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Sandton Convention Centre

17 October
2023

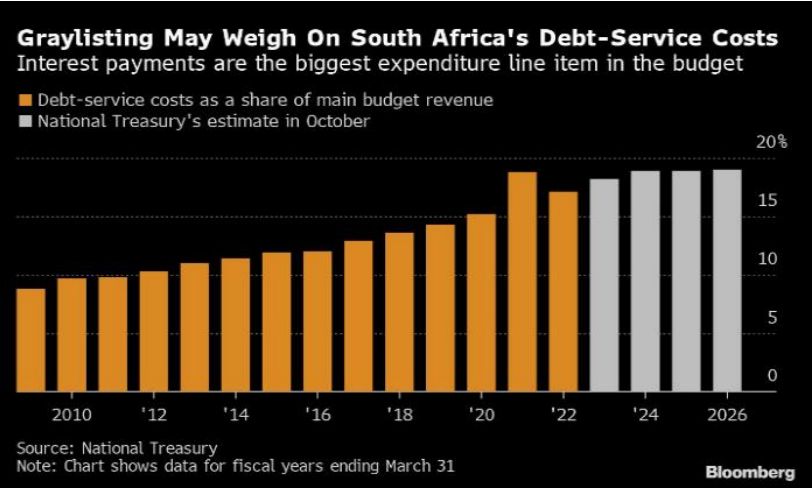
The Foundations to Investment Success

Returns Follow Risk. Full Stop.

Dr Adrian Saville | Professor in Economics, Finance and Strategy, GIBS
Boundless World

📍 savillea
🐦 AdrianSaville

Good Afternoon ... Here Is The Noise



Noise & News

“It’s all very, very noisy out there. Very hard to hear the tune ... Like a piano in the next room, it’s playing your song, but unfortunately, it’s out of whack, some of the strings are missing, and the pianist is tone deaf and drunk – I mean the noise! Impossible!”

Tom Stoppard, *Arcadia*



Let's Play A Game: "What's Your Word?"

PT: Op
age M
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ed a model call
onal way. The d
o answer follow
incorrect prem
ChatGPT is a sibling m
o follow an instruction in a prom
onse.



World Health Organization



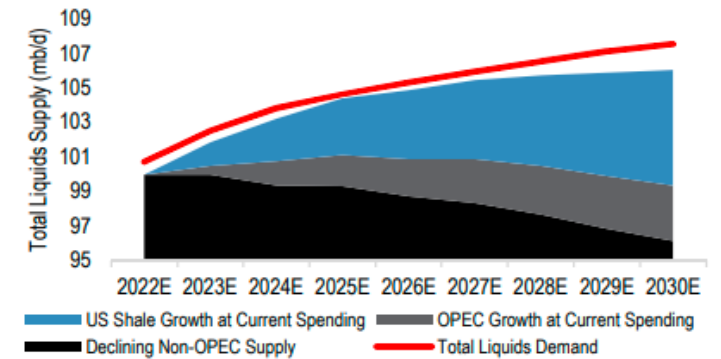
as Stalled
e annual consumer price change by country



Pandemic & Panic: Same Impulse = 180° Different



Figure 8: Oil: Supercycle set to play out as supply growth continues to lag demand; current spend implies 2022-30 avg deficit 0.7mb/d

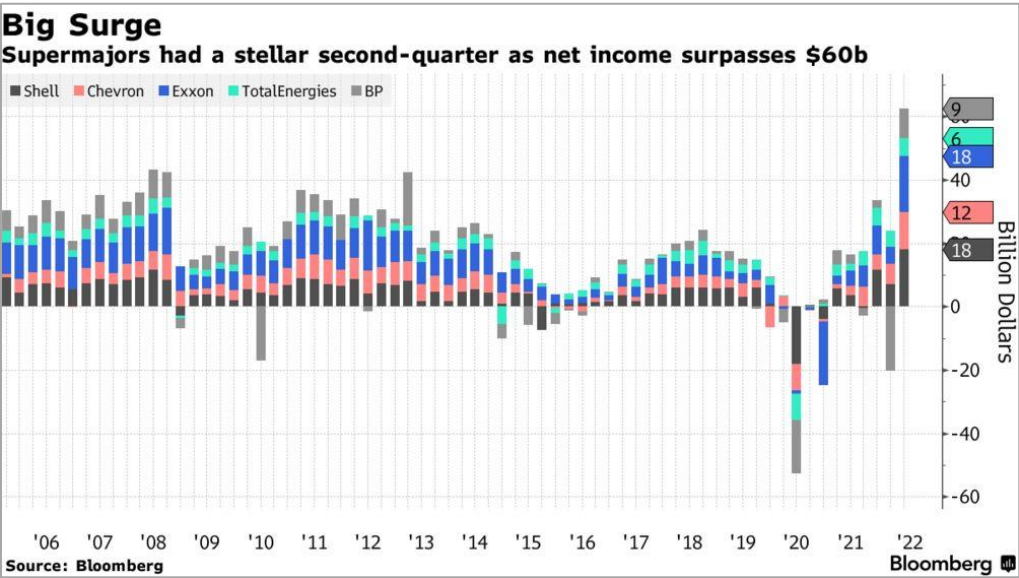
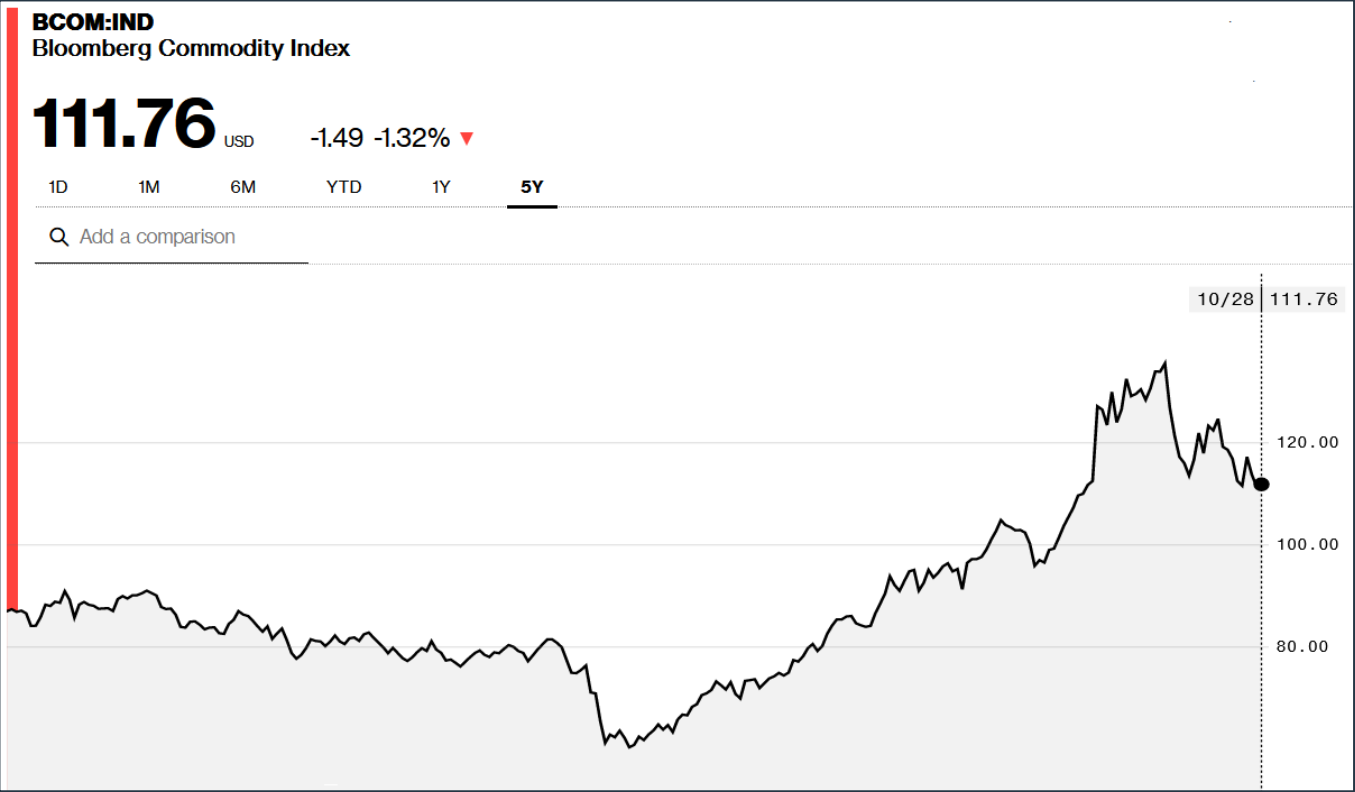


Source: J.P. Morgan estimates.

“Today, the average SPAC that de-SPAC-ed since 2020 by completing an acquisition (in each case, with the approval of its investors) is selling at \$5.25, versus its issue price of \$10.00. This is a good example of a new thing that turned out to be less dependable than investors – who fell once again for a can’t-lose silver bullet – had thought.”

Howard Marks (2022) Oaktree Capital

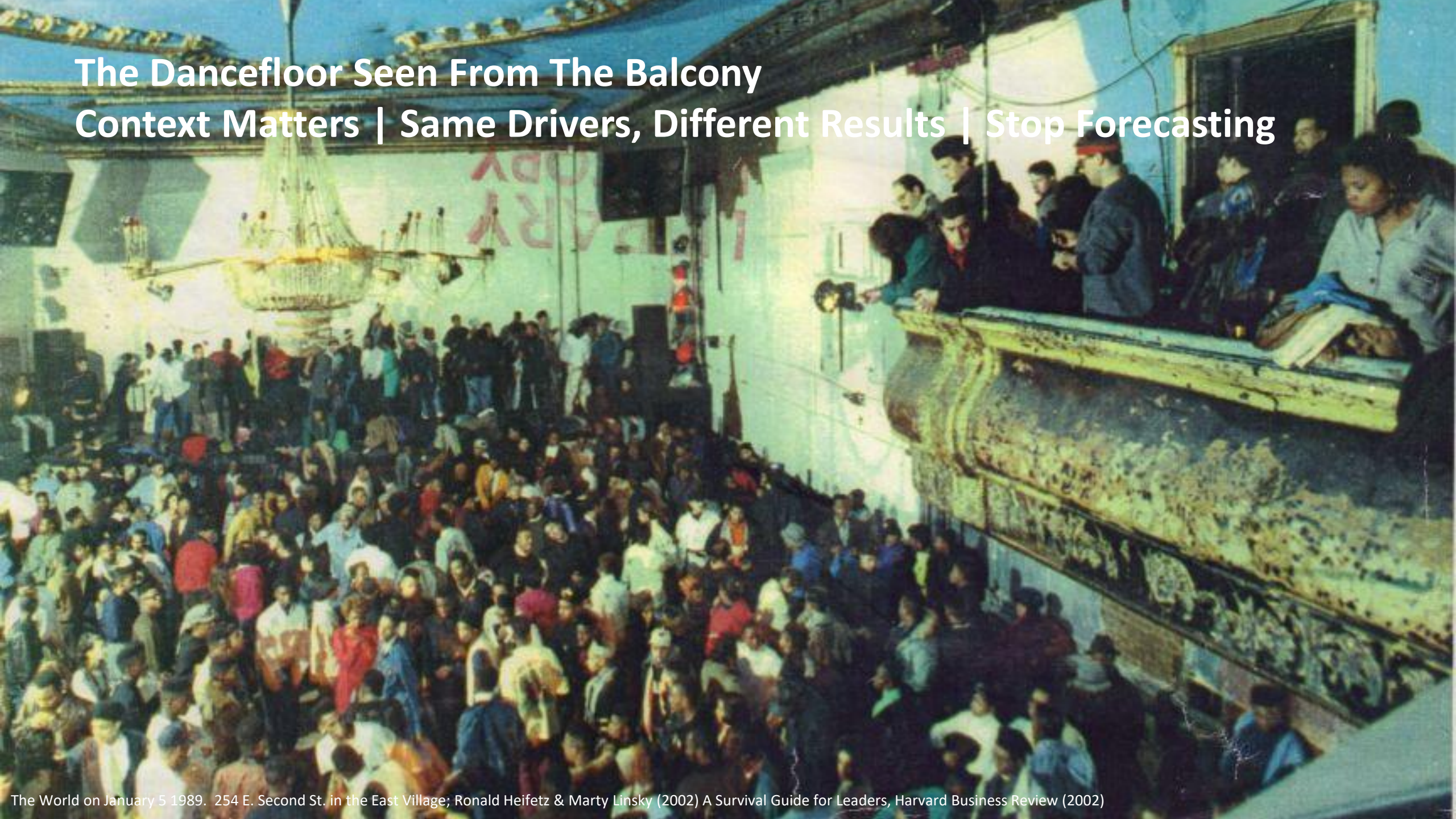
War & Oil: Same Impulse = 180° Different



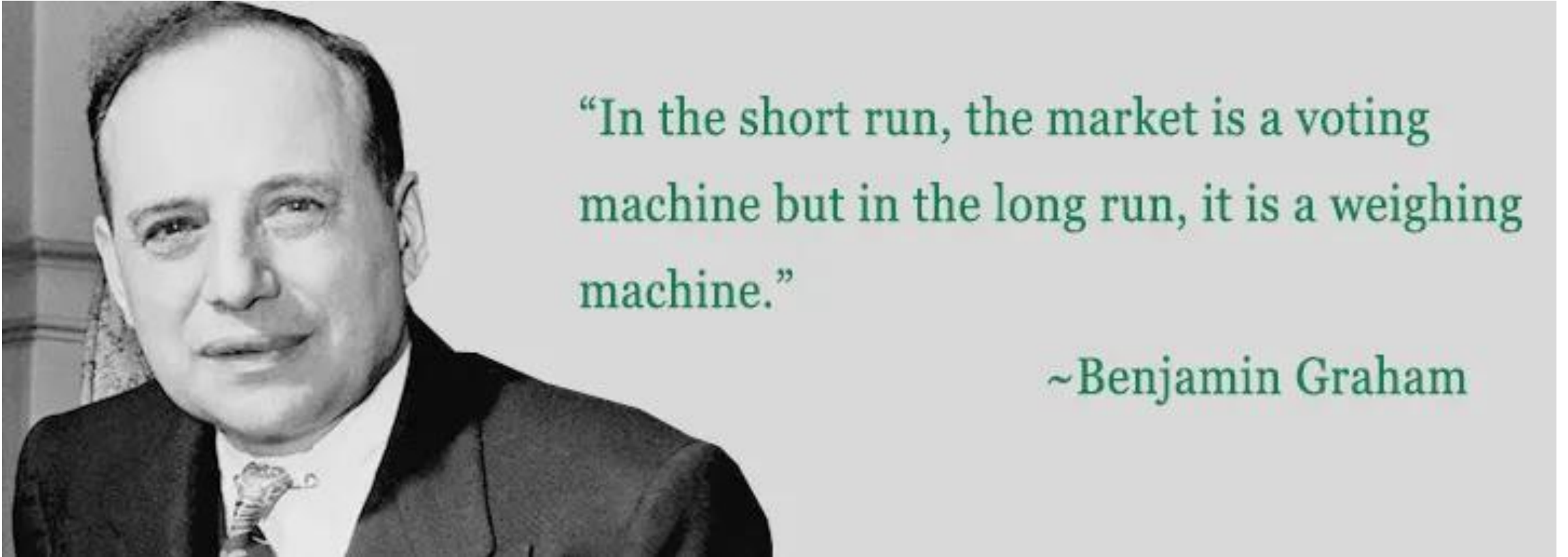
Bloomberg (August 2022) BP Boosts Returns as Oil Refining and Trading Drive Profit Beat

The Dancefloor Seen From The Balcony

Context Matters | Same Drivers, Different Results | Stop Forecasting



Voting Versus Weighing

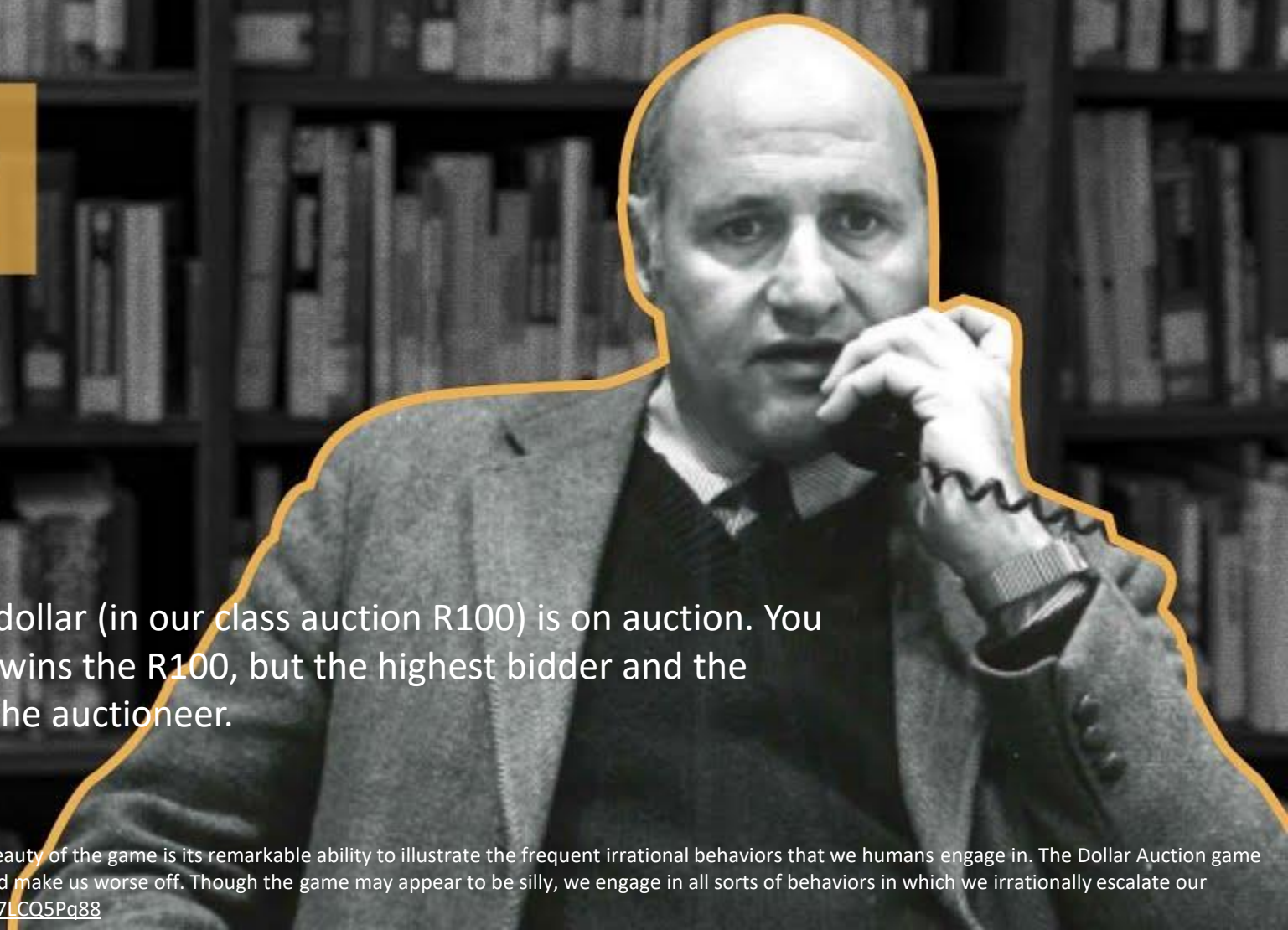


- Voting is sentiment, beliefs, and behaviour – the stuff of psychology
- Weighing is intrinsic value, cash flow, and true worth – the stuff of accounting and finance

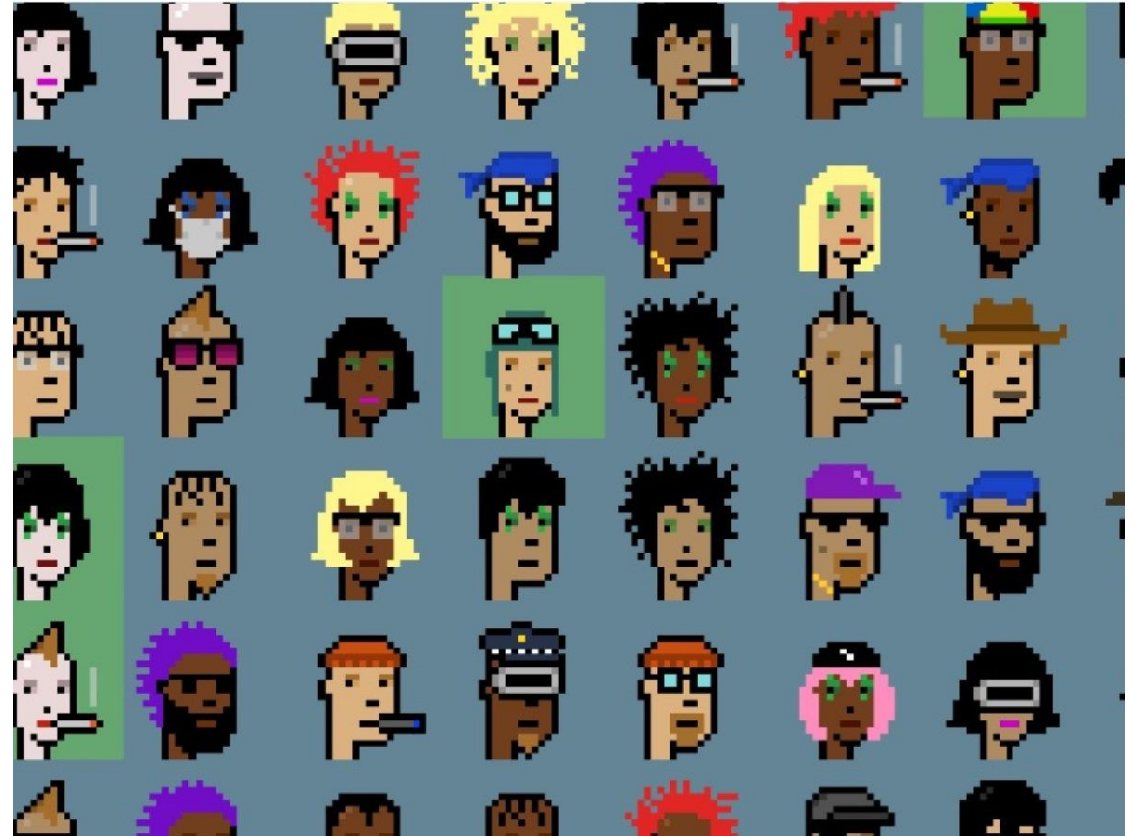
Dollar Auction Game

The rules of the Dollar Auction are simple: A dollar (in our class auction R100) is on auction. You can bid in R5 increments. The highest bidder wins the R100, but the highest bidder and the second highest bidder pay their final bids to the auctioneer.

The Dollar Auction is a simple game devised by economist Martin Shubik in the 1970s. The beauty of the game is its remarkable ability to illustrate the frequent irrational behaviors that we humans engage in. The Dollar Auction game shows how the rational pursuit of our own self interest can lead us into an escalation trap and make us worse off. Though the game may appear to be silly, we engage in all sorts of behaviors in which we irrationally escalate our commitment in hopes of something better; see also <https://www.youtube.com/watch?v=A07LCQ5Pq88>



What Are Coins & Punks Worth?



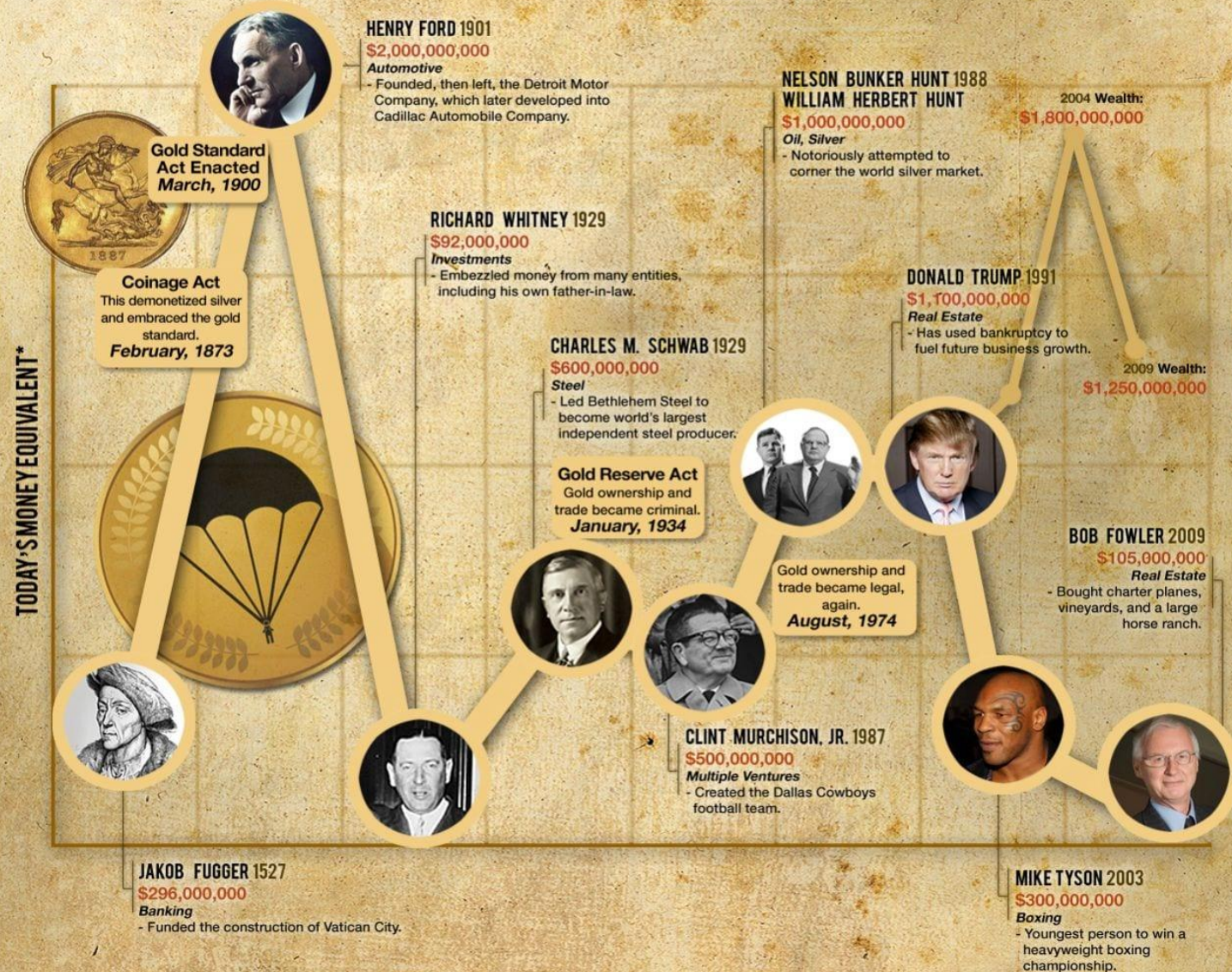
What's It Worth?



The Single Biggest Risk



BIGGEST INDIVIDUAL BANKRUPTCIES IN HISTORY



Pogo On Investing

A Pogo comic strip panel. In the foreground, a large brown bear wearing a green and yellow plaid hat sits on a log, looking towards a small boy. The boy, with spiky hair and wearing a red and black striped shirt, sits on the log and looks back at the bear. They are in a forest where the ground is covered in a massive pile of trash, including a sink, a toilet, a lamp, and various boxes and debris. In the background, there are trees and a small building. Two speech bubbles are present. The first speech bubble, from the bear, says "IT *IS* HARD WALKIN' ON THIS STUFF." The second speech bubble, from the boy, says "YEP, SON, WE HAVE MET THE ENEMY AND HE IS US." The artist's signature "WALT KELLY" is in the bottom right corner.

IT *IS* HARD
WALKIN'
ON THIS
STUFF.

YEP, SON,
WE HAVE MET
THE ENEMY
AND HE IS US.

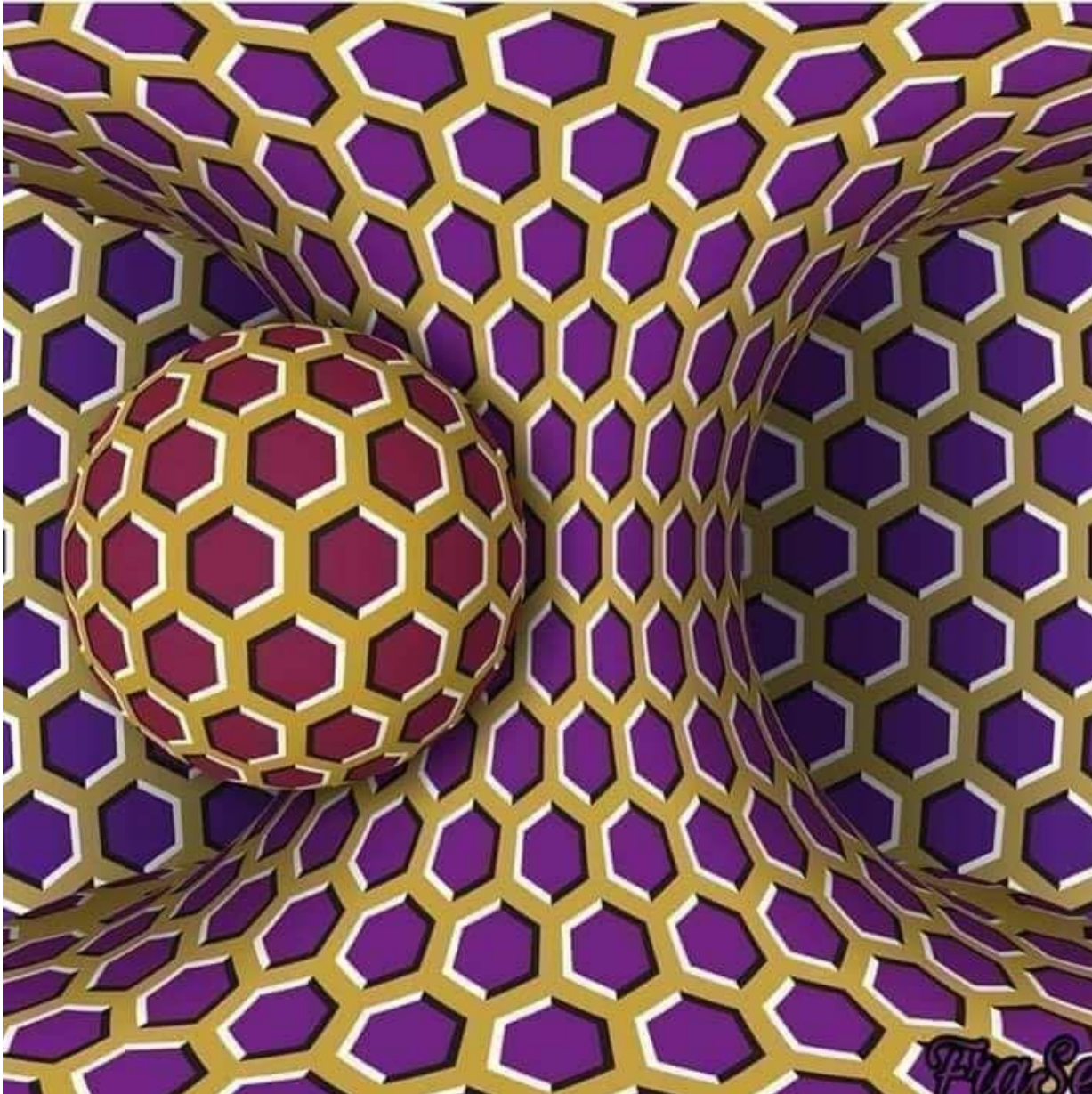
WALT
KELLY



HOW TO SEE THE DRESS BOTH WAYS



It's Not A Video: It's An Optical Illusion



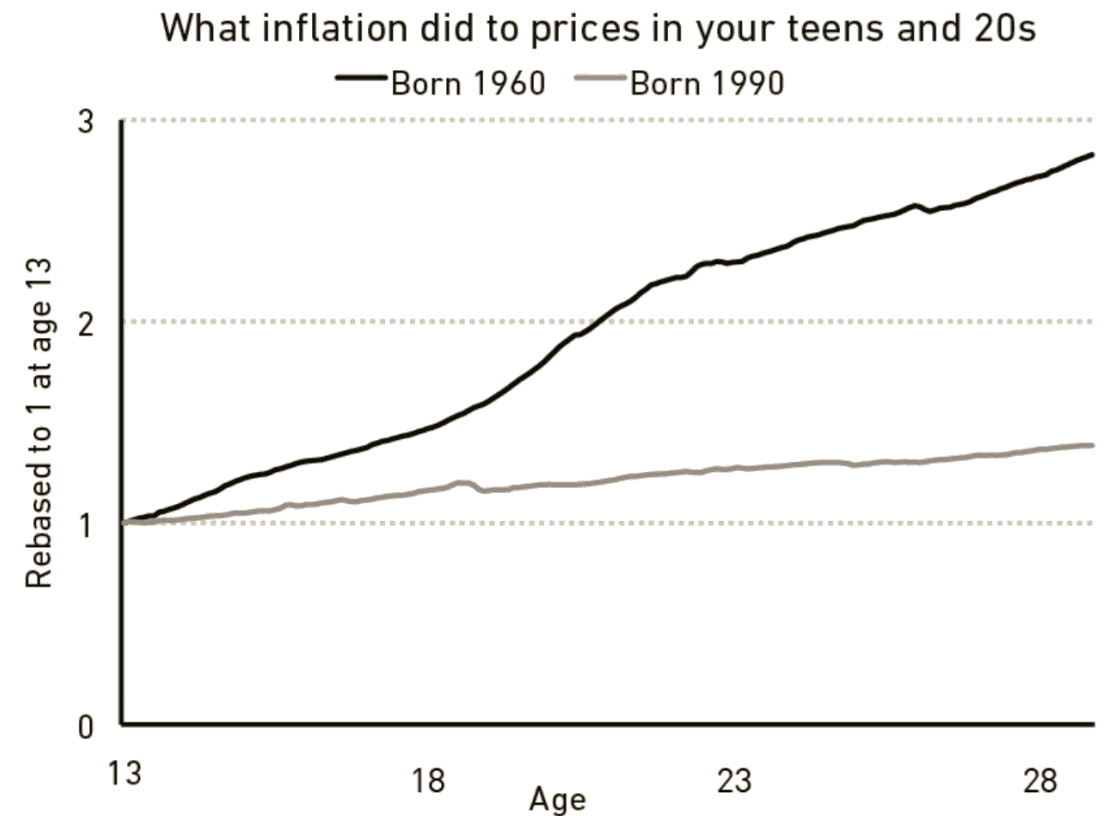
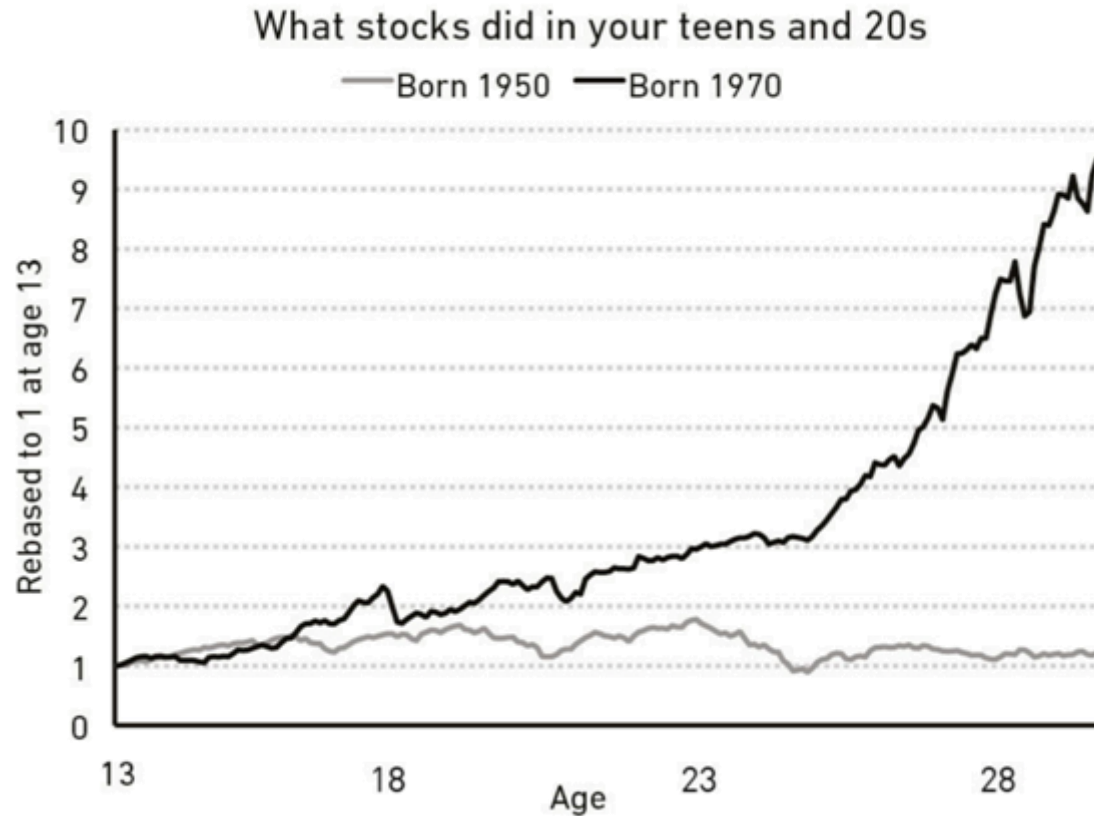
Triop @CosmosDoctor · 22h

Replying to @InterestingSci1

If you move your head to the left, the picture won't move...



Outside In: Context Shapes Belief

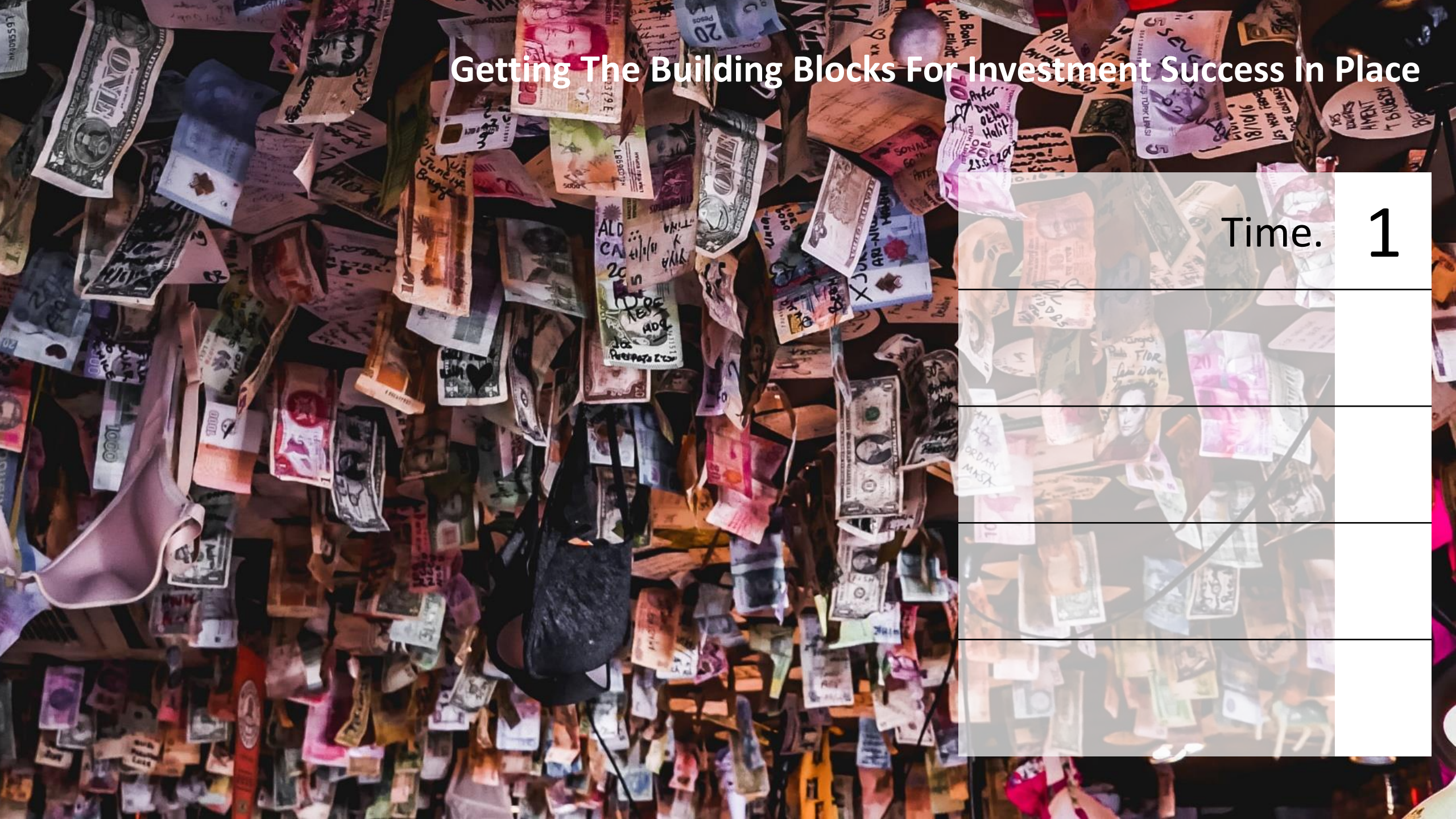


Your personal experiences with money make up maybe 0.00000000001% of what's happened in the world, but maybe 80% of how you think the world works. There's a huge gap between firsthand knowledge and how we parlay those limited insights into making sense of the world. Our experiences color our judgment, but the foundations of that judgement are dubious, incomplete, and full of blind spots.



Investing is
simple, but
not easy...

~Warren Buffett~

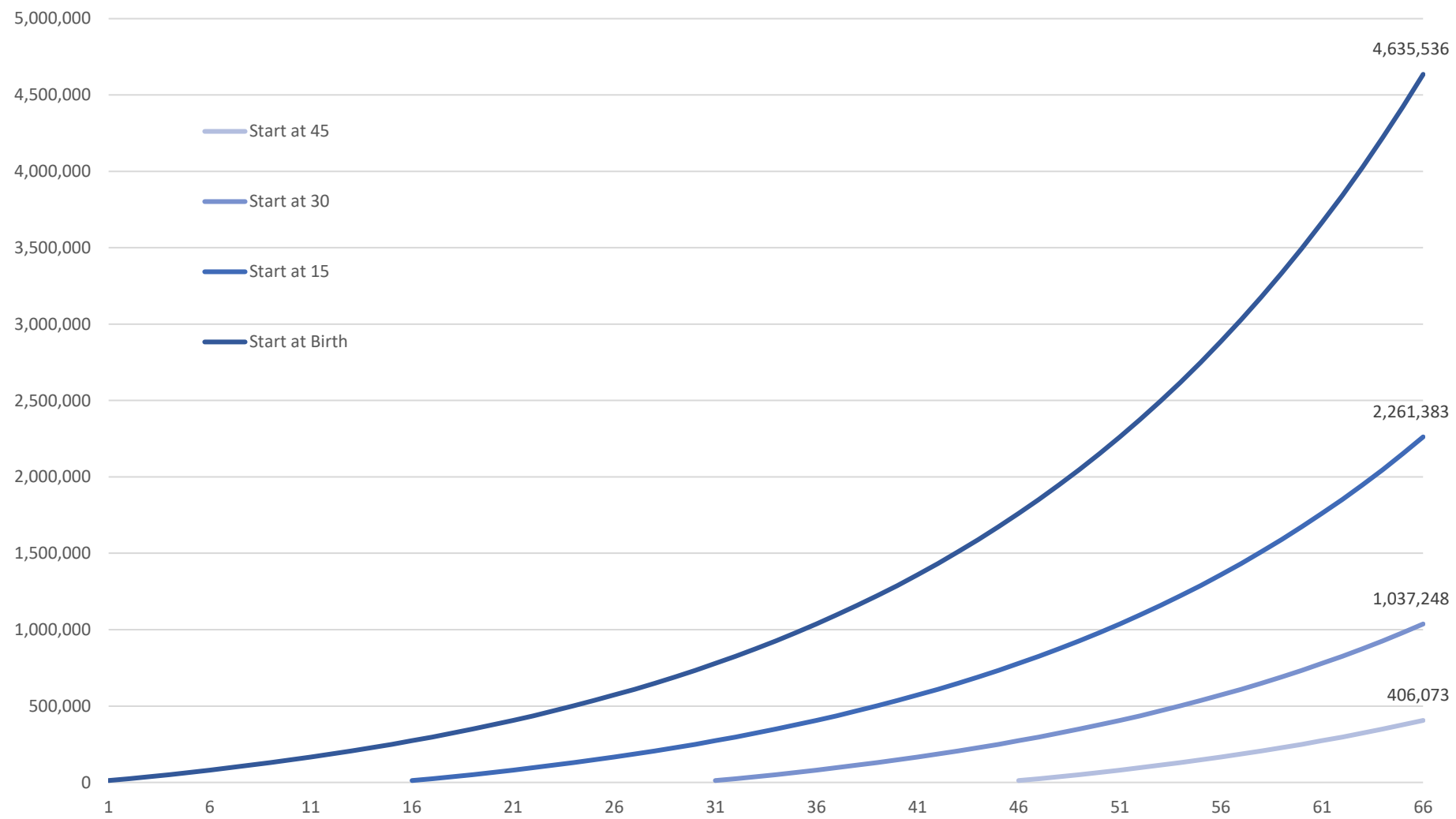


Getting The Building Blocks For Investment Success In Place

Time.

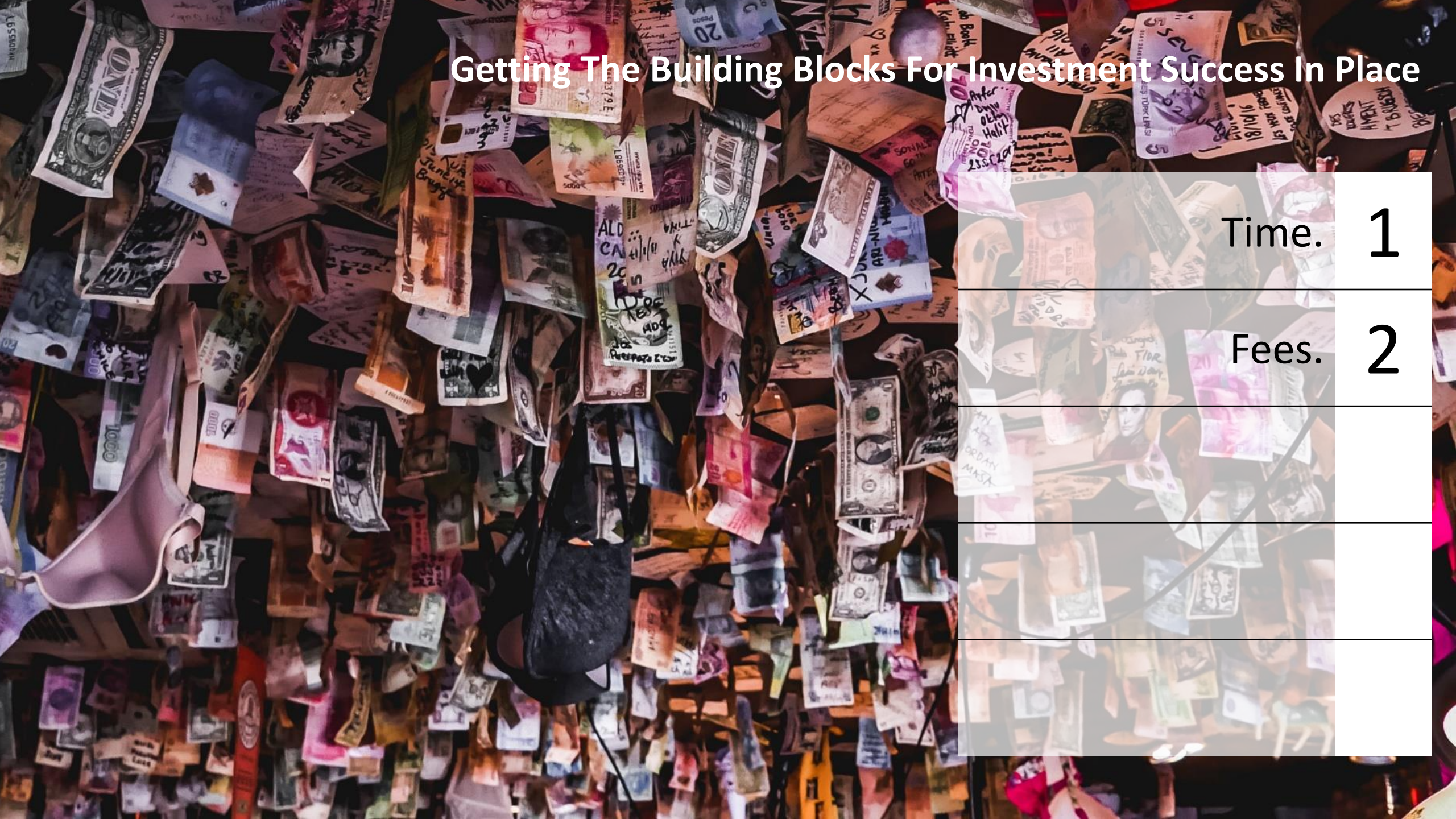
1

Time Is The Greatest Builder



> 10x

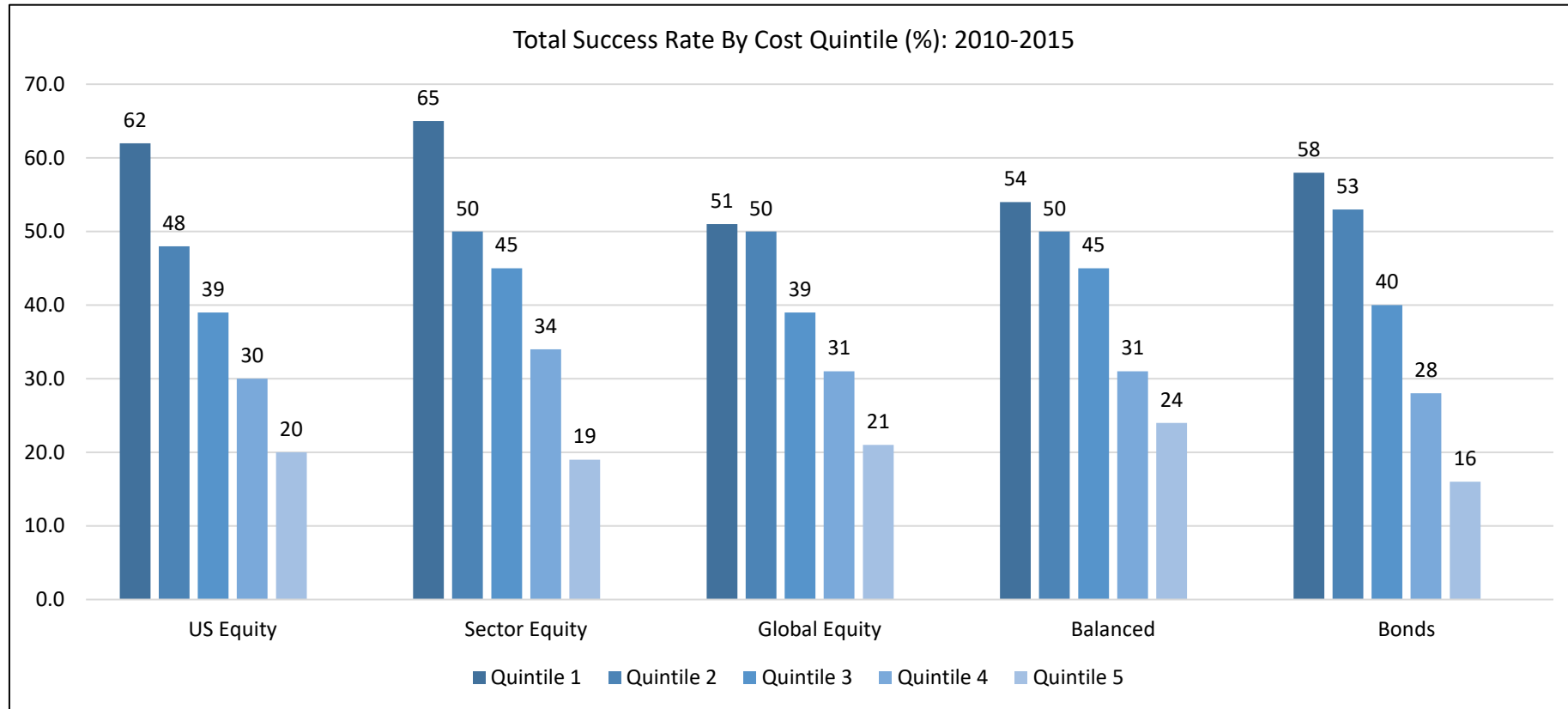
Investment of R1,000 per month; average tax rate of 30%; return of 6.4% per annum net of fees; average fees of 2.5% per annum; fee reduces by 1.0% per annum



Getting The Building Blocks For Investment Success In Place

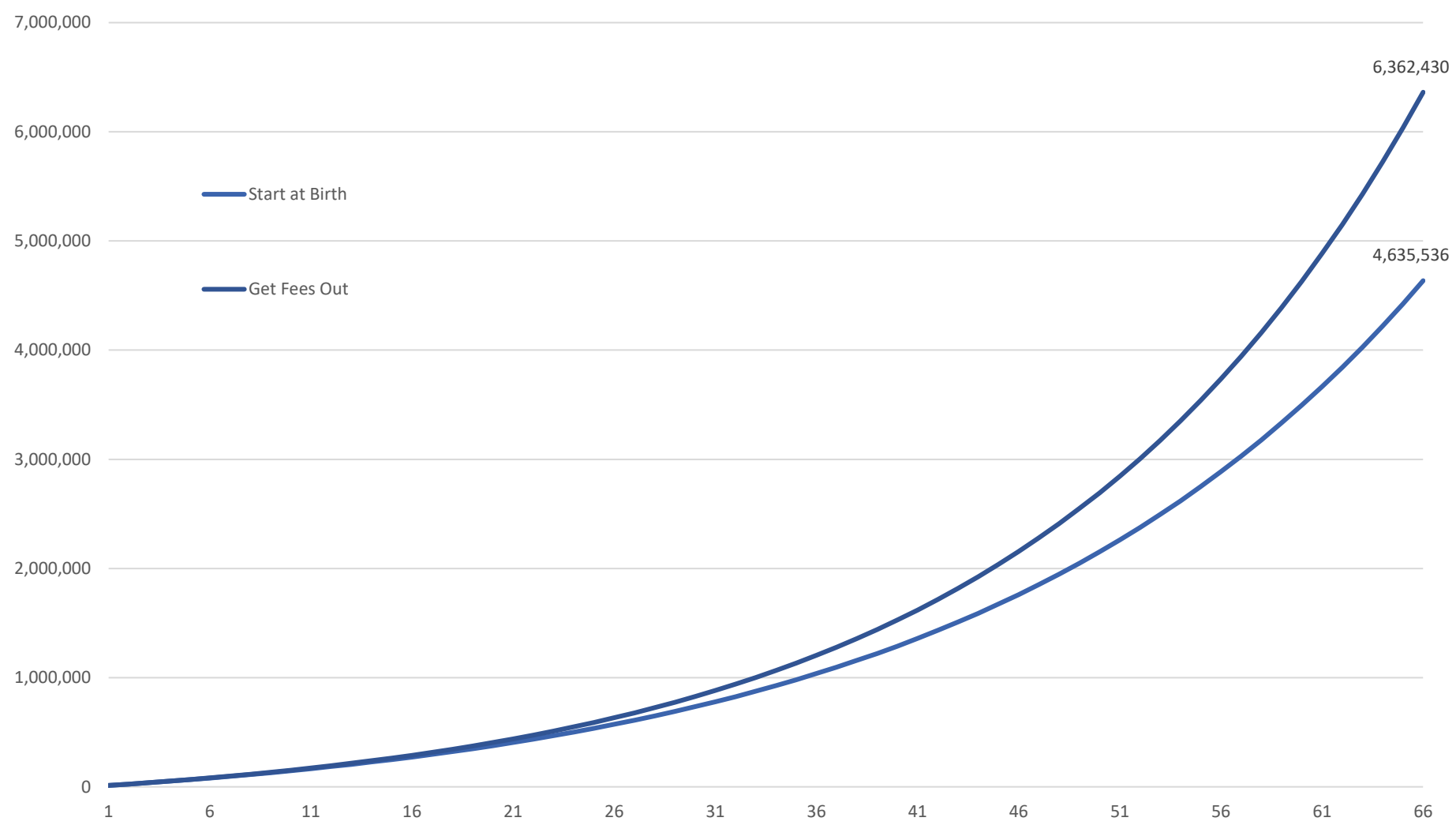
Time.	1
Fees.	2

Get Fees Low



“Success requires that a fund survives and outperforms its category. All told, lowest cost funds are three times as likely to succeed as the priciest quintile.”

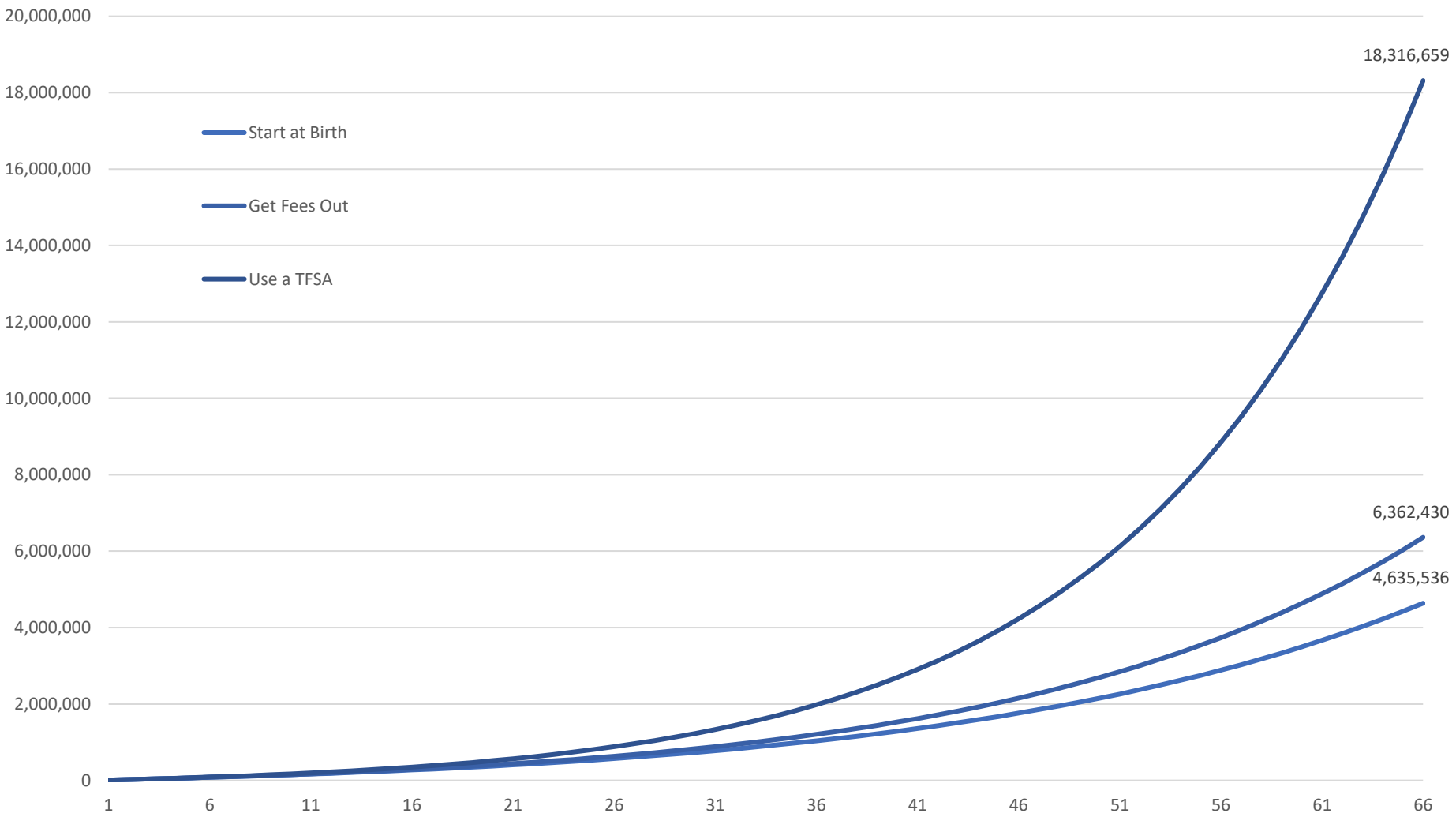
Expenses Eat While You Sleep



Get fees
out

Investment of R1,000 per month; average tax rate of 30%; return of 6.4% per annum net of fees; average fees of 2.5% per annum; fee reduces by 1.0% per annum

Start Early, Get Costs Low & Get Taxes Out



Adios
taxes

Investment of R1,000 per month; average tax rate of 30%; return of 6.4% per annum net of fees; average fees of 2.5% per annum; fee reduces by 1.0% per annum



Getting The Building Blocks For Investment Success In Place

Time.

1

Fees.

2

Buy the Market.

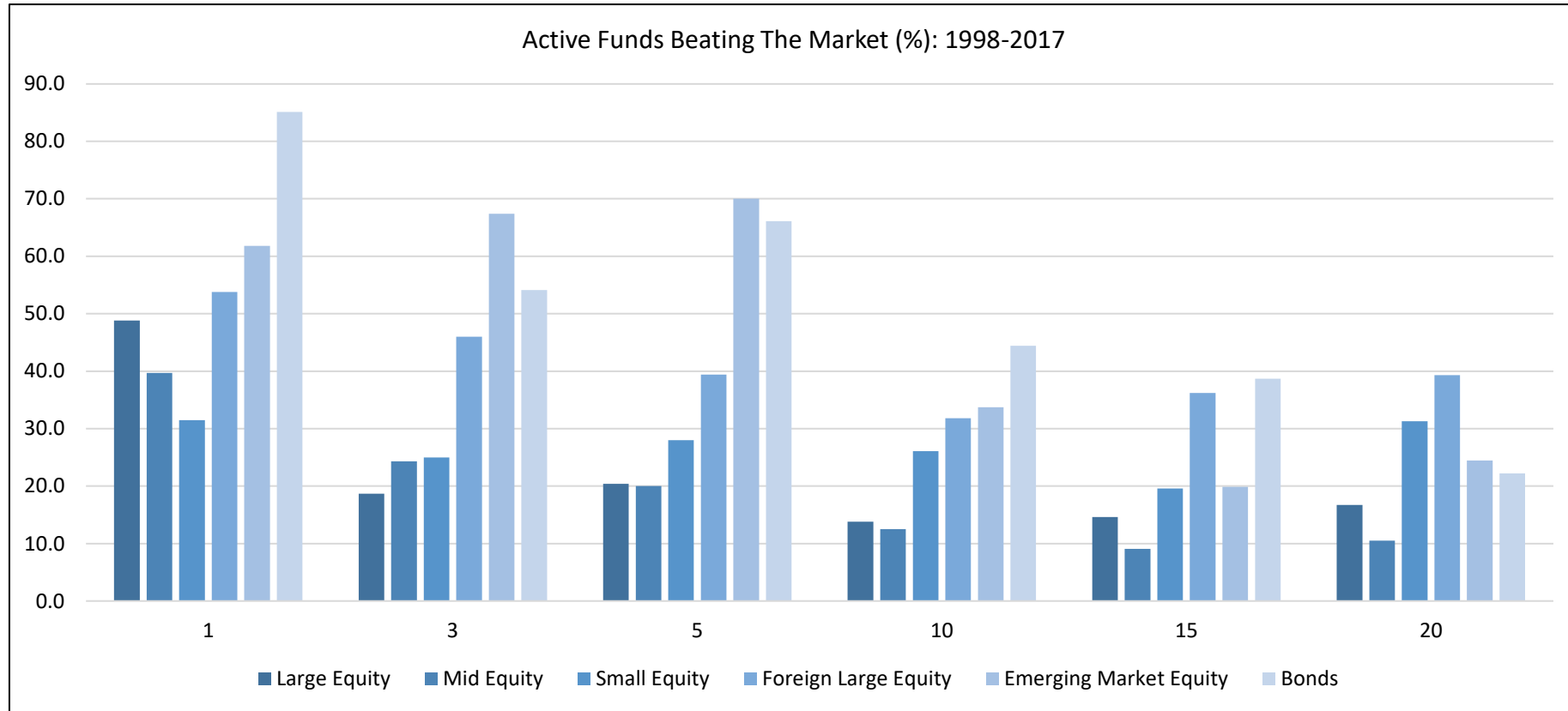
3



“If you are ready to give up everything else and study the whole history and background of the market and all principal companies whose stocks are on the board as carefully as a medical student studies anatomy — if you can do all that and in addition you have the cool nerves of a gambler, the sixth sense of a clairvoyant and the courage of a lion, then you have a ghost of a chance.”

— Bernard Baruch
Financier, investor and
philanthropist
1870-1965

Buying The Market Beats The Market



“There is no category where a majority of active managers beat the market over a 10-year period, let alone longer ones.”



Getting The Building Blocks For Investment Success In Place

Time.

1

Fees.

2

Buy the Market.

3

Diversify.

4

Diversification: The Freest Lunch In Investing

- In times of heightened anxiety and uncertainty, investors will often favour a “safe asset” that gives “a stable 5% return”.

- To get this steady return, investors will sell out of other riskier asset classes, such as real estate and equities which have less knowable returns.

- This may not be as rational as it first seems - especially if you have a long investment timeline.

- To illustrate, let’s imagine you find a stable, single asset investment that will give you a guaranteed 5% per annum over the next 25 years.

- If you invested R100 today, it would then be worth R323 at the end of the term.

- Then, let’s put 20% into each of five assets that have a blended average return of 5,0%

Year	Gold	Cash	Bonds	Property	Equities	Straight Five	Blended Five
	0.0	2.5	5.0	7.5	10.0	5.0	5.0
1	100	100	100	100	100	100	100
2	100	103	105	108	110	105	105
3	100	105	110	116	121	110	110
4	100	108	116	124	133	116	116
5	100	110	122	134	146	122	122
6	100	113	128	144	161	128	129
7	100	116	134	154	177	134	136
8	100	119	141	166	195	141	144
9	100	122	148	178	214	148	152
10	100	125	155	192	236	155	162
11	100	128	163	206	259	163	171
12	100	131	171	222	285	171	182
13	100	134	180	238	314	180	193
14	100	138	189	256	345	189	206
15	100	141	198	275	380	198	219
16	100	145	208	296	418	208	233
17	100	148	218	318	459	218	249
18	100	152	229	342	505	229	266
19	100	156	241	368	556	241	284
20	100	160	253	395	612	253	304
21	100	164	265	425	673	265	325
22	100	168	279	457	740	279	349
23	100	172	293	491	814	293	374
24	100	176	307	528	895	307	401
25	100	181	323	567	985	323	431



Getting The Building Blocks For Investment Success In Place

Time.

1

Fees.

2

Buy the Market.

3

Diversify.

4

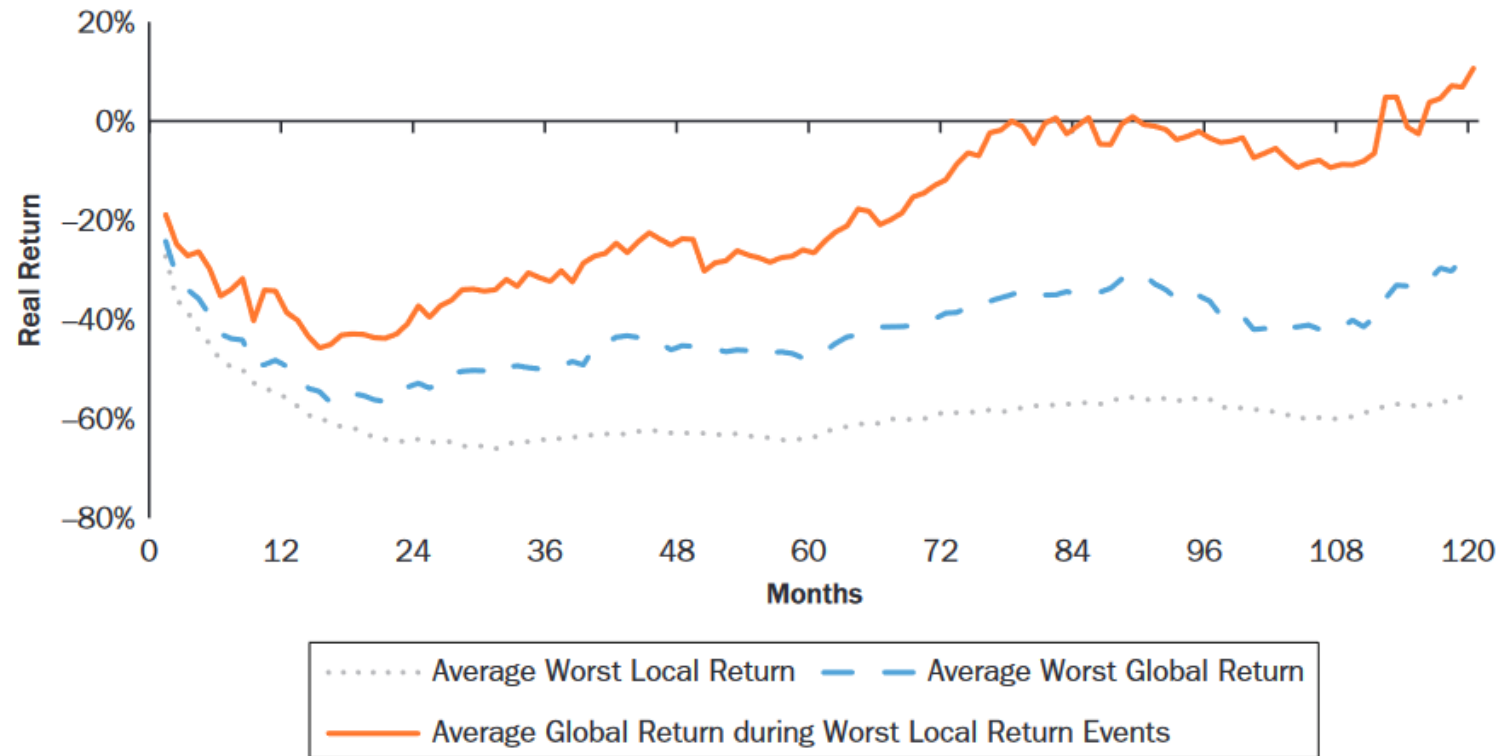
Don't Vote. Weigh.

5

Weighing Machines: Common Sense, Repeatable, Reliable

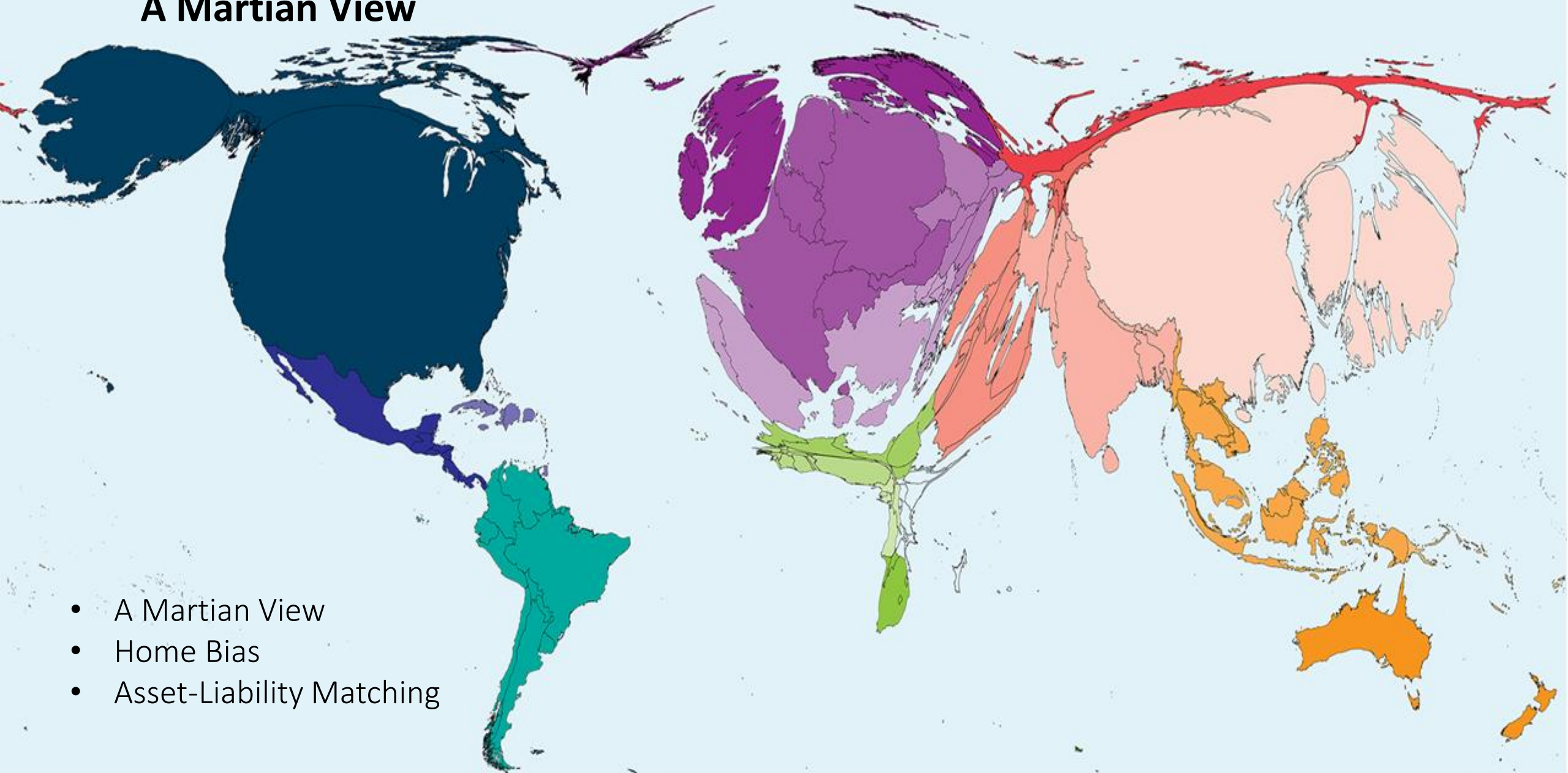
EXHIBIT 1

Average Worst Returns over Various Horizons for Local and Global Portfolios, January 1950–December 2022



- Basic theory and common sense
- Things don't crash together
- Changes in valuations can lead to the wrong conclusions
- International diversification is especially useful for active investors.

A Martian View



- A Martian View
- Home Bias
- Asset-Liability Matching



Thank You

savillea @ AdrianSaville