

Herding

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Herding is demonstrated by individuals who follow the actions of a larger group, even though it may not be in their best interest to do so. This trend is also known as the “lemming effect”. Investors like to feel comfort in what they are doing even if it is not the best decision when looked at in an objective, rational way.

A recent example of herding was during the 1999 tech bubble and subsequent bust. Many people were hearing about friends and neighbours making money in dot com businesses and as a result wanted to jump on board and reap the benefits they had been hearing so much about. Even the most conservative investors were swayed into participating in this tech bubble, although they would find that they ultimately could not stomach the risk.

In today's market environment, we see the herding mentality in the low-risk fixed income category and in commodity and gold sectors. Now, just because there is buying momentum here doesn't mean these asset classes don't have merit. Our approach suggests that it's all a matter of how much is enough for a particular client.

If you are interested in learning more about herding behaviour or behavioural finance in general, visit the following link: http://www.investopedia.com/university/behavioral_finance/behavioral8.asp.