

Invest with your brain not heart for best chance at profit

Today I'm going to tell you a story about how a business professor said he would consider allowing my 14-year-old son to invest \$100,000 of his money.

This story provides a humorous insight into an investing mistake many investors make.

Several business professors and I were talking after lunch a few years ago and the conversation shifted to investments.

Those types of conversations most often concentrate on successful investments that have turned out to be quite profitable.

One of the professors made a lot of money based on an advisor's recommendation.

Of course, everyone wants to find that perfect advisor with the golden touch of knowing what investment to buy and when.

With the emotions of fear and greed influencing our investment decisions, a success story like this can trig-

ger the feeling of greed; that desire for us to want that windfall as well.

At that point I told them of someone I knew who had invested \$1 million and after just three months had made a profit of \$300,000. That is a 30 per cent return, which translates into a 120 per cent profit per year.

There was a great deal of interest in my story because there is not an investor out there who would not like to have that kind of profit.

The \$300,000 windfall is very misleading because there is the implied assumption that once you have made that kind of money it will happen again.

That is entirely wrong. If you are flipping coins and correctly guess getting five heads in a row, the next time you flip, you have an equal chance of getting either a head or a tail, regardless of your past success.

We understand how that works when flipping a coin, but when it comes to investing, that fundamental wis-

dom seems to escape us.

There is extensive research and manager past performance data proving that investing is often just a guess. There is no golden touch that consistently allows one investment manager the ability to just pick the winning investments.

Now back to the lunch conversation.

I asked a question. Who would consider giving the person in my story \$100,000 to invest? One professor volunteered.

That is when I told him the investor in this story was my son, a Grade 7 student. His assignment was to compete with other students, in a \$1,000,000 investment exercise.

In reality you would not give a 14 year old money to invest. Any investment success my son might have had in a school project does not translate into future chances of success.

As it turns out, that is what happens with the most seasoned investment manag-



Dollars & Sense

By Peter Watson

ers. One year they might do well and the next year they might fail.

Manager consistency is something that has gotten worse over the past several decades. There is significant evidence suggesting stock values are fairly and accurately determined by the market.

Therefore, there is no ability for investors or their managers to consistently beat the market; whether you are a 14 year old student or a well regarded investment manager.

You can try to outsmart the market but over the long-term you will not succeed.

If you want proof then examine your own investment returns over the last decade.

Or review the past performances of mutual funds.

Some years you will be successful and some years you will not.

So there is a moral to the story. Invest with your brain and not your heart.

Invest in an extremely well diversified portfolio. Have stocks from all parts of the world and in all types of industries.

Over the years the stock market has done fine. Take those returns and be content.

Try to resist the feeling of greed by picking the best stocks or the best managers and then the best time to invest.

Recognize misleading investment success stories for what they are. They are just stories.

Try to ignore the hype.

Remain focused on what is proven to work and build an extremely well diversified portfolio.

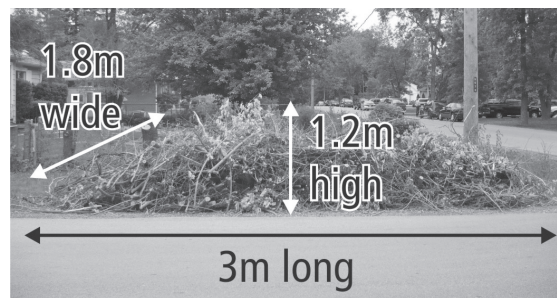
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