This Test Proves You’re Overconfident

Much has been written about the perils of overconfidence in investing. Nobel laureate Daniel Kahneman reported one compelling study in his book, *Thinking, Fast and Slow*.

**CFOs are overconfident**

You might think CFOs of large corporations would have valuable insight about something as basic as projecting the returns of the S&P 500 index. The data, however, proves otherwise. Researchers from Duke University analyzed 11,600 forecasts by CFOs. They asked for both projected returns and the level of returns that participants were 90 percent confident were too high and too low. More than 67 percent of the actual returns were outside the estimated.
Consider your assumptions

The next time you’re tempted to buy or sell stock because you believe it’s mispriced, think about the assumptions you are making.

First, you are assuming the price set by millions traders all over the world (traders who are looking at the same information about the stock you and broker have) are wrong. You would have to believe they missed something that makes the current price of the stock too high or too low.

Second, if you are buying, someone else is selling. They obviously believe it is a good time to sell. How confident are you that they are wrong and you are right?

Third, you don’t have the benefit of knowing who is on the other side of the trade. Would you bet on the outcome of a sporting event without knowing all of the participants in the game? If you are buying, would it make a difference to you if you knew that Goldman Sachs was the seller? Is it likely you and your broker know more than Wall Street insiders?

Take this test

As noted by Andrew Macken, a senior analyst at Montgomery Investment Management, Michael Mauboussin, author of The Success Equation, has posted an online test that permits you to assess your own level of confidence. Macken indicates that more than 700 people have taken this test. Their accuracy rate in responding to the questions posed is 60.5 percent, but their confidence level is 70 percent.
do are less motivated to learn and improve than those who understand their limitations. Indeed, one study showed that the least capable people have the largest gap between what they think they can do and what they actually achieve."

*It's hard to resist*

Even though we know predictions are notoriously unreliable, they are the daily grist of brokers and other self-styled investment “gurus.” Even Macken, who is obviously aware of the data on overconfidence in making predictions, can’t resist the temptation. According to a [May article in Financial Review](https://www.foundersfund.com/), Macken has picked Prada as the “world’s leading short candidate.”

I wonder how confident he is in that prediction.

Dan Solin is a New York Times bestselling author of the Smartest series of books. His latest book is *The Smartest Sales Book You’ll Ever Read*.

The views of the author are his alone and may not represent the views of his affiliated firms. Any data, information and content on this blog is for information purposes only and should not be construed as an offer of advisory services.

Follow Dan Solin on Twitter: [www.twitter.com/DanSolin](https://www.twitter.com/DanSolin)
It’s A Good Thing For Me’

This Blogger’s Books and Other Items from...

The Smartest Investment Book You’ll Ever Read: The Proven Way to Beat the “Pros” and Take Control of Your Financial Future
by Daniel R. Solin

The Smartest Portfolio You’ll Ever Own: A Do-It-Yourself Breakthrough Strategy
by Daniel R. Solin

YOU MAY LIKE

Top Longevity Scientist Provides Leading Expertise For Your Daily Use
Scientific American | Elysium Health

Cable TV Is Dying in 2016. Here’s What Comes Next
The Motley Fool

The No-Show Sock Everyone is Obsessed With
Cool Mom Picks | Bombas Socks

10 Online Dating Sites That Really Work
Top 10 Online Dating Sites

This Test Proves You’re Overconfident
Find Out Why Sleep Experts Are Raving About Lull
Lull.com

What Jeannie Looks Like Now is Incredible
Hooch

Around The Web

10 Part-Time Jobs That Can Earn You Serious Cash
14 Jobs That Surprisingly Demand Six-Figure Salaries
10 Legitimate Businesses You Can Start for Under $20

SUGGESTED FOR YOU

The 6 Stages Of Sharing A Bed With Your Significant Other
Kylie Jenner Slips Into See-Through Lace Jumpsuit For Sunday Night Out
Australian Women’s Water Polo Team Hit By Virus On Way To Rio
The Innovative Way Kenya Is Helping Prevent Moms Dying During Childbirth
The 4 Differences Between Introversion and Social Anxiety

This Test Proves You’re Overconfident
Subway Employee Busted For Allegedly Spiking Cop’s Drink With Meth, THC

Here’s The Most Indecipherable Defense Yet Of Donald Trump’s ‘Second Amendment People’ Remarks

Donald Trump And The Heritage Foundation: Friends With Benefits

Gunfire Erupts In Ferguson After Protester Is Struck By Car

Rising Ocean Temperatures Are Making Us Sick

Trump Campaign Floats Every Defense In the Book For Second Amendment Fiasco

Don’t Call Me ‘Honey’: U.S. Lawyers Barred From Sexist Comments, Discriminatory Behavior

Michael Phelps Wins 20th Gold Medal At Rio Olympics

This Test Proves You’re Overconfident
Part of HuffPost Impact