

RETHINK THE WAY YOU INVEST

PRESENTED BY

THE F. DANIELSON GROUP
ASSANTE FINANCIAL MANAGEMENT LTD.

Eight Common Investment Pitfalls

WRITTEN BY KEITH MATTHEWS

PRESENTED BY FRANK DANIELSON

Keith Matthews
Partner & Portfolio Manger
Tullett, Matthews & Associates
www.tma-invest.com

Frank Danielson, B. Ed, CFP
Senior Financial Planner
Assante Financial Management Ltd.
www.frankdanielson.ca

An excerpt from the National Best Selling Book, *The Empowered Investor: A Guide to Building Better Portfolios* by Keith Matthews (www.empoweredinvestor.ca).

In our quest for a prosperous and financially secure future, we must first review the potential roadblocks that could prevent us from succeeding. All too often, investors rush to implement a solution or buy an investment hoping that it will fill the gap created by previous portfolio hiccups, shortfalls, or downright mistakes. The desire to act and to fix our immediate investment concerns may be quite valid; however, short-term adjustments usually do not result in any meaningful long-term impact. If the winning strategies are to pay off in the long run, investors must be aware of the pitfalls that can await the unsuspecting *before* putting those strategies to work. An awareness of the rules of the playing field will save you a lot of headaches down the road—and can dramatically lengthen your odds of future success.

These common pitfalls trap both beginners and experts alike. As we will see, many of these errors or slip-ups are caused by our emotional ties to money. Family finances, investment portfolios, and personal assets are highly fraught subjects. They conjure up the most basic human feelings of security and our desire to “make it” in life. Add to that the rollercoaster effect of stocks, bonds, and currencies and we may find ourselves living with portfolio decisions that, in hindsight, we deeply regret.

Furthermore, thanks to the brave new field of behavioural finance, we have now become aware that, as individuals and humans, we have a set of biases and filters that can cloud our financial judgment, leading to poor decisions about when to buy or sell stocks, bonds, and other financial assets. While some of these biases—such as high levels of confidence—are very positive attributes in just about everything else in life, having too much confidence or “bravado” as an investor can lead to making poor portfolio decisions.

So what is the real value in reviewing these common portfolio pitfalls? First and foremost, simply becoming aware of them can help you avoid big, costly mistakes. It will also provide you with a foundation on which to base your understanding of the value of the winning investment principles discussed later in the book. Being aware that investment pitfalls exist can empower you to stay clear of them.

More experienced investors may feel they are already aware of the pitfalls and biases that can be detrimental to a portfolio; however, I highly recommend completing an annual review of the eight common investment pitfalls in conjunction with your portfolio review. Constant vigilance has tremendous value. I can’t count the number of times I have met very serious and smart investors who have told me, “I did everything right for ten years, and I know all about investment pitfalls, but last year I let my emotions drive me to do something foolish—and it really set me back!”

Pitfall 1: Lack of an Investment Plan

The lack of an investment plan is at the root of many of the challenges that investors experience. A good investment plan maps out your long-term investment objectives, time horizons, diversification decisions, tax consequences, investment philosophy, decision process, and finally, the risks associated with your plan. Some investors have no plan whatsoever; they attempt to be opportunistic and to buy investments “when they are a good deal.” Others have a plan but deviate from it as time goes on. Either way, when I speak to investors who have experienced difficulties with their investments, are frustrated with or confused by the direction of their portfolio, or are having a hard time understanding the big picture, I often find that they do not have an

investment plan. A good investment plan highlights how all the moving parts work together and will make you aware of your overall investment strategy.

By taking action and creating an investment plan, you will understand more about how markets work. This will allow you to become better informed about the relationship between returns, risk, and time horizons. An investment plan is such a key component of success that I never work without one. We work with plans when we build our dream homes or cottages; successful entrepreneurs and business owners often have a vision and a plan; companies and successful organizations also have plans—so too should our investments.

Pitfall 2: Not Aligning Your Investments with Your Personal Objectives

To achieve success, it is critical to align your investments with your personal objectives. Unfortunately, as obvious as this may seem, many investors do not match their investments to their objectives and may even have investments that work against their objectives. This mistake is a direct consequence of not having an investment plan.

For example, an investor may have a long-term horizon for retirement but an investment portfolio that is heavily concentrated in short-term government bonds or GICs. This can place the investor at significant risk later when he needs to liquidate assets to finance his lifestyle. The investor runs the serious risk of outliving his money because he has focused on the preservation of capital and short-term volatility in equity markets rather than on his long-term investment horizon and the best assets to use for this investment objective. In this case, his assets will not generate adequate investment returns over inflation—which he needs to preserve and grow his buying power over long

periods. As a consequence, the investor simply will not reach his goals.

On the other hand, it is not at all unusual to see an investor with a very short time horizon (five years or less) investing in equities or perhaps even speculating in an attempt to grow her money over a short period. Making it even worse, investors who slip into this habit tend to buy into momentum or story stocks “at the top.” Assets that need to be sold may be subject to significant market volatility or stock correction. This mismatch of investment and time horizons can be absolutely devastating if things go wrong.

Pitfall 3: Miscalculating Your Investment Time Horizon

How long will you live? How long will your spouse live? Is there a large age difference between you? All too often, investors miscalculate their true investment time horizons. For whatever reason, many investors are pessimistic about their life expectancies and have not positioned their portfolios for a longer lifespan. Over the last few decades, however, life expectancies have been increasing, as have lifestyle expenses such as long-term care and other health-related costs. Many Canadians run the risk of depleting their investment savings because they did not plan for a longer lifespan on an asset allocation and cash flow basis.

Another type of miscalculation occurs when investors planning for retirement confuse the start date of their retirement with their true investment horizon. For example, fifty-year-olds planning to retire at age sixty-five may think the time horizon for their investments is fifteen years. However, we know that you do not wake up at sixty-five and switch an entire asset mix to bonds and GICs—

given that you may have up to twenty additional years that will need to be financed. So the fifty-year-olds in this example really have time horizons of thirty to thirty-five years.

Calculating the right investment time horizon is equally important for those Canadians who will be passing assets on to the next generation. Time horizons at that point can become much longer than originally thought. Although calculating your time horizon appears to be a very straightforward exercise, it is quite common to fail to recognize its true length. The good news is that, once investors are made aware of it, this pitfall is probably the easiest to correct.

Pitfall 4: Trying to Profit by Timing the Market

A recently-released study of American investors by Dalbar—one of North America’s leading financial-services research firms—has rocked the industry. Dalbar tracked aggregate cash flows in and out of mutual funds on a monthly basis from 1987 through 2006 and came to the following dismal conclusions:

- ◆ The average U.S. equity investor earned 4.3% annually, just above the rate of inflation of 3.0%, but falling far short of the 11.8% the S&P 500 earned over the last 19 years.
- ◆ The average U.S. bond investor earned 1.7% annually, compared with the long-term government bond index of 8.6%.

It is worth noting that these rates of return are before taxes, commissions, fees, and transaction costs, and were tracked in a period that included one of the best bull markets in history. As one

financial journalist noted dryly, “Investors would have been better served to hide their money under the mattress.” While it is important to recognize that these numbers represent the *average* investor (the numbers can be skewed by a minority of investors who make disastrous choices), the fact remains that the news is not good. What went wrong?

The Dalbar study identifies market timing as the chief culprit. Market timing is the strategy of deciding to buy or sell financial assets (often stocks) by attempting to predict future market price movements. The prediction may be based on an outlook of market or economic conditions resulting from technical or fundamental analysis. This is an investment strategy based on the outlook for an aggregate market, rather than for a particular financial asset (Wikipedia 2007).

Investors are human, after all, and instead of sticking to time-tested, winning strategies based on diversification and long-term asset allocation, we sometimes chase the pot of gold at the end of the rainbow, no matter how often that strategy has been shown to fail.

And then there is the “fear factor.” World events or media frenzy, rather than economic reality, can drive panicked investors to sell. After 9/11, anxiety spurred investors into a wild selling spree that saw the markets crash for several months. And in the fall of 2007, global equity markets were hit hard by the effects of the sub-prime crisis in the United States. Only time will tell how the latter plays out, but I expect that investors will buy and sell stocks at times that will not add real long-term value to their portfolios.

In an article in the *Journal of Financial Research*, Larry L. Fisher and Meir Statman analyzed various market-timing models. The study presumes that investors might want to time the market using

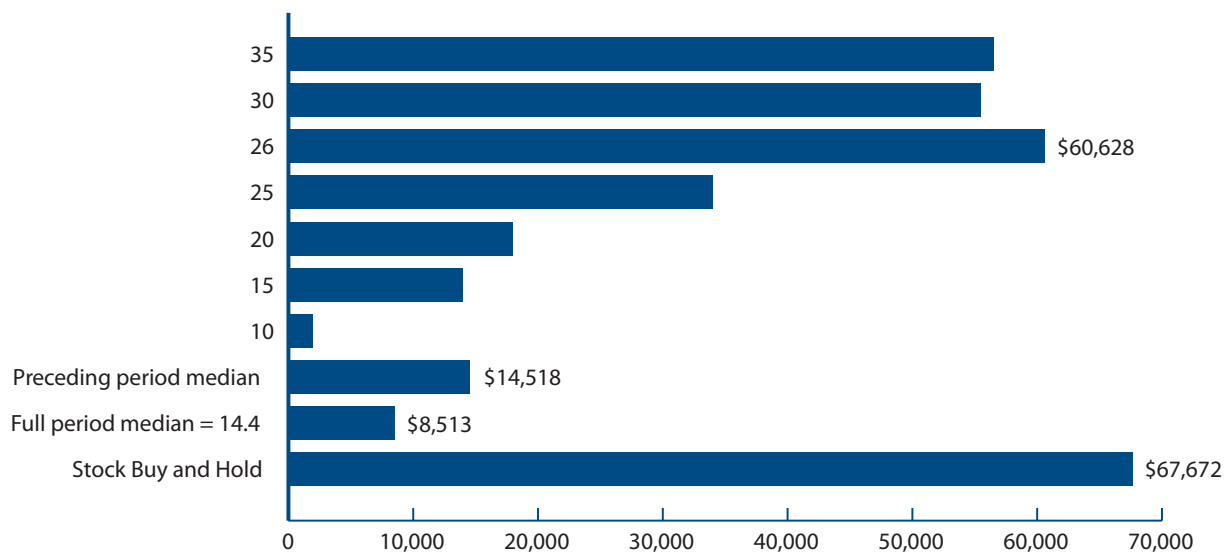


Figure 1: Market Timing Falls Short

Market Timing with P/E Trading Rules: United States 1871–2002. Trading rules: Investors have \$1 at the beginning of 1871 and that money accumulates over time as it is invested in stocks or T-bills. Investors switch from T-bills to stocks when the P/E ratio is lower than the P/E ratio in the trading rule and back to T-bills when it is higher. For example, the trading rule associated with a P/E ratio of 26 calls for switching from T-bills to stocks when the P/E ratio is lower than 26 and back to T-bills when the P/E ratio is higher. The study examined trading rules with P/E as integers from 5 to 40, but we report only some, including the one with the highest accumulation.

Source: Kenneth L. Fisher and Meir Statman, “Market Timing in Regressions and Reality,” *Journal of Financial Research* 29, no. 3 (Fall 2006): 293–304

some basic assumptions as to whether the market is “expensive” and should be sold, or “inexpensive” and should be bought. Figure 1 shows that the “Stock Buy and Hold” approach would have provided the highest growth of assets compared to timing based on P/E trading rules.

It may seem reasonable to try to time when to get in and out of the equity markets, but the strategy comes with huge risks. This type of action in a portfolio can be one of the biggest mistakes you make and can easily lead to falling far short of your investment objectives.

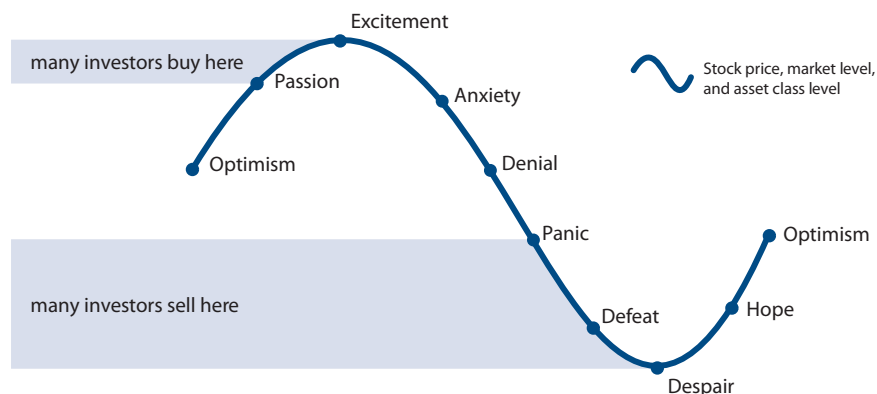
Pitfall 5: Buying High and Selling Low

Have you ever bought a stock that looked like a superstar at the time of purchase only to find that, a year or two later, it had lost 30% of its value and was still dropping? If the truth be told, we all have. To this day, I have yet to meet an investor (myself included) who has not admitted to buying high and selling low at least once in their lives. Hopefully we learn from our mistakes early on; however, because equity markets have a continuum of never-ending, media-hyped stories and a marketplace filled with buyers and sellers who act on emotion, this money-losing pattern can persist throughout one’s lifetime.

Buying individual stocks at their highs or chasing manager and asset class performance is not a new

Figure 2: The Emotional Curve of Investing

Source: National Bank Financial, CEG Worldwide



phenomenon. Sadly, when the initial purchase takes place, we undoubtedly feel that we have a strong premise to support our actions. Usually a sizzling story is behind the stock’s recent appreciation. We are told that it is a “new world” and that prices can still go up. You say to yourself “what if I miss this great buying opportunity” or “this is the stock that will do wonders for my portfolio.” And—bingo—it’s done; you just bought a stock at its historic high!

Chasing stocks has always led investors astray. Investors buying at high levels in the technology, pharmaceutical, banking, consumer, and commodity sectors have all landed in hot water in the last twenty years. These are all great sectors that should be in a long-term portfolio; however, timing your purchase for quick resale is most definitely not your ticket to untold riches. Figure 2 shows the emotions related to the ups and downs of investing. All too often we buy at the peak of the security or asset class price and sell at the trough. Time and time again, we see that investors are not hardwired (thanks in large part to emotions) to succeed through the peaks and valleys of stock price movements.

Buying high and selling low can be extremely destructive to the long-term success of your portfolio. This book highlights strategies that can help you keep your emotions at bay and that will

teach you how to buy stocks or asset classes at a low price and sell them at a higher price—with rigour and in a disciplined fashion.

Pitfall 6: Lack of Proper Diversification

Most investors know that diversification is a sensible, wise, and prudent thing to do with their investments. But do they truly practice it in their portfolios? Some investors may think their investments are well diversified while unknowingly having highly-concentrated and risky portfolios. The lack of proper diversification (by asset class, by industrial sector, by geographic region, and by currency) still ranks as one of the most prominent investment pitfalls affecting the investor community. The consequence of an undiversified portfolio is an excessively high level of risk. This pitfall exposes many investors to much higher levels of potential losses.

Why do investors forego the benefits of diversification? Ironically, for both experienced and inexperienced investors, the answer lies in two opposing human characteristics: overconfidence and lack of awareness. Overconfidence is usually displayed by investors who use bold geopolitical or financial predictions as a basis for their investment decisions. This leads them to intentionally shy away

from diversifying their portfolios by placing large bets on a few companies or a few sectors—resulting in heavily-concentrated investment positions. Conversely, not being aware of the difference between good and bad diversification can lead to unintentionally high concentrations in a given portfolio. These investors might feel that they have an investment plan that offers them the benefits of diversification because they have many mutual funds; however, the funds might have overlapping exposure to certain industries, making their portfolios highly ineffective.

While highly-concentrated portfolios can lead to significant gains, the lack of proper diversification can expose you to significant losses; but all too often we tend to think only about the upside and not the downside. Proper diversification also protects you from unexpected events which, although low in probability, can nonetheless occur during your lifetime as an investor. In *The Black Swan: The Impact of the Highly Improbable*, Nassim Taleb uses the analogy of a black swan¹ to define a large-impact, hard-to-predict, and rare event beyond the realm of normal expectations (the event can be positive or negative). He explains that a black swan has three principal characteristics: it is unpredictable; it has a massive impact; and, after the fact, we concoct an explanation that makes it appear less random, and more predictable, than it was. The astonishing success of Google was a black swan; so was the stock market crash of 1987, as was 9/11.

The common investment pitfalls can be interrelated and may influence each other. In consequence, investment portfolios can become unbalanced, either within the equity component of the portfolio or within the equity and fixed income proportions of a portfolio. Either way, proper diversification is not achieved.

Table 1: Stock Market Forecasting Abilities of Market Gurus

MARKET PUNDITS	BATTING AVERAGE
Abby Joseph Cohen	0.128
Edward Kerschner	0.136
Jeffery Applegate	0.147
Thomas Galvin	0.147
Elaine Garzarelli	0.152
Edward Yardeni	0.152
Lazlo Birinyi	0.157
David Jones	0.164
Richard Bernstein	0.183
Bill Gross	0.189
Tobias Levkovich	0.200
Edward Hyman	0.236

Source: Smartmoney.com (survey conducted from 1997–2002)

Pitfall 7: Building Portfolios Based on Bold Predictions

Through slick marketing campaigns, Wall Street, Bay Street, the brokerage industry, and the financial advisory business have positioned themselves as experts at predicting the markets. These predictions usually appear in the form of stock market tips, market analyses, or mutual fund reports. The traditional service agreement between the investor and the advisory firm goes something like this: the investor pays a commission or a fee and, in return, the advisory firm tells him where things are headed.

SmartMoney.com tracked the forecasts of Wall Street equity market strategists during the bull and bear markets of 1997 to 2002. As table 1 shows, these market pundits—all of whom are regularly quoted for their views on market direction—do not have good batting averages.

T H E F . D A N I E L S O N G R O U P
A S S A N T E F I N A N C I A L M A N A G E M E N T L T D .

Table 2: 2007 Fearless Forecasts

ASSET CLASS OR ECONOMIC VARIABLE	2007 FORECAST	31 OCTOBER 2007 YTD
U.S. dollar to Canadian Dollar	\$0.86	\$1.08
Crude Oil Price (West Texas U.S. \$ per barrel)	\$58.13	\$95.00
SC 91 Day T-Bill Total Return	3.70%	3.07%
SC Universe Bond Total Return	4.10%	1.55%
S&P/TSX Composite Total Return	7.20%	15.56%
S&P 500 Total Return (C\$)	8.20%	-10.19%
MSCI EAFE Total Return (C\$)	8.80%	-4.37%
MSCI Emerging Market Total Return (C\$)	8.00%	21.43%

Source: Mercer Investment Consulting Inc., returns in Canadian dollars

In hindsight, the survey period (1997–2002) offered market strategists a once-in-a-lifetime opportunity to predict (for the benefit of their followers) market movements that included a major market surge followed by a historic market meltdown. What more could a predictor ask for? And yet, as a group, they were still incapable of making accurate market forecasts during this period.

Canadian market strategists are not any better at forecasting future market directions. The “Fearless Forecasts” survey from Toronto-based Mercer Investment Consulting presents the consensus opinions of Canadian and global investment managers on the directions of equity and bond markets, interest rates, CDN\$/US\$ exchange rates, and other macroeconomic variables. Overall, the forecasting abilities of these Canadian strategists were conspicuously off track (so far anyway) for the year 2007. As table 2 shows, they were significantly off in many investment forecast categories (equity markets, bond markets, interest rates, and the Canadian dollar).

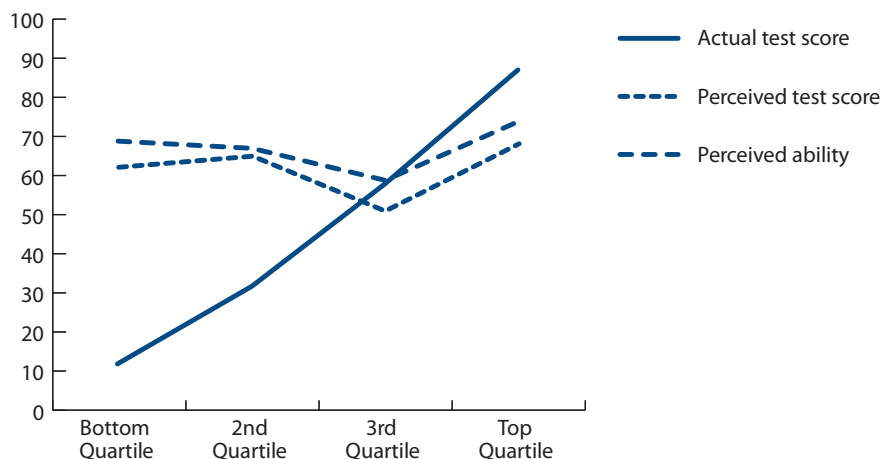
The majority of these managers expected financials to be the top performing industry in 2007 and materials and energy to be the worst performing sector. Ironically, as of 31 October 2007, almost the opposite has occurred.

This survey period (2007) offered Canadian strategists another rare opportunity to predict the historic home-country move in the CDN\$/US\$ rate. The 2007 CDN\$ currency move (as of 27 November 2007, the CDN\$/US\$ rate had reached US\$1.00) was one of the largest swings ever. Some economists predicted parity and more but, as a group, the experts were unable to make accurate market forecasts during this period.

How do poor predictions come about? The professionals surveyed by Mercer Consulting know full well that prediction can be a losing game and would therefore continue to support the concept of portfolio diversification. Unfortunately, there are many individuals with much less credibility who may not suggest balancing and diversifying portfolios. Beware! This is how many investors get into real difficulty. Although predictions may come from individuals you like and respect (friends,

Figure 3: Unskilled and Unaware of It

Source: Kruger and Dunning 1999



family, co-workers, or possibly even advisors), you should remember that these individuals may be unskilled and unaware of it, or overly confident in their abilities.

David Dunning and other researchers have documented an unexpected yet troubling pattern: on a regular basis, those individuals who rank among the worst predictors are the most confident in their abilities.² Kruger and Dunning asked people to rate how they performed on a logic/reasoning test. Figure 3 splits the different ratings for perceived ability, perceived score, and actual score into the four quartiles based on performance. Remarkably, those who did not perform well still had very high levels of confidence in their perceived abilities. It's no wonder that we can get into difficulties given the high levels of confidence so often displayed by those around us.

Why do market analysts continue to make predictions? Partly because it is in the interest of the financial services industry to appear to know what will happen in the future; and partly because

investors take comfort in building strategies around predictions.

Another factor may be that those making the predictions have built-in defense biases that allow them to formulate excuses. Philip Tetlock followed the views of global experts on world politics for more than a decade.³ He writes that “Almost as many experts as not thought that the Soviet Communist Party would remain firmly in the saddle of power in 1993, that Canada was doomed by 1997, that neo-fascism would prevail in Pretoria by 1994, that EMU would collapse by 1997 ... that the Persian Crisis would be resolved peacefully.” Tetlock found that, although these experts rated their confidence in their political and global predictions at 80% or higher, their predictions were correct no more than 45% of the time. He identified strategies frequently used by the predictors to explain their errors in forecasting and which also explain why they continue to make predictions: the “although the forecast was wrong the analysis is still valid” defense; the “I was almost right” defense;

the “it just hasn’t happened yet” defense; and, my personal favourite, the “if only” defense. Tetlock concluded that “expertise thus may not translate into predictive accuracy but it does translate into the ability to generate explanations for predictions that experts themselves find compelling, [in turn] resulting in massive overconfidence.”

Finally, one of the fundamental problems with predictions is that they are easily derailed by unforeseen events: companies and industries find themselves unexpected circumstances; trends change or are morphed by other stronger trends. In the popular book *Boom, Bust & Echo: How to Profit from the Coming Demographic Shift* published in the mid-1990s, David K. Foot boldly predicted that residential real estate would be a poor investment in the future because an aging population would want to downsize. Although the prediction might yet come true, real estate prices have gone through the roof in the last decade as cocooning trends have seen families of all ages invest in and spend more on their homes.

In truth, no one has the ability to consistently forecast important geopolitical and economic outcomes—there are no crystal balls. With catchphrases like “Ten Stocks to Buy Now” and “How to Retire Rich,” the advice business has largely succeeded in convincing investors that it has the inside track. Predicting an uncertain future has become the bread and butter of many in the financial services industry, and the public has been all too willing to buy into it. In the short term, setting the entire direction of your portfolio on the basis of a few predictions may lead to joy or misery; in the long term, it might lead to much less than you’d hoped for—not to mention encouraging you to become that Nervous Nelly investor you never wanted to be.

Pitfall 8: Letting Behavioural Biases Get in the Way

Whether we want to admit it or not, humans are not wired to be great investors. Emotions like fear or greed often cloud our judgment and lead us to do things with our portfolios that we will later regret. In addition to the raw emotions we all share, we also have a set of filters—or thinking biases—that can lead us to make less-than-rational investment decisions. When combined with our raw emotions, these biases often drive us to do things that make no logical sense. Being unaware of these biases can be quite detrimental to you and to your investment experience.

Money is an emotional subject, and the choices we make in the wake of an exciting stock tip or a plummeting portfolio affect our investment results in real and often damaging ways. Behavioural finance is a relatively new field that attempts to better understand and explain how human emotions and cognitive errors influence investors and their decision-making processes.

Quite simply, behavioural finance is a merging of human psychology and the science of economics. This area has critical implications for investing and is far more important in determining the level of success in your investments than many other technical-oriented benchmarks. So powerful and insightful are the findings from behavioural finance that one of the pioneers in this field, Daniel Kahneman, won the 2002 Nobel Prize in Economic Sciences “for having integrated insights from psychological research into economic science, especially concerning human judgment and decision-making under uncertainty.” Kahneman’s work (in collaboration with the late Amos Tversky) laid the foundation for a new field of research by discovering how human judgment may take

shortcuts that systematically depart from the basic principles of probability.

Successful investors are very aware of the impact emotions can have on portfolio decisions. Warren Buffett writes: “Success in investing doesn’t correlate with I.Q. ... Once you have ordinary intelligence, what you need is the temperament to control the urges that get other people into trouble in investing.”

The discovery and identification of a set of cognitive human errors related to investing is one of the most interesting elements of behavioural finance. These biases include:

Availability Bias: When investors make financial decisions based on limited information (and not all information) available to them.

Anchoring Bias: When investors make decisions based on being fixated or “anchored” with the most recent information that has been presented to them.

Confirmation Bias: When investors look for evidence and research that confirm their investment beliefs, but disregard evidence and research that do not support their views.

Hindsight Bias: When, in hindsight, we conclude that we knew a specific financial event was going to occur, providing subconscious support to the belief that we can predict certain financial outcomes.

Confidence Bias: Overconfidence is the opposite of fear of loss and can be just as devastating to your investment portfolio. This behaviour results partly from the optimistic tendency of humans to unrealistically overrate their abilities.

As discussed, human behavioural biases can cause investors—both amateur *and* professional—to make investment mistakes and can often account for irrational investing. The emotional component of investing explains why very smart people still fall prey to classic investment pitfalls. Because we are human, these biases have a high probability of hindering your investment success unless you have a plan in place and the discipline to stick with it.

Behavioural biases can result in the following personal investing outcomes:

- ◆ Herding behaviour driven by a desire to be part of the crowd or an assumption that the crowd is omniscient
- ◆ Treating some money (such as gambling winnings or an unexpected bonus) differently than other money
- ◆ Fear of change, resulting in an excessive bias towards the status quo
- ◆ Overestimating the likelihood of certain events
- ◆ Ignoring important data and focusing excessively on less important information
- ◆ Allowing an overabundance of short-term information to cloud long-term judgments
- ◆ Drawing conclusions from a limited sample size
- ◆ Reluctance to admit mistakes
- ◆ Believing that one’s investment success is due to wisdom rather than a rising market
- ◆ Failing to accurately assess one’s investment time horizon
- ◆ Failing to recognize the large cumulative impact of small amounts over time
- ◆ Confusing familiarity with knowledge
- ◆ Overconfidence⁴

Have you, your investment advisor, or your professional money manager ever been trapped by

one or more of these investment pitfalls? Chances are that you have. Even professional investors—the so-called “experts”—are prone to overconfidence.

What’s an investor to do? Awareness of these human variables is an important first step.

Empower Yourself—Become Aware

Awareness pays off. Given that equity market returns over the next fifteen years may well not be as generous as the bull market of the 1980s and 1990s, it is even more imperative that investors learn from their past mistakes and focus on obtaining the best possible returns available to them. Investors must:

- ◆ Become aware of pitfalls that can endanger their long-term investment success;
- ◆ Educate themselves on capital markets and how they work, the relationship between risk and return, and the strategies to avoid getting trapped in traditional investment mistakes;
- ◆ Build investment plans using time-tested strategies based on diversification and long-term asset allocation; and
- ◆ Execute and maintain their chosen investment plan with discipline.

It’s time for a different kind of investment strategy, one that allows investors to pursue their dreams without endangering their livelihoods. Education and awareness enable investors to see beyond the market hype and invariably empower them in making their investment choices. A structured, well-executed portfolio is critical to producing a profitable and winning strategy for your investments.

NOTES

1. The term “black swan” comes from the ancient Western misconception that all swans were white. In that context, a black swan was a metaphor for something that could not exist. The discovery of black swans in Australia in the seventeenth century metamorphosed the term to connote that the perceived impossibility had actually come to pass (Wikipedia 2007).

2. Justin Kruger and David Dunning, “Unskilled and Unaware of It: How Difficulties in Recognizing One’s Own Incompetence Lead to Inflated Self-Assessments,” *Journal of Personality and Social Psychology* 77, no. 6 (1999): 1121–34.

3. Philip E. Tetlock, “Theory-Driven Reasoning about Plausible Pasts and Probable Futures in World Politics,” *Heuristics ad Biases: The Psychology of Intuitive Judgment*, edited by Gilovich, Griffin, and Kahneman, CUP, 2002.

4. Adapted from an article by Whitney Tilson, “The Perils of Investor Overconfidence,” the Motley Fool web site (www.fool.com), 20 September 1999.

T H E F . D A N I E L S O N G R O U P
A S S A N T E F I N A N C I A L M A N A G E M E N T L T D .

SOURCES & DISCLAIMER:

Eight Common Investment Pitfalls is a research white paper excerpted from the new and revised 2nd edition of the book *The Empowered Investor: A Guide to Building Better Portfolios*. © Keith Matthews 2007.

www.empoweredinvestor.ca

All rights reserved, including the right of reproduction in any form. No part of this publication may be reproduced or retransmitted in any form or by any means, including, but not limited to, electronic, mechanical, photocopying, recording, or any information storage retrieval system, without the prior written permission of the publisher.

All efforts have been made to ensure the accuracy and integrity of the information presented in this white paper and in the book. Although all facts have been obtained from sources believed to be reliable, the information is not guaranteed, and neither the author nor the publisher is liable for any errors, omissions, or contradictions found in the text. Investments and investing strategies should be evaluated based on your own objectives. Readers should use their best judgment and consult a financial expert prior to making any investment decisions based on the information found in this white paper or in the book.

TULETT, MATTHEWS & ASSOC. INC.:

Keith Matthews is a partner and portfolio manager at Tulett, Matthews & Associates Inc. Tulett, Matthews & Associates specializes in discretionary portfolio management services and wealth management solutions designed for Canadian investors who are serious about achieving their long-term investment goals. Our unique consultative approach ensures that we only work with clients for whom we can add real value to their pursuit of a successful investment experience.

Keith Matthews
Partner & Portfolio Manager
Tulett, Matthews & Associates Inc.
3535 St-Charles Blvd, Suite 703
Kirkland, Quebec
514-695-0096 (106)
keith@tma-invest.com
www.tma-invest.com

Portfolios created, managed, and monitored by Tulett, Matthews & Associates Inc. are subject to market fluctuations. The value of most investments, particularly equity investments, can be negatively affected by changes in general market conditions caused by corporate developments, changes in interest rates, changes in the level of inflation, and other political and economic developments.

Frank Danielson, BEd, CFP

Since 1994, Frank Danielson has built a reputation for attentive, client-focused service and valued advice. He currently serves as personal CFO for a number of high net-worth individuals, families, and professionals. Frank assumes responsibility for coordinating and managing the evolving needs of each of his clients, from portfolio strategy to risk management, estate and trust planning to financial planning and modeling.

Born and raised in Nanaimo, Frank attended the University of Victoria and obtained his Bachelor of Education in Biological Sciences. After two years in the teaching profession, Frank decided to focus on his passion for finance and embarked on his career as a financial planner. Since then, he has worked exclusively through referrals from his clients and a select group of CAs and lawyers. Frank, his wife Petra, and young son Dylan live in the UBC area. In addition to serving on several community boards, Frank is a strong supporter of the "Raise a Reader" literacy program. In his spare time, Frank enjoys golf, fitness, photography and expanding his personal knowledge.

Our Approach

At The F. Danielson Group we are passionate about providing our clients with the highest level of wealth planning services through the creation of a trusting, long-term relationship. Our commitment to your financial success and well-being is reflected in our unique consultative approach and client-centered process.

To ensure we are consistently adding value to our clients' overall financial plan we have developed our personal CFO process that continually aligns our ongoing advice and recommendations with your unique financial situation. Our consultative approach is based on a series of five meetings: discovery, planning review, portfolio design, opportunities, and implementation:

Discovery - discovery leads to clarity

The main objective of the Discovery Meeting is to learn more about your financial objectives, personal values, and key financial concerns. Together, we will also determine if there is a mutual fit and if we can add value.

We believe it is important to understand your financial personality, since human behaviour impacts every aspect of building your successful financial plan. We call this assessing your Financial DNA.



Plan Review - your financial roadmap

The main objective of our Plan Review phase is to confirm your financial objectives, then compare those objectives to your probability of achieving them. Most important, this meeting clearly reflects, in a written plan, your aspirations and creates the roadmap for achieving your goals.

Portfolio Design - implement

The main objective of our Portfolio Design phase is to review your unique investment objectives, liquidity needs, growth expectations, tolerance for risk, income requirements, investment time horizon, anticipated changes in lifestyle, tax considerations, and economic variables such as, inflation and market volatility.

These objectives will be reflected in your own Investment Policy Statement (IPS), which provides an account of your investment objectives and describes the strategies that we will employ to meet them.

Wealth Optimization - implementation leads to results

The main objective of the Wealth Optimization phase is to focus on wealth planning opportunities that will have the largest impact on your achieving your most important financial goals.

Using our Diagnostic Checklist (which covers nearly 100 tax, estate, corporate, and risk management opportunities), we ensure you are optimizing and protecting your overall wealth plan. Once the Checklist is complete, together we'll prioritize the results, then create an action plan that assigns realistic timelines for completion.

Financial Planning - implementation is not a "one time only" event

As your life evolves, so will your financial plan and investment portfolio. That is why we hold semi-annual meetings and conduct conference calls throughout the year to learn about the changes going on in your lives, monitor investment performance, and keep your overall wealth plan on track.

We would be pleased to discuss our process with you in person. Contact us at fdanielson@assante.com or by telephone at 604-638-0345.