KALEXIS GROUP

How losses play on your "Mental"

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Have you ever said something like, “I would never even think about running a person over while driving.”? Or maybe you judged someone that has seemingly lost all rationale when it comes to their mate. “What is he thinking? I can’t believe he is so blind!”. We’ve all said there are things we would never do but reality can be harsh. When you listen to a person during an interview, a lot of times they will say, “I never thought I would do something like that. I don’t know what got into me!”. These are situations where emotions overtook logic and rational thinking.

Investing can be very emotional because it deals with money and money has relevance to every part of our lives. We understand the things money can buy and the freedom money brings. When an investor loses a relatively small portion of money, it translates to the lost of a vacation, clothes, mortgage payment, college tuition, car note, and other things. This is why investing can bring out irrational emotions and cause an individual to make poor financial decisions. Money is usually tied to our hopes and dreams in life. Can you think of something you want to achieve in life that doesn’t involve money in some capacity?

There is a solution to not becoming so emotionally tied to any stock or investment. First, we must understand that losses will occur. If we know this fact at the beginning, we should plan for those losses and try to minimize them. The most important thing to do when investing, is to only use money that you can lose. Do not use all your life savings, kids' tuition money, or mortgage payment. You must think to yourself, if I lose every penny of this money will it impact my way of life.

I've had the opportunity to work with many investors and the first thing we talk about is the effect the money will have on their way of life. Many times, the money they invest is just sitting dormant or money they would "blow" on something they don't need. In this case, we would plan an investment strategy. Then there is the occasional investor that says, I need to "flip" this money because I lost my job, and this will help pay my bills. In this case, the investors fear of not having income has kicked in and their emotions are causing irrational decisions. This person must understand that investing has a downside and the lost of this money would be detrimental to their livelihood. So, stop, don't pass go (I know, it's a terrible joke but just laugh to boost my ego). Don't ever invest while in a state of survival.

As mentioned before, the next thing that can help avoid emotional investing is to have a solid plan. We must understand every aspect of the potential trade. The maximum potential loss, the probability of loss, maximum gain, and timing of the trade are all important. However, the most important aspect of the trade is to know the exact price you will exit the trade, both profit and losses. If your loss hits a certain point, know your plan of action. This could be to purchase more, sell what you already have, or place “insurance” to cover any further losses. If you hit a profitable price, will you sell for the profit, buy more, or just keep the stock in hopes of it continuing to rise in value. Plan while you’re thinking rational so it can be executed no matter your future mental state.

Investing doesn’t have to be an emotional roller coaster. Be able to learn from the losses without stress and enjoy the profits while on the ride. Just like everyday life, timing is everything when it comes to investing. Make sure to never sacrifice funds needed to survive in order to invest and make a solid plan for every outcome of the investment. If you start with these two rules, investing becomes a lot easier and less stressful.