

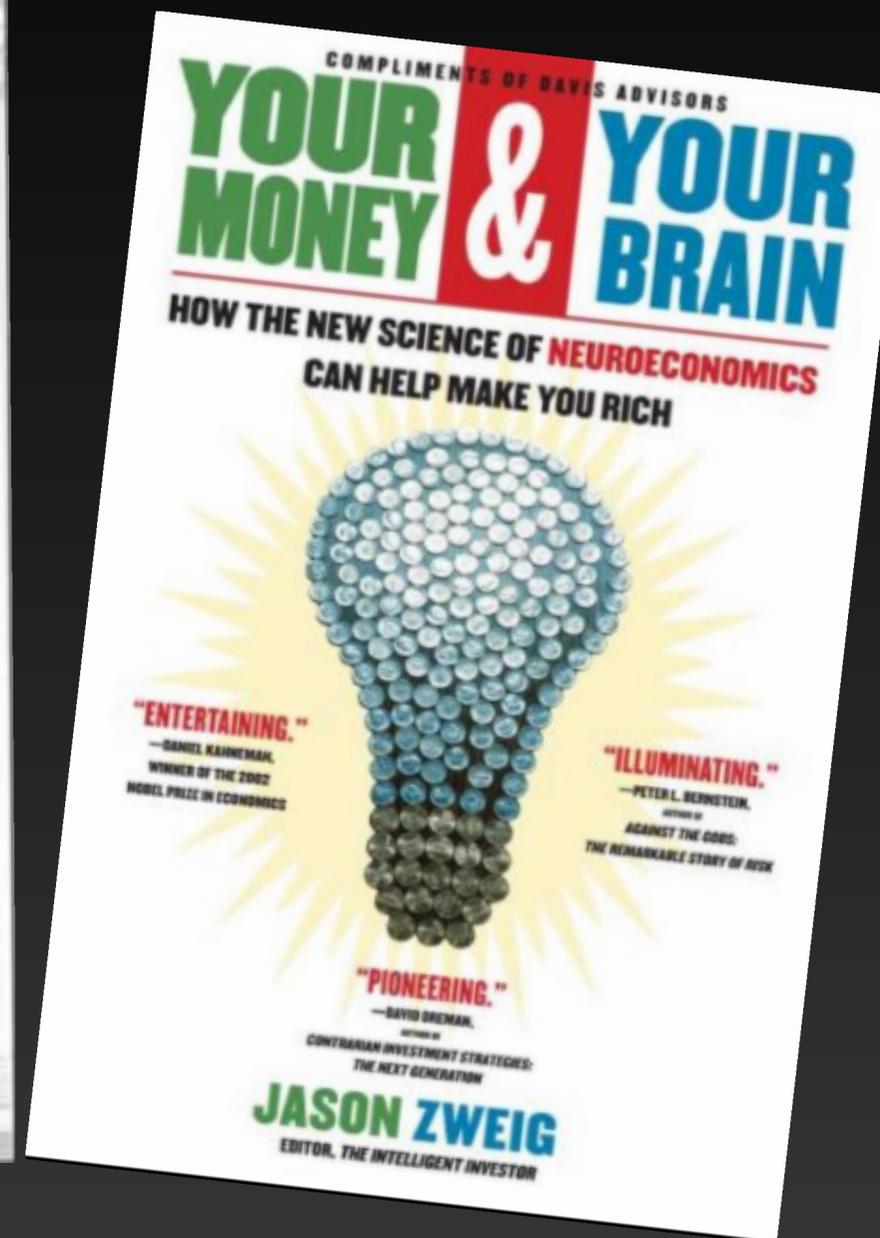
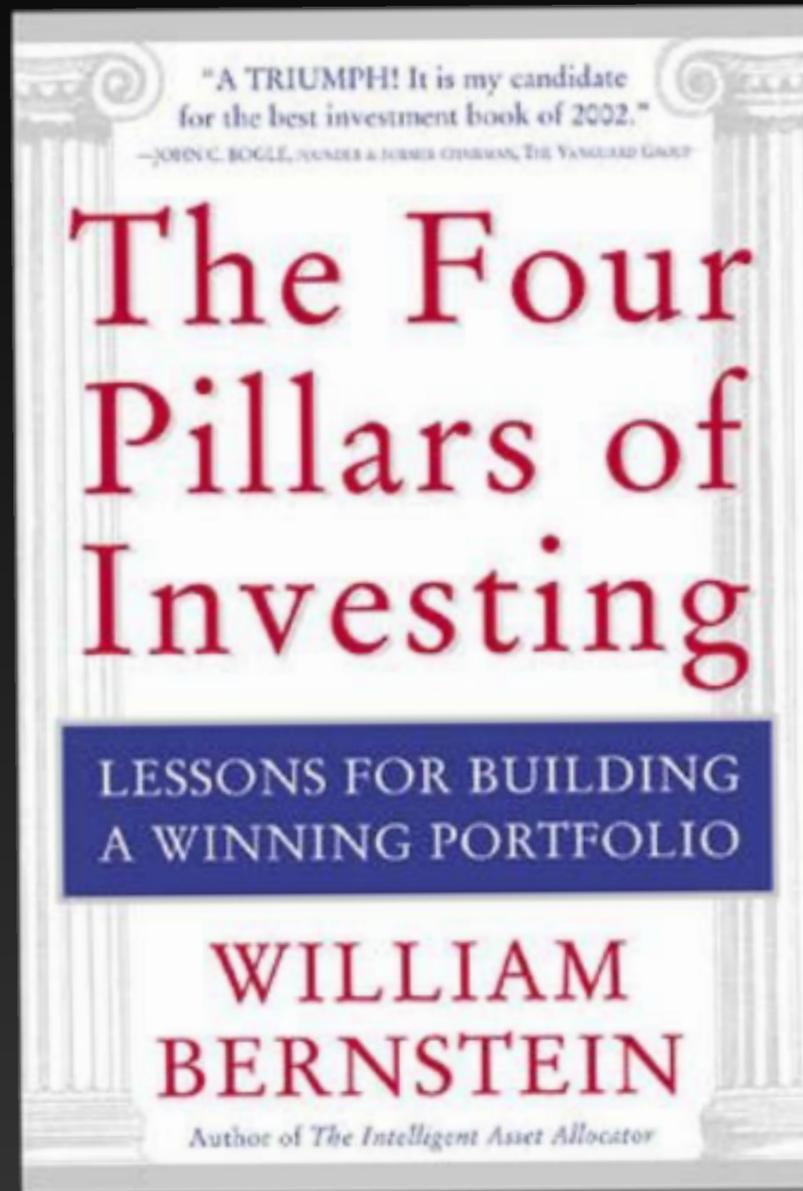
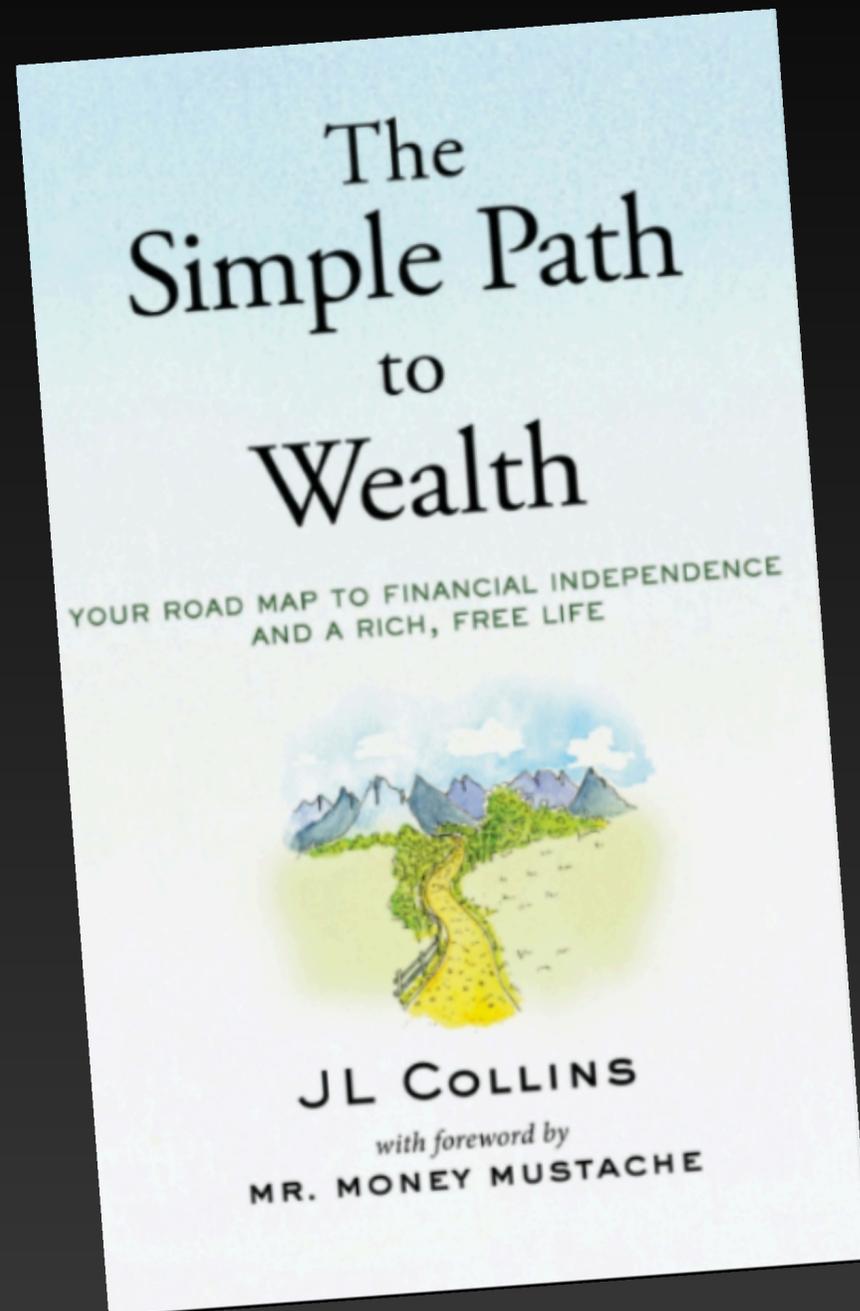
The Four-Letter Words of Investing

Navigating FEAR and RISK Through Volatile Times

By Chris Goslow, Sacramento Bogleheads, June 11, 2022

Stock photos courtesy of [pexels.com](https://www.pexels.com)

Today's expert advice comes from:

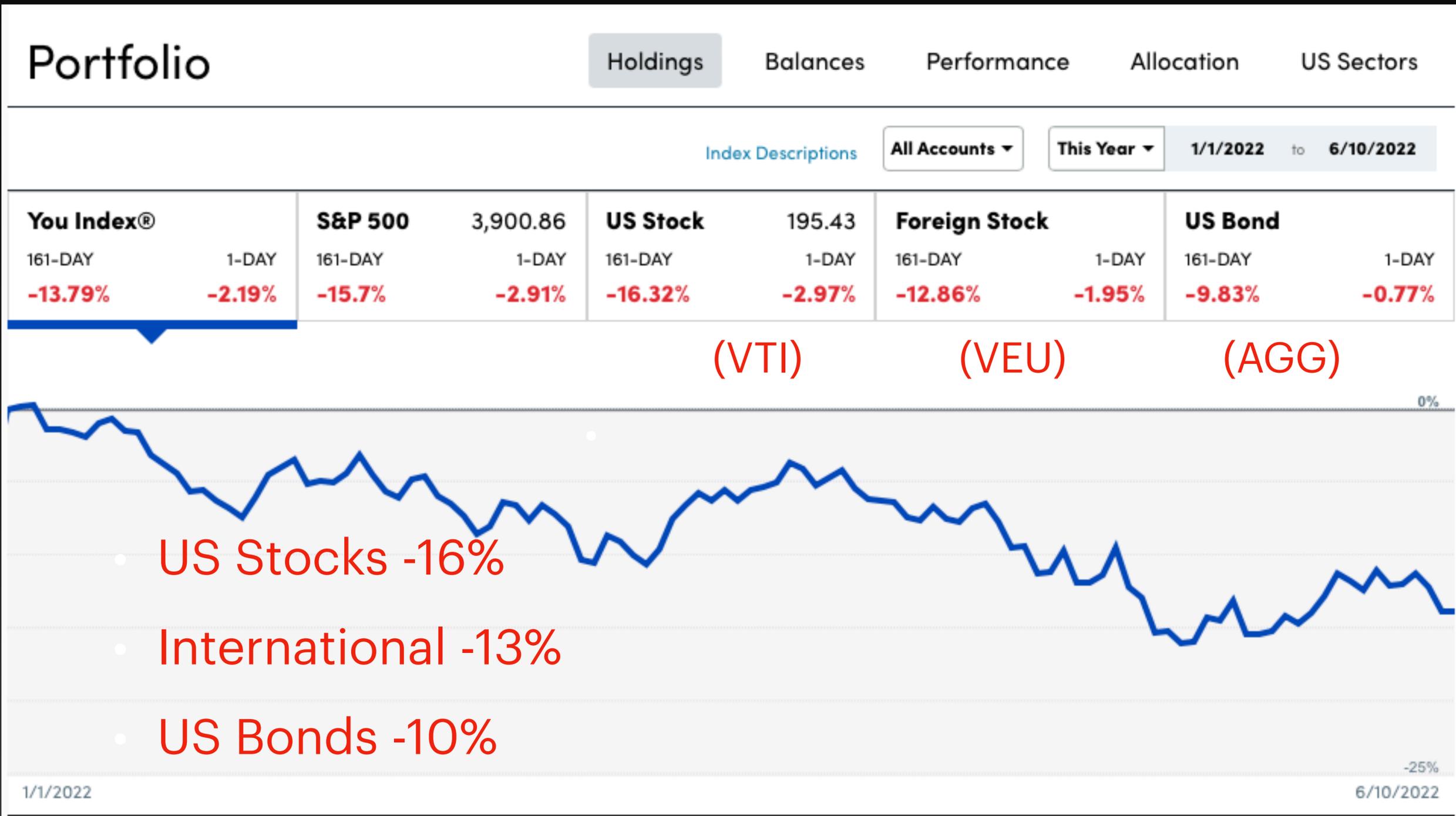


Part 1: 2022 Volatility Recap

The background of the slide is a photograph of a night sky. A vibrant green aurora borealis is visible, with a bright, curved band of light stretching across the upper half of the frame. Below the aurora, a dark, jagged mountain range is silhouetted against the sky. The mountains are covered in snow, and the overall scene is illuminated by the soft, ethereal light of the aurora and the stars in the dark sky.

2022 So far...

(As of 6/10/22 - From Personal Capital)



If It Bleeds.... (From This Week's Headlines)

**“Stocks Drop Amid Concerns
About an Economic Slowdown”
—The Wall Street Journal 6/8/22**

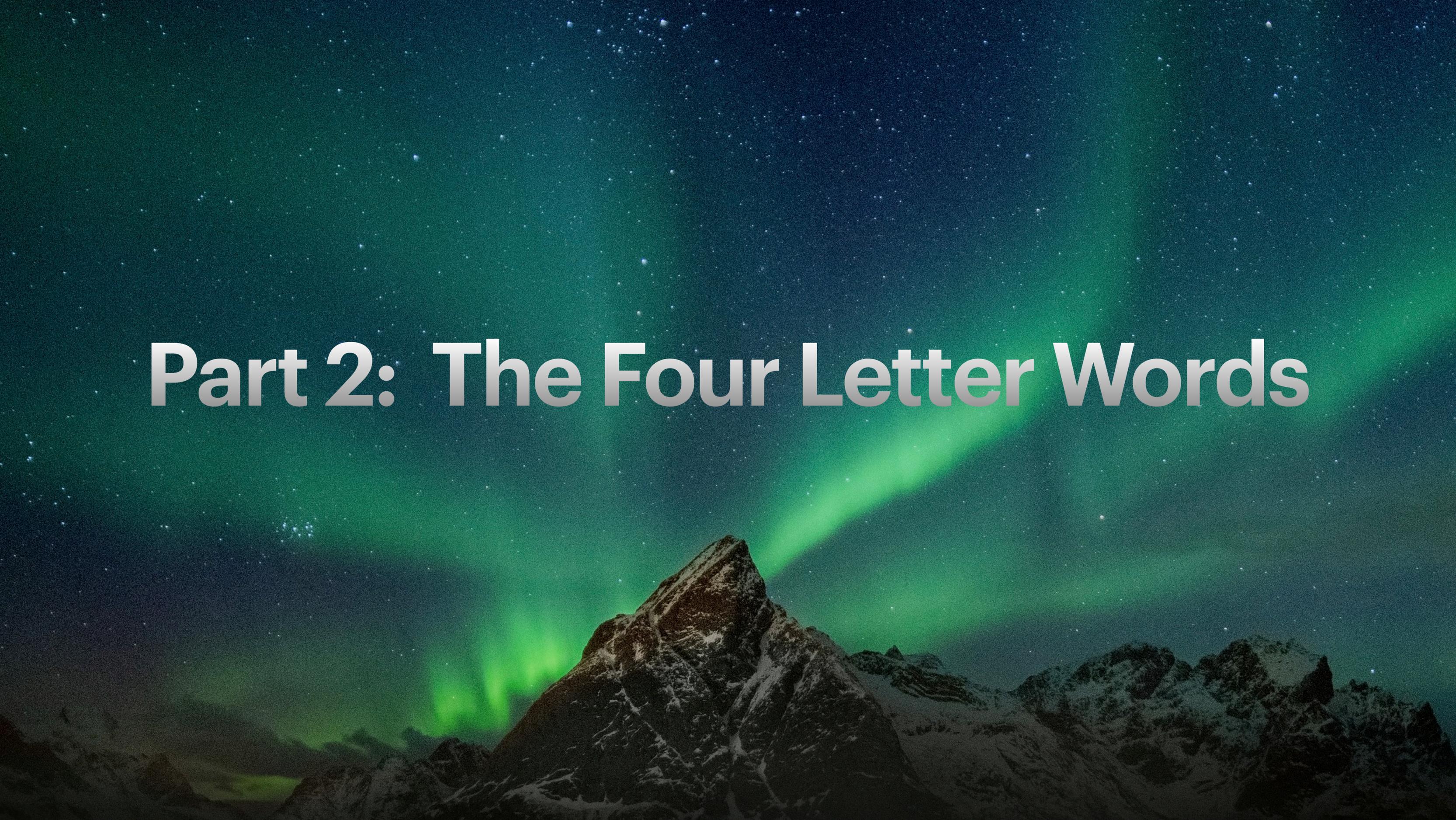
**“Americans lost half a trillion
dollars in wealth in early 2022”
—CNN 6/9/22**

**“S&P 500 posts worst week since
January after inflation hits
40-year high”
—CNBC 6/10/22**

**“‘The persistency of inflation’
could tip us into recession,
Citi managing director says”
—Yahoo! Finance 6/6/22**

Scared yet??

Part 2: The Four Letter Words

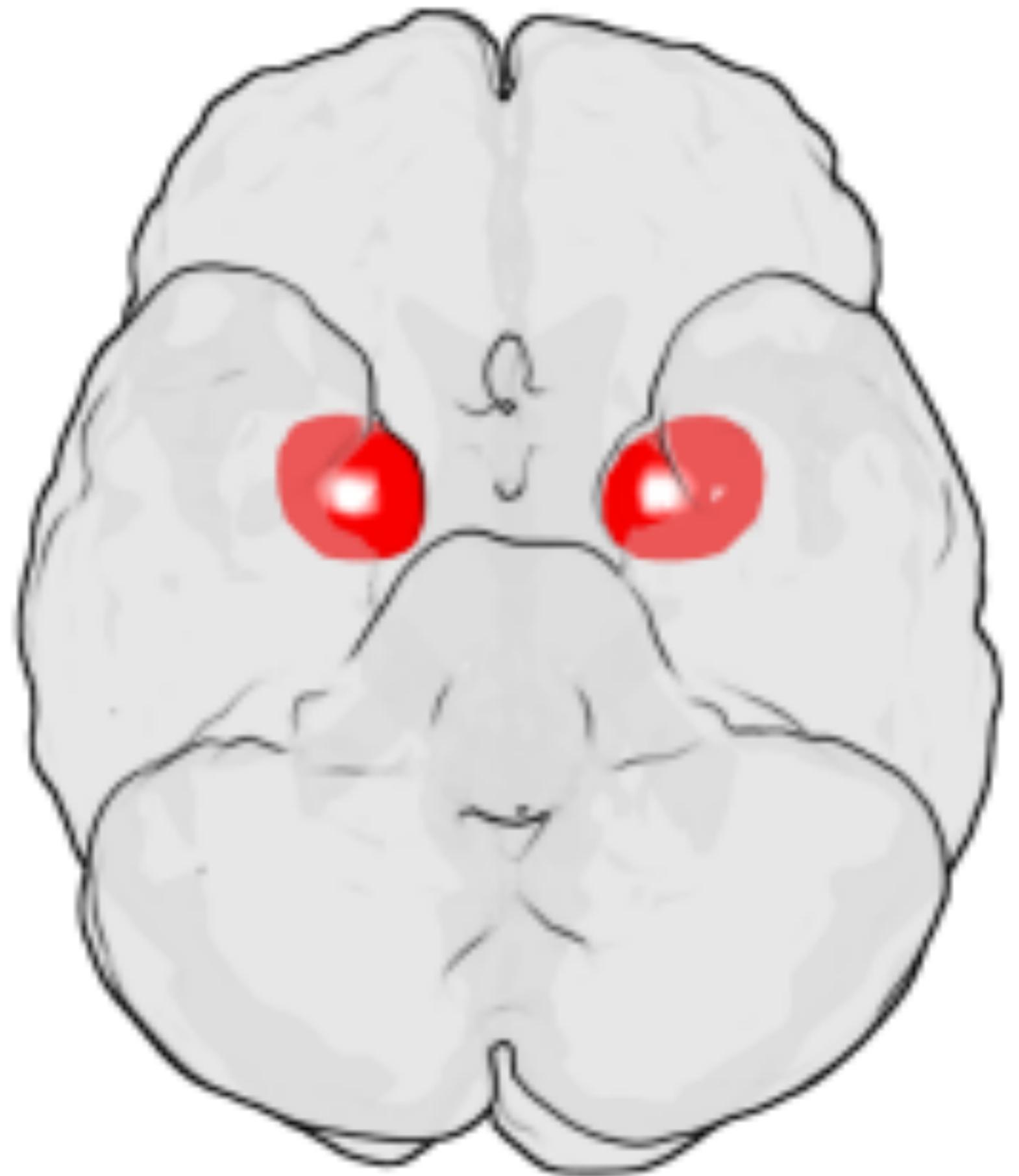
The background of the image is a night sky filled with stars. A vibrant green aurora borealis is visible, arching across the sky and illuminating the scene. In the foreground, there are dark, jagged mountain peaks covered in snow, creating a stark contrast with the bright light of the aurora.

1. FEAR

The Amygdala

“The amygdala is one of two almond-shaped clusters of nuclei deep and medially within the temporal lobes of the brain’s cerebrum... Shown to perform a primary role in the processing of memory, decision making, and emotional responses (including fear, anxiety and aggression), the amygdalae are considered part of the limbic system.”

(Source: Wikipedia)



“Step near a snake, spot a spider, see a sharp object flying toward your face, and your amygdala will jolt you into jumping, ducking, or taking whatever evasive action should get you out of trouble... This same fear reaction is triggered by losing money—or believing that you might.”

Jason Zweig, “Your Money & Your Brain,” p160

“The Crash of 1987 was exactly the kind of event that sparks the amygdala into flashing fear throughout every investor’s brain and body. The memory was hard to erase: In 1988, U.S. investors sold \$15 billion more shares in stock mutual funds than they bought, and their net purchases of stock funds did not recover to precrash levels until 1991.”

Jason Zweig, “Your Money & Your Brain,” p163

“Fear is perfectly understandable. Nobody wants to lose money. But until you master it, such fear will be deadly to your wealth. It will prevent you from investing. Once you are invested, it will cause you to flee in panic for the exits every time the market drops. And drop—repeatedly on its relentless march upward—it will.”

JL Collins, “The Simple Path to Wealth,” p49

2. RISK

What is Risk?

“Risk is defined in financial terms as the chance that an outcome or investment’s actual gains will differ from an expected outcome or return.

Risk includes the possibility of losing some or all of an original investment.”

(Source: Investopedia)

“When an intangible feeling of risk fills the air, you can catch other people’s emotions as easily as you can catch a cold.”

Jason Zweig, “Your Money & Your Brain,” p157

Is our risk tolerance a simple, fixed thing?

“Your attitudes toward financial risks...can differ dramatically depending on how they are framed, whether you are alone or in a group, how your previous bets paid off, how easy it is for you to think about the risk, what mood you are in, even what the weather is like outside.”

Jason Zweig, “Your Money & Your Brain,” p151

A night sky with a green aurora borealis over a snowy mountain range. The aurora is a vibrant green light that curves across the sky, illuminating the dark, rocky peaks of the mountains below. The sky is filled with numerous stars, and the overall scene is serene and majestic.

Part 3: 10 Ways to Stay the Course Through Times of Volatility

“The best investors make a habit of putting procedures in place, in advance, that help inhibit the hot reactions of the emotional brain.”

Jason Zweig, “Your Money & Your Brain,” p171

**1. Focus on What You Can Control
(And Know What You Can't!)**

Things You Can't Control:

What will happen in the market

What others will do

What will happen in the short-run

What will happen in the long-run

Nearly everything! :(

Things You Can Control:

Buying low-cost index funds

Making regular, automatic deposits

Rebalancing

The risks you take (ie Asset allocation)

**“A superior portfolio strategy should be
intrinsically boring.”**

William Bernstein, “The Four Pillars of Investing,” p183

“Letting an index work its magic over the years isn’t very exciting. It is only very profitable.”

JL Collins, “The Simple Path to Wealth,” p96

2. Distinguish short-term vs. Long-term risk

“The intelligent investor knows that the visceral reaction to short-term losses is a profoundly destructive instinct.”

William Bernstein, “The Four Pillars of Investing,” p184

Short-term risks include:

- Uncertainty about where the market is heading
- The possibility of your portfolio going down
- Losing money on paper
- The possibility that an asset underperforms in the next year or two
- Stress, fear, or worry over investments (“sleepless nights”)

“Every investor’s worst nightmare is a stock market collapse like the Crash of 1929... The real risk is not that the stock market will have a meltdown, but that inflation will raise your cost of living and erode your savings.”

Jason Zweig, “Your Money & Your Brain,” p155-6

Long-term risks include:

- Inflation reducing the purchasing power of portfolio
- Portfolio underperformance due to improper asset allocation (too risky or too conservative)
- Behavioral mistakes damaging investing performance, eg panic selling or myopic risk aversion.
- Not having enough money in retirement

“If you can obtain high long-term returns, what does it matter if you have lost and regained 50% or 80% of your principal along the way?”

William Bernstein, “The Four Pillars of Investing, p28

“Get Your Risks Straight:

An investor places \$10,000 in a mutual fund in the mid-1970s and then forgets about it. Shocked by the October 19, 1987, market crash, she panics and calls the fund company to inquire about the state of her account. ‘I’m sorry madam, but the value of your fund holdings has fallen to \$179,623.’”

William Bernstein, “The Four Pillars of Investing,” p184

3. Think Long-Term

.INX · INDEX

2022 Year-to-Date (as of 6/6/22)

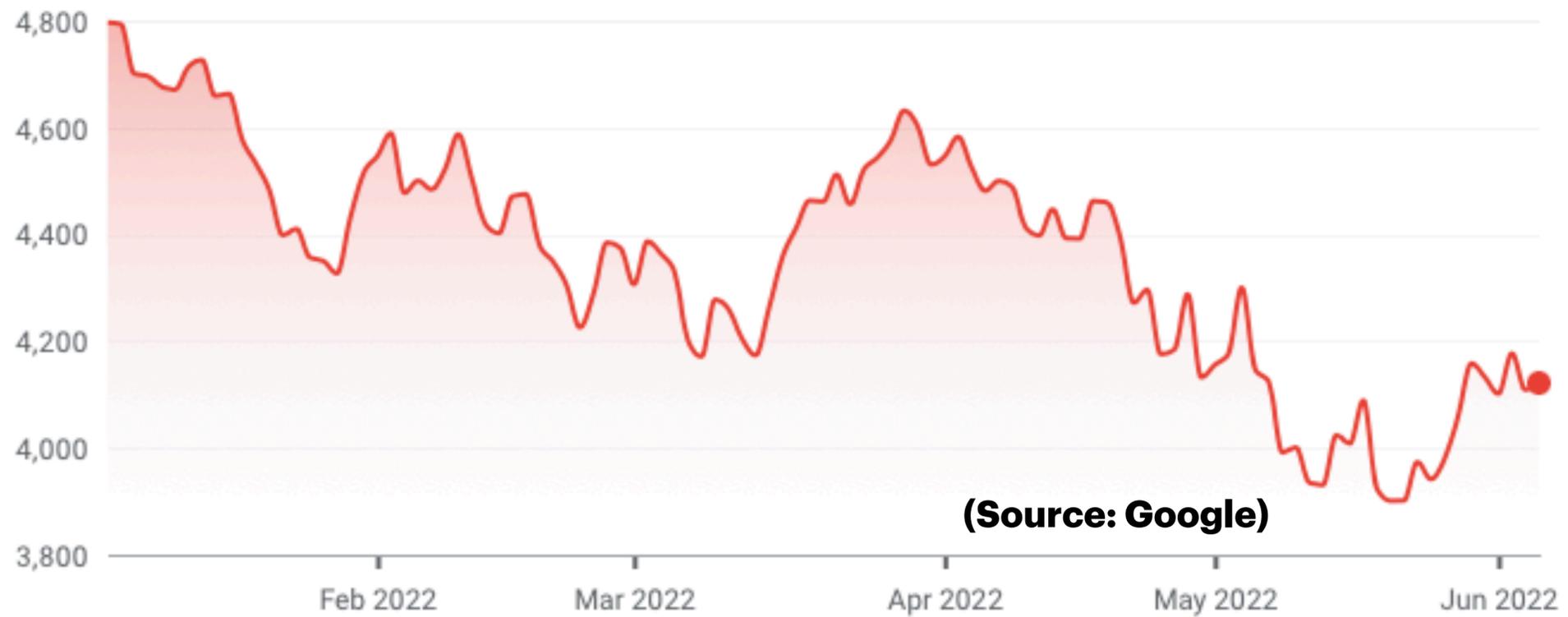
S&P 500

4,121.43

↓ 14.08% -675.13 YTD

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1D 5D 1M 6M YTD 1Y 5Y MAX



(Source: Google)

.INX • INDEX

1 Year Performance (as of 6/6/2022)

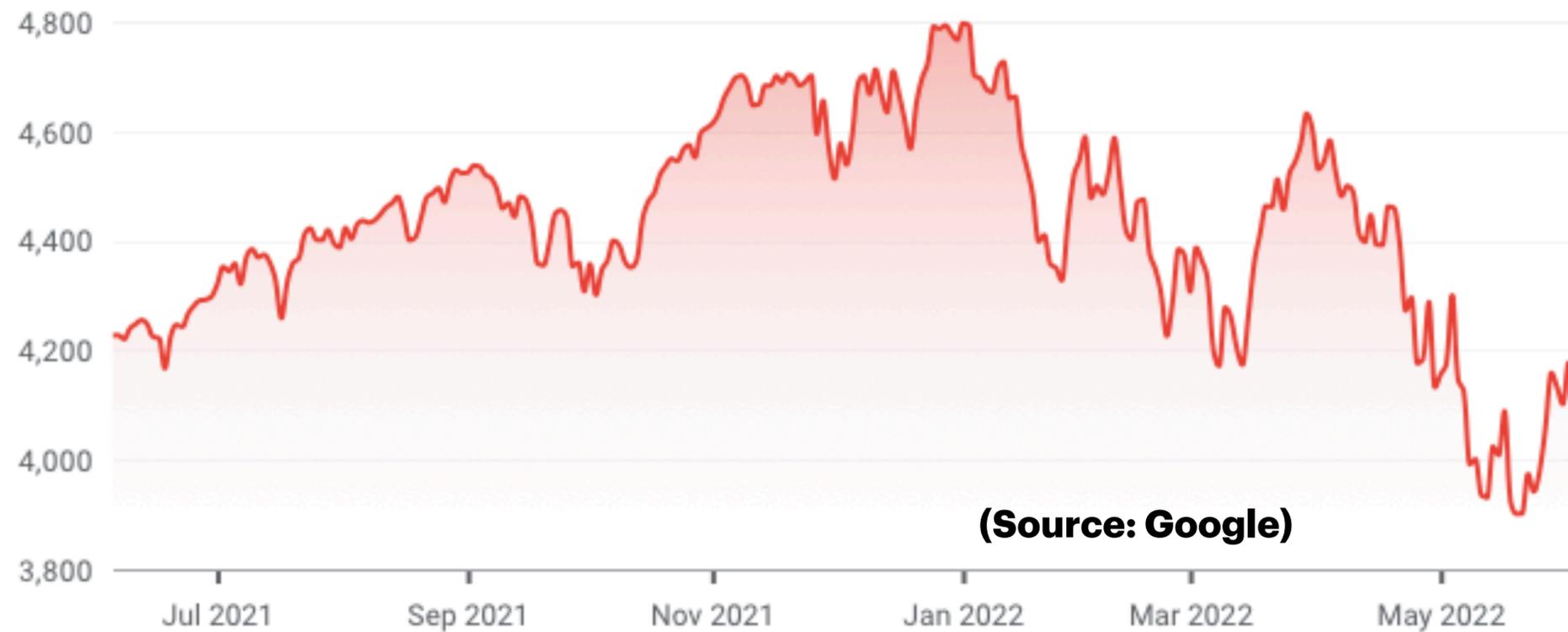
S&P 500

4,121.43

↓ 2.49% -105.09 1Y

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1D 5D 1M 6M YTD 1Y 5Y MAX



(Source: Google)

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5 Year Performance (as of 6/6/2022)

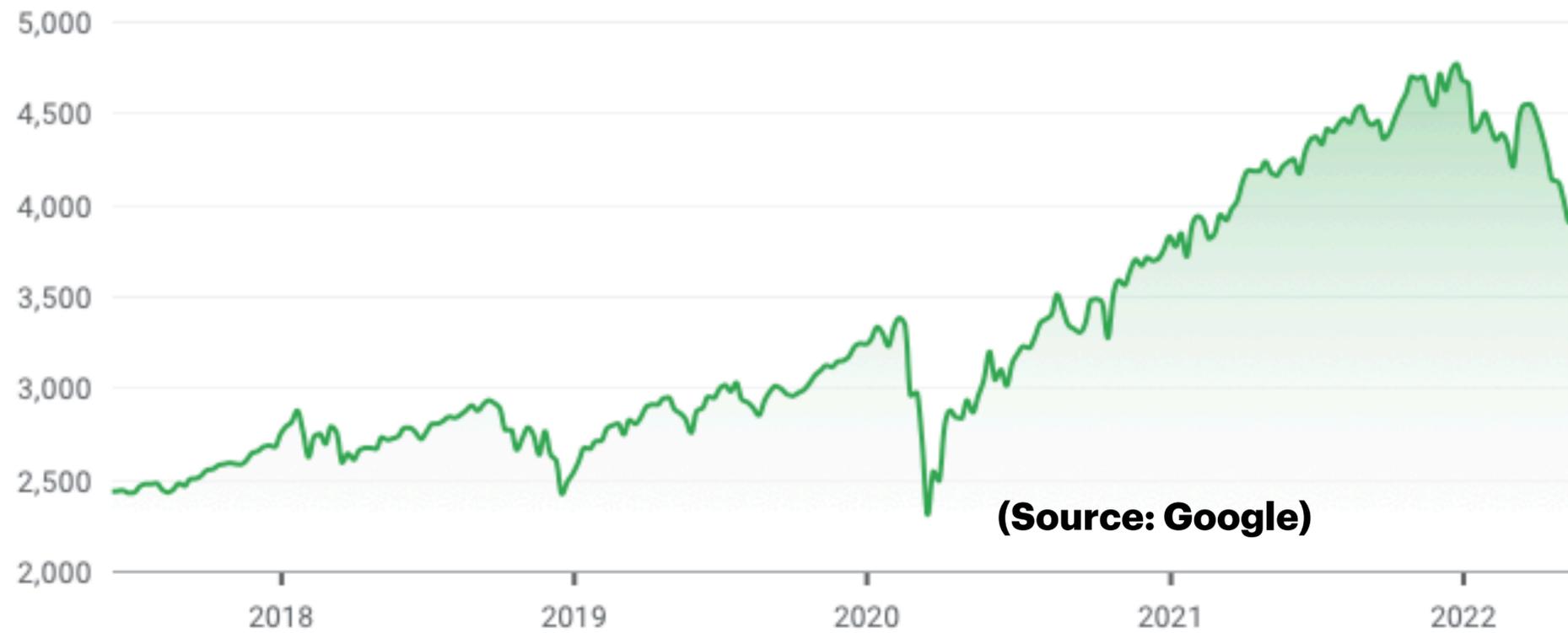
S&P 500

4,121.43

↑ 69.48% +1,689.66 5Y

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1D 5D 1M 6M YTD 1Y 5Y MAX



(Source: Google)

Wow! :)

.INX · INDEX

40 Year Performance 1982-2022 (as of 6/6/22)

S&P 500

4,121.43

↑ 3,604.99% +4,010.19 MAX

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1D 5D 1M 6M YTD 1Y 5Y MAX



(Source: Google)

Where do I sign up!?

“In 1974 the Dow closed at 616. At the end of 2014 it was 17,823. Over the 40 year period (January 1975-January 2015) it grew, with dividends reinvested, at an annualized rate of 11.9%. If you had invested \$1,000 and just let it ride, it would have grown to \$89,790 as 2015 dawned.”

JL Collins, “A Simple Path to Wealth,” p61

4. Reframe Risk as Opportunity

What if you could turn this...

...into this?



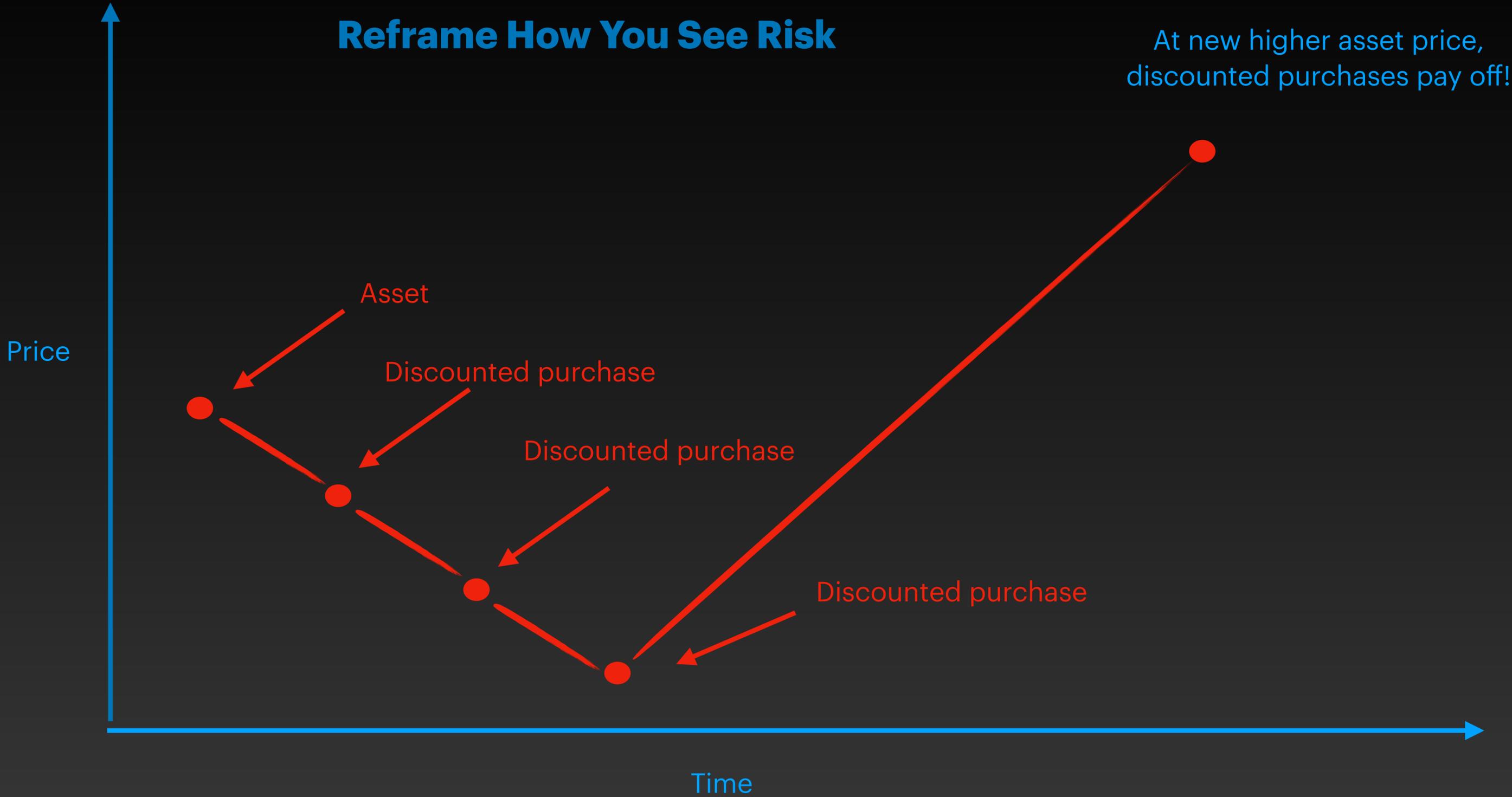
Or this?



“The best possible time to invest is when the sky is black with clouds, because investors discount future stock income at a high rate. This produces low stock prices, which, in turn, beget high future returns.”

William Bernstein, “The Four Pillars of Investing, p66

Reframe How You See Risk



“A young person saving for retirement should get down on his knees and pray for a market crash, so that he can purchase his nest egg at fire sale prices.”

William Bernstein, “The Four Pillars of Investing, p61-2

5. Have a Written Plan



... I find that
... of God for me
... all my prayers
... my heart
... we truly my
... ever yours,

“The best way to prevent yourself from being knocked off track by your emotions is to spell out your investing policies and procedures in advance, in what’s called an ‘investment policy statement,’ or IPS.”

Jason Zweig, “Your Money & Your Brain,” p6

Some Elements of Your Investment Policy Statement

- What is your investment allocation strategy?
- What are your investment goals (time-horizon, plans for the money, etc)
- What actions will you not take, or will control carefully (ie, allocating play money, buying individual stocks, buying options, buying crypto from tips for your neighborhood barista)?
- How often will you review your strategy? (Ex annually)

6. *Accept the Risks*

Invest with eyes open!



“Safety is a bit of an illusion. There is no risk-free investment. Once you begin to accumulate wealth, risk is a fact of life. You can’t avoid it, you only get to choose which kind...If you invest in stocks, you’ll likely outpace inflation and build wealth but you’ll have to endure a volatile ride.”

JL Collins, “The Simple Path to Wealth,” p87

Know the Risks!

**Period:
1926-2019**



100% Fixed income

Average annual return	5.33%
Best year (1982)	32.62%
Worst year (1969)	-8.13%
Years with a loss	14 of 94



50% Equity/50% Fixed income

Average annual return	8.29%
Best year (1933)	36.37%
Worst year (1931)	-23.49%
Years with a loss	18 of 94



70% Equity/30% Fixed income

Average annual return	9.21%
Best year (1933)	44.45%
Worst year (1931)	-31.59%
Years with a loss	23 of 94



100% Equity

Average annual return	10.29%
Best year (1933)	54.20%
Worst year (1931)	-43.13%
Years with a loss	26 of 94

“If you want to earn high returns, be prepared to suffer grievous losses from time to time. And if you want perfect safety, resign yourself to low returns.”

William Bernstein, “The Four Pillars of Investing, p28

Yet keep risk in perspective...

“The market always recovers. Always. And, if someday it really doesn’t, no investment will be safe and none of this financial stuff will matter anyway.”

JL Collins, “A Simple Path to Wealth,” p61

**7. Have a Healthy Skepticism
(Towards Yourself!)**

“Over the years, I’ve grown convinced that there are only three kinds of investors: those who think they are geniuses, those who think they are idiots, and those who aren’t sure. As a general rule, the ones who aren’t sure are the only ones who are right.”

Jason Zweig, “Your Money & Your Brain,” p6

Ways to Keep Yourself in Check:

- Keep an investing log to record why you make the decisions you make
- Study your own investing behavior for cognitive biases. What behavioral mistakes have you been prone to?
- Consult a trusted accountability partner before making portfolio changes (could be spouse, financial advisor, friend/family, or fellow Boglehead)
- Use your Investment Policy Statement to create a procedure you can follow before making portfolio changes

Behavioral mistakes to watch out for:

Overconfidence

Recency bias

Availability bias

Loss aversion

“You must recognize the counterproductive psychology that causes bad investment decisions—such as panic selling—and correct it in yourself. In doing so, your investments will be far simpler and your results far stronger.”

JL Collins, “The Simple Path to Wealth,” p60

“Toughen up cupcake and cure your bad behavior.”

JL Collins, “The Simple Path to Wealth,” p60

If you're unsure, err on the conservative side

“Thinking about the possibility of losing 30% of your capital is like training for an aircraft crash-landing in a simulator; the real thing is a good deal more unpleasant.”

William Bernstein, “The Four Pillars of Investing,” p115

8. Just Say “No”
(Embrace these “Don’ts”)

Don'ts #1 & #2:

Don't look (especially if you are easily spooked)

&

Don't need to know!

“To succeed as an investor, you don’t have to outsmart Wall Street at its own guessing game. A [total stock market index fund] enables you to say seven magic words: ‘I don’t know and I don’t care.’”

Jason Zweig, “Your Money & Your Brain,” p6

Don't #3:

Don't just do something... sit there!

“The French philosopher Blaise Pascal hit the heart of the truth when he wrote, ‘All the misfortunes of men come from only one thing: not knowing how to remain at rest in a room.’”

Jason Zweig, “Your Money & Your Brain,” p226

“You’d get very rich if you thought of yourself as having a card with only twenty punches in a lifetime, and every financial decision used up one punch. You’d resist the temptation to dabble. You’d make more good decisions and you’d make more big decisions.”

Warren Buffett, from Alice Schroeder’s “The Snowball: Warren Buffett and the Business of Life,” p708

Don't #4:
Most of all...

D₂ O₁ N₁ T₁

P₃ A₁ N₁ I₁ C₃

And...

Don't be this guy...

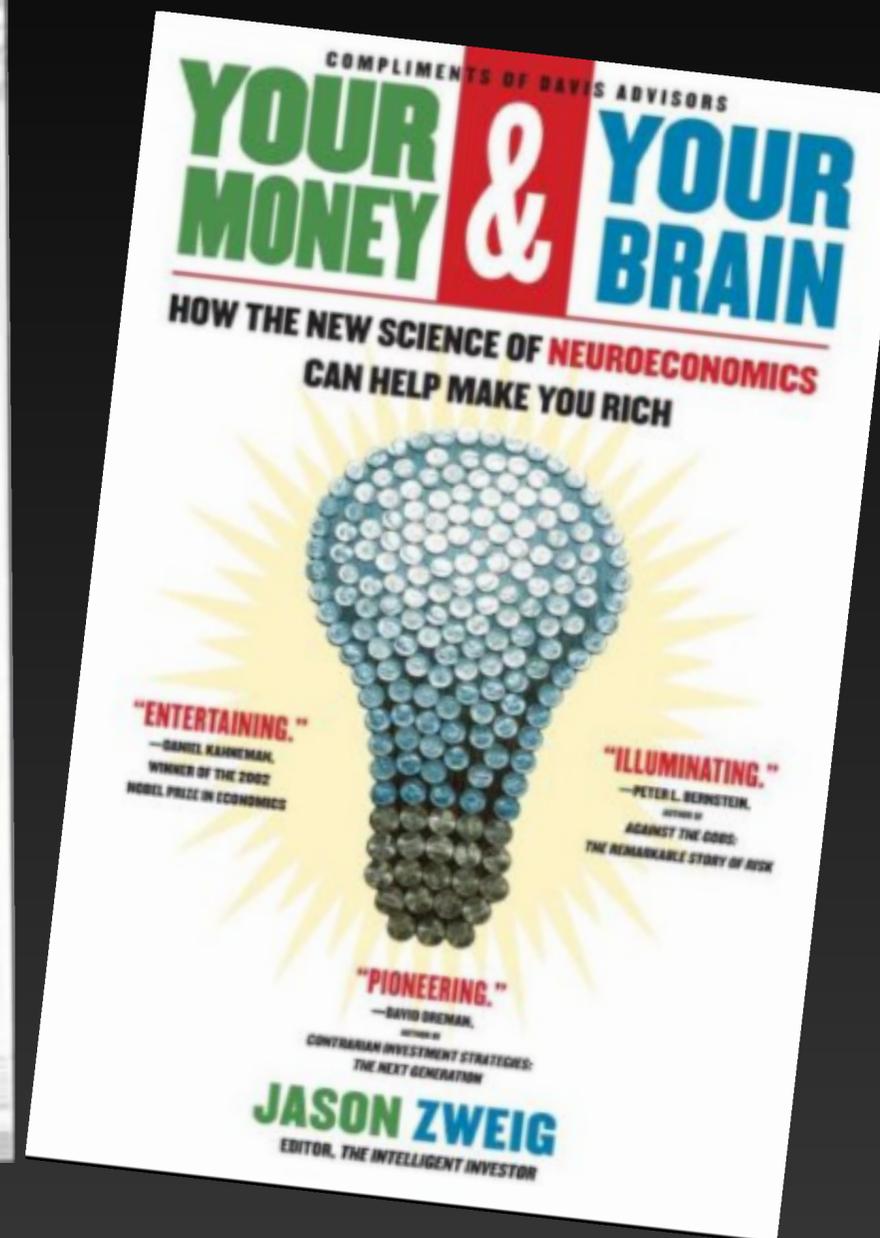
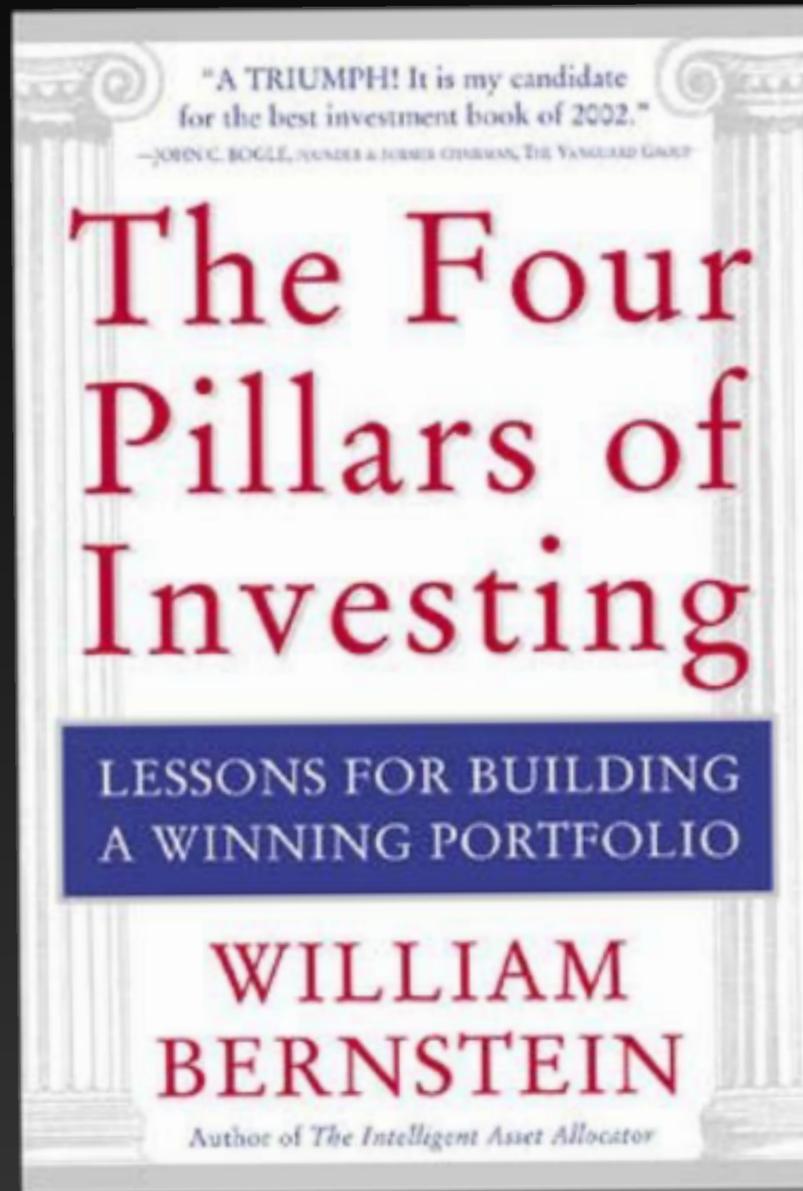
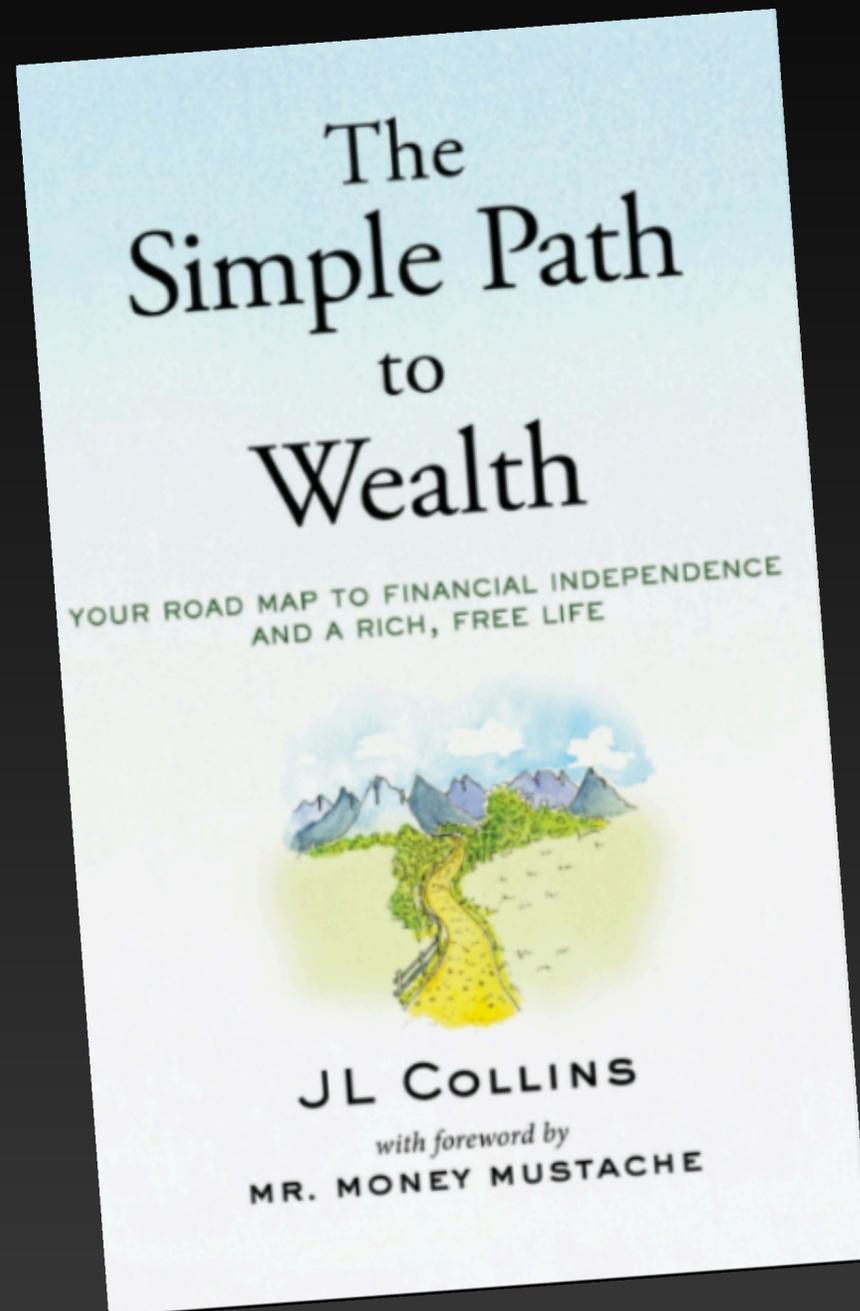


9. Keep Learning & Share What You Know

How to Continue Your Financial Education:

- Read investing books and/or blogs
- Listen to investing-related podcasts
- Participate in Bogleheads meetings!
- Keep investing (and learn from experience)

Today's expert advice comes from:



How to Share Your Investing Ideas and Strategies with Others:

- Start an investing-themed blog
- Discuss investing with interested family/friends
- Give a Bogleheads presentation (like this one!)

“Learning and teaching others are great ways to gain new skills, articulate what matters to you, and maintain your focus on the big picture.”

Me, in this presentation :)

10. Ice Cream!

Enjoy the ride!

Don't Sweat the Small Stuff

**Yum!
:)**

Take it Easy!

**Find things to
Appreciate**

**Look at the
Bright Side**



And now,
something fun...





Thank You!

By Chris Goslow, Sacramento Bogleheads, June 11, 2022