The Wisdom of the Wealthy

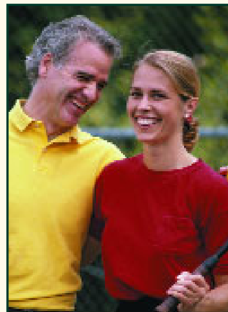
8 Powerful Investor Insights

To ensure that we become financially independent, we need to invest with insight. We become wise by learning from those who have already succeeded. Let's examine eight important insights. This knowledge, when applied to investing can help anyone succeed on the road to creating wealth, and achieving a secure retirement.

1. The Wealthy Know: Diversity protects your portfolio. If you are diversified, investing 30% of your RRSP for example, in economies that are not in a market downturn when Canada is—30% of your portfolio may continue to grow. Thus any loss in Canada is offset by gains in these other economies. Similarly balance your portfolio so as not to be excessively invested in one sector such as technology. Spread your money over a wider "basket of eggs". The differing sectors and economies will work to create a more positive averaging effect. Diversity can minimize initial losses in a market downturn.

2. The Wealthy Know: You can't predict consistently when a market will decline. All investors should know the "bear essentials" of how to approach a bear market without fear. Let's face it, we are all human—market downturns are the last thing anyone really wants to experience, even though informed investors expect them to happen. Without this foresight, an investor may have thought that the bull markets of the 1990's were here to stay. Though you can't predict when, rising markets eventually slow down.

> *"Bear markets have always been temporary". - Sir John Templeton*



Frequent declines range from 5% to 10% occurring from one to three times a year. Let's examine what happens in a bear market. As a rule of thumb, we enter a bear market about once every three to five years and it lasts for a good part of a year. The entire market loses about 20% of its value. Because the market never clearly warns you beforehand, it is important to be intelligently prepared for the bear.

We never know when a market will decline significantly. But how you react to these declines will critically affect the long-term performance of your portfolio. The investor who gets nervous and frightful, usually makes the biggest blunders by selling and sitting on the sidelines until after the recovery is well underway. The result? Mediocre long-term performance.

> *"Constantly switching your money from one fund to another is an expensive habit that is harmful to your net worth". - Peter Lynch*

3. The Wealthy Know: Fear is your worst enemy. For many, the intentions are good. When the markets become jittery, the temptation to redeem investments increases. Some investors understand that investments are long-term, but forget the big picture—you should expect to encounter many market cycles during your long-term investing program. Prepare for much longer timelines that will take you well into retirement; accordingly, do not micro-focus on the market every three months.

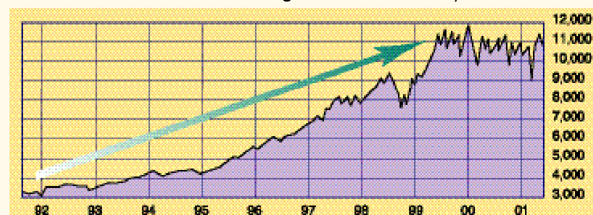
An investor who sells in the midst of a decline, is presented with another decision-making risk. The big question is, "when should I get back into the market?" By indecisively waiting too long, an investor may incur investment losses related to missing the next big move upwards in value. Procrastination is another manifestation of the fear of loss. The successful investor knows—because markets are cyclic—he or she has nothing to fear, except fear itself.

4. The Wealthy Know: What goes down, must come up. Markets are cyclic. Wealthy investors purchase mutual funds and other investments with rational minds that reflect on the history of the markets: they have witnessed and therefore expect market downturns. They know that markets will always recover and boom again, creating more wealth. This long-range approach takes the worry out of investing. It is so simple, yet people forget that what goes down, must come up and visa versa. Downturns and recoveries are both regular market events.

By examining the two ten year graphs of the Toronto Stock Exchange's 300 Composite Index and the US, Dow Jones Industrial Average, you will quickly see that the trend is for growth over time in these major indices. What goes down, over the long term certainly goes way up. You can see the dips occurring in both the Canadian and US markets at random as the market cycles repeat over a ten year period.

TSE 300 Composite Index - 10 Year Weekly Close

Dow Jones Industrial Average - 10 Year Weekly Close



If you are 30, you have 35 years until you're 65, and another potential 25 years of retirement, as life spans are increasing. Furthermore, women live on average, 7 years longer than men.

Most Investors Have a Long Time to Invest

Your Age	Years Before Age 65	Potential Years of Retirement Age 65 to 90	Total Years Remaining to Invest
30	35	25	60
40	25	25	50
50	15	25	40
60	5	25	30

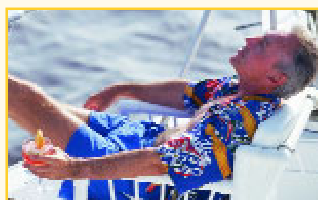
5. The Wealthy Know: Remain invested when others sell. You can never time the market perfectly by selling mutual fund units (or individual stocks) after the market has dropped in value. Inflated markets undergo corrections, where they may lose 10% or more. But they also climb right back up in value. If one sold out of fear, right when it was at 90% of its original pre-market-blues value, the opportunity of recovering that 10% loss would be gone. The novice investor often falls prey to media negativity and in some cases sells the asset to his or her disadvantage.

6. The Wealthy Know: Declining markets present a buying opportunity. When markets lose value, many mutual funds also decrease in value. Wise investors recognize this as a buying opportunity and purchase more mutual fund units. When the market recovers, often the value of these bargain-priced funds rise in tandem, creating greater wealth.

7. The Wealthy Know: You must think contrary to the crowd. Media sensationalism comes and goes. The wealthy exercise a key virtue. They think independently, patiently, and contrary to the crowd. It is exactly when the media is having a hay-day with negative articles and TV market-watch dialogue, when the market is losing value, that wise investors resist the "media noise" and human behaviour based on fear.

"It is impossible to produce a superior performance unless you do something different from the majority". - Sir John Templeton

8. The Wealthy Know: You must think of prosperity today. Economic futurists foretell of a time when trillions of retirement dollars will be spent beginning about 2015. We must realize that, if boomers are to participate in this future spending wave, they will need to invest and build a strong portfolio today. Wise investors continue to increase total investments in mutual funds year after year, despite market corrections. Why is this? If you examined their investor strategies, you might just find that they (a) rejected the fearmongers, (b) acted on the knowledge that weak markets always recover, (c) stayed invested in the market, and (d) concluded that low prices offered during market downturns are a "buy"—so they invested, enacting the principals of the wealthy.



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