# Don't Succumb to Investing Road Rage
# If You Do, It'll Cost You


**I am sure it's a situation we have all experienced, driving along the road, minding your own business in a considerate and safe way when some lead-footed Hamilton/Verstappen wannabe hurtles past and cuts you up, probably driving the ubiquitous white van.**

Now however irritating and annoying that is, you know that by over-reacting and chasing this idiot to say your piece, road rage will, without doubt, not end well for you. You probably just honk your horn or mutter something colourful under your breath, but ultimately just continue on your way, driving in the same safe and thoughtful manner, to your destination.

So why don't many people adopt the same strategy when it comes to investing?

Oxford Risk, a provider of behavioural software for financial institutions undertook some research on the emotional reactions of investors. That research found that over-reacting to economic issues can actually make you poorer, and possibly quite a lot poorer in fact.

The research found that investors lose an average of 3% a year in returns to emotionally-driven investment decisions. The gap widens significantly in times of high volatility such as the recent Covid-19 pandemic.

During periods of high stress, investor losses can rise to about 6% or 7% a year from emotionally-guided investment decisions.

**Behavioural traits to avoid**

In addition, the company found there are behaviours that are common to many investors in volatile times.

During a crisis, investors are likely to focus too much on the present and on the detail, feeling compelled to do something even when doing nothing is the best solution.

They can gravitate towards the familiar, often leading to underinvestment, selling low or decreasing diversification.

Marcus Quierin, chief executive at Oxford Risk, pointed out the obvious, that many of these actions will mean investors turn paper losses into real losses.

The investments in the news are not your investments, so you should avoid watching the markets all day everyday as this will only increase anxiety to no useful end, and make you feel like you should be doing something, without any useful guidance to what that should be.

**Knee-jerk reactions and short-term thinking lead to significant losses**

Loss aversion is a risk for even the most experienced investor, said Greg B Davies, head of behavioural finance at Oxford Risk.

As previously mentioned, some investors are likely to focus too much on the present, rather than the long-term picture, and feel compelled to take action to mitigate short-term discomfort.

“Recency Bias” when it comes to investing, is the assumption that because an investment is underperforming it will continue to underperform, or that when an asset is outperforming, it will continue to rise in value.


This causes investors to sell underperforming assets when they are down, crystallising losses.

A compulsion to buy high and sell low costs investors 1.5% to 2% a year, compared with buy and hold strategies, the researchers found.

A desire to back products and services that feel familiar during times of uncertainty can lead to overexposure and under-investment, or investing in things that are widely popular and likely to be overpriced.

**Two decades of information**

Oxford Risk reached its conclusions about the role of emotions in losses, incorporating two decades of academic studies and economic data on investment.

Investors increasing their cash holdings due to uncertainty is a principal cause of investment own-goals, costing them 4% - 5% a year over the long term, Oxford Risk said. By sitting in cash, investors are buying themselves the ability to sleep better at night, Mr Davies said.

But as you can see, that emotional comfort comes at a price in annual lost returns due to these short term behaviours and emotional decisions in pursuit of that good nights' sleep.

Over a lifetime the lost returns from money sitting on the side-lines in cash mounts up; and investors make avoidable losses from timing mistakes such as buying high when times are good and selling low when times are bad.

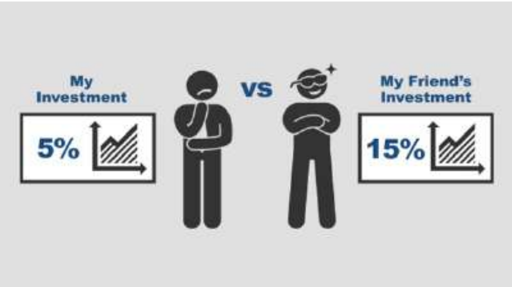
The most important thing is to have a plan and stick to it, in order to ensure that investors have both enough financial liquidity, such as cash on hand to ride out an uncertain time, as well as "emotional liquidity" to avoid emotional decision making.

"Losses are amplified when markets perform more badly because inevitably that's when our emotional response is at its strongest," said James Norton, an adviser at Vanguard UK.

The current global situation with rising inflation, increased interest rates, along with the energy price crisis, the lingering impact of the Covid-19 pandemic, and the

Russian invasion of Ukraine all add to uncertainty and often trigger these emotional responses that result in losses.

More than two out of five investors (41%) identified impulsive decision-making as one of their top three mistakes, followed by evaluating returns over too short a period (33%), and over-confidence (30%).




Other emotional mistakes include investors comparing their returns with other investors, or too much reliance on familiar investments.

Amazingly, as a complete opposite to how 99% react to careless drivers when in our cars, investing decisions are often governed by instinctive reactions to market fluctuations instead of being informed by pre-determined fundamentals.

**How to avoid investing road rage**

It is a recognised fact that private investors generally have lower returns than a long-term focused, considered, highly diversified portfolio.

A 2022 study by US-based independent investment research firm Dalbar found that the average equity fund investor earned over 10% less than the S&P 500 index, a benchmark for investments that is widely considered representative of the US stock market.

The investment process is riddled with pitfalls, and the human brain is not designed to take objective financial decisions or handle the complexities of financial markets.

It is not our nature to keep emotions at bay while making decisions, and attempting this would prove futile.

Instead, of embarking on ‘investing road rage’ and chasing the one that upset you, investing in the interests of your long-term goals, sticking to robust fundamentals, monitoring knee-jerk reactions, maintaining a diversified portfolio, reviewing the status of your investments regularly (but not obsessively), and working with a qualified advisor are steps that you can take.

All, of course, based on your specific tolerance for risk and knowledge of the market.

In this way you can avoid the losses accrued by emotional decisions, continue to drive towards your financial destination in a safe, considered way and not be concerned by the occasional appearance of 'white van man'.