

What I Learned About Money from *Million Dollar Baby*

By Neal Frankle, CFP®

In Clint Eastwood's award-winning movie, *Million Dollar Baby*, we see a positive, respectable, hard-working young woman physically destroyed when her dirty-dealing opponent lands a sucker punch after the bell.



It occurs to me that the same thing can happen with investments. The admirable fighter inside you tries to make your financial dreams come true. That's the inner voice that tells you to work hard and invest smart. Your opponent is the part of you ruled by your emotions. Those emotions look for every opportunity to land a sucker punch and bring you down.

When I first met Bill, for example, he was worth \$10,000,000, yet he was miserable. Because he'd grown up during the depression, he was convinced that he was always one step away from being broke, hungry and homeless. Keep in mind that Bill was taking only \$150,000 a year from his \$10 million nest egg. If you do the math, you'll see that his

withdrawal rate was barely 1.5%. So Bill really didn't have to worry about money ... but he worried anyway, and he was ruled by his fear and greed.

Because Bill was convinced that he was going to run out of money, he continued to make high-risk investments in the hopes of having more. He often lost a great deal of money with these chancy ventures, and this behavior made his fear a self-fulfilling prophecy. As his losses grew, his emotional need to make up for those losses grew, too. He took ever-greater risks and continued to dig himself into a miserable hole. It was a classic emotional smack-down.

Others dance the opposite direction. People who suffer great investment losses understandably become gun-shy. They are afraid of getting pounded again, so they swear off investing forever-and miss out on securing their financial future.

Are your emotions beating up your investments? Do you take risky chances for no good reason? Or is your anxiety making you afraid to come out of your corner fighting? Let me tell you something. In the arena of investments, your emotions are always in the back room working the speed bag just waiting for the chance to floor you. You need an edge if you want to stay in the ring.

How would you like to have the financial equivalent of Muhammad Ali as your trainer?

Here are a few tips that can give you that kind of an edge.

First, recognize that you'll never totally eliminate emotions from your financial decisions. You can't knock them out. **Second, know that you can neutralize them.**

How? Remember the trainer's advice: Always protect yourself.

One way to keep your guard up is to use stop-losses on all your investments. If you're not familiar with a stop-loss, it's a simple tool you use to reduce risk. Let's say you buy a stock at \$50, and you are convinced the stock is going to \$80. Put a stop of \$45 on the position. If the stock goes all the way, the stop doesn't hurt you. But if you're wrong, and the stock hits the mat, the stop-loss becomes very important.

Once the stock drops to a price of \$45 or less, the position is sold. What happens if the stock later renews its strength and climbs back to \$80? Too bad. You sold at \$45, and you no longer hold the position. This is the downside to using stop-loss orders.

What happens if the stock continues its downward spiral and falls to \$15? You don't care because you sold the position at \$45. Could this happen? It happens every day. Just ask people who bought tech stocks in the early part of 2000.

You can effectively use stop-loss orders to limit your downside risk on all your stock and mutual fund investments. If you do this, you'll be able to go the 10 rounds without getting knocked silly by your emotions.

Neal Frankle is the author of Why Smart People Lose a Fortune: 5 Steps to Restoring Your Wealth and Sanity. He helps affluent clients establish and implement a safety-net strategy to protect their wealth. He also helps other professionals, such as CPAs, to do the same thing for their clients.

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