

Behavior Perspectives on Making Investment Mistakes

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Classic economics theory assumes individuals are completely informed and rational when making decisions. However, in reality, decision makers go through both a rational and an emotional process in their brain. In some situations, emotional elements dominate the decision-making process (Ozmete & Hira, 2011; Tilson, 2005). Emotionally driven investment behaviors could lead to unnecessary realization of financial losses, which can impede investors' ability to accumulate wealth and jeopardize their financial goal achievement. Understanding factors that affect investors' decision-making is the first step into the solution to help investors overcome behavior biases and avoid investment mistakes.

Using data from the 2008 FPA-Ameriprise Financial Value of Financial Planning Research Study, this study identifies the factors related to making investment mistakes. Investment mistakes in this study refers to moving assets into more of a cash position in a down market while having an adequate level of emergency fund. Results show that investors who are male, Asian, wealthier, overconfident, loss averse and reported an understanding of financial risks are more likely to make such investment mistakes. These findings have important implications for investors, their financial advisors and financial planning professionals in general.

References

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Tilson, W. (2005). *Applying behavioral finance to value investing*. Retrieved from <http://www.tilsonfunds.com/TilsonBehavioralFinance.pdf>.

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