

Seeds of Thought

An eclectic mix of market commentary, observations and ruminations

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Of Confirmation Bias & The Sex Pistols

Given identical caloric intake and an unchanged exercise regime, over time, we will gradually gain weight, because our bodies become more efficient at calorie utilization. In order to maintain the same weight as we age, we must take in fewer calories or step up our fitness routine. That's a fact.

In his book, *The Power of Habit*, Charles Duhigg talks about the role our basal ganglia play in directing various functions such as "recalling patterns and acting on them." It turns out that our brains are also sticklers for efficiency. In an effort to save energy, we bundle sequences of actions into an automatic routine, known as "chunking". In lay terms, we develop habits. According to a study done by Duke University in 2006, roughly 40% of what we do on a daily basis is driven by routine rather than actual decision-making. The more experience you have with a task, the more "efficient" (read: lazy) your brain becomes at effecting that action and the more likely your actions are the result of chunking rather than thinking.

Could it be then, that our chunkier physical appearance, representative of increased efficiency, can also be seen as an outward representation of our mental physique? The answer is, it's probably worse than you think.

There is a cognitive flaw that humans are prone to, called Confirmation Bias or MySide Bias, which is defined as "the tendency to search for, interpret, or remember information in a way that confirms one's beliefs or hypotheses." We prefer to hear opinions that agree with ours, surround ourselves with others who share our views, and read the research that conforms to our beliefs. Think about how few Catholics attend services at the Synagogue on a regular basis or liberals who watch Fox News, and you understand why it is that so few religious conversions happen and how the country has become more and more polarized. If you are a die-hard conservative, it is uncomfortable, even mentally exhausting to watch MSNBC, so most avoid it.

Now, think about the role technology is meant to serve. It is designed to make humans more efficient. It did so on the farms, then in the factories and now in the mind. So, we have our own internal technology, the brain, designed to maximize efficiency and we have developed external technology with the purpose of compounding that efficiency. It used to be that when we traveled, we needed to find a map, read the map or better yet, interact with locals, struggling with the language, challenging ourselves. We were explorers practicing mental calisthenics.

You want to know why kids learn faster than adults? It isn't because they are smarter or that they can create neural connections easier, it's because in order to create new connections, you must go outside your comfort zone. Kids are constantly being challenged. Left to their own devices, kids are just as lazy as adults, but they don't have a say. They have to attend school and sit through all the subjects, not just the ones they find interesting. The older we get, the more autonomous we become, and we don't like to challenge ourselves. It's unnatural.

When I was a kid, we had 4 TV stations. If you wanted to watch cartoons, you had to wake up early on a Saturday, so I did. If you wanted to watch sports, you had to watch what the producers at ABC's *Wide World of Sports* selected for you. I recall watching, and enjoying, the Pro Bowler's Tour, ping pong tournaments and women's gymnastics. It expanded my mind. Even if I didn't like it, actually, especially if I didn't like a program, it was challenging me mentally. Today, if you want

to watch football, you can watch it 24 hours a day. If you only want to watch a liberal news program, you can.

Speaking of news, there are apps that help us to become more efficient at gathering it. I can select only the type of stories I'm interested in and have them waiting for me in a concise email when I open my eyes. No need to scan the pages, actively avoiding the stories that might make me uncomfortable. I am shielded from anything that might assault my senses.

Now that millions of books, movies and songs are available at the touch of a button, how is a person expected to choose from among them? Don't worry about it. Amazon, Netflix and Spotify will do the thinking for you. No need to explore, they'll show you the books that will interest you based on what you've already read. Netflix will provide suggestions based on the movies you've already enjoyed. Spotify will select "new" songs for you based solely on the songs you already like and thanks to Cox's new Contour, you'll never have to watch a show that doesn't fit in with your viewing history. You no longer need to venture outside your comfort zone. As the Cox commercial says, "It's TV just for YOU!" In fact, we no longer even need to make the effort of setting our own preferences. Technology does it for us. So, yes, theoretically we have far more options available to us, but we are actually reducing both the depth and breadth of the information with which we are interacting.

I wonder, if Spotify's technology for breaking music down into its core components of melodies, rhythms and beats had always existed, would we have ever heard of Beethoven, Elvis, The Beatles, or The Sex Pistols? How will new sounds and genres be discovered if they lie outside the confines of our current playlists?

In the 2 years I have been studying social media, I've discovered some interesting tendencies. My particular artistic endeavor has 2 fundamental components, each of which lies at the opposite end of the spectrum. On the one hand, I create massive installation art using yarn. This has attracted a large number of followers interested in crocheting and knitting. Unlike the other yarnbombers, though, my installations take place up in the mountains, far from civilization, which tends to attract people interested in the rugged outdoors. There are very few who share my combined passion for fiber and forests. So, when I post images that would appeal to crafters, I tend to lose the interest of the outdoorsmen. Too many pics of the boulders at Lizard's Mouth and I'll lose my fiber followers. Here is the lesson learned. If you want to build a following via social media, you must be one dimensional. You're either a crafter or an outdoorsmen, and don't even think about posting pics of your dog or kids. They're a distraction, creating confusion for your followers. The audience wants what it knows, and expects. You can be unique, just make sure you are predictably unique.

The same occurs in our own industry. Take this excerpt from Mark Buchanan's *The Social Atom*. "A few years ago, for example, the economics consultancy London Economics assessed the predictions of more than thirty of the top British economic forecasting groups, including the Treasury, the National Institute, and the London Business School. They concluded: It is a conventional joke that there are as many different opinions about the future of the economy as there are economists. The truth is quite the opposite. Economic forecasters . . . all say more or less the same thing at the same time; the degree of agreement is astounding. The differences between forecasts are trivial relative to the differences between all forecasts and what happens...what they say is almost always wrong."

It's not surprising that this would be the case. Having participated in hundreds and hundreds of IC meetings and investor calls, I can tell you this, the questions follow an extraordinarily similar pattern. Patterns which also emerge in response rates depending on the subject line of an email, content of the bullet points and time of day it is sent out. Since the tendencies are so consistent and every analyst/salesperson is trying to trigger the same high response rate, it's only natural that all the content, opinions, delivery mechanisms would become eerily similar too.

Of course, no one wants to admit to being part of the flock. Everyone is looking for “uncorrelated”, perhaps the most overused, least sincere term in our industry. Here’s the thing about being uncorrelated. In order to achieve uncorrelated returns, you must think in an uncorrelated way. Remember, uncorrelated is not the same as negatively correlated. Contrarians provide negatively correlated returns, but fundamentally, they are still driven by the same inputs as consensus thinkers. In order to truly deliver uncorrelated returns, you must derive and process your information differently. While uncorrelated returns are very desirable, because of their many benefits, in order to achieve them, you must be willing to delve into things that, by their very nature, will make you uncomfortable, even frightened. You must be willing to challenge yourself, and your beliefs. And therein lies the reason so few achieve uncorrelated performance and even fewer allocate to it. Confirmation bias is a far more powerful force than the desire to outperform.

I will close with this. Since 2002, I have managed an investment portfolio. Even more than the 20.3% average annualized returns, and the positive performance during low vol periods as well as the financial crisis, what I am most proud of is the lack of correlation between my returns and every major index, both over the short and long term. In order to do so, I have developed some very unique research and trading practices. Through the years, those practices have incited confusion, amusement and even anger. Of course, it would be far easier to conform, but to be honest, I enjoy listening to new music, exploring new trails, and reading books on unfamiliar topics. Most of all, I enjoy challenging myself.

It is true, what Bija Advisors publishes won’t look or feel like what everyone else is producing. At times, you may read a piece and think, “I need to know what he thinks of the USD, not how I should be picking a movie to watch.” That’s your basal ganglia at work. The question is, are you willing to consider the possibility that perhaps how you go about picking movies is affecting your ability to make better investment decisions?

Happy Holidays

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