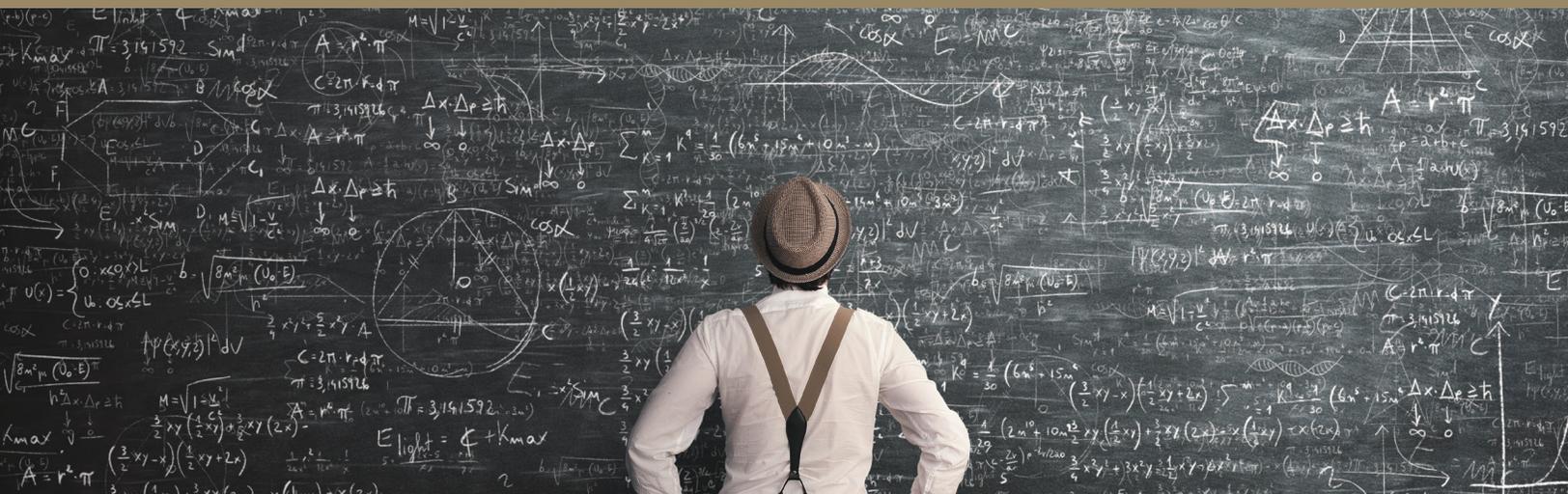


UNCOMMON PERSPECTIVE

Critical Thinking: The Key to Independent Decision-Making

FEBRUARY 2021



Key Takeaways:

- Critical thinking is essential for sound, independent decision-making
- An open mind and the willingness to ask questions are essential to making rational choices
- Cognitive biases, often driven by emotion, can lead to suboptimal decisions

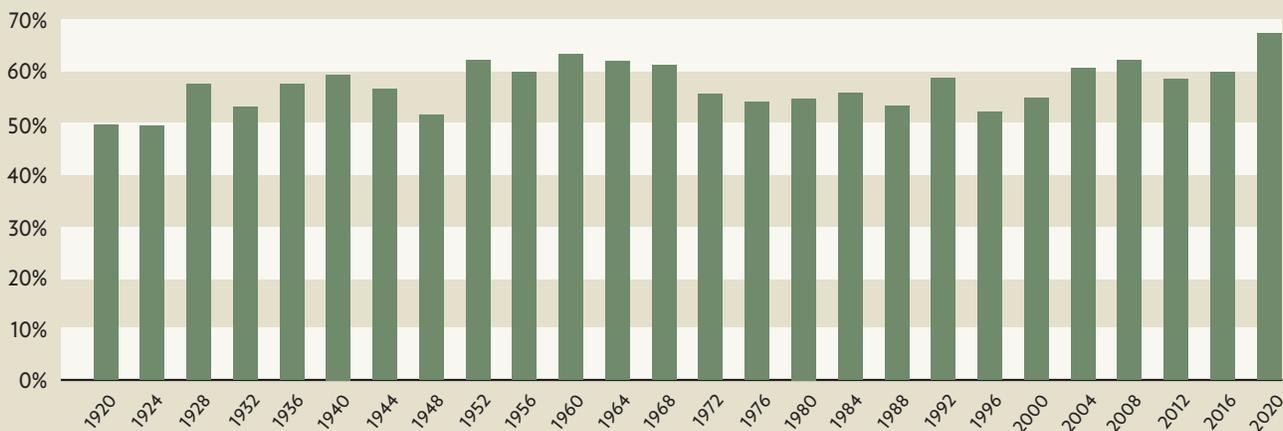
Thinking Critically to Achieve Your Goals

“It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness.” So begins Charles Dickens’ famous novel, *A Tale of Two Cities*, capturing the stark contradictions in pre-revolutionary London and Paris in the late 1700s. Fast-forward to America in 2020 and Dickens’ words seem eerily apropos.

As we welcome the end of a protracted election period, we are struck by the deterioration in the quality and tone of our country’s political and social discourse. While political engagement hit record levels, individuals with different political affiliations remain mistrustful of each other and seem unable to find common ground on almost any subject.

Continued

2020 Election Had Highest Turnout in the Past 100 Years



Source: United States Elections Project

At the same time, science appears to be on the verge of winning the war against the global scourge of the pandemic. An unwavering commitment to rigorous research, testing, analysis, and application has produced what seem to be effective and safe vaccines in record time.

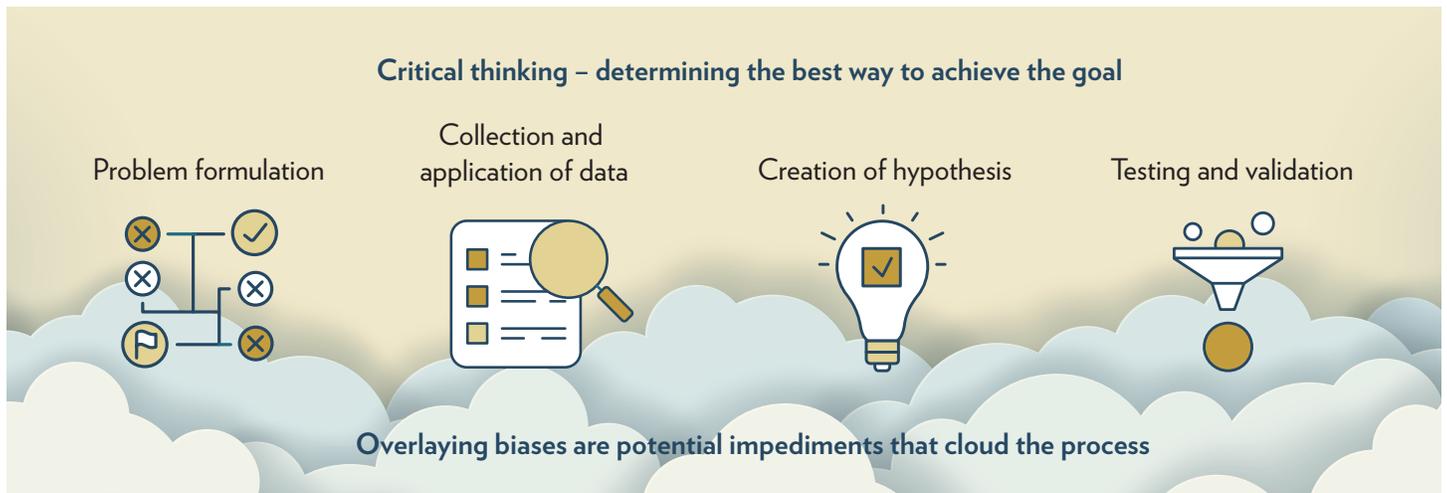
Given this extraordinary backdrop, it seems an appropriate time to reflect on our processes of decision-making. What is the key to making wise, independent decisions that align with sound reasoning and real-world conditions? And how do we avoid the danger of acting on untruths and erroneous judgments?

To answer these questions, let's revisit some basic principles of "critical thinking." These principles form the foundation for reasoned discussion and problem solving across many disciplines, including investing and financial management. We will also explore common cognitive biases that circumvent critical thinking and ultimately lead to counter-productive decision-making. These biases are often driven by our natural tendencies for self-preservation and self-fulfillment.

Critical Thinking

Critical thinking, or goal-directed thinking, guides us in our beliefs and actions. It is a disciplined process of conceptualizing, analyzing, evaluating, and applying information toward specific ends. Regardless of the subject matter, it requires the acceptance and application of clarity, accuracy, precision, consistency, relevance, sound evidence, valid reasoning, depth, breadth, and fairness.

Critical thinkers are open-minded and willing to ask questions even when they think they know the answer, and they accept that further evidence or reasoning might change their minds.



Critical thinkers employ three basic techniques:

1. They raise vital questions and confront problems

Facing problems is an essential part of life, and we all make hundreds of decisions each day. Most of these are inconsequential, like what we are going to eat for breakfast or which route we will take to work. For these decisions, we often turn, by necessity, to intellectual shortcuts. While this convenient approach to problem solving may not be optimal, perfect, or rational, it is sufficient to reach an immediate, short-term goal.

To solve consequential problems, critical thinkers identify and clearly define problems of significance. For example, in our wealth management practice, our first step is to clarify our clients' financial and life goals. This is a serious, reflective process that demands self-awareness, honesty, and grounding in reality. Knowing, with precision, where a client wants to go guides the wealth management strategy of how to get there. The proper allocation of assets, selection of securities, and frequency of rebalancing portfolios all hinge on the goals we are trying to reach.

2. They gather and assess information and draw well-reasoned conclusions and solutions, testing them against relevant criteria, data and standards

Effective problem solving is guided by the identification, collection, and assimilation of relevant information. Today, we are fortunate to live in an age where information is abundant and increasingly easy to access. But this excess of information can also

be our downfall. The challenge for the critical thinker is to select only the information relevant to the problem at hand. And it's just as important to verify that information selected is accurate and complete.

An astute thinker will explore possible solutions by building and testing hypotheses for how to solve a problem. With these hypotheses in mind, a plan can be implemented to identify and validate data and information.

Our investment management process provides a good example of this critical approach to problem solving. We begin with a set of performance and risk targets based on our understanding of our clients' financial goals. With these targets in mind, we propose a set of hypothetical portfolios of potential investment types across asset classes. The portfolios are tested based on analyzing historical behavior of similar portfolios coupled with a reasoned expectation of how these portfolios could perform under future market conditions. We implement portfolios that have the highest probability for meeting these targets.

3. They are open-minded and are willing to explore alternative systems of thought, recognizing and assessing, as need be, assumptions, implications, and practical consequences

In conceptualizing a new problem, we rarely begin from scratch. Rather, we start by asking questions built around existing concepts or ideas as a guide to best thinking in each novel circumstance.

Critical thinkers approach questions with an open mind, weighing conceptual frameworks in the light of their assumptions, their implications, and the practical consequences of their application to the problem at hand. Open-mindedness includes reconsidering whether you are asking the right questions before embracing an answer. You don't want to get trapped in a solution driven by the old saying that "when all you have is a hammer, every problem looks like a nail."

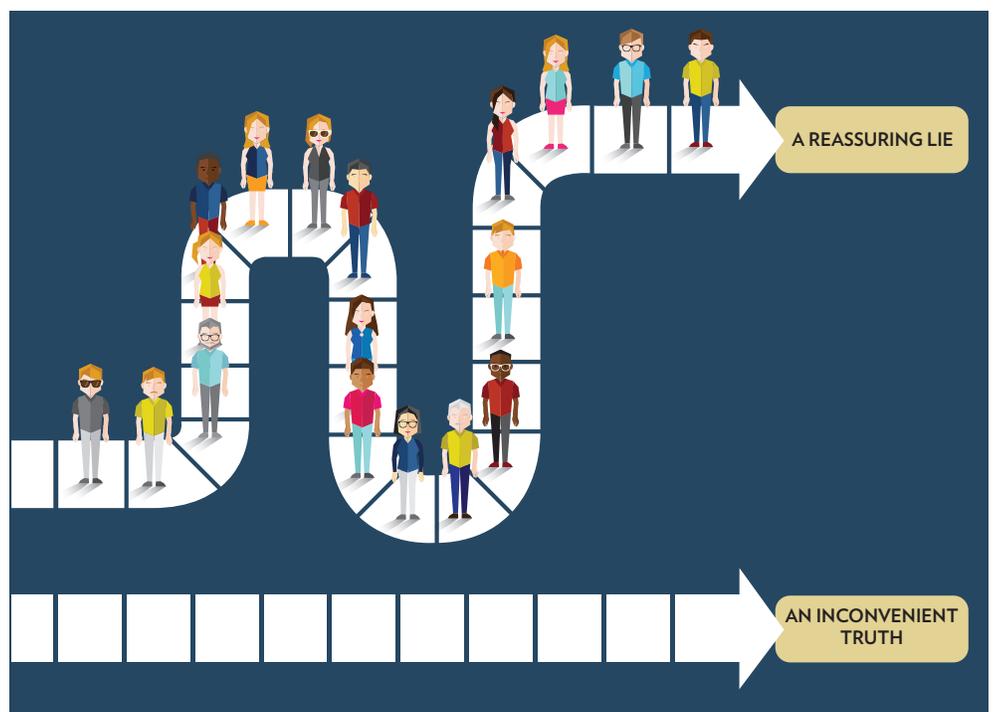
This concept is applicable to investment management. Certain investment styles or asset classes will meet with success for a period of time, suggesting that their interpretation of market forces aligns with reality. But in time, their performance often lags as market dynamics change and the investment style remains static. This is why we believe in a long-term approach and recommend that investors remain open-minded and flexible regarding investment styles, avoid taking extreme positions, and take steps toward diversification to manage the risk in their portfolios.

Biases

Cognitive biases are systematic patterns of deviation from rational judgments. They are often the result of emotional forces such as self-preservation, self-aggrandizement, or self-satisfaction. Cognitive biases can result in a perception of reality that is subjective and distorted, and this misalignment can produce suboptimal decisions that are out of sync with reality.

Along with faithfully applying the principles of critical thinking, awareness of biases is an important step to avoiding their traps. Let's look at two of the more common cognitive biases.

Confirmation Bias



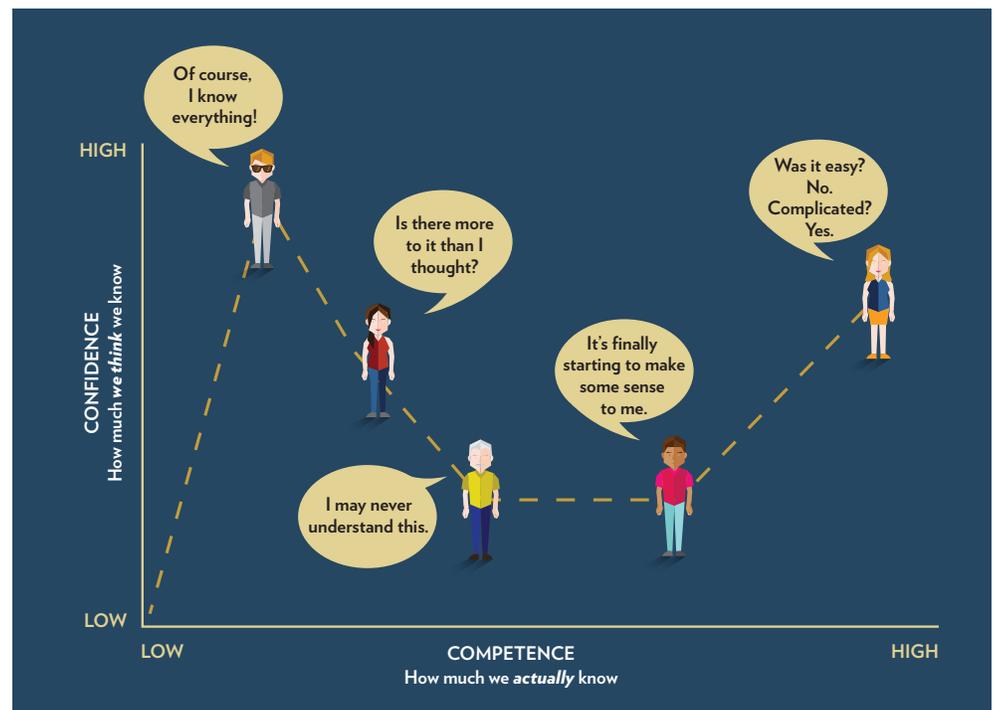
Confirmation bias describes our underlying tendency to notice, focus on, and give greater credence to evidence that fits with our existing beliefs. Confirmation bias is a cognitive shortcut that we use when gathering and interpreting information. It contravenes the rational principle of the independent “objective” selection of relevant information in formulating and solving problems. Confirmation bias is driven, in part, by our need for self-esteem, self-protection, and belonging.

Awareness of confirmation bias is especially important in the age of social media and artificial intelligence. Social media platforms have developed sophisticated mechanisms designed to establish and reinforce group identities by targeting specific, carefully curated

information to individuals with propensities to approve the content of this information. Much of the tribalism on every side in current politics and culture is the product of these mechanisms.

Confirmation bias can also be highly detrimental to successful investment management. Even professional investors, at times, compromise their process by overweighting positive news in security selection.

Dunning-Kruger Effect



The Dunning-Kruger effect describes people who perform a certain task poorly while simultaneously overestimating their ability and knowledge in the relevant area. The gap between perceived and actual knowledge and ability is problematic because it makes us believe that there is a greater chance that our decisions will be good ones than is truly the case. At the same time, it increases our difficulty in identifying bad decisions and learning from our mistakes.

The Dunning-Kruger effect can, of course, be detrimental to the individuals suffering from it in that their decision-making will be suboptimal while also difficult to self-correct. But the effect can also negatively impact group decision-making. Often, in groups, the loudest and apparently most confident person gets the most attention and dominates

the discussion. As a result, the quieter, but actually more capable people end up not making the decisions while those with the greatest perceived ability assume precedence. Such situations are commonplace both in corporate and political spheres, as well as among our friends and families.

In summary, we believe that independent thinking and avoiding biases are core to creating portfolios aligned with client goals. While it takes effort and discipline to think critically, the rewards for doing so, whether in politics, social relations, or wealth management, are too important to ignore. We are confident that wisdom will guide us in the new year and that the “best of times” are to come.

Stay well,



Principle Wealth Partners LLC is an SEC registered investment advisor. Advisory services are only offered to clients or prospective clients where Principle Wealth Partners and its representatives are properly licensed or exempt from licensure.

Out of 32,000 advisors nominated by their firms, 4,010 received the award. The 2020 Forbes Best-In-State Wealth Advisors rankings were developed in coordination with SHOOK research. This award is based on an algorithm of qualitative criterion for advisors who have a minimum of seven years of experience. This algorithm is qualitatively based, through due diligence reviews and quantitative data, factoring revenue trends, assets under management, compliance records, industry experience, and the encompassment of standards of preferred best practices. Portfolio performance is not considered as a part of the criteria. The Advisor does not pay Forbes or SHOOK in exchange for either the nomination or recognition. However, the Advisor does pay a fee for any marketing materials used that include the award's ribbon. Principle Wealth Partners is not affiliated with Forbes or SHOOK Research, LLC. This ranking is not indicative of an advisor's future performance, is not an endorsement, and may not be representative of individual clients' experience. The foregoing information has been obtained from sources considered to be reliable, but we do not guarantee that it is accurate or complete, it is not a statement of all available data necessary for making an investment decision, and it does not constitute a recommendation.