THE SEVEN DEADLY SINS OF INVESTOR BEHAVIOUR

SIMON BARRETT
MERIAN GLOBAL INVESTORS
HERDING BEHAVIOUR IS FOUND IN NATURE...
HERDING

SECTORS CHANGING DIRECTION

Q4 2018

-24.4%

Energy

Industrials

IT

Consumer Discretionary

Financials

Consumer Services

Materials

Healthcare

Consumer Staples

Utilities

Real Estate

YTD 2019

14.2%

Source: Bloomberg, as at 26/02/2019. S&P 500 Sectors.
LOSS AVERSION
Loss Aversion

MSCI World Index

Nov 2018

Source: Bloomberg, as at 15/02/2019.

MSCI World Index.

Feb 2019

-13%

+14%
CONFIRMATION BIAS

Everything you look for and all that you perceive has a way of proving whatever you believe.
CONFIRMATION BIAS

Filtering out what does not confirm existing beliefs
ANCHORING IS A BIAS THAT IS SOMETIMES EXPLOITED

TIP?

8-10%
ANCHORING

Inflation expectations

Oil

Yen

Emerging Markets

Gold

German bunds

Utilities equities

Real estate equities
ENDOWMENT EFFECT

SELLING MY MUG $7.12

BUYING A MUG $2.87

BUYING A MUG $2.87

SELLING MY MUG $7.12
## Endowment Effect

Price change over subsequent 5 years relative to S&P 500

<table>
<thead>
<tr>
<th>Year</th>
<th>Effect</th>
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<tbody>
<tr>
<td>1969</td>
<td>-17%</td>
</tr>
<tr>
<td>1991</td>
<td>-17%</td>
</tr>
<tr>
<td>2000</td>
<td>-21%</td>
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INSTEAD OF THE ENDOWMENT EFFECT, RENT STOCKS

Open long position

Close position

Source: MGI. For illustrative purposes only.
CONSERVATISM

Source: CRSP database, as at 31/12/2018. Log scale.
OVERREACTION

AN EXCESSIVE EMOTIONAL RESPONSE
Past performance is not a guide to future performance. The value of investments can go down as well as up and is not guaranteed. Source: MGI, as at 28/02/2019. White circles, as at 31/10/2017. Light purple circles, as at 30/09/2018. Dark purple circles, as at 31/01/2019.
SUMMARY

• Behavioural finance draws on psychology to explain cognitive and emotional errors made by investors.

• Typical behavioural biases include herding, loss aversion, confirmation bias, anchoring and the endowment effect.

• Markets are not wholly efficient, and there may be opportunities for active fund management to exploit mispricing.
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