

MOVING WITH THE HERD

# Humans seek safety but bolt when danger looms

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The hierarchy of world sciences arguably goes something like this: physics, chemistry, geology, hydrology, meteorology, biology, psychology, sociology and, somewhere up the rear, economics and finance.

Yet all too often discussions about investment focus on economics and finance and ignore very important topics back up the pecking order.

After listening to some of WA's best investment brains for more than 90 minutes as part of the *West Business/Curtin University Outlook Series*, this reporter walked away none-the-wiser about where markets will be in one week, one month or 12 months time.

There is also no more confidence that the US Federal Reserve and low interest rates will save the world, or more belief that Wall Street will be pulled back down to size again and our market will again be crushed.

On one hand, the sharemarket could be a Ponzi scheme with investors flocking for yielding stocks. On the other, low bank interest rates make a compelling case for yield plays. By the time you get to your third hand, markets worldwide come a cropper when the Fed stops printing money.

Economics has more hands than Kali, the Hindu goddess.

What seems more important in investment decision-making is psychology and sociology: what goes on inside your head and the heads of other investors, and how group behaviour can move markets.

Despite claiming to be advanced mammals, humans are not much better than buffalo or cows. We move with an illusory safety in numbers then bolt when danger looms.

Good luck to you if you think you know when the herd will stop stampeding away from low-yielding bank accounts, and then turn around to flee the sharemarket in fear at some conceivable or unimaginable event.

What we can do is be aware of how we might react to such an event, and ensure that our finances are structured in such a way that most major negative events are at least emotionally tolerable. This



Fear can be useful. With apologies to US heavy metal band Hellyeah, who released *Stampede* in 2010.

requires a bit of thinking.

Do you want to be rich in retirement, driving around Australia in a \$100,000 Land Cruiser or just living comfortably in a modest house, and getting around in a Corolla.

Are you willing and able to sacrifice consumption now in a bid to improve your quality of life later?

How much risk do you realistically have to take to achieve your goals? Do you need to modify your goals to suit a level of risk you are more comfortable with?

How much market fluctuation are you willing and able to take now and at future stages of your life. As a 30-year-old investor going hard in growth plays, could you accept a GFC-style fall in your portfolio of 30 per cent or more knowing you have at least 30 years to recover?

Yes, maybe. But could you tolerate a whopping tumble as a 60-year-old? If you said yes, you are either seriously rich or need help.

What is clear is that the experts

## Fear is the enemy of measured thinking.

who took part in the Business Outlook Series, a joint initiative with Curtin University, have thought about these questions a lot more than most of us ever have.

Curtin University professor Robert Durand is a specialist in behavioural finance and economics and points to the relationship between neuro-psychology and decision making. His discipline lifts economics and its bastard brother.

People procrastinate about complex and important decisions, often to their detriment. They embark on

aggressive investment strategies without properly understanding the risk and then, when things go wrong, become too timid for their own good. Fear can make you procrastinate, while a combination of fear and greed can make you take on excessive risks. Fear is the enemy of measured thinking but, when understood and controlled, can be a useful stimulus.

Just witness the hoards of people who retreated to cash after their superannuation nest eggs got smashed in the GFC, but then missed the bargains in the aftermath and are belatedly trying to join the herd again.

The laws of physics dictate that a herd moving at 40kmh will run over an animal heading on the same vector at 5kmh. The laws of physics, biology, hydrology and chemistry dictate such a collision will be very messy indeed.

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