TRAIN YOUR BRAIN TO WIN BIG

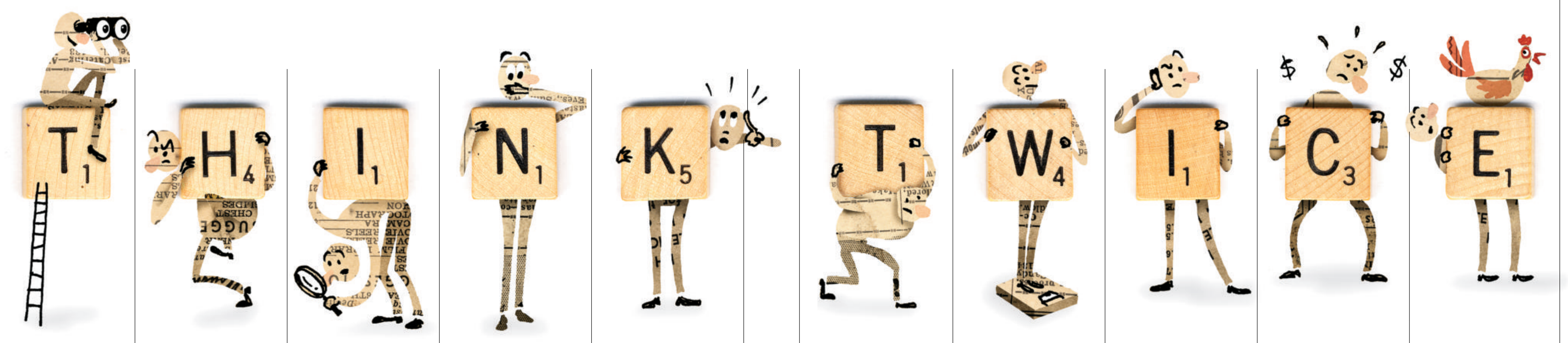
When playing the investing game, it's easy to let your impulses make all the wrong moves. Learning to trick yourself can help. **BY JASON ZWEIG**

WHY DO SMART PEOPLE do such stupid things with their money? The answer often lies in neuroeconomics, a hybrid of neuroscience, economics, and psychology that drills down to the biological bedrock of decision-making. Using MRI scans and EEG recordings, neuroeconomists observe the neural pathways along which investing decisions flow. What have they learned? That financial decisions are driven by feelings to an astounding extent. Even when we think we are being rational, we are often driven by impetuous emotions of which we are barely conscious. Therefore, the keys to investing success, whether it's for retirement or just for fun, are strategies and tricks to prevent the heat of the moment from melting your better judgment.

ADAPTED FROM *Jason Zweig's new book,* **Your Money and Your Brain: How the New Science of Neuroeconomics Can Help Make You Rich,** *available from Simon & Schuster.*

INSIDE: Turn the page for our "Ten Tricks" tear-out guide. →

ILLUSTRATIONS BY DAVID GOLDIN



Take the Global View
Keep calm by using a spreadsheet that emphasizes your total net worth, not the changes in each holding. Before you buy a stock or mutual fund, check whether it overlaps what you already own—try the Instant X-Ray tool at Morningstar.com.

Hope for the Best—But Expect the Worst
Being braced for disaster—by diversifying and learning market history—can help keep you from panicking. Every good investment performs badly some of the time. Intelligent investors stick with solid companies that hit rough patches.

Investigate, Then Invest
A stock is not just a price; it's a piece of a living corporate organism. Study the company's financial statements. Read a mutual fund's prospectus before you buy. If you want to hire a broker or financial planner, do a background check before you write a check.

Never Say Always
No matter how sure you are that an investment is a winner, don't put more than 10% of your portfolio in it. If you turn out to be right, you'll still make plenty of money, but if you turn out to be wrong, you'll be glad you kept most of your powder dry.

Know What You Don't Know
Don't believe you are already an expert. Compare stock and fund returns against the overall market and across different time periods. Ask what might make this investment go down; find out if the people marketing it to you have their own money in it.

The Past Is Not a Prologue
On Wall Street, what goes up must come down, and what goes way up usually comes down with a sickening crunch. Never buy a stock or mutual fund just because it has been going up. Intelligent investors buy low and sell high, not the other way around.

Weigh What They Say
The easiest way to silence a market forecaster is to ask for the complete track record of all his or her predictions. If you can't get a complete list, don't listen. Before trying any strategy, gather objective evidence on the performance of others who have used it.

If It Sounds Too Good to Be True, It Probably Is
More precisely: If it sounds too good to be true, it *absolutely* is. Anyone who offers a high return at a low risk in a short time is probably a fraud. Anyone who listens is definitely a fool.

Costs Are Killers
Trading costs can eat up 1% of your money per year, while taxes and mutual fund fees can take another 1% to 2%. If middlemen take 3% to 5% of your money per year, they will get rich. If you want to get rich, comparison shop and trade at a snail's pace.

Eggs Go Splat
Never keep all your eggs in one basket. Spread your bets across U.S. and foreign stocks, bonds, and cash. No matter how much you like your job, don't put all your 401(k) into your company's stock; employees at Enron and WorldCom liked their company too.

POP QUIZ: YOUR HEART OR YOUR MIND?

Gut, impulse, a feeling—these emotional signals come in handy for lots of things in life. But as neuroeconomics teaches us, they're not the right tools for money management. Try these quick investing brain teasers pitting your intuition against cold, hard logic. The answers may surprise you.

I. Which is the better investment strategy?

A. Gaining $300 for sure.
B. An 80% chance of gaining $400 with a 20% chance of gaining zero.

*Most people say **A,** going for the sure thing. But over time, **B** is the better choice. An 80% chance of gaining $400 works out to an average gain of $320.*

How about these two?

C. Losing $300 for sure.
D. An 80% chance of losing $400 with a 20% chance of losing nothing.

*This time, most avoid the sure thing, switching to **D.** But the math points to **C,** because the average loss on the riskier bet is $320. The example illustrates our tendency to cash in winners too soon and hang on to losers for too long. Over the course of a lifetime, you'll do better by letting winners ride and ditching your obvious losers promptly.*

II. It's lunchtime. A colleague offers you this choice:

A. $10 today.
B. $11 tomorrow.

Okay. Now what if she made this offer?

A. $10 a year from now.
B. $11 a year and a day from now.

*Most people tend to prefer **A** in the first choice but **B** in the second. Yet in both cases the take improves $1 by waiting just 24 hours. As this example shows, we are suckers for short-term rewards, even though we know perfectly well we should be more patient in the long term. This explains why people who "can't afford" to save for their retirement have no problem spending $4.79 for a cup of boiled beans at Starbucks three times a day. Instant gratification feels a lot better than saving for the future.*

III. If you flip a coin six times, which sequence of heads (H) and tails (T) is more likely to occur?

A. HHHHHH
B. HTTHTH

Both have identical 1-in-64 odds of occurring, because each coin flip is independent. One outcome never predicts another. But our gut tends to see patterns where there aren't any. Like thinking that a stock falling all week is due for a good day. Or that a rising stock will just keep going up. Stocks aren't quite as random as coins, but they're close—and it's smarter to prepare for the unexpected.