



## The Older I Get, The Better I Was

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"The older I get, the better I was." A while back my kids gave me a T-shirt with those words printed on it. As you no doubt can gather from my newsletters, I like to tell stories. Over the years, my kids have heard many of them and have questioned the veracity of some of my claims. I think they have a hard time imagining their dad of a dad could have been a stud at one time. As I like to remind them, "Children think there are three genders: male, female, and parents." But my children's perceptions aren't the only reasons to doubt the veracity of my stories: my memories of past experiences may not be accurate.

In his book, *Thinking, Fast and Slow*, Daniel Kahneman says we have two selves, "the experiencing self and the remembering self." And, since "memories are all we get to keep from our experience of living, the only perspective that we can adopt as we think about our lives is therefore that of the remembering self... the experiencing self does not have a voice." So, the life narratives we tell ourselves are not based on experiences, but on our memories of those experiences and our memories could be wrong.

The reason memories can be so wrong, says Jason Zweig in *Your Money and Your Brain*, is that they are "...not just recollections. They are also reconstructions." We revise the past in order to feel better about ourselves. Nassim Taleb explains in the *Black Swan*, "Memory is more of a self-serving dynamic revision machine: you remember the last time you remembered the event and, without realizing it, change the story at every subsequent remembrance...to make what we think of as logical sense after the fact."

Since memories are convenient cognitive deviations from reality, "...it makes it difficult to learn from experience," writes Philip Tetlock in *Expert Political Judgment*. This is true, not only because our memories deviate from reality, but also because the constant rewriting of events to make logical sense makes us feel like we knew what was coming all along. He reports that this knew-it-all-along effect, known as hindsight bias, "...forecloses the possibility of surprises, and surprises — because they are hard to forget — play a critical role in learning when and where our beliefs failed us."

Interestingly, one of the most common mistaken beliefs perpetuated by hindsight bias is that the future is predictable. As Kahneman explains, "The illusion that one has understood the past feeds the further illusion that one can predict and control the future." A perfect example of this is the adoration investors have for Morningstar ratings, which ranks mutual funds from five stars (top) to one star (bottom) based on past performance. And, while Morningstar prominently displays its "past performance is not a guarantee of future results" disclaimer, Jane Bryant Quinn says, in a CBS Money Watch article (May 6, 2010), that "Money pours into the four and five star funds...[However,] Morningstar's own research shows how little its stars are worth as investment guides." That's because experience shows that mutual fund returns are random and unknowable. Four and five star funds inevitably fall back to the pack, while the lower rated ones routinely rise toward the top.

But, investors stubbornly hold to their misguided belief in the usefulness of Morningstar ratings, like I cling to the veracity of my stories. We do so because our brains ignore the voice of experience in favor of the self-serving revisionist voice of remembrance. It's not that we are stupid, just flawed. Without realizing it, we construct plausible sounding memories that are wrong. This causes investors to believe Morningstar ratings are more predictive than they are, and me to believe I was better than I was.

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