Discover Your Investment EQ

"The most common cause of low prices is pessimism…
It's optimism that is the enemy of the rational buyer."- Warren Buffett

Historically, ask a group of investors to share the 'secret' to successful investing, and you're likely to get many different quantitatively focused answers, ranging from, hold for the long-term, diversified asset allocation, quality research to the much touted 'buy low, sell high' mantra.

Now with turbulent financial markets more focus is coming on to the more qualitative factors like financial behaviour. There is no doubt that pressure will cause more panic and hence potentially very emotional decisions to get made. For many, your true financial behaviour will have been masked by the good times when markets and the economy have been riding high and there has been no financial chaos. The decision making patterns for many of us can change radically when the good times turn to bad. This is when our true natural instincts take over and our true financial behaviour comes into play. So a big key to successful long-term investing is learning to understand your own financial behaviour under pressure and also that of others who you have relationships with.

Recent research into the human mind has found that the secret to success in any long-term endeavor, whether it be in business, relationships or investing, is an attribute called 'Emotional Intelligence' (otherwise known as 'EQ'). EQ is a type of intelligence that's significantly different to the standard IQ-based definition of 'smart' we're all used to. The topic of 'EQ' has received significant coverage in the business world in the last few years, fueled in particular by Daniel Goleman's books which are aimed at helping business people use the skill to further their careers and effectiveness.

Following the four facet Goleman model for EQ, the emotionally intelligent investor would, for instance, make investment decisions calmly based on a higher consciousness of who they are and with a positive personal relationship to money (the first facet of "self-awareness"). This is instead of making decisions based on an emotional impulse which sabotages their financial position. They also handle stress, disappointment and uncertainty more rationally, and don't allow those feelings or circumstances to control or initiate their decisions (the second facet of "self management").

Going further, the emotionally intelligent investor would also understand the emotions of others such as their partner, spouse or family members, recognizing them and responding with empathy (the third facet of "social awareness"). Finally, a person with high Investment EQ would have the ability to maintain quality relationships with others around them when making investment decisions knowing how to, effectively and appropriately motivate them and manage their money energy using subtlety, delicacy and tact (the fourth facet of "managing others").

But the role of EQ in investment has been little publicized, even though its application can be invaluable for investors. Whether this is because the investment process is seen as an objective, numbers-based, non-emotional process, or whether the investment industry has simply not been made sufficiently aware of the existence of EQ, is unclear. Certainly, we believe that both a high level of EQ, combined with sound financial knowledge, strategy and advice, can make the difference between great investors and the also-rans. But sound financial knowledge will not do it alone.

So why is understanding Investment EQ so powerful? It is the ability to give a person enough confidence, focus and rationality to remain committed to their strategies even when the market value of their portfolio is declining, not living up to expectations, or being superseded by other strategies. Investors with a high EQ, in the long term, worry less about their investments, reap higher returns, and make fewer mistakes.

Daniel Goleman, with his co-authors Annie McKee and Richard E. Boyatzis wrote in Primal Leadership, "Negative emotional surges can be overwhelming; they're the brain's way of making us pay attention to a perceived threat. The result is that these emotions swamp the thinking brain's capacity to focus on the task at hand, whether it's strategic planning or dealing with news of a drop in market share." For investors, the 'perceived threat,' whether it be sluggish investments or a drop in portfolio value, causes the brain to be overwhelmed with negative emotions. Without EQ, or an awareness and ability to manage these emotions, they can and do cause havoc for individual investors, and on a larger scale, for investment markets generally.

It's a reasonably well-documented fact that chasing last year's great performers is a poor investment strategy. However, that's how many players in the investment game, even seasoned investors, have made decisions. How often do you see investors with a strategy then not stick to it? It hurts to see someone else doing better than you are, it hurts to see your portfolio performance lagging behind the investment of the moment. It's not the feeling of hurt per se that causes investment damage, but allowing it, even subconsciously, to determine your next investment move.

Emotionally intelligent investors are like the patient driver, sticking to their 'lane'. This doesn't necessarily mean that they'll put up with a poor investment past its used-by date. However, because they have researched their strategies thoroughly, invested in asset classes they understand, and undertaken the volatility level they know they are comfortable with, these investors are able to operate above the emotional level, sticking to their plans unless there are reasonable and rational arguments to do otherwise. They take time to rationally consider their past successes and mistakes, and analyze possible consequences before making the deal.

However, emotionally unintelligent investors often let fear or panic take control, and are more like the aggressive driver, switching lanes whenever something more profitable comes along. They are often after the 'quick kill,' looking for that one deal that they're going to be able to talk about for years to come, even if this desire is subconscious. These investors often commit to investments they know little about or are not suited to, and when things don't go as planned, panic and confusion sets in – the worst possible state of mind in which to be making investment decisions. This is certainly not a deliberate strategy, but when our brain chemistry reacts to danger, it causes us to become emotionally charged – a 'fight or flight' reaction.

Another dangerous trait of the emotionally unintelligent investor is that there's a high likelihood he or she possesses an inflated ego. Research shows that most investors believe, even subconsciously, that they have an edge on others in the market, that they have better intuition than most players and that their technique, whether it be watching stock indices, predicting the behaviour of businesses or CEOs or taking the 'pulse' of the investment community, is inherently better than those techniques employed by others.

Ask most players in the investment game which investor they would most like to emulate, and there are good odds that most of them would answer 'Warren Buffett.' Buffett is a prime example of emotionally intelligent investing. His success, in his own words, is not a result of academic-style intelligence, luck or intuition, but rationality, a key factor of EQ. It was this rationality that keeps Buffett committed to his strategy. During the tech bubble, Buffett was widely criticized for not investing in technology stocks, despite their meteoric rises. His rationale was that he didn't understand them, so he wasn't going to invest in them – an approach that caused more than one of his critics to label him 'irrelevant'. But even if tech stocks hadn't had their dramatic rise and fall, from an EQ perspective, Buffett still did the right thing – he stuck to his very rational and logical guns – guns which he knows intimately.

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The good news is that your Investment EQ can be developed. However, remember that anything developmental is a process and there is no "magic wand". The starting point is with you learning more about your unique financial behavioral style or what we call your "Financial DNA®". The following steps will help you with developing your Investment EQ:

- Starting with the the Financial DNA Core Life Motivations Profile, understand and accept your natural instinctive propensities to risk. This will provide very predictive insights into how much uncertainty you will be willing to bear over the long-term and hence how committed you will be to a long-term strategy particularly, when under pressure.
- Then complete the Financial Directions Profile to understand the influences of your environment, experiences and education on the preferences you have for making investment choices. There will be investment strategies which you will have a greater aptitude towards based on what you have learned, whether they be in the stock market, managed funds, real estate/property or with other investment classes.

- Then analyze the Financial Behaviour Report which documents your complete "Financial DNA" and provides an analysis of your "financial emotional intelligence". This involves reviewing your level of investment alignment by comparing your natural instinctive propensities based on how you are "hard-wired" to your learned preferences which are indicative of how you are currently behaving. These insights may expose some blind-spots.
- Another important step will be comparing your "Financial DNA" to the good and poor financial decisions you have actually made in the past. This will help you pinpoint the investment decisions you will be comfortable in making in the future and to identify areas where greater investment education is required.
- Finally, use this behavioural knowledge of your Financial DNA to help you become personally aligned and become more aware in an overall life sense of what decisions you will be comfortable with. It is important to recognize the overall dynamics of your life will impact every investment decision and the lives of others you have relationships with.

About the Author:

Hugh Massie is the President of Financial DNA Resources. In his work as a Wealth Mentor, Hugh specializes in human behavioural discovery using the proprietary Financial DNA® Discovery Process to liberate and empower people, families and organizations internationally to implement committed wealth creation decisions aligned to the core of who they are. Hugh is the author of a book "Financial DNA® – Discover Your Unique Financial Personality for a Quality Life". If you would like to learn more about Financial DNA visit www.financialdnaresources.com. Hugh can be contacted at inquiries@financialdna.com