Issue 138

A Peek into the PRIME QUADRANT

Registration is now open

2018 Prime Quadrant Conference

Nov 1, 2018

www.pqconference.com to register!

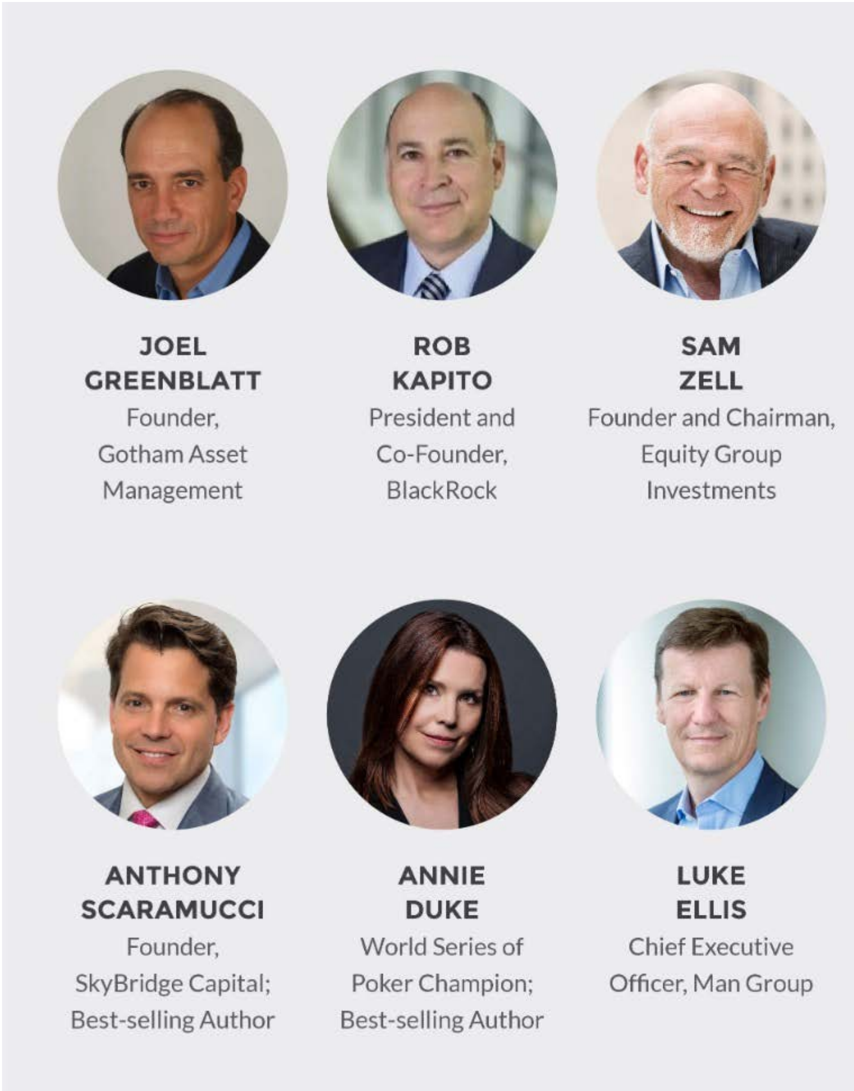
Some of our 2018 Speakers include:

Upcoming Investor IQ Workshops

June 27, 2018
Selling Your Business & Beyond

September 5, 2018
A Primer on Investing in Credit

November 1, 2018
The 2018 PQ Conference



Stories of Interest

Is Investment Management a Science?
How can we test if investment management is a science? And if it is, is there any value to knowing that?

The Costliest Bias of All
Watch the video below for a deeper look into how many ways your overconfidence is costing you money.

What is the PQ?

In financial terms, the Prime Quadrant is the optimal zone in which you achieve the highest return per unit of risk.

Being in the Prime Quadrant requires seeing the big picture and making intelligent choices, from among all investment options and strategies, to best meet your goals.

Prime Quadrant is an investment research and consulting firm that helps high-net-worth Canadians make better investment decisions.

[It Seemed Like a Good Idea at the Time]
Even Charlie Munger can attest to the paragon of rationality, thinking differently in a "hot state" than he would in a "cold state."

[Obvious Things that Easily Escape Attention]
Attention is drawn to what appears most consequential. This results in deceptions that can significantly hinder your success and investment returns.

The Way We See It

Below is an excerpt from a recent presentation by Mo Lidsky.

Unrealistic Expectations

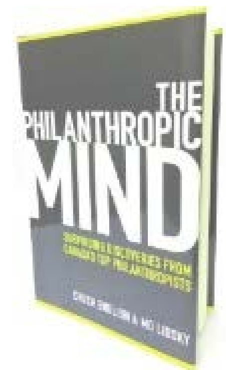
In February of 2016, Natixis Global Asset Management surveyed 550 financial advisors across 15 countries. The study revealed that global investors expect to achieve an annual return of 9.5% percent on their investments. The 2016 Schroders Global Investor Study, which studied 22,000 people in 30 counties around the globe, seemed to suggest investors expect an average return of 10.2% from their portfolios (and 13% of investors' surveyed expected returns of 20% or more).

Have investors completely lost their minds???

When the global bond market is yielding lower than 1.6% and dividends in stocks on the S&P 500 are yielding between 2-3%, where do investors think these 8.5-9.5% returns will come from? Unless interest rates fall further (which is highly unlikely), people apply a great deal of leverage (which is highly imprudent), or the masses can access asset classes not available to them (which is improbable), these expectations are just an illusory dream. The problem is that this is somewhat ubiquitous. Investors have long had unrealistic expectations and these expectations manifest themselves in a variety of ways.

1. **Unrealistic about asset classes.** Research suggests that investors get consistently excited about individual asset classes at the wrong points in the cycle (i.e. on the highs, rather than the lows). Think about investor sentiment at the peak of asset classes like: technology, real estate and now crypto-currencies.
2. **Unrealistic about MY returns.** We all believe we're better looking, more intelligent and have a better sense of humor than the average Joe. The same optimism bias permeates our expectations about the markets. A 2013 survey by Fidelity suggested that 77% of high-net-worth investors believe they will beat the market. Now, obviously, 77% can't be better than average. But human folly and rationality based on real data rarely share the same bed.
3. **Unrealistic about where we are in the cycle.** Averages are deceiving. As we saw earlier, the stock market might average 7% over a 100-year period, but there's no assurance that it will happen in any given period. Moreover, Murphy's law would suggest that the disappointing news will arrive precisely when you are most reliant on that 7% to sustain you.
4. **Unrealistic about money managers, chasing recent performers and expecting consistency.** We are constantly committing sampling error. We're like the children who go to a baseball game, see a player get out three consecutive times and assume they're atrocious. Or we'll see another player who gets on base three straight times and assume they're a star. Nothing can be determined in three at-bats. Though, after seeing 500 at-bats, reality is much more self-evident. The smaller the sample size, the more extreme the outcomes; the larger the sample size, and more reliable the outcomes. Identifying what is an appropriate sample size with money managers is critical.

The Philanthropic Mind is also available on Amazon, Indigo and Barnes & Noble.



5. **Unrealistic due to survivorship bias.** Survivorship bias is the tendency for us to overestimate past performance because we only see the returns of those companies and funds that survived, and forget those with poor performance that have been buried in history. This phenomenon skews the averages and thereby skews our expectations.

When this unreal-ism leads us to over-shoot or, worse yet, to consume on the assumption that the unrealistic returns will be there, trouble is looming. The world's greatest investors are not necessarily exceptional money makers. Rather, they are merely exceptional at not losing it, and at having reasonable expectations. A 2010 study by Ipsos Reid, entitled *Investor Research: The Value of Advice*, demonstrates that over a 15-plus year period, families who use an investment advisor have, on average, 2.7 times more investable assets than families who have never used an investment advisor. The reason may, in part, be simply a moderating voice that can lower expectations, restrain the chasing of performance and mitigate imprudent behaviors.

> **"The investor's chief problem and even his worst enemy is likely to be himself."**
>
> ***- Benjamin Graham***

PRIME QUADRANT

BETTER INVESTMENT DECISIONS

investments and income can go down as well as up (which may be caused by exchange rate fluctuations). The past is not necessarily a guide to future performance.

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