

Instinctive Behaviors That Can Sabotage Your Financial Goals

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One of the biggest challenges to our own success can be our own instinctive behaviors. Doubts, procrastination, fear of the unknown, trying to plan for every contingency, and overthinking are instinctive coping mechanisms that can delay action and prevent us from starting the processes that are the keys to our success.

The goals that are the most important to us – including important financial goals - can be the hardest to start working toward, because of the fear of failure: what if we're not good enough, make bad decisions, or otherwise are not able to accomplish our goal? Emotionally charged activities that we really care about can be the hardest to start because the outcome matters so much. While not starting reduces risk, it also guarantees failure, or, as Benjamin Franklin put it, "By failing to prepare, you are preparing to fail."

When these instinctive behaviors come into play, they can keep us from reaching the goals that matter the most. From the standpoint of financial goals, consider the fact that males born in 1985 and retiring at the age of 67 can expect to live for an additional 19 years and therefore need to fund nearly two decades of retirement. Females will need to fund 22 years, according to the Social Security Administration life expectancy calculations¹ and, with advances in medicine, those numbers are likely to increase even further. Successful funding of 19 to 22 years of retirement (as an average) is more likely to occur if not deterred by instinctive behaviors that prevent us from starting early and reaching our financial goals.

One of the keys to success is recognizing and changing the things that interfere with our success. Identifying and understanding how we feel about money and what impact instinctive emotional behaviors have on our financial decisions may be just what is needed to propel us to action.

Here are 9 common instinctive behaviors that can sabotage financial goals.

1) Responding to Markets Out of Emotion

Instincts do not always point us in the right direction, especially when strong emotions, such as fear or greed, are a factor.

Fears can range from fear of losing our investment money to a fear of the unknown.

For instance, Individual investors often buy high, then, when the investment starts to adjust and the price falls, panic sets in and they sell low, so as not to incur further losses.

An overly cautious investor may try to time the markets and buy only when prices are low or taking off, and therefore end up sitting the sidelines during a market rally. This strategy can also result in buying lower quality investments.

Investors who are fearful of the unknown may be drawn towards investments in lower risk vehicles, such as fixed income. When this occurs more money is required to reach your goals, rather than creating a balanced portfolio of both fixed and variable investments.

Greed, too, can be an emotional driver when it comes to investments.

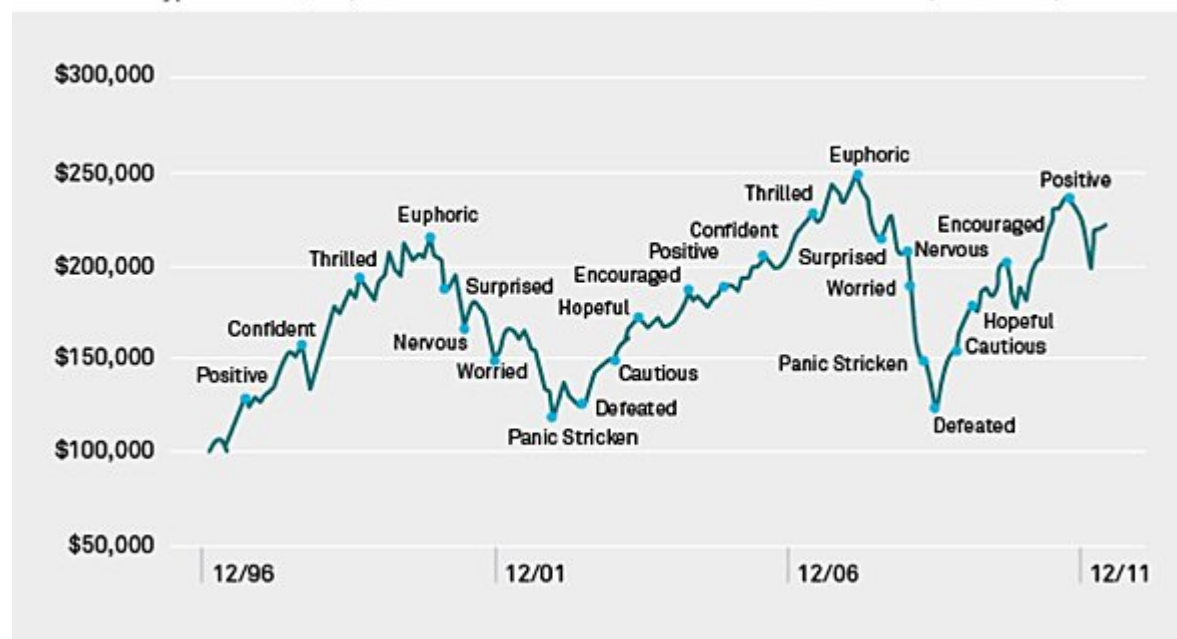
When your neighbor or co-worker brags about how much money she has made in the market with a “hot stock pick,” it can be tempting to run out and buy shares, hoping for similar returns. When an investment is going up quickly it’s a natural instinct to want to jump in and buy so you don’t miss out on the gains but, as we all know, there are no guarantees it will continue to perform on that level. This strategy can lead to buying high.

Greed can also result in holding positions too long. Selling an investment that is having a great run might seem counter-intuitive, but may be the right decision based on your goals. The markets adjust on a regular basis and that may mean a solid performer might take a turn downward when markets correct.

How do we prevent our fears and greed from leading to bad investment decisions? Education and understanding how markets work and how risk impacts return on investments will help mitigate fears and help us make sound financial decisions based on research rather than emotion.

Staying focused on long-term goals and the parameters of each investment will help maintain focus and stay the course when market corrections occur. The graph below shows our natural emotional cycle as investments fluctuate over time. Understanding that all variable investments will go up and down will help you stay on course. The overall goal should be to have an investment that is trending upward - as a whole - over time, not an investment with no downward movement. Only CD’s and other fixed, low return, investments have a lack of downward movement and often they move upward at a pace that trails inflation, creating a different kind of risk.

Growth of a Hypothetical \$100,000 Investment in the S&P 500 Index Over 15 Years (1997-2011)



<http://static2.businessinsider.com/image/51a90538ecad04ef4f000019-616-354/emotions-money.jpg>

Investing at regular intervals, preferably automatically, at the market price means that, when the share price dips, more shares will be purchased and, when the price is higher, fewer shares will be bought, which may be a good way to truly “buy low.” Of course, you should consider your financial ability to continue such purchases through periods of lower and higher price levels.

Creating an investment plan based on well-researched products, taking into account your risk tolerance and financial goals, will help take some of the fear out of investing. This will allow you to make decisions based on sound practices rather than the emotional roller coaster the markets can produce.

2) Money and Its Connection With Your Identity

Money can produce powerful emotions that frequently have roots in childhood. These emotions and triggers influence the value we place on money, how we feel about money, and how it defines us. Understanding our financial and spending triggers can go a long way to helping us understand the connection between our emotions and our spending behavior.

The National Foundation for Credit Counseling completed a survey that revealed that 44% of Americans learned their financial habits from their parents.³ The challenge is that much of those learned financial behaviors are not positive and often come with negative feelings that include anger, guilt and shame.

Having our sense of self attached to our income level, for instance, can lead to overspending, as we try to show others that we are successful. In other cases, spending might create a sense of guilt that results in binge spending or an inability to stick to a budget. If we have been taught to save and sacrifice, for instance, we might feel uncomfortable spending anything on ourselves and, instead, try to make others – such as our children or partner - happy by overspending on them. Our spending patterns, alternately, might be to reward ourselves because we feel we deserve it.

Emotions about money and finance can have a large impact on how we spend, save, invest, give, receive and manage money. It can dictate what car we feel the need to drive, what neighborhoods we choose to live in, the clothes we wear, and what electronic devices we define as must-haves. It also has a large impact on our willingness and desire to save and invest in the future. If we saw our parents lose their life savings in the market, for instance, we may be more risk averse than if our family's investments performed well.

“Only when we come to terms with our preconceived beliefs about and emotional attachment to money can we achieve inner peace and be on the road to financial

freedom.”⁴ writes Sherry Shoemaker, about the importance of connecting emotions with particular money habits. If we can connect with these emotions and how we feel about money, we can create positive influences and establish new patterns for our own family. Only when we are not spending money as an emotional reaction, are we free to budget and save based on our goals rather than our emotions.

When you see money as a tool or means to reach financial goals, it takes on new meaning. When this happens you are no longer defined by the money you earn; instead it will work for you as you set and reach personal and family goals. Whether you want to plan for a big vacation, improve your education, or save for retirement, each objective has a financial element that must be met in order for the goal to be reached.

Finding the balance between spending - which covers today's needs; paying down debt - which covers yesterday's spending; and saving for your future - which pays for tomorrow's needs, may bring peace and reduced stress. Understanding what triggers spending (pleasure, guilt, security, etc.), can help you make better financial decisions, control spending, and ultimately allow money to be a vehicle for reaching the goals that are most important to you.

3) Not Partnering With A Spouse or Significant Other

Your spouse or significant other can be your most important financial decision. Understanding how they feel about money, and spend or save money, will have a significant impact on your relationship. The ability to talk about finances and financial decisions and trust each other to work toward common goals can help build a stronger relationship. On the other hand, a partner who spends without communicating, and does not involve you in financial matters can be a warning sign. When 100 experts were polled about the causes of divorce, finances and not having a shared vision for success were among the top ten reasons couples divorce⁵.

Both partners should be involved in financial decisions particularly when it comes to taking on debt, investments, estate planning and other matters that will impact the long term financial health as a couple or family.

Look for red flags when it comes to finances. How does he/she spend money? Are they thinking about and planning for the future or only considering today? Are spending and savings habits consistent? Talking about money, financial goals and spending patterns can also help partners understand the best ways to reach goals.

“According to a report released last month from UBS Wealth Management Americas, you might be more confident and satisfied with your finances if you share responsibility for them with your partner.”⁶

It's important to partner with your spouse to reach financial goals. If you are both working towards a shared vision for the future that is supported by common goals then it is easier to stay in track. This also creates a support system where you help each other keep sight of your long-term financial goals. Without that, it is easy to let the daily

sacrifices or, worse, one partner straying from the shared plan, lead to resentment and a breakdown in communication.

Taking the shared approach will generally lead to less fights about money and a better understanding of current financial goals and challenges. Regardless of what the financial goals are or what the current financial status for the family is, working together will lead to greater satisfaction and greater success than going it alone.

4) Not Establishing a Strategic Financial Plan: A Planner or Spontaneous?

In the story of Alice in Wonderland, Alice is traveling along a road when she comes to a crossroads and has the following exchange with the Cheshire cat:

"Would you tell me, please, which way I ought to go from here?"

"That depends a good deal on where you want to get to."

"I don't much care where –"

"Then it doesn't matter which way you go." ⁷

Financial plans may seem like that crossroads in Alice in Wonderland unless we have a specific vision of where we want to end up and the flexibility to continually self-correct to make sure we're still heading in the right directions.

Most people tend to gravitate toward one or two personality traits - planning or spontaneity – both of which can hinder our ability to make realistic commitments to achieving our financial goals.

Planners are more likely to strictly manage time, set strict budgets, and maintain rigid rules around spending and saving. They set clear goals and planning for things like retirement and college come naturally. The challenge for planners is that their investments generally don't go like clockwork. Most investments will not have consistent or guaranteed returns, which can be frustrating when their carefully laid plans don't have the desired results. And it can be difficult for planners to change course when circumstances suggest it is time to change plans.

More spontaneous people, on the other hand, may find it difficult to remain focused on a long-term goal that is 30 years or even more in the future. The idea of setting up a logical system that must be strictly adhered to when life is not neat or strict can be difficult to commit to. This can lead to procrastination and delays, and have serious consequences as retirement comes into full view.

The first item of business for any investment strategy is setting a specific goal that is measurable and time-specific. "Lots of money for retirement" is not enough of a focus to help us weather financial challenges, such as mortgages or kids who are asking for money to meet their latest must-haves.

The more specific the vision the better. What does retirement look like? Does it involve lounging on the beach with our favorite cocktail, a daily round of golf, finally writing

that novel, or being able to volunteer time with an international charity? Having a clearly defined personal vision, whatever it is, motivates us to stay on track. The same strategy of clearly defined goals should be used for college funds, vacation planning, and any other worthwhile goal.

Planners will have an easier time setting specific goals with actionable steps. The challenge planners face is in staying the course when the numbers change or unexpected events occur. If one part of the portfolio is over performing there will be the temptation to move everything to the successes. If a particular component is underperforming the temptation is to sell it all when it's down.

Realizing that fluctuation is built into the allocation is why diversification is so important. Keeping focused on long-term goals and the overall portfolio performance, rather than zeroing in on one specific piece will help planners stay the course. And consulting a good financial advisor is important when it comes to evaluating whether your current plan could use some adjustments or reallocation.

Spontaneous investors will have a much harder time actually setting the goals and sticking to a strict plan. Fortunately there are many roads to a happy retirement and not all of them involve living on a strict budget. Consider automating the process: automatic deductions from your paycheck will fund long term goals while still leaving other funds that can be spent without such detailed planning.

If it's too overwhelming to think about setting aside 6 months' worth of money in the bank, set a goal to set aside one month in savings over the next 3 to 6 months. Then determine an action plan that will reach the goal. Looking over the budget to reduce expenses will help to create a plan that will successfully accomplish the goals.

Whether you are a planner or more spontaneous, recognize that there is a happy medium and that a financial planner can help you see where your impulses might be preventing you from making changes that will allow you to more successfully reach your financial goals.

5) Complacency: Not Reviewing and/or Adjusting The Plan on a Regular Basis

Once a plan is in place and automated there is the temptation to set it and forget about it: to let the investments do their thing and pay more attention to your busy life and work and family obligations than to that monthly investment report in your inbox.

Life happens, though, which can lead to changes in both long-term goals and the ability to meet the goals already in place. Periods of unemployment, illness, or any number of events can create a need to reevaluate the strategic plan. Changes in employment, family size, health of family members, and other - often unforeseen - events can change financial goals over time. It may be necessary to alter contributions to various goals or adjust expectations or timeframes. A regular review of your strategic plan and making adjustments early will help you remain on track.

Most employees no longer work at the same place for an entire career, for instance. Often benefits must be obtained through individual plans and we have become primarily responsible for our own retirement. These changes have altered the landscape for financial investing along with expectations of both employers and employees.

Reaching investment goals is like following a flight plan. Even being off by a little bit, over a long period of time, can have a dramatic effect on our success rate. At the same time, when adjustments are made early, those small changes can lead to large results over the course of a few decades.

Increasing contributions in small increments will make a surprising difference to the overall investment goal, while only reducing disposable income by a small amount. Consider that 5% of a \$50,000 paycheck that is received weekly is around \$48. Raising that to 6% reduces gross income by less than \$10 a week. At a 6.5% return on investment, with all other things being equal, this small increase will add nearly \$20,000 over a 20-year investment timeframe. Small things matter, when it comes to long term investing.

If, on the other hand, you need to decrease contributions to a retirement account in your twenties or thirties, you will still have a few decades to recover, whereas a period of lower contributions in your 50's would require a much larger adjustment because the timeframe is shortened. In that case you might find yourself working for additional years to remain on course or living a very different retirement.

Too much complacency and not enough attention can have a dramatic effect on how successfully you achieve your goals. Have your advisor review your investments and investment rate with you frequently to make sure you are on track.

6) Not Using Tax Efficient Accounts Due To Anxiety about Taxes and Penalties

Tax efficient accounts are available for long-term financial goals such as retirement, college savings and health care savings. These accounts can offer tax-free or tax deferred growth depending on the type of account selected. This can have an impact on taxes today and taxes down the road, providing higher effective returns.

Tax-deferred accounts generally offer a tax deduction today and then grow tax deferred. This means taxes will not be paid on the growth until funds are withdrawn. Using this strategy can result in lower taxable income today and lead to a high effective return because income is not taxed each year. It also provides the ability to invest more funds in the account today due to the immediate tax savings.

Tax-free accounts, on the other hand, generally do not offer a tax deduction when a contribution is made, but then grow without any annual tax obligation. When funds are withdrawn, as long as the IRS rules are followed, no taxes will be owed.

Unfortunately, for some investors, anxiety can play a large role in influencing behavior in two important ways when it comes to taxes and retirement accounts.

The first is due to anxiety surrounding the power of the IRS. With the large number of complex rules that must be followed and the high tax consequences for non-compliance, investors are often anxious about taking advantage of these tax-efficient accounts.

The other fear is that we might need the money sooner than the magic age of 59 ½, resulting in both taxes and a penalty for accessing funds early.

The key to alleviating concerns about the IRS is through education and working with a financial advisor who really understands the ins and outs of each requirement. This will allow you to safely take advantage of the tax benefits without fear of triggering an audit. The best way to avoid anxiety about the potential need for early withdrawal is through creating an emergency fund with investments in to short term vehicles that will enable money to be available when unexpected events happen.

Over the last several years, new tax-advantaged accounts have become available in an effort to help individuals save money for long-term financial goals. Working with an accountant or tax adviser will help to determine which options are best based on goals and long-term needs and consulting with a tax professional will provide updated rules and details of how each account works.

7) Risking Too Much by Investing Without a Thorough Risk Assessment

Risk – and risk tolerance - is not always easy to understand and evaluate. As a result, it's easy to be overwhelmed as you try to determine which risks you are comfortable taking. Emotions surrounding risk can lead to either procrastination or taking on an inappropriate amount of risk. Setting aside emotions and looking at data is the appropriate way to assess the risk of each investment you are considering.

According to Investopedia, risk is defined as:

“The chance that an investment’s actual return will be different than expected. Risk includes the possibility of losing some or all of the original investment. Different versions of risk are usually measured by calculating the standard deviation of the historical returns or average returns of a specific investment. A high standard deviation indicates a high degree of risk.”⁹

When selecting an investment, understanding the risk is important because, if you can obtain similar returns on investments that carry less overall risk, those investments will provide greater stability. Risk should also be partnered with diversification, which means capitalizing on various investment classes with the goal of reducing the overall risk of a portfolio.

An investment advisor is a good partner when it comes to selecting specific investments that will take into account the risks associated with each investment and your own risk tolerance, as well as enable you to make sound financial decisions about our financial goals.

8) Addressing Your Finances Without a Holistic Approach

Financial planning is more than just planning for retirement and leaving money for heirs. Good financial planning addresses all your financial goals, whether it is planning for a dream trip, putting children through college, upgrading your home, caring for elderly parents, or preparing for life's contingencies without using up your financial reserves when unexpected events occur.

Taking a holistic approach to financial planning means working to meet all your life goals through careful allocation, management, and planning. Holistic financial planning includes reviewing insurance needs, everything from health insurance, life and disability insurance, to coverage and deductibles for home and car insurance. In addition to insurance, estate planning is essential. This provides for loved ones in the event of an early death. Estate planning can also pave the way for gifting, caring for minor children and ensuring our spouse is well taken care of financially.

Looking at the big picture or thinking about getting older, however, can be intimidating and overwhelming, however, which can lead to procrastination, avoidance, or tunnel vision.

While it may be intimidating, taking a holistic approach and covering all of the areas that impact your finances will give you greater control over your future and will help you care for your family with greater confidence.

A good financial planner can ease that sense of being overwhelmed or intimidated by looking at the big, holistic picture. A planner can help break it down into smaller goals that are easier to digest, and emotionally easier to handle.

9) Trying To Go It Alone In An Effort To Maintain Control

Control over our circumstances, and our lives, is a powerful emotional motivator. While everyone has a different level of need when it comes to what they control, financial goals are an area where trial and error is never the best method.

When you go it alone you give up professional advice from those who have navigated these roads. You also do not build a support system that will answer all of the legal questions and investment questions that come up in the process of establishing a strategic plan. Investing in your future is not a static exercise that is only done once - it will change over time as circumstances change. There are a lot of moving parts to financial planning and having the right partners will increase your chances for success.

Working with trusted professionals offers you a more direct path to reaching financial goals and will eliminate the trial and error approach that can result in costly investment losses, inadequate insurance, or other expenses that can take years to recover from.

A good financial advisor has a wealth of experience and can help guide you through the minefield of investment options.

Finding someone to work with when you don't have large assets or high income can be a challenge for Millennials. Seasoned advisors often want \$500,000 to a million dollars in current assets to qualify for their services, but how are you supposed to accumulate that wealth without guidance from the beginning?

Sherman Wealth advisors specialize in working with Millennials and understanding your needs and challenges. With a no-cost initial consultation, meeting with an advisor is a low-risk proposition. Bring your vision for the future and let us help to create a plan designed to help you achieve your vision of success.

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Resources

¹ <http://www.goodreads.com/quotes/460142-if-you-fail-to-plan-you-are-planning-to-fail>

² <http://www.ssa.gov/planners/lifeexpectancy.html>

³ <http://www.moneymanagement.org/Community/Blogs/Blogging-for-Change/2012/June/Study-reveals-who-really-influences-the-financial-behavior-of-children.aspx>

⁴ <http://abouther.pwbn.org/understanding-your-emotional-connection-to-money/>

⁵ <http://www.yourtango.com/experts/yourtango-experts/top-causes-divorce-expert>

⁶ <http://money.usnews.com/money/blogs/alpha-consumer/2014/05/09/couples-are-happier-sharing-money-decisions>

⁷ <http://www.goodreads.com/work/quotes/2933712-alice-s-adventures-in-wonderland>

⁸ <http://www.abc.net.au/radionational/programs/ockhamsrazor/mount-erebus-plane-crash/3387448>

⁹ <http://www.investopedia.com/terms/r/risk.asp>

¹⁰ <http://finance.yahoo.com/blogs/the-exchange/half-americans-set-die-without-193140015.html>