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INTELLIGENT INVESTING IN IRRATIONAL MARKETS

Panos Mourdoukoutas

Intelligent Investing in Irrational Markets

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To my Professors and Mentors, Theofanis Benos and Michael Hatziprokopiou

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A Personal Story

People are under the impression that economists coming off the graduate school are immersed in investing theory and practice. This isn't necessarily true. Economists spend a great deal of time developing mathematical models and studying the principles that guide markets, but very little time in studying institutions, including financial markets and the behavior of investors—I do know this very well. When I graduated with a Ph.D. in Economics, sometime in the last century, I had no idea about investing. That's why I hired Sam to manage my little savings chest.

The problem, however, is that Sam didn't manage my money himself. He handed it to a mutual fund manager. In the first two years, my portfolio was performing modestly, earning a little-bit more than the money market account it was invested in before it was handed over to Sam. But when the stock market crashed in 1987, it lost 30 percent of its value!

In the beginning, I was angry with Sam because he failed to explain to me the risks my portfolio was exposed to-though he handed me a 50-page prospectus that explained these risks in a batch of footnotes. The truth of the matter, however, is that equity markets are highly volatile, and at times crash. But they usually recover.

Anyone who was in the market at that time suffered losses in the neighborhood of 30 percent; no one could have anticipated the crash with certainty; following a big dose of money injections by the Fed chairman Alan Greenspan, the market recovered quickly and investors

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who stayed put and weathered the storm (or even better doubled-down) did very well over a 12-month period.

Not me. By then, I had already cashed my chips counting my losses. That's when I stopped being angry with Sam and became angry with myself, raising a question again and again: what did Sam know about investing that I didn't? What were his credentials? A Series 7 (Federal) and a Series 63 (New York State) securities license. Before long, I did fire Sam, took the necessary exams, and became a licensed investment advisor myself.

My career as an investment advisor was brief, as I was disenchanted with the way the industry operates. Besides, I was too sophisticated to be a good salesperson. But my career as an individual investor has been long and taught me valuable lessons which I discuss in Forbes.com, Barron's, Seekingalpha.com, and this book.

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