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'Tis The Same Old Story

"THIS time it's different." Don't you hear this very often from people when you show concern about the continuous rise in stock prices and the sustainability of the current bull run? Conventional wisdom is in doubt and every valuation parameter is challenged. When this happens, people start joining the herd and do what the majority does. Thus, you have everyone talking about the great Indian growth story and everyone starts buying stocks at any available price. Everyone buys stocks at stretched valuations and remains equally confident of successfully offloading to another fool who will be willing to buy at a still higher price. Go back to five years ago. Those were the heydays of the technology boom. A similar phenomenon was happening then too, only the rules of the game were very different. People chose not to look at profits, instead, the mantra then was "eyeballs". During that time if you went by the conventional wisdom and asked someone the sanctity of the euphoria you were also told "This time it's different." The new economy was emerging.

Coming back to the present. The new buzzwords are "infrastructure" and "real estate". To cash on this craze you have managements selling stories about plans to develop and grow their infrastructure and real-estate businesses. The euphoria of real estate is so overpowering that even companies having car parking spaces are given high valuations in view of the high real estate prices.

Why do such things happen during a bull run? Why do people behave in such an irrational manner? The unique part about the stock market is that it is devoid of any institutional memory. Stock markets, being gambling dens, attract different types of people in the guise of investors. People start entering the market in a bull run, swayed by the lure of easy and quick money. When things come crashing down, these people exit the market vowing never to return.

IN the next bull phase you have a very different set of players entering the stock market who do not have any institutional memory of the past crash. Until they lose money they don't realise that it's a dangerous game. Thus, at any time in the market we find that those with institutional memory constitutes only about 30% which includes hardcore long-term investors and the broking community.

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EVEN MANY of the qualified institutional investors cannot claim to have a sound institutional memory, as attrition rate is high in that profession. Moreover, the job market also fluctuates with the bull and bear cycles. When you have such a bad institutional memory there is no learning from past mistakes. Hence, we find that the investors keep making the same mistakes over and over again.

Then you have the remaining 30% who have an institutional memory. They are the ones who are surviving the ups and downs of the market and learning from the mistakes. They are consistent and do not leave the market when it crashes. In fact, they look at opportunities during such times. They are a part of the market and, therefore, the market never lets them down. Irrespective of the bull and the bear cycles, it is these 30% who survive the storms. The only time they get hit is when they turn greedy.

Stock markets are interesting places for the wise who are willing to be investors and stay invested for the long run. If you want to be successful, understand that there are no shortcuts for making money. Do not be swayed when you hear stories of how people have made big fortunes in the stock market because you do not know the real facts and, also, no one likes to talk about losses. As Warren Buffet says, "I've always believed that of all the seven deadly sins, envy is the silliest. When you're envious, you're making yourself miserable. At least, with the other deadly sins, you're enjoying yourself."

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