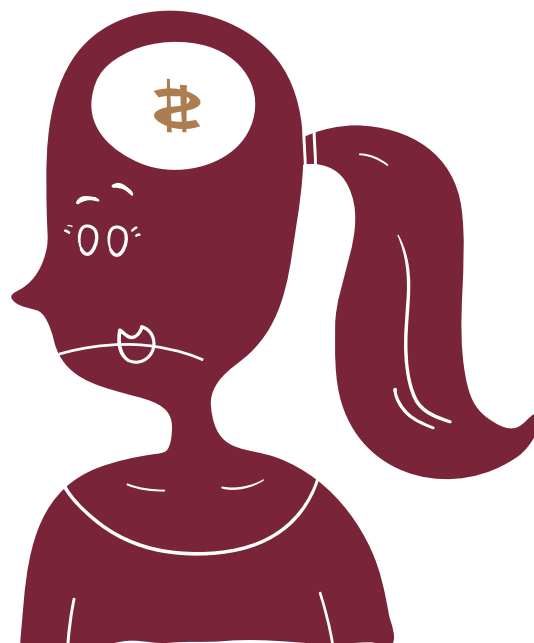


DO-IT YOURSELF: INVESTING DANGEROUSLY

by Marvin L. Barron III, CFP®



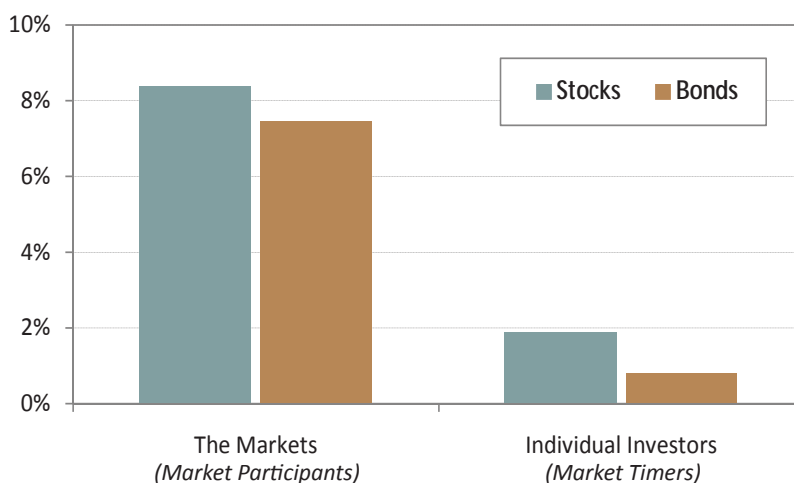
Spring is here! My favorite time of year. The NFL draft is next week, the Phillies are defending their title, and Dalbar, Inc. has just published its annual *Quantitative Analysis of Investor Behavior* (QAIB for short). This is the stuff dreams are made of. Well, my dreams anyway.

The QAIB is great because Dalbar has the best data on the behavior of individual investors. In particular, they are able to study the flow of money into (and out of) mutual funds over time. This allows them to re-create the average investor's portfolio and simulate it over time.

With this information Dalbar compares the average investor's portfolio with the actual market returns. That tells us whether or not individual investors have been making good decisions in moving their money around. It's like a yearly reality check for market timers (who move money from one mutual fund to an-

other) and market participants (who just keep chugging along). The results aren't pretty for the timers.

Average % Return per Year (1989-2008)



Two observations jump out of this chart:

First, it's been a close horserace between stock and bonds.

Over the last twenty years, bonds and stocks have deliv-

ered similar returns. Despite being mostly useless, this statistic has gotten loads of press. Of course bonds can be competitive – therefore we usually own both stocks and bonds. However, we have no reason to think that this is normal. We can only say this now that the stock market has tanked. Observations like this are good at making us feel bad, but are worthless for doing useful work (like predicting when bonds will be competitive before it happens).

Secondly, the jockey can make any horse look bad.

The gap in “stocks versus bonds” is tiny compared to the gap in “market participant versus market timer.” The gap between stocks and bonds was about 1% per year, whether you were a market timer or a market participant. However the gap between market timers and market participants was more than 6% per year, whether you were a stock investor or a bond investor.

To put that in perspective, at 1.3% per year (the average of what the stock and bond *timers* got), it takes 54 years to double your money. At 7.9% (the average of what the stock and bond *participants* got), it takes 10 years.

What’s going on? The QAIB hints at one reason. Individual investors hold onto a mutual fund for three years, on average, before switching to something else. Their timing couldn’t get much worse. The average credit cycle lasts seven years.

Why do they do it? Who knows? Most likely they saw another investment fund performing better than the one they owned, and they chased it. I’m guessing that these same investors don’t smash their light bulbs after ten hours of daylight, or burn their mittens after five months of warm weather. But they seem to systematically change their investment strategies halfway through the credit cycle.

The field of behavioral finance has launched careers in discussing why so many investors have this particular blind spot. It’s a topic I’ve covered in this space, many times. However, behavioral finance has little to

say about the role of the financial media in promoting such a short-term mindset. As useful as the QAIB is, you’ll never encounter it on cable news or read about in a popular financial magazines.

It’s unfortunate, but that’s how it goes. Your butcher doesn’t talk about cholesterol, your bookstore doesn’t issue library cards, and the IRS has never once accused anybody of overpaying.

In these cases, we know to be on guard (especially with the IRS). However, it is easy to forget that the financial media makes money by selling ads, not by improving our lives. This may not be in the strict realm of behavioral finance, but spending your hours watching CNBC might just be the most costly mistake of all.

TGS FINANCIAL ADVISORS PRESENTS **SPRING EDUCATION SERIES**

We’re excited to announce the following upcoming events as part of our *Spring Education Series*:

Retiring After the Market Crash

How Much is Enough? What Should I Do Now?

Thursday, May 14th @ 12:00 p.m.

Tuesday, May 19th @ 6:00 p.m.

Doctors: The Retirement Alternative

What delaying retirement for two years could do for your portfolio and your life

Two sessions in June to be announced

How We Got GREAT Jobs

Sunday, August 2nd @ 2:00 p.m.

All events will be held at our Radnor, PA office and will be limited in size. We will schedule additional meetings if needed. All events are open to our clients and their invited guests. Invitations will be mailed and e-mailed shortly. *To reserve your spaces, place call Shauna Mace at (610) 892-9900 or e-mail her at shauna.mace@tgsfinancial.com.*