JW S04E02 Robin Powell

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SPEAKERS

Robin Powell, Pat Bolland

Pat Bolland 00:15

Our next guest is an internationally renowned guy that deals in investing in finance. He's the founder, as well as the editor of the evidence based investor. Robin Powell joins us ... Robert, a real pleasure to meet you.

Robin Powell 00:57

And you, sir, thank you for having me. Yeah,

Pat Bolland 00:59

I read with interest, the Evidence Based Investor blog, if you will, but you say that the focus of the Evidence Based Investor is education, and that some of the principles that go behind investing, go back to the 1950s or so. And they're in the academic domain? Why are they not in the public? And what are some of the tenants of Evidence Based Investing and that style of investing?

Robin Powell 01:27

Well, that's right. I mean, when I when I started looking into this whole subject about 12 years ago, now, I mean, just just just my background very briefly, I'm, I'm a kind of general news reporter, if you like, with no particular expertise in investing at all. And about 12 years ago, I made a documentary about investing. And I was asked to do it by a wealth management firm here in the UK, who use predominantly passive or broadly passive funds. And I was quite skeptical about passive investing. But I looked into it, and it traveled to North America and various other places, to interview experts and so on. I was bowled over by the fact there is all this evidence out there academic evidence, peer reviewed, independent time tested evidence about how to invest. And yet we almost have a whole industry, if you like, financial industry that is almost designed to, to get us to do the very opposite of what the academics say we should be doing. And so the academic evidence, as you say, largely dates back to the 1950s. And particularly with the advent of, of, of computers. And just very, very broadly, it says simply diversify. Diversification is very good, not just to reducing risk, but it's also good for improving long term returns. And we also know that costs make a huge, huge difference in investing, so it really pays to keep your costs down. And those two things, you know, diversifying and keeping the cost down, there's one product that does that better than any other, and that's the index fund. And index funds are a great, great way to invest. And the other I suppose, main lesson from academic finance is that behavior is really, really important. You know, you can have an evidence based investment portfolio, but if you can't manage your, your own emotions, and your own behavioral biases, biases, you can come badly unstuck.

Pat Bolland 03:52
We could spend a whole time on behavioral finance, but I do want to kind of explore this whole concept of passive investing and indices because passive investing is just buying a whole bunch of stocks as opposed to stock picking, individual stock picking and yet if you look at social media, it's all about stock picking, buy XYZ moves past your mind's and all the other stuff that goes on. Are you ,,, do like stock picking?

Robin Powell 04:19
Um, look, I mean, people are welcome to you know, spend time, effort, money, energy on whatever they want to, but it's not a useful activity. It's certainly not a lucrative activity. Yes, you know, by the law of averages, you're going to, you know, strike lucky occasionally, but on the whole, you can expect to underperform the broader market. And there's one I suppose one main reason why and that is cost you know that every time you trade it, it cost you money. And also, you know, there's been research by a guy in America called Hendrik Besson binder, which shows that in the long run only around 4% It's a staggering statistic. A staggeringly small number 4% of stocks actually beat bonds, which are essentially a fairly safe investment government bonds anyway. Only 4% Beat bonds in the long term. So, you know, the vast majority of stocks, if you like, are duds. So picking the those very few winners, if you like the, the Amazons, the apples, the Googles, and so on, that really are going to drive the bulk of market returns. We all know what those hugely successful companies are, with the benefit of hindsight, the key is to identify them before they start outperforming and the evidence shows again, and again, that active stock pickers, whether just ordinary retail investors, or the professionals, frankly, they just cannot do it with any consistency. Wow.

Pat Bolland 06:16
The Evidence Based Investor does give seven, I saw an article there that talks about the seven steps for successful investing. They're fascinating. The first one that popped up, interestingly, was humility, humility. So let's walk through the seven steps starting with humility.

Robin Powell 06:33
Well, I'm a big fan of Warren Buffett, and, and if anyone knows anything about Warren Buffett, it's that he's a very, very successful investor. And he's also actually an active investor. You know, he, he, over the years has, has bought into and bought whole companies. And he's been very, very successful at it, he's been much less successful, he must be said, at actually beating the market, since the global financial crisis of 2008. Nine. And what Warren Buffett says is, look, the vast majority of investors ought to be just simply investing in the whole market, and not trying to sort of jump in and out of the market trying to be clever, they should just stay in the market, if you like. And his big thing is humility, you know, and particularly staying within your sphere of competence, as he calls it. So when you trade stocks,

what people underestimate is that they are taking on the combined wisdom of around 10 million traders all around the world. And that is really, really hard. So do you, you know, sitting at home in Toronto, or here in the UK, or whatever? Do you as an individual know more than all those investors combined? Surely not? Surely not. So it pays to be humbled. That's the first one. The second rule I touched on earlier diversification, is a guy called Harry Markowitz, sadly, died last year. But he was a winner of the Nobel Prize in economics. And he demonstrated how having a diversified portfolio reduces your risk and improves your returns in the long run. The other thing again, which I've mentioned is paying less. It might seem quite a boring issue, fees and charges compared with you know, fund performance and so on. The industry, the fund industry likes to talk about performance, it doesn't like to talk about costs. And the reason why is that actively managed funds are expensive, they're expensive in terms of the fees they charge, but also when the fund manager trade stocks, you know, you have to pay a range of expenses every time they trade, so, so pay less and over the long term, compounded over many years, that makes a big difference. The next rule is to automate. You know, we're not great investors, human beings, you know, we are prone to all sorts of behavioral biases and we we just aren't very good at making rational decisions. So the thing to do is to take yourself out of the process, if you like and just automate things as much as possible, you know, just just invest the same amount on the same day, every month. That's the easiest way to do it. You've got to consider taxes, like costs, they really can erode your your eventual returns. though, you know, your rules in Canada will differ from from those here in the United States and so on. But wherever you are in the world, you need to be looking at the tax situation. And the sixth one is to ignore forecasts, you know, we, as human beings love to predict the future. And and it's, it's partly behavioral scientists have explained this, it's actually to do with our, our need for certainty or need to understand a very complex world if you like. But forecasting the future, you know, all the experts say that, it's very, very hard to do. And forecasting the economy is very difficult, forecasting events of elections and so on, is very difficult. And then even if you can correctly forecast those things, you've then got to forecast the impact of those events on the markets. And that's even harder. And then the seventh and final rule for successful investing, if you like, it is is the simplest one, but in many ways, the hardest one to actually do. And that's just to stay invested, you know, don't run for the hills when markets suddenly fall. By the same token don't get overexcited when markets are going up and up, and you think they will carry on going up and up and up forever, they won't, and nor will they carry on going down forever. Just stay rational, stay calm, stay invested.

Pat Bolland 11:39
I was looking at some of the returns over a longer period of time, talk about staying in, like the returns can be on average 11-12%. It's phenomenal returns by just staying in. You also talk about a balance. This is another article at the Evidence Based Investor, you talk about a balanced portfolio, I assume that that means stocks and bonds. Is that correct? Number one, and number two, how do you put that together?

Robin Powell 12:08
Well, that's right. I mean, stocks and bonds really are the the two main asset classes that people should be investing in. And it's really quite simple, you should think about investing as taking a stake in global capitalism. And if you think about that, human beings are amazingly resilient. I mean, just look at the last century, for example, what we went through together two world wars, you know, nearly a third world war, you know, the rise of global terror, and, and, and so on. And it was kind of one crisis after another

stock market crashes, economic recessions, terrible recessions, particularly in America in the 1930s. But the market went up and up. Gradually, okay, yes, it went down at times, but on the whole, it went up. So when you're investing in stocks, you're investing, if you're like, in that hue, human resilience, that bounce back ability, I mean, and no one's actually showed that better than that Japan and Germany, of course, who, you know, lost in, in, in the, in the wars. So that's what you're investing in. So you're either buying stakes in companies by owning shares, or you're lending to those companies or to governments in the form of bonds. And those are the two main building blocks, if you like, of every, every portfolio. Now there are other asset classes that you might want to consider. I mean, one is commercial property. And we've seen, haven't we how commercial property has really suffered all around the world. And actually, I was reading the other day, it's very much happened in Canada too. But, you know, when things go down, very often they go up and get well, they almost invariably do go up again. So who knows, maybe maybe commercial property, it's actually a good time to maybe own a little bit of commercial property as well. I would steer clear of of things like private equity and hedge funds. Venture capital, largely because they are expensive. They lack transparency. And frankly, if you're in stocks and bonds, you really, really don't need them. And very finally, you know, a balanced portfolio is all about, as you say, stocks and bonds, but it's also about getting a geographical balance. In terms of stocks, you should have a balance between different sectors. Yeah, it's just having a little bit of a stake in in every I think

Pat Bolland 15:01
I want to finish our discussion talking about risk, because everybody talks about risk. But how do you actually measure it or or find it a level that you're comfortable with yourself?

Robin Powell 15:14
Now, this is a really, really important question. And so many investors just kind of launch into investing without really properly thinking about it, there are three main considerations. First of all, do you actually need to take risk at all, you know, maybe you're comfortably well off and you have enough money, you've done a cash flow modeling, and your financial advisor has assured you that you've got enough comfortably to last you for the rest of your life, very minor cost that a lot of us are living, you know, much longer now. So do you actually need to take a risk. And it might be actually that you need to take quite a lot of risk. So for example, you may have left investing far too late, you may not have invested anything in your pension until you're sort of mid 40s, or whatever, in which case, you really do need to take more of a risk in terms of buying more equities, more shares, if you like, going forward. The second question is, can I afford to take it, you know, markets can go down sharply, you know, they can go down 2030 40% even more. And, you know, if you're heavily invested in equities, and say, I don't know, you're, you're in your 70s or whatever, or, you know, you've got major financial responsibilities, you know, can you actually afford to lose that kind of money, even if, you know, just kind of fur for a few years or whatever. So that's the second thing. And the third thing is, what sort of risk do you feel comfortable taking, you know, and this really boils down to are you a half glass empty or a half glass full person, I'll be honest, I've changed my tune a little bit on this personally, I always from a, from an investing standpoint, used to be a half glass, empty person, I used to be very, very cautious. I've got my fingers burnt once or twice with sort of market falls and so on. But actually, the more I've kind of learned about investing and read about it and read market history, the more I realized, actually that if you are genuinely in it for the very long term, like you should be, then you know, try to see the half glass full.

And and stay invested take us as much risk as you reasonably can and your you know, comfortable taking, and just just stay with it and ride out the volatility. It'll pay off in the end.

Pat Bolland 17:55
Robin, very wise words. Thank you.

Robin Powell 17:58
Thank you.

Pat Bolland 18:00
Robin Powell is the founder and editor of Evidence Based Investor.