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Beware of Emotions Affecting Your Money Decisions

Today's impulsive moves could breed tomorrow's regrets.

Provided by Chris Eller

When emotions and money intersect, the effects can be financially injurious. Emotions can cause us to overreact – or not act at all when we should.

Think of the investors who always respond to sudden Wall Street volatility. That emotional response may not be warranted, and they may come to regret it.

In a typical market year, Wall Street can see big waves of volatility. This year, it has been easy to forget that truth. During the first third of 2017, the S&P 500 saw only 3 trading days with a 1% or greater swing – or to put it another way, 1% swings occurred just 3.5% of the time. Compare that to 2015, when the S&P moved 1% or more in 29% of its trading sessions.[1]

The 1.80% May 17 drop of the S&P stirred up fear in some investors. The plunge felt earthshaking to some, given the placid climate on the Street this year. Daily retreats of this magnitude have been seen before, will be seen again, and should be taken in stride.[2]

Fear and anxiety can also cause stubbornness. Some people have looked at money one way all their lives. Others have always seen investing from one perspective. Then, something happens that does not mesh with their outlook or perspective. In the face of such an event, they refuse to change or admit that their opinion may be wrong. To lose faith in their entrenched point of view would make them feel uneasy or lost. So, they doggedly cling to that point of view and do things the same way as they always have, even though it no longer makes any sense for their financial present or future. In this case, emotion is simply overriding logic.

What about those who treat revolving debt nonchalantly? Some people treat a credit card purchase like a cash purchase – or worse yet, they adopt a psychology in which buying something with a credit card feels like they are "getting it for free." A kind of euphoria can set in: they have that dining room set or that ATV in their possession now; they can deal with paying it off tomorrow. This blissful ignorance (or dismissal) of the real cost of borrowing can dig a household deeper and deeper into debt, to the point where drawing down savings may be the only way to wipe it out.

How about those who put off important financial decisions? Postponing a retirement or estate planning decision does not always reflect caution or contemplation. Sometimes, it reflects a lack of knowledge or confidence. Worry and fear are the emotions clouding the picture. What clears things up? What makes these decisions easier? Communication with professionals. When the investor or saver recognizes a lack of understanding, shares his or her need to know with a financial professional, and asks for assistance, certainty can replace ambiguity.

Emotions can keep people from doing the right things with their money – or lead them to keep doing the wrong things. As you save, invest, and plan for your future, try to let logic rule. Years from now, you may be thankful you did.

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Citations.
1 - nytimes.com/2017/05/09/upshot/the-stock-market-is-weirdly-calm-heres-a-theory-of-why.html [5/9/17]
2 - google.com/finance?q=INDEXSP:.INX&ei=6RMeWfG_JMO7euKQkagG [5/18/17]