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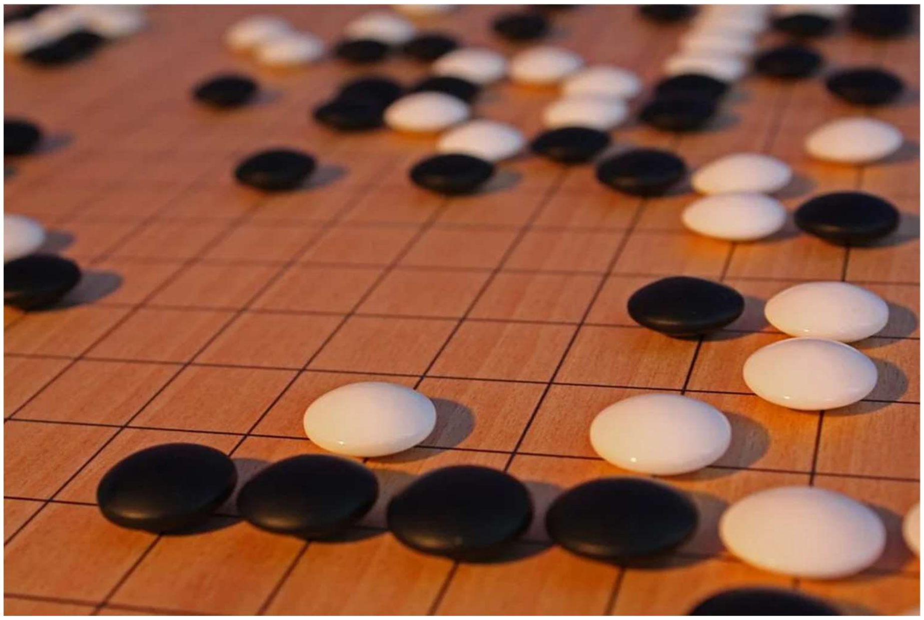
Rosefinch Research | 2022 Series # 17

Investing and the Game of Go



As Shanghai people return to their office, their desk calendars are still showing the March date when the city-wide lockdown was suddenly announced. It was as if we had skipped a whole Spring season… A-shares meanwhile has also stepped over Spring and gone straight from cold winter to the hot summer. The market sentiment had been in a deep quagmire as black swans came in droves: sticky pandemic, Real Estate Debts, Russia-Ukraine bombs, Fed hikes… The turning point came quietly in late April, with Chi-Next leading the way with a 20% rebound. The New Energy index rose nearly 40%, with some stocks up even as high as 70%. With the upward trend materializing, the hot topic of "where is the bottom" has been quickly replaced by "will Chi-Next repeat its massive 2012 bull run?"

It almost feels like we are heading straight from ICU to the block party. Sounds familiar? **Benjamin Graham once said: Mister Market is a schizophrenic in the short term but regains his sanity in the long term.** When the market is depressed, all he sees is stress, so he will give lower prices and hope you can take away his troubles; when the market is happy, all he sees is profits, so he will mark higher prices for the same securities. The young A-share market is a typical example of such behavior: there's rarely a gradual long bull market, but mostly a fast and furious bull markets. The return on equity investment comes from profit and revaluations. In the last few rounds of bull markets in A-shares, revaluation had far more impact than the actual company profit growth. Valuation changes reflect market's sentiment shifts, and will swing like the pendulum between greed and fear.

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During the Vietnam war, Navy Admiral Stockdale was captured along others. He was a POW for 8 long years, suffering over 20 interrogations. By the time he was released, many of his cellmates have died while in captivity. As one of the few survivors, he was asked two questions: "why did others die? And how did you survive the tough 8 years?" Admiral Stockdale replied: "The optimists. Oh, they were the ones who said, 'We're going to be out by Christmas.' And Christmas would come, and Christmas would go. Then they'd say, 'We're going to be out by Easter.' And Easter would come, and Easter would go. And then Thanksgiving, and then it would be Christmas again. And they died of a broken heart." **Admiral Stockdale explained: "You must never confuse faith that you will prevail in the end — which you can never afford to lose — with the discipline to confront the most brutal facts of your current reality, whatever they might be."**

Optimism is a key ingredient for investment, but blind optimism can be deadly. Charles Munger has said: investment is not supposed to be easy. Anyone who finds it easy is stupid. Cautious and optimistic are opposite attributes that often show up together in investment gurus. They believe economy will grow up like a spiral; they believe there is a market trend; they believe entrepreneur spirit can lead the way. At the same time, they know human nature well, respect the market rhythms and cycles, build optimism on rationale, and wait for the mispricing opportunities by those deep in the "greed and fear" emotions.

In Warren Buffett's desk, there's a poster of American baseball legend Ted Williams. Ted played for the Boston Red Sox and was often cited as the Best Hitter in the history of baseball. There are two types of hitters in baseball: one will hit whatever pitch that comes and swing for the fence; the other will only hit what they deem to be high-percentage shots. Ted was the later. He divided the strike zone into 77 smaller areas, each the size of a baseball. **Ted Williams would only swing if the pitch comes in his ideal zones, so he can maintain a high RBI. To date, he's the last baseball player to hit over 0.400 in a season, in 1941.** During the game, even as the balls zoom by outside his target zones, Ted will not swing. He once said: true ball-strike only starts when you know which balls not to hit. Buffett said: what's nice about investing is you don't have to swing at pitches. In the 1998 Berkshire Hathaway shareholder meeting, one investor questioned Buffett's investment: the investor bought Berkshire stocks and had a so-so return, but he made a ton when he bought some high-tech shares. He asked Buffett to invest some funds in high-tech shares. In 1999, a Times front page had the title: "What's Wrong Warren?" That year, Buffett's heavy consumer and insurance holdings again lagged the high-tech stocks. As the internet bubbled busted, Buffett and Munger took it in stride. Munger concluded in the 2002 shareholder meeting: Investor should develop habit of not worried about holding stocks. If you focus on market price of the company, that means you believe market knows more than you about the company; but if you focus on the company's value, then you can sleep well at night. Buffett added that: investment is not an intelligence test, so someone with a 160 IQ may not beat someone with a 130 IQ. If you want to be a successful investor, you don't need to have the IQ of a genius, nor extraordinary business sense or inside information. **What you really need is a healthy and comprehensive investment framework, and prevent your emotion from damaging the framework.**

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If we paraphrase this into playing philosophy of Go, it's: don't go for the extraordinary, do what you know well, and improve the sub-standard areas. It's of course great to have an extraordinary master stroke, but these are few and far in between. What you do well is within your capabilities and reinforced through years of practice and training. Only when you achieve expert status in what you do, can you start to have moments of extraordinary genius. Otherwise, you will just end up making more silly mistakes. Worse yet, when you constantly chase for the extraordinary moves, you may get lost in the chase and end up losing the game over the ill-conceived move. **Go prodigy Lee Chang-ho was world champion at age of 16. When asked about his secret of success, Lee said: I never play for the extraordinary move, I just play each move at 51% success rate rather than beating the opponent in one move.** Most commentators would agree: Lee Chang-ho's style is consistently building small advantages that eventually lead to a landslide victory.

Those who win the Go match may not have any extraordinary move in the whole game. **Market is like playing Go: what's important is not winning or losing a single piece, but having a long game with strategic vision.**

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