



The Investor in the Mirror

Master the psychology behind your money to stop outsmarting your own success

Why do intelligent, capable people make irrational investment decisions? If everyone knows the goal is to “buy low and sell high,” why do so many investors end up doing the opposite?

The issue rarely comes down to knowledge. It comes down to psychology.

Your Brain Wasn't Built for Modern Markets

Market volatility triggers a deeply wired human instinct that signals danger. When we sense danger, our brains urge us to act quickly. That reaction helped humans survive thousands of years ago. In long-term investing, it often causes more harm than good.

This is why advisors often say financial planning is 10% math and 90% temperament. The math behind diversification, asset allocation, and tax efficiency is important, but it only works if your behavior allows it to work.

During periods of uncertainty, investors often struggle to manage their emotions. Uncertainty creates discomfort, and discomfort pushes people to take action so that they feel in control, even when the wiser move might be to stay the course.

The Blind Spots Investors Overlook

After working with thousands of households, our advisors at Klaas Financial consistently see three psychological patterns that cause investors to work against their own long-term success.

1. Loss Aversion: Losses Hurt More Than Gains Feel Good

The pain of losing \$1,000 is much stronger than the joy of gaining \$1,000. Because losses feel so intense, even temporary portfolio declines can feel like something is wrong. This often leads investors to pull back at exactly the wrong moment.

This emotional breaking point commonly appears during routine market cycles. A normal correction can feel catastrophic. When that happens, fear-driven decisions can interrupt long-term growth.

2. Recency Bias: Assuming Today's Market Will Continue Forever

People tend to believe that whatever just happened will keep happening.

If markets have been strong, it feels like the growth will continue. If markets have struggled, it feels like the downturn will last indefinitely. This is when investors often say one of the costliest phrases in finance: “This time is different.”

During the COVID-19 selloff in March 2020, many investors felt certain markets would not recover. Yet roughly five months later, the market had bounced back to its previous high and has grown significantly since.

Headlines always feel unprecedented. Circumstances always feel unique. Market cycles are normal, and emotional decisions during these cycles often come at a steep cost.

3. Anchoring: Fixating on the Peak Value

Many investors anchor to the highest value their portfolio has ever reached. When their account drops below that number, even if they are still far ahead over several years, it can feel like a permanent loss.

This distorted perspective shifts attention away from long-term progress and toward short-term frustration. That frustration increases the temptation to make reactive changes.

The Hidden Role of a Financial Advisor

A large part of an advisor's value comes from serving as an emotional circuit breaker. Advisors help clients avoid permanent mistakes triggered by temporary emotions.

At Klaas Financial, that process begins with building a written investment policy, including:

- a target asset allocation
- acceptable ranges for each allocation
- a disciplined rebalancing strategy

When volatility hits, the plan guides the next decision. The more choices you make in advance, the fewer decisions you need to make during stressful periods.

This discipline is especially important today. Economic conversations move quickly, and headlines can create a sense of urgency. A retirement plan should not change because of a news cycle or a conversation in a coffee shop. It should reflect personal goals, timelines, and the cost of maintaining your lifestyle over time.

Why Systems Help You Stay the Course

Rules-based rebalancing keeps investors disciplined throughout the market cycle.

If stocks rise ahead of target, you trim them. If stocks fall below target, you buy more.

This simple framework:

- removes emotion from decisions
- encourages buying low and trimming high
- prevents risk from drifting higher than intended during bull markets

It also helps separate short-term money from long-term money. When dollars you need soon are mixed with dollars meant for future growth, every bit of volatility feels like a crisis. Keeping these timelines distinct reduces stress and makes it easier to stay invested.

Does Your Portfolio Match Your Emotional Tolerance?

A useful starting point is to ask yourself:

“What percentage drop would make me want to change strategies?”

10 percent, 20 percent, 30 percent.

Many investors overestimate their tolerance for risk when markets are calm. The real test comes during a downturn. If your portfolio is designed for a 25 percent swing but your breaking point is closer to 15 percent, that mismatch becomes a structural risk. Eventually, emotions win, and a reactive decision can undo years of disciplined saving.

The best portfolio is not the one with the highest projected return. It is the one you can confidently stick with when the market becomes turbulent.

Discipline compounds. Every time you stay invested during volatility, you allow compounding to continue its work. Every time you abandon a strategy because of fear, you interrupt that process.

Final Thoughts: You Can Prepare for Volatility

You cannot remove uncertainty from investing, and you do not need to. Markets move in cycles, and downturns will always occur.

However, you can prepare for them.

- Build a plan that assumes volatility will happen.
- Align your investments with both your goals and your comfort level.
- Use systems instead of emotion to guide decisions.
- Evaluate whether your portfolio truly matches your tolerance for risk.

If you are unsure whether your investment strategy fits your temperament, consider speaking with a financial advisor or completing a formal risk assessment. Understanding your own emotional limits is one of the most powerful tools you can have.

The market will always test you. Successful investing is not about predicting the next headline. It is about mastering your behavior.

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