

Long-Term Investing Amid an Uncertain Future

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When I was a teenager a family connection lead me to spend a good deal of time in the courts. Eventually I came to work there in the school holidays, working as a solicitor's clerk, sitting behind the barristers, supposedly to "take a note" but none of my notes were ever consulted. The barrister was not supposed to talk to the client without a solicitor's clerk present and I was the cheapest form of chaperone. So I spent many days sitting through criminal trials with nothing else to do but pay attention to the evidence, the process and the many interesting parties - the police, judges, juries and criminals - brought to that place. Trials would last for days or weeks but they were always fascinating. As the case neared its conclusion, with prosecuting and defence barristers making their closing arguments, the judge summing up and the jury sent into cloister there was a rising tension in the room. Everyone would hang around until the usher hurried in to announce that the jury had reached their verdict. Then, like in the last scene of an Agatha Christie novel, everyone reassembled to hear if the defendant had dunnit.

The tension is all in that moment. What would it be, freedom or ten years in jail? My mind would race through the evidence and the arguments, trying to guess what the jury would decide. Both barristers had made good cases. There was always some doubt. So the verdict, when it came, always seemed arbitrary. Worse, if it was guilty, the judge always sounded so certain in the homily that accompanied the sentence. *You are a bad man, you have done a wicked thing.* How could they be so sure when a moment ago no one knew anything? That was the whole point of the proceedings, of course, to sound certain, to give finality. We were there precisely to decide guilt and any uncertainty that remained undermined the system.

The law, sports, and history itself, are all lived forward and only understood backwards, at the end. Stocks, too. Every thesis, every analysis rendered redundant by the facts. But this is a perfectly useless philosophy in practice and it deserves to be reversed: life may be reviewed as a whole backwards but can only be experienced forward. Stocks will ultimately be accounted on sale but can only be assessed on purchase.

It is what it is: we shall be judged by our fruits but we cannot know them until it is too late. So we reach for what is available, heuristics, rules of thumb, annual reports, broker research, ratios. This stock is trading at a multiple of 15 but the sector is at 20, so maybe it will catch up. This stock has insider sales so we sell. All of these techniques are, in our opinion, ways to avoid the most difficult task an investor must undertake: to predict the future.

We make estimates, provisions, calculate intrinsic value and design elaborate models; but what you most need to know is whether you are moving in the right direction. How? Here is a good exercise: For a given company you follow, close your eyes and imagine what it will look like in ten years' time. If the answer is "no idea" you probably don't know the company well enough to invest in it. If the answer is "much the same as today", all of the value will be in the price. You might pay a P/E of five because you believe the right number is ten, so gains will be on revaluation and any growth in the company itself is incidental. And if the answer is "I don't know but it will be certainly be a lot more profitable", then the math may be trickier

but your price will not be geared to what other people think but to that profitable future. This is where most gains are made in stock investing.

A neurologist will tell you that the brain is a machine for making predictions. All sensory data is compared not just to memories but to our working model of what we believe will happen next.

Investing, if it is to be done well, does not depend on only looking backwards but harnesses that brain power and develops our gift for looking into the unknown and making it knowable.

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