

Book Summary

MORGAN HOUSEL

The Psychology *of* Money

Timeless Lessons on Wealth,
Greed, and Happiness



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No One's Crazy

Your personal experiences with money make up may be 0.00000001% of what's happened in the world, but maybe 80% of how you think the world works.



People do some crazy thing with money. But no one is crazy.

People from different generations, raised by different parents who earned different incomes and held different values, in different parts of the world, born into different economies, experiencing different job markets with different incentives and different degrees of luck, learn very different lessons. WHAT SEEMS CRAZY TO YOU MIGHT MAKE SENSE TO ME.

Every decision people make with money is justified by taking the information they have at the moment and plugging it into their unique mental model of how the world works. But every financial decision a person makes, makes sense to them in that moment and checks the boxes they need to check.

Few people make financial decisions purely with a spreadsheet. They make them at the dinner, or in a company meeting. Places where personal history, your own unique view of the world, ego, pride, marketing and odd incentives are scrambled together into a narrative that works for you.



Luck & Risk

Nothing is as Good or Bad as it seems.



Other person's failure is usually attributed to bad decisions, while your own failures are usually chalked up to the dark side of risk. When judging your failures, I'm likely to prefer a clean and simple story of cause and effect, because I don't know what's going on inside your head. "You had a bad outcome so it must have been caused by a bad decision" is a story that makes more sense to someone. But when judging oneself we can make up a wild narrative justifying past decisions and attributing bad outcomes to risk.



Never Enough

There is no reason to risk what you have and need for what you don't have and don't need



Few of us will ever be billionaires. But a measurable percentage of people, at some point in their life, earn a salary or have a sum of money sufficient to cover every reasonable thing they need and a lot of what they want.

If you're one of them, remember a few things.

1 The hardest financial skill is getting the goalpost to stop moving.

If expectations rise with results there is no logic in striving for more because you'll feel the same after putting in extra effort. It gets dangerous when the taste of having more - more money, more power, more prestige - increases ambition faster than satisfaction. In that case one step forward pushes the goalpost two steps ahead. You feel as if you're falling behind, and the only way to catch up is to take greater and greater amounts of risk.

Modern capitalism is a pro at two things: generating wealth and generating envy. Perhaps they go hand in hand; wanting to surpass your peers can be the fuel of hard work. But life isn't any fun without a sense of enough.

$$\text{Happiness} = \text{Results} - \text{Expectations}$$

2 Social comparison is the problem here.

The ceiling of social comparison is so high that virtually no one will ever hit it. Which means it's a battle that can never be won, or that the only way to win is to not fight to begin with - to accept that you might have enough, even if it's less than those around you.

3 "Enough" is not too little.

The idea of having "enough" might look like conservatism, leaving opportunity and potential on the table. "Enough" is realizing that the opposite - an insatiable appetite for more - will push you to the point of regret.

4 There are many things never worth risking, no matter the potential gain.

- Reputation is invaluable.
- Freedom and Independence are invaluable
- Family and Friends are invaluable.
- Being loved by those who you want to love you is invaluable.
- Happiness is invaluable



And your best shot at keeping these things is knowing when it's time to stop taking risks that might harm them. Knowing when you have *enough*.

Luck & Risk are siblings. They are both the reality that every outcome in life is guided by forces other than individual effort.

They are so similar that you can't believe in one without equally respecting the other. They both happen because the world is too complex to allow 100% of your actions to dictate 100% of your outcomes. They are driven by the same thing: You are one person in a game with several billion people and infinite moving parts. The accidental impact of actions outside of your control can be more consequential than the ones you consciously take. But both are so hard to measure, and hard to accept and are often overlooked.

If you give luck and risk their proper respect, you realize that when judging people's financial success - both your own and others' - it's never as good or as bad as it seems.

WHAT IS LUCK? WHAT IS SKILL? WHAT IS RISK?

Identifying them is one of the biggest problems we face when trying to learn about the best way to manage money. But two things can point you in a better direction.

1

Be careful who you praise and admire. Be careful who you look down upon and wish to avoid becoming.

Some people are born into families that encourage education; others are against it. Some are born into flourishing economies encouraging of entrepreneurship, others are born into war and destitution.

Realize that not all success is due to hard work, and not all poverty is due to laziness.

Keep this in mind when judging people, including yourself.

2

Therefore, focus less on specific individuals and case studies and more on broad patterns.

Studying a specific person can be dangerous because we tend to study extreme examples - the billionaires, the CEOs, or the massive failures that dominate the news - and extreme examples are often the least applicable to other situations, given their complexity.

The more extreme the outcome, the less likely you can apply its lessons to your own life, because the more likely the outcome was influenced by extreme ends of luck and risk.

You'll get closer to actionable takeaways by looking for broad patterns of success and failure. The more common the pattern, the more it is applicable.



Trying to emulate Warren Buffett's investment success is hard, because his results are so extreme that the role of luck in his lifetime performance is very likely high, and luck isn't something you can reliably emulate

Confounding Compounding

\$81.5 billion of Warren Buffet's \$84.5 billion net worth came after his 65th birthday. Our minds are not built to handle such absurdities.



If something compounds - if a little growth serves as the fuel for future growth - a small starting base can lead to results so extraordinary they seem to defy logic. It can be so logic-defying that you underestimate what's possible, where growth comes from, and what it can lead to.

More than 2000 books are dedicated to how Warren Buffett built his fortune. But few pay enough attention to the simplest fact: Buffett's fortune isn't due to just being a good investor, but being a good investor since he was literally a child. Had he started investing in his 30s and retired in his 60s, few people would have ever heard of him.

Good investing isn't necessarily about earning the highest returns, because the highest returns tend to be one-off hits that can't be repeated. It's about earning pretty good returns that you can stick with and which can be repeated for the longest periods of time. That's when compounding runs wild.



Getting Wealthy vs Staying Wealthy

Good investing is not necessarily about making good decisions. It's about consistently not screwing up.



There are a million ways to get wealthy, but there's only one way to stay wealthy: some combination of frugality and paranoia.

Getting more requires taking risks, being optimistic, and putting yourself out there.

But keeping money requires the opposite of taking risk. It requires humility, and fear that what you've made can be taken away from you just as fast. It requires frugality and an acceptance that at least some of what you've made is attributable to luck, so past success can't be relied upon to repeat indefinitely.

Not “growth” or “brains” or “insight” is key ingredient for Success, but survival is. The ability to stick around for a long time, without wiping out of being forced to give up, is what makes the biggest difference. This should be the cornerstone of your strategy, whether it’s in investing or your career or a business.

There are two reasons why a survival mentality is so key with money.

One is obvious: few gains are so great that they’re worth wiping yourself out. The other, is the counterintuitive math of compounding.

Compounding only works if you can give an asset years and years to grow.

Applying the survival mindset to the real world comes down to appreciating three things.

1 More than I want big returns, I want to be financially unbreakable. And if I’m unbreakable I actually think I’ll get the biggest returns, because I’ll be able to stick around long enough for compounding to work wonders.

2 Planning is important, but the most important part of every plan is to plan on the plan not going according to plan.

A plan is only useful if it can survive reality. And a future filled with unknowns is everyone’s reality. Many bets fail not because they were wrong, but because they were mostly right in a situation that required things to be exactly right. Room for error - often called **margin of safety** - is one of the most under appreciated forces in finance. It comes in many forms: A frugal budget, flexible thinking, and a loose timeline - anything that lets you live happily with a range of outcomes.

It’s different from being conservative. **Conservative** is avoiding a certain level of risk. Margin of safety is raising the odds of success at a given level of risk by increasing your chances of survival.

3 A barbelled personality - optimistic about the future, but paranoid about what will prevent you from getting to the future - is vital.

Optimism is usually defined as a belief that things will go well. But that's incomplete. **Sensible optimism** is a belief that the odds are in your favor, and over time things will balance out to a good outcome even if what happens in between is filled with misery.

A mindset that can be paranoid and optimistic at the same time is hard to maintain, because seeing things as black or white takes less effort than accepting nuance. But you need short-term paranoia to keep you alive long enough to exploit long-term optimism.

Tails, You Win

You can be wrong half the time and still make a fortune.

"I've been banging away at this thing for 30 years. I think the simple math is, some projects work and some don't. There's no reason to belabor either one. Just get on to the next"

-Brad Pitt accepting a Screen Actors Guild Award

A lot of things in business and investing work this way. Long tails. the farthest ends of distribution of outcomes - have tremendous influence in finance, where a small number of events can account for the majority of the outcomes.

That can be hard to deal with, even if you understand the math. It is not intuitive that an investor can be wrong half the time and still make a fortune. It means we underestimate how normal it is for a lot of things to fail.

When you accept that tails drive everything in business, investing, and finance you realize that it's normal for lots of things to go wrong, break, fail and fall.

If you're a good stock picker, you'll be right may be half the time.

If you're a good business leader may be half of your product and strategy will work.

If you're a good investor most years will be just OK, and plenty will be bad.

If you're a good worker you'll find the right company in the right field after several attempts and trials.

And that's if you are good.

Role model's Success

When we pay special attention to a role model's successes (like Warren Buffett in investing), we overlook that their gains came from a small percent of their actions. That makes our own failures, losses and setbacks feel like we're doing something wrong. But it's possible we are wrong, or just sort of right, just as often as the masters are. They may have been *more right* when they were right, but they could have been wrong just often as anyone else.

"It's not whether you're right or wrong that's important," George Soros once said, "but how much money you make when you're right and how much you lose when you're wrong.!"

You can be wrong half the time and still make a fortune.



Freedom

Controlling your time is the highest dividend money pays.



The highest form of wealth is the ability to wake up every morning and say, “I can do whatever I want today”.

People want to become wealthier to make them happier. Happiness is a complicated subject because everyone’s different. But if there’s a common denominator in happiness - it’s that people want to control their lives.

The ability to do what you want, when you want, with who you want, for as long as you want, is priceless. It is the highest dividend money pays.

Most of the jobs like managers, professionals are decision-making jobs. This means our days don’t end when we clock out. We’re constantly working in our heads, which means it feels like work never ends. You might be thinking about work during your commute, while making dinner, while putting kids to sleep and when you wake up stressed in the morning.

Compared to generations prior, control over your time has diminished. And since controlling your time is such a key happiness influencer, we shouldn’t be surprised that people don’t feel much happier even though, we are, on average, richer than ever.

In the book *30 Lessons for Living*, gerontologist Karl Pillemer interviewed a thousand elderly Americans looking for the most important lessons they learned from decades of life experience. He wrote:

No one - not a single person out of a thousand - said that to be happy you should try to work as hard as you can make money to buy the things you want.

No one - not a single person - said it’s important to be at least as wealthy as the people around you, and if you have more than they do it’s real success.

No one - not a single person - said you should choose your work based on your desired future earning power.

What they did value were things like quality friendships, being part of something bigger than themselves and spending quality, unstructured time with their children.

Man in the Car Paradox

No one is impressed with your possessions as much as you are.



When you see someone driving a nice car, you rarely think, “Wow, the guy driving that car is cool.” Instead, you think, “Wow, if I had that car people would think I’m cool.” Subconscious or not, this is how people think.

There is a paradox here: people tend to want wealth to signal to others that they should be liked and admired. But in reality those other people often bypass admiring you, not because they don’t think wealth is admirable but because they use your wealth as a benchmark for their own desire to be liked and admired.

It’s a subtle recognition that people generally aspire to be respected and admired by others, and using money to buy fancy things may bring less of it than you imagine. If respect and admiration are your goal, be careful how you seek it. Humility, kindness and empathy will bring you more respect than horsepower ever will.



Wealth is What You Don’t See

Spending money to show people how much money you have is the fastest way to have less money.



Money has many ironies. Here’s the important one: Wealth is what you don’t see.

We tend to judge wealth by what we see, because that’s the information we have in front of us. We can’t see people’s bank accounts or brokerage statements. So we rely on outward appearances to gauge financial success. Cars. Homes. Instagram photos.

Wealth is the nice cars not purchased. The diamonds not bought. The watches not worn, the clothes forgone and the first-class upgrade declined. Wealth is financial assets that haven’t yet been converted into the stuff you see.

When most people say they want to be a millionaire, what they might actually mean is “I’d like to spend a million dollars.” And that is literally the opposite of being a millionaire.

Investor Bill Mann once wrote: “There is no faster way to feel rich than to spend lots of money on really nice things. But the way to be rich is to spend money you have, and to not spend money you don’t have. It’s really simple.”

RICH

VS

WEALTHY

Rich is a current income. Someone driving expensive car is almost certainly rich, because even if they purchased the car with debt you need certain level of income to afford. Same with big homes. It’s not hard to spot rich people. They often go out of their way to make themselves known.

Wealth is hidden. It’s income not spent. It’s an option not yet taken to buy something later. It’s value lies in offering you options, flexibility, and growth to one day purchase more stuff than you could right now.

Exercise is like being rich. “I did the work out and I now deserve to treat myself to a big meal.”

Wealth is turning down that treat meal, & burning net calories. It’s hard and requires self-control.

The problem is it is easy to find “Rich” role models & harder to find “Wealthy” role models because by definition their success is more hidden.

Most people deep down want to be wealthy. They want freedom and flexibility. But it is so ingrained in us that to have money is to spend money that we don’t get to see the restraint it takes to actually be wealthy.

People are good at learning by imitation. But the hidden nature of wealth makes it hard to imitate others & learn from their ways.

The world is filled with people who look modest but are actually wealthy and people who look rich who live at the razor’s edge of insolvency. Keep this in mind when quickly judging others’ success and setting your own goals.

Save Money

The only factor you can control generates one of the only things that matters. How wonderful.



Past a certain level of income people fall into three groups:

***those who save
those who don't think they can save
those who don't think they need to save***

The first idea - simple, but easy to overlook - is that building wealth has little to do with your income or investment returns, and lots to do with your savings rate.

Investment returns will make you rich. But whether an investing strategy will work, and how long it will work for, and whether markets will cooperate is always in doubt. Personal savings and frugality - finance's conversation and efficiency - are parts of the money equation that are more in your control and have a 100% chance of being as effective in the future as they are today.

More importantly, the value of wealth is relative to what you need.

Past a certain level of income, what you need is just what sits below your ego.

Everyone needs the basics. Once they're covered there's another level of comfortable basics, and past that there's basics that are both comfortable, entertaining and enlightening.

But spending beyond a pretty low level of materialism is mostly a reflection of ego approaching income. One of the most powerful ways to increase your savings isn't to raise your income. It's to raise your humility.

When you define savings as the gap between your ego and your income you realize why many people with decent incomes save so little.



So people's ability to save is more in their control than they might think.

Savings can be created by spending less.

You can spend less if you desire less.

And you will desire less if you care less about what others think of you.

And you don't need a specific reason to save.

Savings without a spending goal gives you options and flexibility, the ability to wait and the opportunity to pounce. It gives you time to think.

That flexibility and control over your time is an unseen return on wealth and that hidden return is becoming more important.

A question you should ask as the range of your competition expands is, "How do I stand out?"

Intelligence is not a reliable advantage in a world that's become as connected as ours has. But flexibility is. In a world where intelligence is hyper-competitive and many previous technical skills have become automated, competitive advantages tilt towards nuanced and soft skills - like communication, empathy, and perhaps most of all, flexibility.

If you have flexibility, you can wait for good opportunities, both in your career and for your investments. You'll have a better chance of being able to learn a new skill when it's necessary. You'll feel less urgency to chase competitors who can do things you can't, and have more leeway to find your passion and your niche at your own pace. You can find a new routine, a slower pace, and think about life with a different set of assumptions. The ability to do those things when most others can't is one of the few things that will set you apart in a world where intelligence is no longer a sustainable advantage.

Having more control over your time and options is becoming one of the most valuable currencies in the world.

That's why more people can, and more people should, save money.

Reasonable > Rational

Aiming to be mostly reasonable works better than trying to be coldly rational.



You're not a spreadsheet. You're a person. A screwed up, emotional person.

Do not aim to be coldly rational when making financial decisions. Aim to just be pretty reasonable. Reasonable is more realistic and you have better chance of sticking with it for the long run, which is what matters most when managing money.

Academic finance is devoted to finding the mathematical optimal investment strategies. In real world, people do not want the mathematically optimal strategy. We want the strategy that maximizes for how well we sleep at night.

“Minimizing future regret” - A reasonable investor makes an investment in the conference room with co-workers who thinks highly of you, with a spouse you don't want to let down & your own personal doubts. Investing has a social component that's often ignored when viewed through a strictly financial lens.

“Home Bias” - where people prefer to invest in companies from the country they live in while ignoring the other 95%+ of the planet. It's not rational, until you consider that investing is effectively giving money to strangers. If familiarity helps you take the leap of faith required to remain backing those strangers, it's reasonable.



Surprise!

History is the study of change, ironically used as a map of the future.



History is mostly the study of surprising events. But it is often used by investors and economists as an unassailable guide to the future. An over reliance on past data as a signal to future conditions in a field where innovation and change are lifeblood of progress.

Geologists can look at a billion years of historical data and form models of how the earth behaves. Kidneys operate the same way now as they did in 1020.

Investing is not a hard-science. It's a massive group of people making imperfect decisions with limited information about things that will have a massive impact on their well-being, which can make even smart people nervous, greedy and paranoid.


Two dangerous things happen when you rely too heavily on investment history as a guide to what's going to happen next.

- *You'll likely miss the outlier events that move the needle the most. (like the Great Depression, World War II, dot-com bubble, September 11th etc)*
- *History can be a misleading guide to the future of the economy and stock market because it doesn't account for structural changes that are relevant to today's world.*



Room for Error

The most important part of every plan is planning on your plan not going according to plan.



Benjamin Graham is known for his concept "Margin of Safety" - Call it "Room for Error" or "Redundancy" - It is the only effective way to safely navigate a world that is governed by odds, not certainties. And almost everything related to money exists in that kind of world.

Forecasting with precision is hard. Graham's margin of safety is a simple suggestion that we don't need to view the world as black or white, predictable or crapshoot. The grey area - pursuing things where a range of potential outcomes are acceptable - is the smart way to proceed.

Two things cause us to avoid room for error:

1. Idea that somebody must know what the future holds, driven by the uncomfortable feeling that comes from admitting the opposite.
2. You're therefore doing yourself harm by not taking actions that fully exploit an accurate view of that future coming true.

But room for error is under appreciated and misunderstood. It's often viewed as a conservative hedge, used by those who don't want to take much risk or aren't confident in their views. But when used appropriately, it's the opposite.

There are a few specific places for investors to think about room for error.

- **Volatility** - Can you survive your assets declining by 30%? On a spreadsheet, may be yes - in terms of actually paying your bills and staying cash-flow positive. But what about mentally? It is easy to underestimate what a 30% decline does to your psyche. Spreadsheets are good at telling you when the numbers do or don't add up. They're are not good at modeling how you'll feel. **Having a gap between what you can technically endure versus what's emotionally possible is an overlooked version of room for error.**
- **Saving for retirement** - You won't be able to retire like you once predicted. This is more art than science. Markets crash, wars happen. The future might be worse or better than today.

"Optimism Bias" - Cousin of room for error - The idea is that you have to take risk to get ahead but no risk that can wipe you out is ever worth taking.

Barbelled personality - A person with a balanced mindset characterized by optimism about the future and paranoia about potential risks. This personality type is ambitious in pursuing long-term goals but simultaneously maintains a vigilant, "protection-first" approach, anticipating what could go wrong and preparing for it.

Think of your own money as barbelled. Take risks with one portion and be terrified with the other. This is inconsistent, but the psychology of money would lead you to believe that it is.

Avoid Single points of failure - A good rule of thumb for a lot of things in life is that everything can break with eventually break. So if many things rely on one thing working, and that thing breaks, you are counting the days to catastrophe.

Predicting what you'll use your savings for assumes you live in a world where you know exactly what your future expenses will be, which no one does. I save a lot, and I have no idea what I'll use the savings for in the future. Few financial plans that only prepare for known risks have enough margin of safety to survive the real world.

In fact, the most important part of every plan is planning on your plan not going according to plan.

You'll Change

Long-term planning is harder than it seems because people's goals and desires change over time.



Harvard psychologist Daniel Gilbert once said:

“At every stage of our lives we make decisions that will profoundly influence the lives of the people we’re going to become, and then when we become those people, we’re not always thrilled with the decisions we made. So young people pay good money to get tattoos removed that teenagers paid good money to get. Middle-aged people rushed to divorce people who young adults rushed to marry. Older adults work hard to lose what middle-aged adults worked hard to gain. On and on and on.”

His research shows people from age 18 to 68 underestimate how much they will change in the future.

There are two things to keep in mind when making what you think are long-term decisions.

We should avoid the extreme ends of financial planning

Assuming you'll be happy with a very low income, or choosing to work endless hours in pursuit of a high one, increases the odds that you'll one day find yourself at a point of regret. People adapt to most circumstances, so the benefits of an extreme plan - the simplicity of having hardly anything, or the thrill of having almost everything - wear off. But the downsides of those extremes - not being able to afford retirement, or looking back at a life spent devoted to chasing money - become enduring regrets. Regrets are painful when you abandon a previous plan and feel like you have to run in the other direction twice as fast to make up for lost time. Compounding works best when you give a plan years or decades to grow. Endurance is key.

We should also come to accept the reality of changing our minds

Sunk costs - anchoring decisions to past efforts that can't be refunded - are a devil in a world where people change over time. They make our future selves prisoners to our past, different, selves. It's the equivalent of a stranger making major life decisions for you.

Nothing's Free

Everything has a price, but not all prices appear on labels



“Every job looks easy when you’re not the one doing it.”

This is because the challenges faced by someone in the arena are often invisible to those in the crowd. Most things are harder in practice than they are in theory. Sometimes this is because we’re overconfident. More often it’s because we’re not good at identifying what the price of success is, which prevents us from being able to pay it.

The question is: Why do so many people who are willing to pay the price of cars, houses, food and vacations try so hard to avoid paying the price of good investment returns?

The answer is simple: The price of investing success is not immediately obvious. It’s not a price tag you can see, so when the bill comes due it doesn’t feel like a fee for getting something good. It feels like a fine for doing something wrong. We are fine with paying fees, fines are supposed to be avoided. The natural response for anyone who watches their wealth decline and views that drop as a fine is to avoid future fines.

Think market volatility as a fee rather than a fine. Having this mindset lets you stick around long enough for investing gains to work in your favor.

Disneyland tickets cost 100 dollars. But you get an awesome day with your kids you’ll never forget.

Market returns are never free and never will be. They demand you pay a price, like any other product. You’re not forced to pay this fee, just like you’re not forced to go to Disneyland. You can go to county fair or sit at home and have nice time. But you’ll usually get what you pay for. Same with markets. The volatility/uncertainty fee - the price of returns - is the cost of admission to get returns greater than low-fee parks like cash and bonds.

The trick is convincing yourself that the market’s fee is worth it. There’s no guarantee it is worth it. You know, sometimes it rains at Disneyland. But if you view admission fee as a fine, you’ll never enjoy the magic.

You & Me

Beware taking financial cues from people playing a different game than you are



When some expert says, “You should buy this stock,” keep in mind that they do not know who you are. Are you a teenager trading for fun? An elderly person on a limited budget? A hedge fund manager trying to shore up your books before the quarter ends? Are we supposed to think those three people have the same priorities, and that whatever level a particular stock is trading at is right for all three of them?

It’s hard to grasp that other investors have different goals than we do. Rising prices persuade all investors in ways the best marketers envy. They are a drug that can turn value-conscious investors into dewy-eyed optimists, detached from their own reality by the actions of someone playing a different game.

Being swayed by people playing a different game can also throw off how you think you’re supposed to spend your money. So much consumer spending, particularly in developed countries is socially driven: subtly influenced by people you admire, and done because you subtly want people to admire you.

While we can see how much money other people spend on cars, homes, clothes, vacations, we don’t see their goals, worries and aspirations. A young lawyer aiming to be a partner at a prestigious law firm might need to maintain an appearance that a writer who can work in sweatpants, have no need for. But when his purchases set the writer’s expectations, he’s wandering down a path of potential disappointment because the writer is spending the money without the career boost lawyer gets.

A takeaway here is that few things matter more with money than understanding your own time horizon and not being persuaded by the actions and behaviors of people playing different games than you are.

The main thing is going out of your way to identify what game you’re playing.

The Seduction of Pessimism

***Optimism sounds like a sales pitch.
Pessimism sounds like someone trying to help you.***



Optimism is a belief that the odds of a good outcome are in your favor over time, even when there will be setbacks along the way. Optimism's most compelling sibling is Pessimism. Pessimism just sounds smarter and more plausible than optimism.

Tell someone that everything will be great and they're likely to either shrug you off or offer a skeptical eye. Tell someone they're in danger and you have their undivided attention.

There are valid reasons why pessimism is seductive when dealing with money. Part of it is instinctual and unavoidable. Daniel Kahneman (author of *Thinking Fast and Slow*) says the asymmetric aversion to loss:

When directly compared or weighted against each other, losses loom larger than gains. This asymmetry between the power of positive and negative expectations or experiences has an evolutionary history. Organisms that treat threats as more urgent than opportunities have a better chance to survive and reproduce.

But a few other things makes financial pessimism easy, common and more persuasive than optimism.

1. *Money is ubiquitous, so something bad happening tends to affect everyone and captures everyone's attention.*
2. *Pessimists often extrapolate present trends without accounting for how markets adapt -Assuming that something ugly will stay ugly is an easy forecast to make. And it's persuasive, because it doesn't require imagining the world changing. But problems correct and people adapt. Threats incentivize solutions in equal magnitude. That's a common plot of economic history that is too easily forgotten by pessimists who forecast in straight lines.*
3. *Progress happens too slowly to notice but setbacks happen too quickly to ignore.*

Expecting things to be great means a best-case scenario that feels flat. Pessimism reduces expectations, narrowing the gap between possible outcomes and outcomes you feel great about. May be that's why it's so seductive. Expecting things to be bad is the best way to be pleasantly surprised when they're not. Which, ironically, is something to be optimistic about.

When You'll Believe Anything

Appealing fictions, and why stories are more powerful than statistics



There are two things to keep in mind about a story-driven world when managing your money.

1. The more you want something to be true, the more likely you are to believe a story that overestimates the odds of it being true. This seems crazy. But if you desperately need a solution and a good one isn't known or readily available to you, the path of least resistance is towards "willing to believe anything. Not just try anything, but believe it."
2. Everyone has an incomplete view of the world. But we form a complete narrative to fill in the gaps.

Psychologist Philip Tetlock once wrote: "We need to believe we live in a predictable, controllable world, so we turn to authoritative-sounding people who promise to satisfy that need." Wanting to believe we are in control is an emotional itch that needs to be scratched, rather than an analytical problem to be calculated and solved. The illusion of control is more persuasive than the reality of uncertainty. So we cling to stories about outcomes being in our control.

Know Yourself:

- When planning we focus on what we want to do and can do, neglecting the plans and skills of others whose decisions might affect our outcomes.
- Both in explaining the past and in predicting the future, we focus on the casual role of skill and neglect the role of luck.
- We focus on what we know and neglect what we do not know, which makes us overly confident in our beliefs.

Quick Summary & Short Recommendations



Go out of your way to find humility when things are going right and forgiveness/compassion when they go wrong.

The world is big and complex. Luck and risk are both real & hard to identify. Do so when judging both yourself and others. Respect the power of luck & risk and you'll have a better chance of focusing on things that you can actually control.

Less ego, more wealth.

Saving money is the gap between your ego and your income, and wealth is what you don't see. So wealth is created by suppressing what you could buy today in order to have more stuff or options in the future. No matter how much you earn, you will never build wealth unless you can put a lid on how much fun you can have with your money right now, today.

Manage your money in a way that helps you sleep at night.

That's different from saying you should aim to earn the highest returns or save a specific percentage of your income. Some people won't sleep well unless they're earning the highest returns; others will only get a good rest if they're conservatively invested. But the foundation of, "does this help me sleep at night?" is the best universal guidepost for all financial decisions.

If you want to do better as an investor, the single most powerful thing you can do is increase your time horizon.

Time is the most powerful force in investing. It makes little things grow big and big mistakes fade away. It can't neutralize luck and risk, but it pushes results closer towards what people deserve.

Become OK with a lot of things going wrong. You can be wrong half the time and still make a fortune.

No matter what you're doing with your money, you should be comfortable with a lot of stuff not working. That's how the world is. So you should always measure how you've done by looking at your full portfolio, rather than individual investments. It's fine to have a large chunk of poor investments and a few outstanding ones. That's usually the best-case scenario. Judging how you've done by focussing on individual investments makes winners look more brilliant they were, and losers appear more regrettable than they should.

Use money to gain control over your time

Not having control of your time is such a powerful and universal drag on happiness. The ability to do what you want, when you want, with who you want, for as long as you want to, pays the highest dividend that exists in finance.

Be nicer and less flashy

No one is impressed with your possessions as much as you are. You might think you want a fancy car or a nice watch. But what you probably want is respect and admiration. And you're more likely to gain those things through kindness and humility than horsepower and chrome.

Save. Just save. You don't need a specific reason to save.

It's great to save for a car, or a downpayment, or a medical emergency. But saving for things that are impossible to predict or define is one of the best reasons to save. Everyone's life is a continuous chain of surprises. Savings that aren't earmarked for anything in particular is a hedge against life's inevitable ability to surprise the hell out of you at the worst possible moment.

Define the cost of success and be ready to pay it.

Nothing worthwhile is free. And remember that most financial costs don't have visible price tags. Uncertainty, doubt, and regret are common costs in the finance world. They're often worth paying. But you have to view them fees (a price worth paying to get something nice in exchange) rather than fines (a penalty you should avoid).

Worship room for error.

A gap between what could happen in the future and what you need to happen in the future in order to do well is what gives you endurance, and endurance is what makes compounding magic over time. Room for error often looks like a conservative hedge, but if it keeps you in the game it can pay for itself many times over.

Avoid the extreme ends of financial decisions

Everyone's goals and desires will change over time, and the more extreme your past decisions were the more you may regret them as you evolve.

You should like risk because it pays off over time.

But you should be paranoid of ruinous risk because it prevents you from taking future risks that will pay off over time.

Define the game you're playing

and make sure your actions are not being influenced by people playing a different game.

Respect the mess.

Smart, informed and reasonable people can disagree in finance, because people have vastly different goals and desires. There is no single right answer, just the answer that works for you.

Understand your own psychology of money 😊

