

Sell warriors; buy wizards

“You think the odds look right, that they are in your favour ?

This is a billiard table. An easy, flat, green billiard table. And you have hit your white ball and it is travelling easily and quietly towards the red. The pocket is alongside. Fatally, inevitably, you are going to hit the red and the red is going into that pocket. It is the law of the billiard table, the law of the billiard room.

But outside the orbit of these things, a jet pilot has fainted and his plane is diving straight at that billiard room, or a gas main is about to explode, or lightning is about to strike.

And the building collapses on top of you and on top of the billiard table. Then what has happened to that white ball that could not miss the red ball, and to the red ball that could not miss the pocket ? The white ball could not miss according to the laws of the billiard table. But the laws of the billiard table are not the only laws in this particular game.”

- Extract from the novel ‘From Russia with Love’, by Ian Fleming.

Whether in the form of Ian Fleming’s James Bond or John le Carré’s George Smiley, spies are big business. Without Bond as *ur-Spy* we might never have had Smiley. But they are hardly comparable. Bond is a glamorous, libidinous, fast assassin equipped with deadly toys. Smiley is quiet, unathletic and conscientious, methodical, perceptive and wise. Where Bond is fascistic, the supreme embodiment of belief in the superiority of action over thought, Smiley is contemplative. Where Bond is a warrior, Smiley is a wizard.

Do these characteristics hold in fund managers ? The active management of assets requires at least two things: the promise, or at least the potential, of generating superior returns (wizardry ?); and the ability to win over those assets in the first place (warriorship ?). As the more successful fund managers morph, by dint of increasing size of AUM, into asset gatherers, the management of reputation really starts to matter. In this regard, as with politicians, most fund managers’ careers end in failure. Warriors overreach. Anthony Bolton decided to come out of retirement having managed British equities well over a long period – and to invest in China, of all places. Peter Lynch was shrewd enough to leave Fidelity’s Magellan fund having shepherded growth in assets from \$18 million to \$14 billion. Most managers are not so adept at market timing. The jury is out over Neil Woodford’s future performance having left Invesco Perpetual in 2014 to set up a variety of new funds under his own brand, but the profits warnings or negative corporate developments that have recently overshadowed three of the largest investments in his Equity Income Fund (from AstraZeneca, Imperial Brands and

Provident Financial) are unwelcome stones in his shoe. Perhaps it's industrial espionage. Ian Fleming writes that there's a saying in Chicago:

Once is happenstance. Twice is coincidence. The third time it's enemy action.

There is a fundamental tension at the heart of the asset management business, a dirty little secret that the industry would prefer to stay uncommunicated to its customers. **Growth in assets is highly correlated with diminishing returns.** Warren Buffett may be the only manager in the world to have transcended the \$100 billion asset barrier without tarnishing his long term reputation. Even then, Berkshire Hathaway's recent returns are modest by comparison to those of Buffett's salad days. [Ben Carlson](#) recently ran the numbers on Berkshire Hathaway by decade, and they are instructive. The bigger Berkshire has become, the smaller its margin of outperformance versus the market. And this from an investment vehicle which has been one of the most successful in the world.

	Berkshire Hathaway	S&P 500	Annual Outperformance
1960s	28.3%	5.0%	23.3%
1970s	22.2%	5.9%	16.3%
1980s	39.1%	17.3%	21.7%
1990s	20.5%	18.0%	2.5%
2000s	5.9%	-1.0%	6.8%
2010s	17.9%	15.3%	2.6%

Nor has Buffett ever denied this. Size, as he has publicly remarked, is an anchor to performance.

So the fund management industry (and it is an industry) is ultimately peddling a colossal lie. The largest asset gathering machines tout their AUM like some kind of virility symbol, when it is more likely to betoken inevitable underperformance versus smaller, nimbler rivals. Well, those who live by the sword get to die by the sword.

But there's also a tension at the other end of this battlefield. We only want to invest with like-minded boutique managers willing to limit capacity in **their** funds in order to concentrate purely on performance. Given that the noise from well-funded asset gathering machines tends to drown out the marketing signals sent out by smaller but more disciplined asset managers, how do we get to hear from the latter ? The answer, perversely, given the sophistication and proliferation of digital media, lies in good old-fashioned word of mouth.

There's another answer, too. How do **we** hope to attract clients, given that we never intend to advertise at all, at least in the conventional sense ? One way is clearly to focus on investment returns above all else, and to partner only with the like-minded. Another is to adopt the approach that Albert Jay Nock discusses in his essay [Isaiah's Job](#). This is a long read, but it well repays the effort. An extract:

In the year of Uzziah's death, the Lord commissioned the prophet to go out and warn the people of the wrath to come. "Tell them what a worthless lot they are." He said, "Tell them what is wrong, and why and what is going to happen unless they have a change of heart and straighten up. Don't mince matters. Make it clear that they are positively down to their last chance. Give it to them good and strong and keep on giving it to them. I suppose perhaps I ought to tell you," He added, "that it won't do any good. The official class and their intelligentsia will turn up their noses at you and the masses will not even listen. They will all keep on in their own ways until they carry everything down to destruction, and you will probably be lucky if you get out with your life."

Isaiah had been very willing to take on the job — in fact, he had asked for it — but the prospect put a new face on the situation. It raised the obvious question: Why, if all that were so — if the enterprise were to be a failure from the start — was there any sense in starting it? "Ah," the Lord said, "you do not get the point. There is a Remnant there that you know nothing about. They are obscure, unorganized, inarticulate, each one rubbing along as best he can. They need to be encouraged and braced up because when everything has gone completely to the dogs, they are the ones who will come back and build up a new society; and meanwhile, your preaching will reassure them and keep them hanging on. Your job is to take care of the Remnant, so be off now and set about it..

Isaiah.. preached to the masses only in the sense that he preached publicly. Anyone who liked might listen; anyone who liked might pass by. He knew that the Remnant would listen; and knowing also that nothing was to be expected of the masses under any circumstances, he made no specific appeal to them, did not accommodate his message to their measure in any way, and did not care two straws whether they heeded it or not. As a modern publisher might put it, he was not worrying about circulation or about advertising. Hence, with all such obsessions quite out of the way, he was in a position to do his level best, without fear or favour, and answerable only to his august Boss.

If a prophet were not too particular about making money out of his mission or getting a dubious sort of notoriety out of it, the foregoing considerations would lead one to say that serving the Remnant looks like a good job. An assignment that you can really put your back into, and do your best without thinking about results, is a real job; whereas serving the masses is at best only half a job, considering the inexorable conditions that the masses impose upon their servants. They ask you to give them what they want, they insist upon it, and will take nothing else; and following their whims, their irrational changes of fancy, their hot and cold fits, is a tedious business, to say nothing of the fact that what they want at any time makes very little call on one's resources of prophesy. The Remnant, on the other hand, want only the best you have, whatever that may be. Give them that, and they are satisfied; you have nothing more to worry about. The prophet of the American masses must aim consciously at the lowest common denominator of intellect, taste, and character among 120,000,000 people; and this is a distressing task. The prophet of the Remnant, on the contrary, is in the enviable position of Papa Haydn in the household of Prince Esterhazy. All Haydn had to do was keep forking out the very best music he knew how to produce, knowing it would be understood and appreciated by those for whom he produced it, and caring not a button what anyone else thought of it — and that makes a good job..

We all know innumerable politicians, journalists, dramatists, novelists and the like, who have done extremely well by themselves in these ways. Taking care of the Remnant, on the contrary, holds little promise of any such rewards. A prophet of the Remnant will not grow purple proud on the financial returns from his work, nor is it likely that he will get any great renown out of it. Isaiah's case was exceptional to this second rule, and there are others, but not many.

It may be thought, then, that while taking care of the Remnant is no doubt a good job, it is not an especially interesting job because it is as a rule so poorly paid. I have my doubts about this. There are other compensations to be got out of a job besides money and notoriety, and some of them seem substantial enough to be attractive. Many jobs which do not pay well are yet profoundly interesting, as, for instance, the job of research student in the sciences is said to be; and the job of looking after the Remnant seems to me, as I have surveyed it for many years from my seat in the grandstand, to be as interesting as any that can be found in the world.

The beauty of the worldwide web and of social media (we favour Twitter over Facebook, which we no longer use) is that they have the potential to facilitate all sorts of serendipitous exchanges between like-minded people. We can use them to share our own thoughts about asset management, about valuation opportunities in otherwise overbought markets, and compare notes with managers of a similar hue. And if we can manage to attract the attention of one or two members of the Remnant into the bargain, well, as Nock says, the job of looking after the Remnant seems.. as interesting as any that can be found in the world.

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