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BLINDLY FOLLOWING THE CROWD

DON'T BE A LEMMING

LEMMINGS are small rodents. According to a myth, they possess instincts that cause them to periodically charge en masse off cliffs to their deaths.

The myth of mass lemming suicide provides an irresistible metaphor for human behaviour. Someone blindly following the crowd — maybe towards catastrophe — is disparagingly called a lemming.

Over the past century, the lemming's suicidal myth has been invoked to express modern anxieties about how individuality could be submerged and destroyed by mass phenomena, such as extreme market price movements.

So, if we are investors who are easily swayed by the irrationality of market price action and jump in for fear of missing out on what we falsely believe is a golden opportunity, we are like lemmings.

Lemming investors exhibit herd mentality and invest without doing their research, which often leads to losses. This herd mentality typically increases the chances of losing money because investors either leave the market too early or get into it too late when prices are too high to make a profit.

The noise from the market is often so deafening that we can hardly hear ourselves speak.

We give in to the seductively tempting noise and succumb to

it. When we become a part of the noise, it is easy to be engulfed by the noise. What is required is for us to take a step back and observe the noise for what it is — noise.

Studies have found that investors are most influenced by current events — market news, political events, earnings, etc — and ignore long-term investment and economic fundamentals.

Quarterly results provide a constant flow of financial information, and we sometimes end up living from a quarter to a quarter.

There is not enough time to take a longer-term view. Furthermore, if a movement starts in one direction, it tends to pick up more and more investors with time and momentum.

The impact of such lemming-like behaviour has been made worse in recent years due to an abundance of sensationalist financial, economic and other news that bombards the sensibilities of investors.

This proliferation of financial media inevitably affects investor psychology and gives birth to lemmings.

There will never be a substitute for conducting the necessary due diligence. To keep from becoming a lemming investor, one must keep one's emotions under control. In other words, consider only the analysis that is critical to placing a trade.

An investor that is successful in doing this can possibly spot lem-

ming activity and consider exploiting it for gains by moving in a contrarian fashion.

The contrarian

Thinking like a contrarian is a much better strategy than succumbing to a lemming mentality, especially when irrational exuberance seems to have gripped the market. To counter the herd mentality, many sophisticated investors, such as contrarian traders, react oppositely when they sense that market movement is due to the influx of lemmings.

For example, if investors are in a buying frenzy, contrarians will sell, and when lemmings sell, these investors will buy instead.

Warren Buffet has summarised this approach as being greedy when others are fearful and being fearful when others are greedy.

Conducting the necessary due diligence, or thinking like a contrarian, is a much better strategy. Extreme optimism often coincides with market tops and extreme pessimism is quite apparent at market bottoms.

The obvious point is that these market extremes can only be factually identified after the fact. In other words, with the clarity that only comes with hindsight.

Savvy investors know that the time to sell is when prices are higher than fundamentals suggest and that the time to buy is when the prices are much lower

than is reasonably warranted.

Extreme optimism should be viewed in a bearish vein and extreme pessimism should be viewed as bullish perspective, which is the opposite of how a lemming thinks.

Storytime

To understand the lemming behaviour, Buffett shared one of Ben Graham's favourite stories.

An oil prospector, moving to his heavenly reward, was met by St Peter with bad news.

"You're qualified for residence, but as you can see, the compound for oilmen is packed. There's no way to squeeze you in."

After thinking for a moment, the prospector asked if he might say just four words to the present occupants.

That seemed harmless to St Peter, so he gave his okay. The prospector cupped his hand and yelled, "Oil discovered in hell."

Immediately the gates to the compound opened and all the oilmen rushed out.

Impressed, St Peter invited the prospector to move in and make himself comfortable. The prospector paused.

"No," he said. "I think I'll go along with the rest of the boys. There might be some truth to that rumour after all."

The writer is chief executive officer of Minority Shareholders Watch Group

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