

## Blind Spot for Bernie

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Everyone wants to believe that their investment professional can help them. Even the advisors themselves want to believe this. And, those that flocked to Bernie Madoff thought they had found their man—he provided high returns with supposedly little risk. What they overlooked was that there is no such thing. The reason they disregarded it was due to their own inner demons, a concept explained later. These professionals had a blind spot. One reason this occurs is because human beings attempt to get rid of truth that doesn't suit their goals. They do this by diminishing negatives and enhancing positives. People weave a story that is convenient to themselves, but that might not fit the facts.

An extreme example of this is a clinical condition, Korsakoff's syndrome. Those affected by this disease have alcoholism-related damage to the brain area where recent memory is stored, the hippocampus. For that reason, they don't remember new events. So, when asked a question, instead of saying that they don't remember or know, they make up a response. They don't realize that they are wrong. This is self-delusion without knowledge. Two areas of the brain must be malfunctioning to make this happen. Recent memory storage is damaged as well as the brain monitoring system. Otherwise the Korsakoff's patient would know that his answer was absurd. William Hirstein, in his book [Brain Fiction](#), discusses defects that cause these clinical syndromes. He suggests that Korsakoff's syndrome is due to either damage in both the recent memory and monitoring areas, or it is secondary to a communication defect between the two.

Normal people are different. They realize they don't have information about recent events if they weren't present. Furthermore, they don't try to conjure up an answer. This is because their brain's frontal lobe keeps them in check by scrutinizing their answers.

On the other end of the spectrum is an individual with obsessive-compulsive disorder (OCD). This person is super-conscientious. His reflective faculties are extremely well developed. His brain monitoring is hyper-vigilant. These patients have a normal hippocampus (short term memory), but a hyper-functional orbital frontal cortex (monitoring area). As a result of this imbalance, the OCD patient scrutinizes activities and words excessively. He is super cautious, the antithesis of Madoff investors.

Somewhere between Korsakoff's syndrome and the OCD individual is a normal person. In his book, Hirstein names nine categories of syndromes between the two. Among them is a self-deceived person who is described in two flavors: with and without tension. The self-deceived person without tension is someone who deceived himself and doesn't know that he has done so (without tension). This is serious because a falsehood is retained as real. Yes, the sufferer doesn't know it. Some of Madoff's victims may have been in this category. Unfortunately, they may not learn from their experience because they don't realize they allowed themselves to be deceived, though information was available that might have

helped in this regard. As early as 2001, Michael Ocrant wrote an article questioning Madoff's returns ([The Madoff Scandal: Old News is New News](#)). It was largely ignored.

Between the normal person and the OCD individual is the self-deceived person with internal tension. This is someone who deceives himself, but feels uncomfortable about it. He knows something is wrong, but may not be sure what it is. This individual too could have been a Madoff victim, but might have felt uneasy about his investment and might even have bailed.

When self-deceived people made financial mistakes, it is the one with the internal tension that is most likely to learn from his mistake. This individual is receptive to relearning because he already had uncomfortable feelings (tension) and wants to alleviate them.

The self-deceived person without tension, on the other hand, is different. That individual has no inkling that he has allowed himself to be deceived. Therefore, he is unable to learn from his mistake. He would have a blind spot for Bernie.

In between the self-deceived individuals with and without tension is the normal person. He is a careful creature who remembers facts accurately and scrutinizes incoming information precisely, including that which pertains to him personally. Also, he monitors his feelings effectively. These characteristics mean he is not self-deceived. Thus, he is able to learn from his mistakes. This is an enormous advantage in investing.

The truth of the matter is that most of us are normal, but probably have a leaning toward one side or the other of center toward self-deception with or without tension. Recognizing such a tendency and working with it to reduce its effect could be helpful in future investment decisions. As Warren Buffet says, "Risk comes from not knowing what you're doing," and understanding yourself must surely be one of the first commandments of investing.

For some investing hints from William Hirstein please see [Avoid Self-deception While Investing](#).