Saving us from ourselves

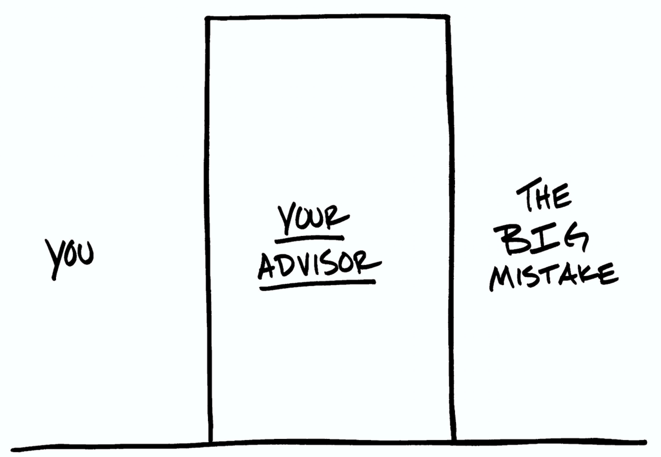
Issue 83: August 2018

It is not easy to provide a perspective when we have been saying the same thing the last several months. Nothing has really changed and everyone remains worried about their savings and the political rhetoric. This is perhaps why the seasoned investors keep on referring to temperance. It is our ability to manage our behaviour when things do seem odd and out of control, while ignoring the alluring schemes such as a Bitcoin, a Sharemax, switching to cash, or whatever comes next.

I thought it appropriate to share a few thoughts by Jason Zweig. He is a reputable columnist at the Wall Street Journal in the USA and offer remarkable insight and perspective. I have adapted an article of 5 years ago (28 June 2013) titled "*Saving Investors from Themselves*" and trust you will appreciate the commentary. The image I borrowed from Carl Richards at "The Behavior Gap".

Stating the obvious

Apparently Mr Zweig was once asked how he defined his job. His response was simple: "*My duty is to write the exact same thing between 50 and 100 times a year in such a way that neither my editors nor my readers will ever think I am repeating myself*". While financial markets might change constantly, surely good advice should be a constant, right? The temptation to tamper with your strategy is almost irresistible.



What could sound advice be worth?

While people seek and need good advice, they often want advice (or perhaps a free tip) that sounds great – also propagated by financial news and networks. Advice that sounds the best in the short run could be the most dangerous over the long term. Just think about it: avoiding the big mistakes could be invaluable over the long term – take the Steinhoff saga for example. It is easier said than done and we admit that! Hindsight is always perfect.

Everyone wants the "secret sauce", the magic wand, or a roadmap to the mythical low-risk, high-return investment that could double your money in no time. There are many who look for the returns of whatever has been latest and greatest and shun whatever seems dull or boring. Most financial journalists, like global stock exchanges, are dedicated to a mantra of marketing: "*When the ducks quack, feed 'em*". That means telling investors to buy Internet and small companies in 1999 and early 2000; explaining in 2005 and 2006 how to buy and sell properties in a low interest environment; in 2008 and 2009 it meant convincing people to dump their investments on the JSE (Johannesburg Stock Exchange); and ever since 2008, it has meant telling people that bonds are "safe" like high-dividend-paying companies and so-called minimum-volatility stocks.

Striking that, as brilliant research by the psychologist Paul Andreassen showed many years ago, people who receive frequent news updates on their investments earn lower returns than those who get no news. It's also no wonder that the media has ignored those findings. So people don't care to admit that they spend a lifetime being part of a problem instead of trying to be part of the solution.

Returning to an average is golden

Our job is to learn from other people's mistakes (and our own). Above all, it means trying to save people from themselves. As the legendary founder of security analysis, Benjamin Graham (and role model of Warren Buffett), wrote in The Intelligent Investor in 1949: "*The investor's chief problem – and even his worst enemy – is likely to be himself.*" One of the main reasons we are all our worst enemies as investors, is that the financial maze is somehow set up to deceive us. These are harsh words indeed.

From data points and experience, many concluded long ago that the statistical regression to a mean is the most powerful law in financial physics; i.e. periods of <u>above</u>-average performance are inevitably followed by <u>below</u>-average returns, and bad times inevitably set the stage for surprisingly good performance. This could be the case for South Africa (remember 2002 and the recovery of the Rand in subsequent years).

Unfortunately *homo sapiens* perceive reality in short time-frames, making a long-term perspective almost impossible to sustain – and making most people prone to believe that every blip is the beginning of something durable.

Our role, therefore, is to factor in a regression to the mean even as most others believe in headlines. We prefer talking clients out of whatever is hot and, instead, to think about investing in what is boring but sustainable. Unfortunately we push back. Our role as an advisory practice, is also to remind clients constantly that knowing what not to do is much more important than what to do. Approximately 90% of the time, the single most important thing investors should do is absolutely nothing. Yes, this might sound very strange to most of us!

In conclusion...

It always seems different. History does not necessarily repeat itself, but it rhymes. Even with AI (Artificial Intelligence), human nature will never change. We should always be sceptical of anything that has recently soared in price, and you should always become more enthusiastic about something that has recently fallen in price (and then do your homework). That's what it means to seek value and opportunity.

The last few years have proven to be challenging for South Africa and its citizens. We therefore repeat and encourage our clients to stick with a personalised long-term financial plan.