

3 biases to watch out for in a volatile market

And how to help clients overcome them



When markets are in turmoil, clients get anxious—and anxiety often leads to poor investment decisions. We created this short guide to help you ease your clients' concerns and guide them through periods of market volatility. Here are the three biases we've found most prominent in a crisis, along with suggested remedies to keep your clients on track.



Recency bias

Putting too much emphasis on recent events

What behaviors to look for

Your client wants to chase recent performance winners or sell everything during a downturn.

How you can address it

- Explain that the recent past doesn't predict future performance
- Keep your clients' portfolios diversified with the proper risk profile
- Avoid concentrated positions in specific stocks

Investment strategies and solutions to consider

Model portfolios: Informed by investor behaviors, these rule-based portfolios avoid concentrated stocks in favor of increased diversification at an affordable cost.

Tax-loss harvesting: This strategy can help clients reduce exposure after a downturn. By selling securities at a loss, clients can offset capital gains and associated taxes and add investments with better potential.



Regret aversion

Avoiding financial decisions out of fear of making the wrong decision and regretting it

What behaviors to look for

Your client avoids selling a losing stock, decides to move to cash or stops investing altogether after taking losses.

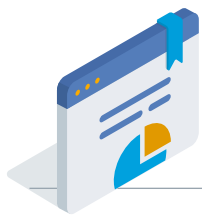
How you can address it

- Make sure your client's portfolio has the right risk profile and can withstand the associated risk
- Avoid staying too conservative or taking excessive risks by buying double the exposure of losing stock
- Allocate a predetermined % of client income to investments to benefit from cost averaging and keep from focusing on a particular investment time or decision

Investment strategies and solutions to consider

Fundamental index strategies: These strategies tend to be less affected by market corrections given their focus on companies with strong fundamentals.

Target Date Funds (TDFs): TDFs become more conservative over time, helping align an investor's risk profile and encourage automatic investment.



Anchoring bias

Anchoring too heavily to a specific belief, price or performance when making decisions

What behaviors to look for

Your client thinks active investments are better than passive, because higher costs mean better performance; gets upset that an index didn't return as much as annualized past performance; or isn't willing to sell stocks until losses are recovered.

How you can address it

- Reset your clients' expectations using market history
- Encourage clients to maintain a healthy balance of active/passive investments
- Make sure your clients are diversified; use tax-loss harvesting to free them of losing investments

Investment strategies and solutions to consider

Auto-rebalancing: Automated rebalancing adjusts the mix of your clients' portfolios when the asset class weightings drift too far from their targets.

Robo-advisor: Automated investing platforms build, monitor and automatically rebalance a diversified portfolio based on your clients' goals.

Uncover other client biases and mitigation strategies

Use our **Advisor Playbook** and **Investor Workbook** to identify other biases and mitigation tactics with your clients. Also visit our **Biagnostics Toolkit page** for tips on how to incorporate behavioral finance into your practice.

For additional behavioral finance insights and tools, visit schwabassetmanagement.com/behavioralfinance



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