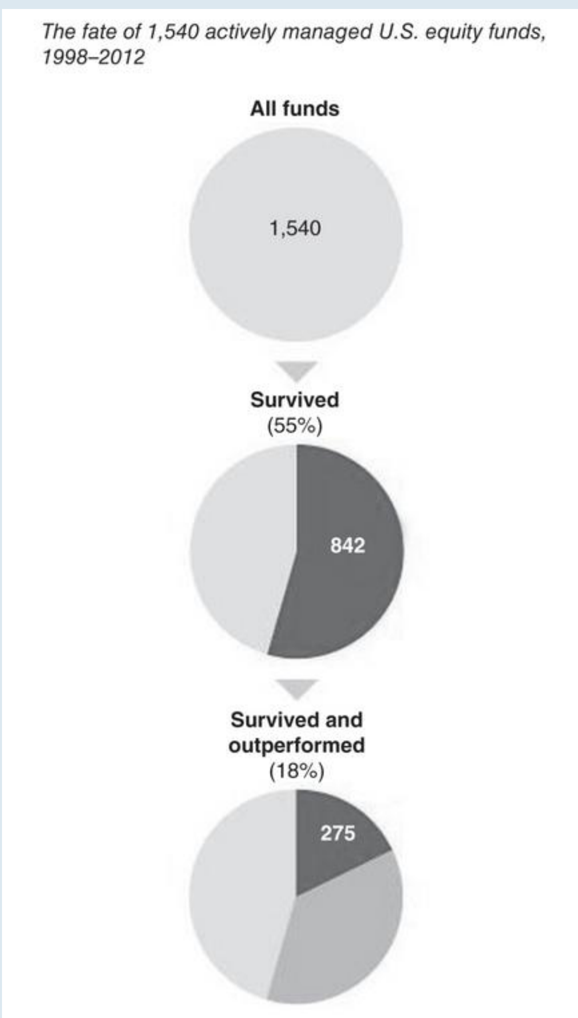
CONSISTENT PERFORMANCE: MOST INDEX FUNDS OUTPERFORM THE MAJORITY OF ACTIVELY MANAGED FUNDS OVER TIME.

STUDIES SHOW 71-85% OF ACTIVELY MANAGED FUNDS UNDERPERFORM THEIR BENCHMARKS OVER LONG PERIODS.

SURVIVOR BIAS AND ACTIVE FUND PERFORMANCE

Survivor Bias Distorts Results

Many underperforming mutual funds are closed and excluded from performance databases, giving a misleading impression of better results.



From 1998 to 2012, only **55%** of 1,540 mutual funds survived, and a mere **18%** both survived and outperformed their benchmarks.

Even among surviving funds, consistent outperformance is rare.

What does this mean?

This graph illustrates the relationship between mutual fund Morningstar ratings and their **subsequent performance** over **36 months**.

Surprisingly, funds with higher star ratings (4 or 5 stars) tended to underperform their benchmarks significantly compared to funds with lower ratings (1 or 2 stars).

WHY THIS HAPPENS: MORNINGSTAR RATINGS ARE BASED ON **HISTORICAL PERFORMANCE**, NOT PREDICTIVE INDICATORS.

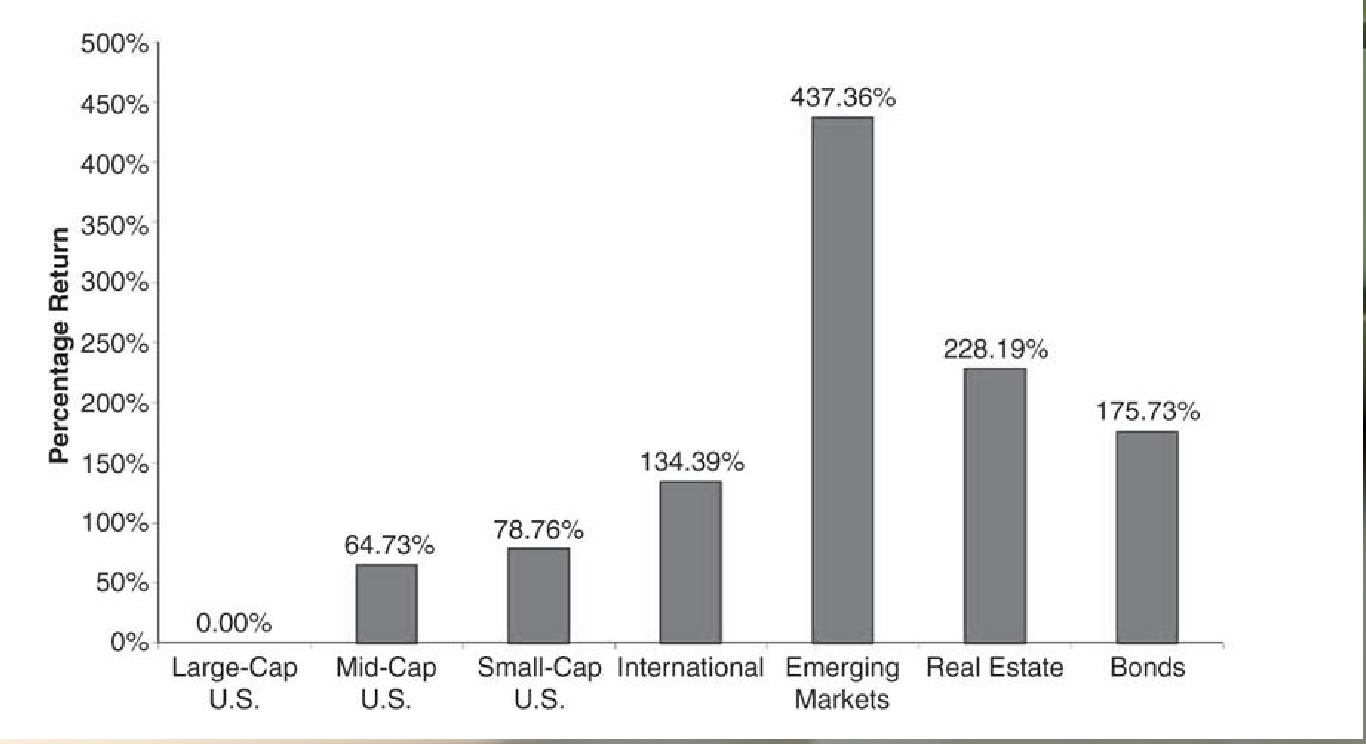
HIGH RATINGS OFTEN REFLECT PAST SUCCESS THAT IS **UNLIKELY TO PERSIST**, WHILE LOWER RATINGS REFLECT POOR PAST PERFORMANCE, WHICH MAY IMPROVE DUE TO MEAN REVERSION OR MARKET CONDITIONS.

S&P 500 Here I come!

The "Lost Decade" (2000-2010) is often cited as proof that investing in the market doesn't work, but this interpretation **misses key details**. While the S&P 500 Index—a representation of large-cap U.S. stocks—had flat returns, this index only reflects **one part of the market.**

Proper diversification and asset allocation reveal a different story. **Investments in mid-cap, small-cap, international, real estate, and emerging markets significantly outperformed during this period, with emerging markets yielding over 400% returns.**

Even the S&P 500, when including dividend reinvestments, showed slight positive returns.



How to AVOID MISTAKE #2

01

HIGH COSTS

Active management typically incurs higher fees than passive investing in index funds.

02

INCREASED TAXES

More frequent trades lead to higher taxable events, further eroding returns.

03

INCONSISTENT OUTPERFORMANCE

Even when an active manager outperforms, there's no evidence that success will continue. In fact, most active managers underperform the market.

04

STACKED ODDS

The majority of investors, whether they are professionals or individuals, lose to the market after accounting for fees, taxes, and other costs.

MISTAKE #3

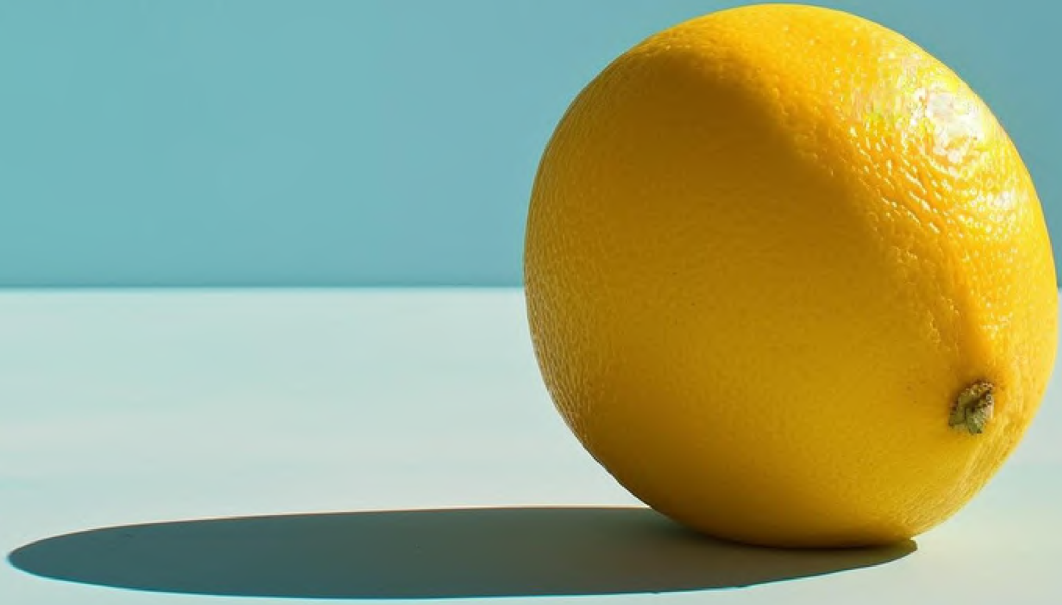
JUSDGING PERFORMANCE IN A VACUUM

MISUNDERSTANDING #1

MISUNDERSTANDING PERFORMANCE AND FINANCIAL INFORMATION

"Hey, look at how awesomely this portfolio has performed; put your money here!"

While this may be the single worst way to decide on investments, this is how most people choose their portfolio.



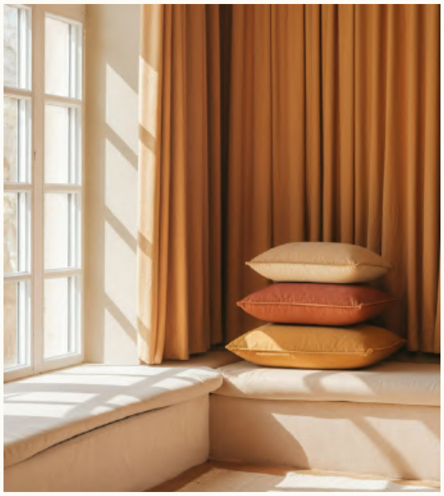
INVESTORS OFTEN MAKE THE MISTAKE OF CHOOSING A MONEY MANAGER BASED ON IMPRESSIVE PAST PERFORMANCE, ASSUMING IT INDICATES FUTURE SUCCESS. HOWEVER, THIS APPROACH IGNORES THE CONCEPT OF "REFERENCE SETS."

For example, if 12,000 people flip a coin 13 times, statistically, someone will achieve "perfect success" by flipping heads every time—yet this is **purely random**, **not skill**.

The same principle applies to money managers: among thousands of portfolio managers, a few will appear to have exceptional track records simply due to chance.

Portfolio managers market their success stories by showcasing their **best-performing funds** while conveniently ignoring the majority that underperformed. A manager might run multiple portfolios, and while one or two may beat the market, the rest often fail. **Yet, investors only hear about the winners.**

When a money manager tries to sell you on their performance, ask for the performance of **ALL their strategies**—not just the one they cherry-pick to impress you. Recognizing this bias is critical to making **informed investment decisions** rather than falling for selective marketing tactics.



MISUNDERSTANDING #2

BELIEVING THE FINANCIAL MEDIA IS OUR THERE TO HELP YOU

"Do you know what investing for the long run but listening to market news every day is like? It's like a man walking up a big hill with a yo-yo and keeping his eyes fixed on the yo-yo instead of the hill."

— Alan Abelson

Financial media thrives on fear, sensationalism, and keeping viewers engaged

Since the early 1900s, financial news has **exaggerated crises** to boost ratings, from market crashes to economic downturns. The goal is not to inform but to attract as many viewers as possible, selling ad space at higher prices.

The media uses **storytelling techniques** to **create urgency**, much like a suspenseful movie with a ticking clock. **This stress-inducing approach makes investors panic,** often leading them to make **poor financial decisions**, like selling investments at the worst possible time.

Studies show that watching financial news increases stress levels—even when the news is positive—leading to impulsive reactions. Much like The Weather Channel exaggerates storms to keep viewers watching, financial networks highlight market volatility to keep investors tuned in.

THE KEY TAKEAWAY

Recognize the noise and shut it out. A disciplined investor ignores the hype, sticks to their long-term strategy, and avoids the emotional rollercoaster of daily financial news.

MISUNDERSTANDING #3

BELIEVING THE MARKET CARES ABOUT TODAY

WHAT MAKES THE STOCK MARKET MOVE UP AND DOWN?

Some might say unemployment, housing, monetary policy, consumer confidence etc.

The answer is a big NO. All the stock market cares about is ANTICIPATED EARNINGS.

STOCK PRICES REFLECT A COMPANY'S EXPECTED PROFITABILITY, NOT ITS PAST PERFORMANCE OR SHORT-TERM NEWS.

During economic downturns, investors shift their money based on **expected earnings**. For example, in a recession, Walmart stock might rise as consumers spend less at high-end retailers. The market is always **forward-looking**, moving before economic changes occur.

Short-term fluctuations in stock prices are inevitable, and the market is not always right in the short run. However, history shows that the stock market is **resilient**, **consistently growing** over time as companies find ways to become more profitable.

THE KEY TAKEAWAY

Ignore short term noise and focus on long-term growth.

MISUNDERSTANDING #4

BELIEVING AN ALL TIME HIGH MEANS THE MARKET IS DUE FOR A PULL-BACK

An all-time high in the stock market does not automatically mean a crash or correction is imminent.

Every time markets hit new highs, media and investors often panic, assuming a downturn is inevitable.

MARKET MOVEMENTS ARE DRIVEN BY **FUTURE EARNINGS EXPECTATIONS**, AND LONG-TERM INVESTORS SHOULD REMAIN STEADY RATHER THAN REACTING EMOTIONALLY TO HEADLINES ABOUT NEW HIGHS.

(BASIC INFLATION IS PARTLY RESPONSIBLE, BUT THE REST, GOES BEYOND THE SCOPE OF TODAY’S PRESNTATION)

MISTAKE #4

LETTING YOURSELF GET IN THE WAY

THE MOST IMPORTANT quality for an investor is temperament, not intellect.

-Warren Buffet

WHAT WE'RE DICUSSING NEXT IS SOMETHING CLALED "BEHAVIOURAL FINANCE" - ONE OF MY GREATEST PASSIONS.

RECOGNIZE YOUR BEHAVIOURAL BIASES!!

01

FEAR, GREED, AND HERDING

INVESTORS ARE DRIVEN BY FEAR AND GREED, OFTEN FOLLOWING THE CROWD INSTEAD OF MAKING RATIONAL DECISIONS.

HERD MENTALITY CAUSES PEOPLE TO SELL IN DOWNTURNS (OUT OF FEAR) AND **BUY IN RALLIES** (OUT OF GREED), LEADING TO POOR INVESTMENT OUTCOMES.

HISTORY SHOWS THAT INVESTORS WHO STAY DISCIPLINED AND TAKE **ADVANTAGE OF MARKET DROPS** (RATHER THAN PANIC-SELLING) DO MUCH BETTER.

02

OVERCONFIDENCE EFFECT

INVESTORS TEND TO **OVERESTIMATE THEIR ABILITY** TO PREDICT MARKET MOVEMENTS.

STUDIES SHOW THAT OVERCONFIDENT INVESTORS **TRADE MORE FREQUENTLY,** LEADING TO **WORSE RETURNS** DUE TO TRANSACTION COSTS AND POOR DECISION-MAKING.

OVERCONFIDENCE IN FUND MANAGERS CAN ALSO BE MISLEADING—MANY **CLAIM PAST SUCCESSES WITHOUT ACKNOWLEDGING THE FULL PERFORMANCE OF ALL STRATEGIES** (THE "REFERENCE SET" ISSUE).

CONTINUED...

03

CONFIRMATION BIAS

INVESTORS SEEK OUT INFORMATION THAT **CONFIRMS THEIR EXISTING BELIEFS** AND IGNORE CONFLICTING EVIDENCE.

THIS CAN LEAD TO **POOR DECISION-MAKING**, AS INVESTORS FAIL TO OBJECTIVELY ASSESS RISKS AND OPPORTUNITIES.

TO COUNTERACT THIS, ONE MUST **ACTIVELY SEEK OUT OPPOSING VIEWS** AND CHALLENGE THEIR OWN ASSUMPTIONS.

04

ANCHORING

INVESTORS FIXATE ON **ARBITRARY PRICE POINTS** (SUCH AS A STOCK'S PREVIOUS HIGH OR PURCHASE PRICE) INSTEAD OF EVALUATING **CURRENT FUNDAMENTALS.**

THIS CAN CAUSE THEM TO **HOLD ONTO LOSING STOCKS** TOO LONG OR **AVOID BUYING ASSETS THAT HAVE ALREADY APPRECIATED,** DESPITE CONTINUED GROWTH POTENTIAL.

OH THERE'S MORE...

05

LOSS AVERSION

THE PAIN OF **LOSING MONEY IS PSYCHOLOGICALLY TWICE AS INTENSE AS THE PLEASURE OF MAKING MONEY.**

THIS LEADS TO IRRATIONAL BEHAVIORS SUCH AS **HOLDING ONTO LOSING INVESTMENTS** HOPING THEY RECOVER, OR SITTING ON CASH OUT OF FEAR OF LOSSES, MISSING LONG-TERM GAINS.

INVESTORS MUST LEARN TO **EMBRACE VOLATILITY** AND VIEW MARKET DROPS AS OPPORTUNITIES RATHER THAN THREATS.

06

MENTAL ACCOUNTING

INVESTORS MENTALLY SEPARATE MONEY INTO DIFFERENT "**ACCOUNTS**" BASED ON ITS ORIGIN OR INTENDED USE, **RATHER THAN TREATING ALL MONEY THE SAME.**

THIS LEADS TO INCONSISTENT DECISION-MAKING.

THE BEST APPROACH IS TO VIEW THE **ENTIRE PORTFOLIO HOLISTICALLY RATHER THAN MAKING ISOLATED DECISIONS.**

JUST BECAUSE IT EXCITES ME.

07

RECENCY BIAS

INVESTORS TEND TO BELIEVE THAT **RECENT MARKET TRENDS WILL CONTINUE INDEFINITELY.**

THIS BIAS LEADS TO MISTAKES LIKE ASSUMING A BULL MARKET WILL LAST FOREVER OR PANICKING DURING DOWNTURNS.

HISTORICAL DATA SHOWS MARKETS MOVE IN CYCLES, AND DISCIPLINED INVESTORS WHO **IGNORE SHORT-TERM TRENDS** DO BEST OVER TIME.

08

NEGATIVITY BIAS

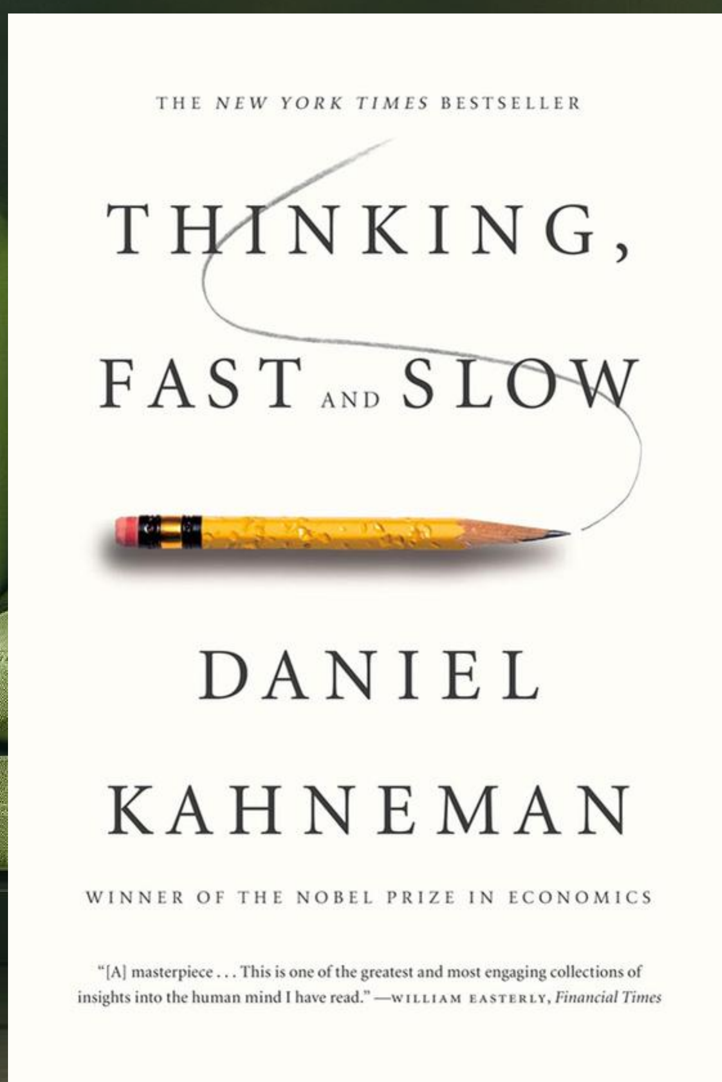
PEOPLE REMEMBER AND REACT MORE STRONGLY TO **NEGATIVE NEWS** THAN POSITIVE NEWS.

THIS MAKES THEM **PRONE TO PANIC** DURING MARKET DOWNTURNS, EVEN THOUGH MARKETS HAVE HISTORICALLY RECOVERED FROM EVERY CRISIS.

THE FINANCIAL MEDIA AMPLIFIES NEGATIVITY TO ATTRACT VIEWERS, SO INVESTORS MUST LEARN TO TUNE OUT THE NOISE AND FOCUS ON LONG-TERM TRENDS.

ONE OF MY FAVOURITE BOOKS ON

BEHAVIOURAL ECONOMICS



KEY TAKEAWAY

Emotions and cognitive biases are the **biggest obstacles** to successful investing. To succeed, investors must recognize and manage their own psychological tendencies—controlling fear, greed, and impulsive decision-making—while maintaining a **disciplined, long-term strategy.**

MISTAKE #5

CHOOSING THE WRONG ADVISOR

MOST ADVISORS DO

MORE HARM THAN GOOD,

often falling into three categories:

- THOSE WHO TAKE CUSTODY OF CLIENT FUNDS (HIGH RISK)
- SALESPEOPLE DISGUISED AS ADVISORS.
- ADVISORS PUSHING HARMFUL STRATEGIES TO MAKE COMMISSIONS

> *Brokerages and advisers should have independent custodians, and the government should have forced me to have an independent custodian. Client funds should be held by independent custodians. If they had, I would have been caught long ago. If I had had an inspection by the SEC, they would have looked at the custodian accounts and seen the funds on my books did not match the funds in the accounts, and I would have been caught.*
>
> —Bernie Madoff (Patel 2013)

The Bernie Madoff scandal is used as an example of why custody matters. **Madoff had direct control over client assets, making his Ponzi scheme possible.**

Investors should ensure their funds are held by a **third-party custodian**, rather than giving an advisor direct access.

AVOIDING CONFLICTS OF INTEREST

Many advisors earn **commissions** from selling certain financial products, creating a conflict of interest.

Independent Registered Investment Advisors (RIAs) operate under a fiduciary duty, meaning they are **legally required to act in a client's best interest**—unlike **brokers, who may sell proprietary products.**

Identifying the Right Advisor: The 3 Tests

Test #1: Independent Advisor vs. Broker?

Brokers are NOT held to a fiduciary standard.

Investment advisors (RIAs) have a legal duty to act in the client's best interest.

Test #2: Pure Independent vs. Dual-Registered Advisor?

Dual-registered advisors can switch between acting as fiduciaries and brokers within the same conversation—creating a major conflict of interest.

Test #3: Proprietary Funds vs. No Proprietary Funds?

If an advisor's firm sells proprietary products (like in-house mutual funds), it's a red flag. Advisors should recommend what's best for you, not what benefits their company.

COMPETENCE MATTERS

When selecting a financial advisor, look for key credentials that reflect advanced education and expertise in financial planning and investment management.

Certified Financial Planner (CFP): One of the most recognized financial planning credentials, signifying a commitment to putting clients' best interests first through ethical standards and comprehensive financial planning knowledge.

Chartered Financial Analyst (CFA): A rigorous designation focused on investment analysis and portfolio management, often pursued by advisors managing large institutional accounts.

Certified Public Accountant (CPA): Indicates expertise in accounting and tax planning, which can be valuable for complex financial situations.

Chartered Life Underwriter (CLU): Specializes in life insurance and estate planning, demonstrating knowledge in risk management and wealth transfer strategies.

Personal Financial Specialist (PFS): A designation for CPAs with additional training in personal financial planning.

Chartered Investment Manager (CIM): A credential for professionals skilled in investment management and portfolio construction.

These certifications signify a strong commitment to professional standards and financial proficiency.

Choosing an advisor.

THE CHECKLIST

01 **WHERE WILL MY MONEY BE HELD?**
RIGHT ANSWER: SOMEWHERE ELSE!

02 **ARE YOU A BROKER?**
RIGHT ANSWER: NO!

03 **ARE YOU A DUALLY REGISTERED ADVISOR?**
RIGHT ANSWER: NO!

04 **DO YOU OR ANY AFFILIATE SELL PROPRIETARY INVESTMENTS OF ANY KIND?**
RIGHT ANSWER: NO!

05 **HOW ARE YOU COMPENSATED?**
RIGHT ANSWER: TOTAL DISCLOSURE IN WRITING AND NEVER MAKE COMMISSIONS ON ANY INVESTMENT PRODUCT.

06 **WHAT ARE THE CREDENTIALS OF YOU AND YOUR TEAM?**
RIGHT ANSWER: IF PLANNING IS INVOLVED, A CFP® IS IDEAL TO HAVE ON THE TEAM.

FINAL THOUGHT

WHEN CHOOSING A FINANCIAL ADVISOR, YOU WANT TO FIND SOMEONE WHO FOLLOWS A CONSISTENT PHILOSOPHY AND GENUINELY BELIEVES IN THEIR APPROACH—RATHER THAN ONE WHO OFFERS A MIX OF CONFLICTING STRATEGIES JUST TO MAKE A SALE.

Too many advisors push **market timing**, **tactical strategies**, and **hedge funds**, not because they believe in them, but because they know it **attracts clients**. That's not the kind of advisor I'd want.

I wouldn't trust a doctor who prescribes treatments they don't believe in, and I won't trust an advisor who does the same with investments.

HAVING GONE OVER THE KEY MISTAKES...

WE CAN MOVE ON TO OPTIMIZING RESULTS.

RULE 1

HAVE A PLAN

Investment Planning in 5 Steps

Investing without a clear goal is like setting off without a destination. A solid financial plan provides direction and keeps you on track.

Step 1: Assess Your Starting Point

- Create a **net worth statement** listing assets and liabilities to establish a baseline.

Step 2: Set a Clear Goal

- Make it **specific and realistic** (e.g., “Retire at 62 with $100,000 per year post-tax income”).
- Vague goals like “retire with a lot of money” don’t work.

Step 3: Run Projections

- Use online tools or an advisor to assess if you’re on track.
- Exclude funds earmarked for other expenses (e.g., kids’ education).
- Factor in all income sources like pensions or rental income.

Step 4: Adjust as Needed

- If hitting your goal requires **unrealistic** returns (e.g., 20% per year), adjust by:
  - Saving more
  - Lowering income needs
  - Delaying retirement

Step 5: Build and Maintain Your Portfolio

- Align investments with specific goals: retirement, education, or major purchases.
- If you have **excess wealth**, you can take more aggressive investment approaches.

RULE 2

AVOID ASSET CLASSES THAT DIMINISH RESULTS

Cash – The Illusion of Safety

- Cash is often seen as safe, but it is the **worst-performing asset class** over time.
- It consistently loses value due to **inflation**, meaning holding large cash reserves guarantees a decline in purchasing power.
- Investors sometimes hoard cash to time the market, but studies show that consistently moving in and out of the market leads to **underperformance**.
- Even in worst-case economic scenarios, holding cash offers no real advantage, as strong corporations and economies recover.

Gold – The Illusion of Growth

- Many investors flock to gold out of **fear** that currencies will collapse or inflation will surge.
- Unlike stocks, real estate, or energy, gold does **not** generate income, create jobs, or have intrinsic value beyond speculation.
- Historically, **gold has underperformed stocks, bonds, and real estate**, often barely keeping up with inflation.
- While gold has had periods of dramatic gains, these have ultimately led to declines, making it an unreliable long-term investment.

RULE 3

USE STOCKS AND BONDS AS YOUR PORTFOLIOS CORE

Bonds

- Bonds provide stability and consistent, though generally lower, returns.
- They act as a form of insurance, reducing the impact of stock market volatility.
- While stocks generally outperform bonds over time, bonds help cover short-term income needs, especially in retirement.
- A well-balanced portfolio should include enough bonds to cover several years of income needs, preventing the need to sell stocks in a downturn.

Stocks

- Stocks are unpredictable in the short term but have historically provided superior long-term returns.
- They come with higher volatility but offer a "risk premium" that rewards patient investors.
- Investors should allocate a portion of their portfolio to stocks that match their risk tolerance and time horizon.
- For long investment horizons (10+ years), investing in mid-cap, small-cap, and emerging market stocks can enhance returns.

Alternative Investments

- These include private equity, private lending, and private real estate.
- While they offer diversification, they often come with high complexity, illiquidity, and access requirements.
- Most investors are better off sticking to a simple stock and bond portfolio to meet their financial goals.

RULES 4,5 AND 6

Rule #4: Take a Global Approach

Investors often have a "home country bias," meaning they over-invest in domestic companies instead of diversifying globally. While U.S. investors can justify some bias due to the country's economic dominance, having international exposure is essential. Global diversification reduces risk, as different markets outperform at different times. Investors can achieve this by allocating a portion of their stock and bond portfolios to international index funds or ETFs.

Rule #5: Use Primarily Index-Based Positions

Index funds consistently outperform actively managed investments over time. Actively trading securities in any asset class tends to yield lower returns due to fees, taxes, and timing mistakes. A well-constructed portfolio should rely primarily on index-based investments, reducing the risk of underperformance caused by unnecessary speculation.

Rule #6: Don't Blow Out Your Existing Holdings

When adjusting your portfolio, be mindful of tax implications and existing positions. Instead of selling everything at once to reach your ideal allocation, work toward it strategically. Selling taxable holdings could trigger capital gains taxes, potentially negating any benefits from switching. In some cases, such as annuities with high surrender charges or stocks with significant appreciation, it may be better to hold rather than sell. A thoughtful approach ensures better after-tax results and avoids unnecessary losses.

RULES 7, 8 AND 9

Rule #7: Be Sure You Can Live with Your Allocation

- Investing is like choosing a rollercoaster—some people can handle the highs and lows, while others get sick from the ride.
- The key is to build a portfolio that aligns with your comfort level, time horizon, and ability to withstand volatility.
- Instead of making emotional decisions when markets are unstable, evaluate your risk tolerance when things are calm.
- A well-structured portfolio should meet short-, intermediate-, and long-term needs while staying within your ability to handle market swings.

Rule #8: Rebalance

- Rebalancing is essential for maintaining the right mix of stocks and bonds over time.
- Without rebalancing, portfolios tend to drift toward riskier assets, increasing volatility.
- While some rebalance frequently (quarterly or yearly), this can lead to unnecessary transactions and taxes.
- A more effective approach is opportunistic rebalancing—adjusting the portfolio when markets drop, increasing exposure to lower-priced assets.
- At minimum, investors should review and rebalance their portfolios two to four times a year.

Rule #9: Revisit the Plan

- Life changes—so should your investment plan. Reassess your portfolio annually or whenever a major life event occurs (e.g., a new job, inheritance, marriage, or retirement).
- Adjustments should be based on personal circumstances rather than short-term market fluctuations.
- Example: If an investor needs a 6% return but a bull market gives them 20%, they can shift to a lower-risk portfolio with a 5% return goal to reduce volatility.
- Staying flexible and making thoughtful adjustments ensures the portfolio continues to meet long-term financial objectives.

THE CONVERSATION CONTINUES IN OUR GROUP

We did it everyone! Remember this is about increasing our confidence and comfort when managing and building wealth for our families.