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Subpar Performance: The Value of Process over Outcome in Golf and Investing

by Dr. Frank Murtha and Bob Schmidt

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Golf great Bobby Locke once famously observed, "You drive for show, but putt for dough."[1]

PGA Tour pros know this to be true. That's why they spend countless hours on their putting, developing a repeatable process designed for maximum accuracy. Their livelihood depends on it. Despite all the painstaking work to develop their best putting technique, they do something odd, but utterly human; they sometimes decide not to use it.

A study[2] by Pope and Schweitzer at the Wharton School of Business using millions of strokes, laser-precision and controlling for other variables, found that professional golfers often abandon their best practice approach when putting for a birdie (a shot that would leave the golfer one stroke under par for the hole).

Leaving it Short

Pro golfers' fear of missing a putt for par can force them to follow their approach more closely. But why don't they follow the same process with <u>every</u> putt?

Specifically, the study found that professional golfers make par putts at a higher rate (by "going for it"), but leave birdie putts short of the cup (by "playing it safe"). (Par is the number of strokes it should take a golfer to complete a hole.)

Tour pros don't deny it. "Par putts just seem to be more critical because if you miss you drop a shot—if you miss a birdie putt, it doesn't seem to have the same effect," admitted PGA Tour pro Jim Furyk.[3] This makes golfers "loss averse." It also makes them poorer. Scorecards don't know (and wouldn't care) whether the stroke lost was for a birdie or for a par—every stroke counts the same.

Pope and Schweitzer concluded that the inability/unwillingness to follow the optimal putting approach on average cost pro golfers more than one stroke every tournament, which translated to hundreds of thousands ofdollars less in prize money each year between 2004 and 2008 when the study was conducted. We revisit this research because we believe it still has merit. Pro golfers (and investors) often have a sound process—but when they don't follow it consistently, it could be to their detriment.

[1] Allauthor.com website: https://allauthor.com/quotes/92517/
[2] Pope, Devin G. and Schweitzer, Maurice E., "Is Tiger Woods Loss Averse? Persistent Bias in the Face of Experience, Competition, and High Stakes." (June 13, 2009). https://ssrn.com/abstract=1419027 or http://dx.doi.org/10.2139/ssrn.1419027
[3] Schwarz, Alan. "Settling for Par: Pros More Likely to Play It Safe." *The New York Times*. June 15, 2009. https://www.nytimes.com/2009/06/16/sports/golf/16study.html

PUTTING AND INVESTING

If this putting situation sounds like investing, it should. What happens to PGA Tour professionals can happen to investors. Psychologist Daniel Kahneman described this phenomenon in what he termed “Prospect Theory,” for which he won the Nobel Prize in Economics. In short, Kahneman (along with his late partner Amos Tversky) found the emotional impact of losses is about twice as great as the emotional impact of equivalent gains. Thus, many investors are wired to avoid losses by selling winning positions early to be “conservative,” while avoiding losses in down positions by being more aggressive.

But giving away a percentage point or two is like giving away a couple strokes; it can cost investors vast sums in the long run. Consider a hypothetical $100,000 investment put away for college when your children are young. Scenario 1) You make a plan and stick to it. The portfolio earns a hypothetical 10% average annual return over 15 years. Scenario 2) Loss aversion creeps into the process. You get a little conservative on your investing “birdie putts” (i.e., gains) and a little (over)aggressive on your investing “bogey putts” (i.e., losses; a bogey is a shot that leaves a golfer one stroke over par) which costs you a couple of percentage points a year—down to 8% from 10%.

Ten vs. eight percent per year; they sound pretty similar. In fact, they both sound good. What’s the difference? $100,000. The account in Scenario 2 would in theory be worth $317,000 while the account in Scenario 1 would be worth $417,000.[4] The caution-induced tweaks ironically can lead to real life losses—and real life consequences for everyday investors.

How do you break out of this performance-draining mindset? How do you stick to your best practice? In the case of the professional golfer and the investor, there are two keys; both involve maintaining the proper mindset or “frame.”

PROCESS and OUTCOME

Armed with a proper long-term time frame, you are ready to place your attention where we believe it needs to be—on process over outcome. It is difficult to overstate the importance of the following point: In order to focus on a process, you need to have one. One way to establish an investment process (the “how” of investing) is to start with goals (the “why” of investing).

Your investing process should be something you understand and something you believe in because the fluctuations of markets and account values are a constant stream of “outcomes” that can distract you from your formula.

There are any number of “right” ways to invest, but not one of them will work if you cannot stick to it. That’s why a focus on process over outcome is so critical. Even seemingly small deviations from your best practices can cost you—as shown in the college savings example above. A trusted financial advisor can be of tremendous value in this regard by putting in place a goal-based plan with clear procedures to guide financial decisions.

Dr. Frank Murtha’s Best Practice Ideas

1. Make an investment plan that reflects life goals to help retain long-term focus.
2. Work with a professional advisor.

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[4] This hypothetical example is for illustrative purposes only. It does not represent any particular investment. Actual results will vary.

BEST PRACTICES

1. Root investment decisions in real life goals to be pursued. Money amounts are amorphous. What's more, they're ultimately a means to end (i.e., what you want your life to look like). Focusing on life goals (the clearer, the better) helps us focus on what matters and inherently moves us to a longer-term outlook.

2. Enlist the services of a trusted advisor.[5] A trusted advisor is like an investing GPS system, helping you in three critical areas of your journey: a) Establishing your destination(s) b) mapping your route and c) keeping you on the path.

We believe following this practical advice may enhance your long-term returns. Wishing you success when investing—and on the putting green.

[5] Although there is no assurance that working with a financial advisor will improve investment results, a financial professional who focuses on your overall financial objectives can help you consider decisions that could have a substantial effect on your long-term financial situation.