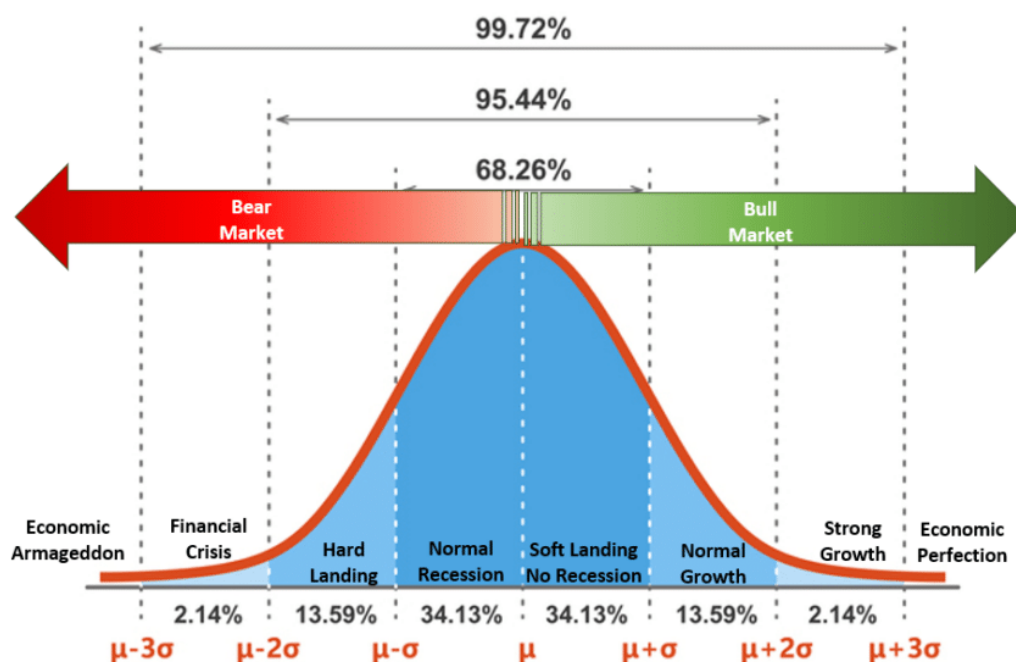


While often difficult, investing rules can help us maintain our focus and investment discipline in volatile or uncertain markets. This year, such has certainly been the case with surging interest rates, expectations of a recession, and geopolitical conflicts in two countries. In times like this, it is easy for us to imagine the worst of possible outcomes. However, [in last week's newsletter](#), we discussed the "probabilities" and "possibilities" of macro outcomes. To wit:

*"On [Wednesday's Real Investment Show](#), I spent a good bit of time discussing the normal distribution of events in the economy. The chart below is a normally distributed "bell curve" of potential events and outcomes. In simple terms, 68.26% of the time, normal outcomes occur. Economically speaking, such would be a normal recession or the avoidance of a recession. 95.44% of the time, we are most likely dealing with a range of outcomes between a fairly deep recession and normal economic growth rates. However, there is a 2.14% chance that we could see another economic crisis like the 2008 Financial Crisis.*

***But what about "economic armageddon?"*** An event where nothing matters but "gold, beanie weenies, and bunker." is just a 0.14% possibility."



While "fear sells," we must assess the "probabilities" versus "possibilities" of various outcomes.

Poker is always an easy way to understand this concept.

If you were playing a hand of poker and were dealt a ?pair of deuces,? would you go ?all-in??

Of course not.

The reason is you intuitively understand the other factors *?at play?* **Even a cursory understanding of the game of poker suggests other players at the table are probably holding better hands, which will rapidly reduce your wealth.**

Investing in the financial markets is one of the purest forms of speculation. Every day, investors make bets on the future and must weigh the possibilities and probabilities of winning or losing. The size of the *"bet"* should ultimately be determined by the *"potential loss"* of being wrong.

Ultimately, investing is about managing those risks that will substantially reduce your ability to *?stay in the game long enough?* to *?win.?*

So, how do you navigate volatile markets and stay within the "probabilities" of outcomes when emotions run high? Here are ten basic investing rules that have historically kept investors out of trouble over the long term. These are not unique by any means but rather a list of investment rules that, in some shape or form, have been uttered by every great investor in history.



Need a plan to protect your hard earned savings from the next bear market?

> Schedule your consultation today

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## Investing Rule #1) You Are A ?Saver? ? Not An Investor



Unlike Warren Buffet, who takes control of a company and can affect its financial direction ? you are speculating that a purchase of a share of stock today can be sold at a higher price in the future. Furthermore, you are doing this with your hard-earned savings. If you ask most people if they would bet their retirement savings on a hand of poker in Vegas, they would tell you *?no.?* When asked why, they will say they don't have the skill to be successful at winning at poker. However, daily, these same individuals will buy shares of a company in which they have no knowledge of operations, revenue, profitability, or future viability simply because someone on television told them to do so.

Keeping the right frame of mind about the *risk* that is undertaken in a portfolio can help stem the tide of loss when things inevitably go wrong. Like any professional gambler the secret to long-term success was best sung by Kenny Rogers; *You gotta know when to hold'em?know when to fold'em.*

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## Investing Rule #2) Don't Forget The Income

**“Investment** - Is an asset or item that is purchased with the hope that it will generate income or appreciate in the future. ”

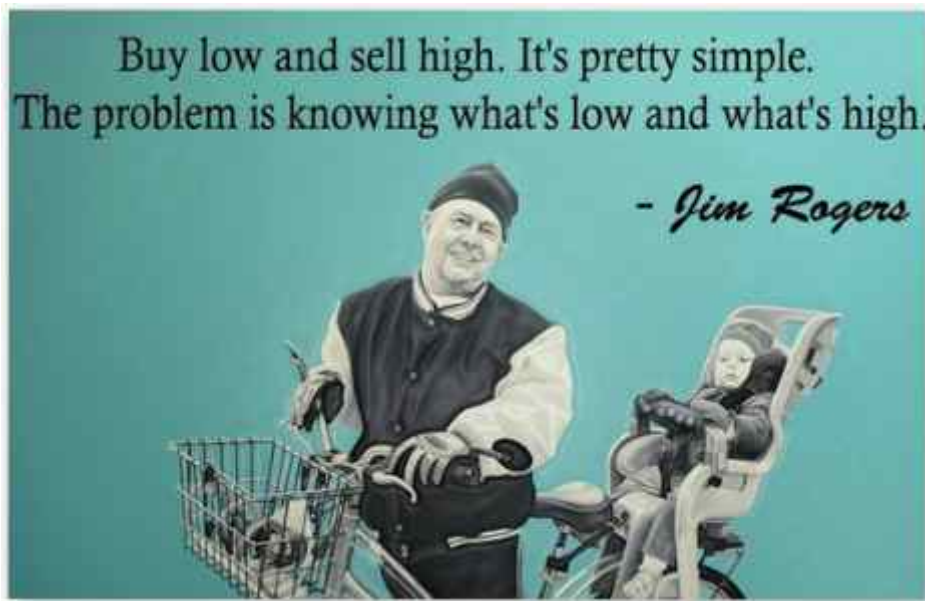
Investment Brothers

22 Nov 2012 5:16 pm

An investment is an asset or item that will generate appreciation OR income in the future. Little diversification is left between asset classes in today's highly correlated world. Markets rise and fall in unison as high-frequency trading and monetary flows push related asset classes in a singular direction. This is why including other asset classes, like fixed income, which provides a return of capital function with an income stream, can reduce portfolio volatility. Lower volatility portfolios will consistently outperform over the long term by reducing the emotional mistakes caused by large portfolio swings.

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## Investing Rule #3) You Can't Buy Low If You Don't Sell High?



Most investors do fairly well at *buying* but stink at *selling*. The reason is purely emotional, driven primarily by *greed* and *fear*. Like pruning and weeding a garden, a solid discipline of regularly taking profits, selling laggards, and rebalancing the allocation leads to a healthier portfolio over time.

Most importantly, while you may *beat the market* with *paper profits* in the short term, it is only the realization of those gains that generate *spendable wealth*.

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## Investing Rule #4) Patience And Discipline Are What Wins

Learn the art of patience. Apply discipline to your thoughts when they become anxious over the outcome of a goal. Impatience breeds anxiety, fear, discouragement and failure. Patience creates confidence, decisiveness, and a rational outlook, which eventually leads to success.

(Brian Adams)

izquotes.com

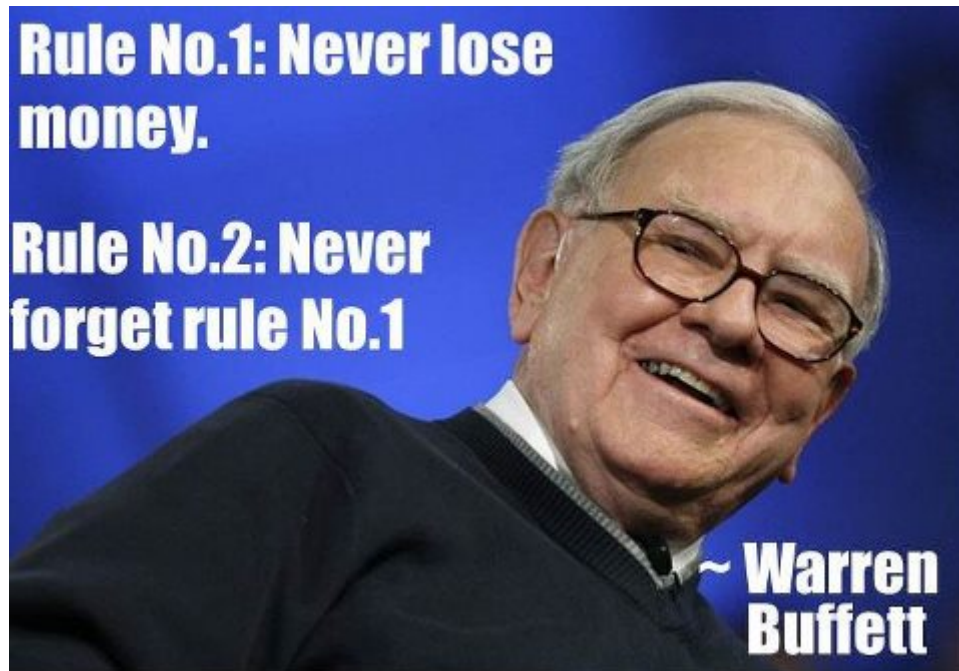
Most individuals will tell you they are *long-term investors*. However, as Dalbar studies have repeatedly shown, investors are driven more by emotions than not. The problem is that while individuals have the best of intentions of investing long-term, they ultimately allow *greed* to force them to chase last year's hot performers. However, this has generally resulted in severe

underperformance in the subsequent year as individuals sell at a loss and then repeat the process.

This is why truly great investors stick to their discipline in good times and bad. Over the long term ? sticking to what you know and understand will perform better than continually jumping from the ?frying pan into the fire.?

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## Investing Rule #5) Don?t Forget Rule No. 1



As any good poker player knows, you are out of the game once you run out of chips. This is why knowing both ?when? and ?how much? to bet is critical to winning the game. The problem for most investors is that they are consistently betting ?all in, all of the time.?

Over time, the ?fear? of missing out in a rising market leads to excessive risk buildup in portfolios. It also leads to a violation of the simple rule of ?sell high.?

The reality is that opportunities to invest in the market come along as often as taxi cabs in New York City. However, trying to make up lost capital by not paying attention to the risk is a much more difficult thing to do, which brings us to Rule #6.

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## Investing Rule #6) Your Most Irreplaceable Commodity Is ?Time.?





**Time is more valuable  
than money.**

**You can get  
more money,  
but you cannot  
get more time.**



Since the turn of the century, investors have theoretically recovered from two massive bear market corrections. After 15 years, investors finally returned to where they were in 2000. Such is a hollow victory when considering that 15 years to prepare for retirement are gone. Permanently.

For investors, getting back to even is not an investment strategy. We are all *savers* with a limited amount of time to save money for our retirement. Those retirement plans were vaporized if we were 15 years from retirement in 2000. Could such an environment happen again? Absolutely. It is ultimately a function of valuations. Will it happen? No one knows.

Do not discount the value of *time* in your investment strategy.

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**Investing Rule #7) Don't Mistake A *Cyclical Trend* As An *Infinite Direction*.**



An old Wall Street axiom says the *?trend is your friend.?* Unfortunately, investors repeatedly extrapolate the current trend into infinity. In 2007, the markets were expected to continue to grow as investors piled into the market top. In late 2008, individuals were convinced that the market was going to zero. Extremes are never the case. The same occurred at the bottom of the market in March 2020.

It is important to remember that the *?trend is your friend.?* That is, as long as you pay attention to it and respect its direction. Get on the wrong side of the trend; it can become your worst enemy.

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## **Investing Rule #8) Success Breeds Over-Confidence**

We tend to  
think we are  
better investors  
than we really  
are

Individuals attend college to become doctors, lawyers, and even circus clowns. Yet, every day, individuals pile into one of the most complicated games on the planet with their hard-earned savings and little or no education.

When the markets are rising, most individuals' success breeds confidence. The longer the market rises, the more individuals attribute their success to their own skills. The reality is that a rising market covers the multitude of investment mistakes individuals make by taking on excessive risk, poor asset selection, or weak management skills. These errors are always revealed by the forthcoming correction.

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## **Investing Rule #9) Being A Contrarian Is Tough, Lonely & Generally Right.**

Successful contrarian investing requires us to live with discomfort, for being "wrong" and alone. But bargains do not exist in the absence of fear.

Robert D. Arnott

quote fancy

Howard Marks once wrote that:

*Resisting ? and thereby achieving success as a contrarian ? isn't easy. Things combine to make it difficult; including natural herd tendencies and the pain imposed by being out of step, since momentum invariably makes pro-cyclical actions look correct for a while. (That's why it's essential to remember that ?being too far ahead of your time is indistinguishable from being wrong.?)*

*Given the uncertain nature of the future, and thus the difficulty of being confident your position is the right one ? especially as price moves against you ? it's challenging to be a lonely contrarian.?*

Historically, making the best investments occurs when going against the herd. Selling to the *?greedy?* and buying from the *?fearful?* are extremely difficult things to do without a very strong investment discipline, management protocol, and intestinal fortitude. For most investors, the reality is they are inundated by *?media chatter.?* That "noise" keeps them from making logical and intelligent investment decisions regarding their money, which, unfortunately, leads to bad outcomes.

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## Investing Rule #10) Comparison Is Your Worst Investment Enemy



**“INVESTING SHOULD BE MORE LIKE WATCHING  
PAINT DRY OR WATCHING GRASS GROW. IF YOU  
WANT EXCITEMENT, TAKE \$800 AND GO TO  
LAS VEGAS.”**

**PAUL SAMUELSON**

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The best thing you can do for your portfolio is to stop benchmarking against a random market index. That index has nothing to do with your goals, risk tolerance, or time horizon.

Comparison in the financial arena is the main reason clients have trouble patiently sitting on their hands, letting whatever process they are comfortable with work for them. Unfortunately, some comparison along the way causes investors to lose their focus.

It is pleasing to inform clients they made 12% on their account. However, if you inform them that ?everyone else? made 14%, you have upset them. As it is constructed now, the financial services industry intentionally upsets people, so they move money around in a frenzy. Money in motion creates fees and commissions.

Creating more benchmarks and style boxes is nothing more than creating more things to COMPARE to, allowing clients to stay in a perpetual state of outrage. The only benchmark that matters is the required annual return to obtain your future retirement goal. If that rate is 4%, then trying to obtain 6% more than doubles the risk you have to take to achieve that return. The end result of taking on more risk than necessary will cause you to deviate from your goals when something inevitably goes wrong.

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## It's All In The Risk

Robert Rubin, former Secretary of the Treasury, changed the way I thought about risk when he wrote:

*?As I think back over the years, I have been guided by four principles for decision making. First, the only certainty is that there is no certainty. Second, every decision, as a consequence, is a matter of weighing probabilities. Third, despite uncertainty we must decide and we must act. And lastly, we need to judge decisions not only on the results, but on how they were made.*

*Most people are in denial about uncertainty. They assume they're lucky, and that the unpredictable can be reliably forecast. This keeps business brisk for palm readers, psychics, and stockbrokers, but it's a terrible way to deal with uncertainty. If there are no absolutes, then all decisions become matters of judging the probability of different outcomes, and the costs and benefits of each. Then, on that basis, you can make a good decision.?*

It should be obvious that an honest assessment of uncertainty leads to better decisions, but the benefits of Rubin's approach go beyond that. Although it may seem contradictory, embracing uncertainty reduces risk while denial increases it. Another benefit of ?acknowledged uncertainty? is it keeps you honest. A healthy respect for uncertainty and a focus on probabilities drives you never to be satisfied with your conclusions. It keeps you moving forward to seek more information, question conventional thinking, continually refine your judgments, and understand that certainty and likelihood can make all the difference.

The reality is that we can't control outcomes; the most we can do is influence the probability of certain outcomes, which is why the day-to-day management of risks and investing based on probabilities rather than possibilities is important not only to capital preservation but to investment success over time.