

We All Have Behavioral Problems

November 10, 2003

As you know GDP numbers are first preliminary estimated, then revised, and later finalized. It generally takes three months for this process, and of course every three years or so final revisions are made. The reason we mention this is that, as a postscript to our last Web Buzz, we promised a hard look at the GDP numbers. As we began to delve into these numbers (preliminary), we found non-adding columns. Being an old CPA, I get hot flashes when things don't add up – therefore we are going on to other things and will analyze GDP when the revision comes out later this month. Can you imagine that anyone in government would put out numbers that don't add up to a reported total? Of course not!

If you will recall, we visited last week about investment behavior that keeps the average investor from achieving good long-term results. We mentioned volatility as being one of those real investment “killers.” By the way, we came by this saying from a sophisticated and bright client of ours during the recent back up in government long-term interest rates. The following illustrates what can happen if one becomes obsessed with volatility (of course it's always downside volatility). Upside is rarely a problem psychologically. Please follow the following:

Bison Bond I Central Plains Advisors, Inc.
(Gross of Fees)

1 st Quarter 2003	+ 0.73%
2 nd Quarter 2003	+ 12.24%
3 rd Quarter 2003	- 6.07%
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YTD 2003	+ 6.20%

To obtain a total return of 6% for nine months from a government bond (arguably the highest quality asset in the world) in today's environment is very good. That is if it was 2% + 2% + 2%. But as it was 0.73% + 12.24% -6.07%, it became a problem and quite a few bailed out. When? During the -6.07% of course. Many managers knowing these seemingly inescapable behavioral tendencies spend many hours “dumbing down” their operations in order to hold their client base, but in so doing, deliver much lower returns. This is universally practiced and seems to be acceptable, but for us to do so, we believe, prostitutes our fundamental economic approach to bond market investing. That it seems is our behavioral problem – but you know what? We learned long ago that one must never negate his discipline. To do so violates one of the major tenets of good managers.