



## TALEB IS COMING TO TOWN

My ticket is booked and the excitement is building because Taleb is coming to town! Yes, world famous author, Nassim Nicholas Taleb is coming to Kilkenny to speak at this years “Kilkenomics” festival. The date for this extravaganza is Nov. 7<sup>th</sup>, the place is St. Canice’s Cathedral and luckily the Rugby World Cup final is the week before!

I first mentioned Taleb exactly one year ago (Opinion piece 91) when I wrote about reading his book “The Black Swan”. Since then I have also read “Fooled by Randomness” and his writing impressed me so much that I even referred to him in my last opinion piece when I wrote about the banking inquiry.

I have also enjoyed watching him on YouTube and for anyone unable to make it to Kilkenny I think it is well worth watching him. (One of my favourites You Tube videos has David Cameron asking him questions, it can be found at: <https://www.youtube.com/watch?v=QQAVDg4yqUU>)

I hope I get the chance to read his other book “Anti-Fragile” before November because I guess that an understanding of this concept will be useful on the night.

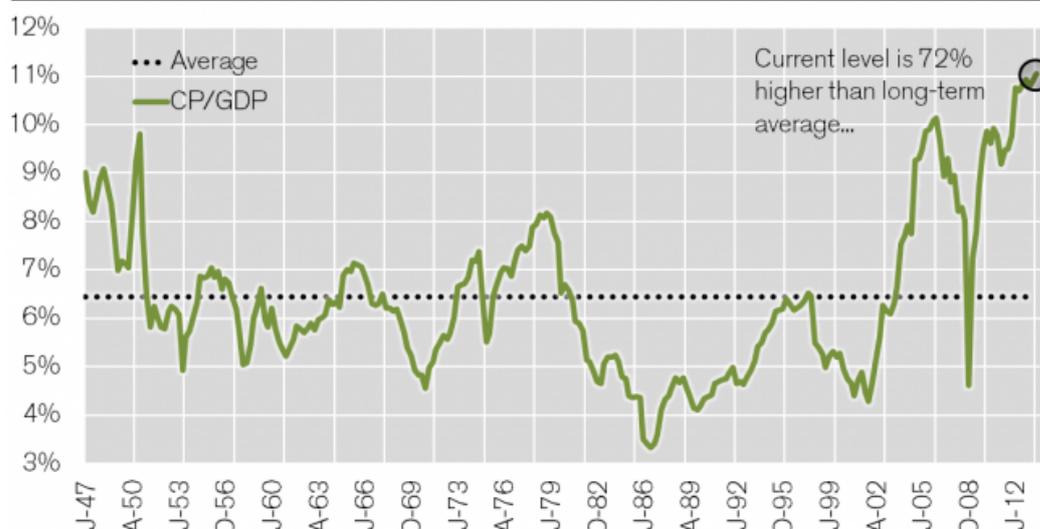
I’m not sure what subject matter will be covered in his Kilkenomics appearance but I do hope at some stage his concept of “Extremistan” and “Mediocristan” come up in the discussion. (For anyone unfamiliar with “Extremistan and “Mediocristan, they will have to read the description at the following link in order to appreciate the rest of this opinion piece: <http://www.wou.edu/~shawd/mediocristan--extremistan.html>) I am particularly interested in his thoughts on “Extremistan” and “Mediocristan” because I believe they have relevance for our understanding of world stock markets. In particular I think it is quite possible that valuations are being influenced by companies that are scalable (Extremistan) as opposed to companies that are not scalable (Mediocristan). In The Black Swan he states the following: *“globalisation has allowed the United States to specialise in the creative aspects of things, the production of concepts and ideas, that is, the scalable part of the products and increasingly by exporting jobs, separate the less scalable components and assign them to those happy to be paid by the hour. There is more money in designing a shoe than in actually making it: Nike, Dell and Boeing can get paid for just thinking, organizing, and leveraging their know-how and ideas while subcontracted factories in developing countries do the grunt work and engineers in cultured and mathematical states do the non-creative technical grind. The American economy has leveraged itself heavily on the idea generation, which explains why losing manufacturing jobs can be coupled with a rising standard of living. Clearly the drawback of a world economy*

where the payoff goes to ideas is higher inequality among the idea generators together with a greater role for opportunity and luck”

I think this is important because I think he is highlighting that America with companies like Nike (or Apple, Google, Facebook etc.) is “Extremistan” whereas a country like Japan where Toyota is the largest company is an example of a country that is remaining in “Mediocristan”.

If America is increasingly becoming “Extremistan” I wonder whether this might go some of the way to help explain why American profit margins are at all-time highs. The chart below illustrates this situation.

### Corporate Profits As % Of GDP

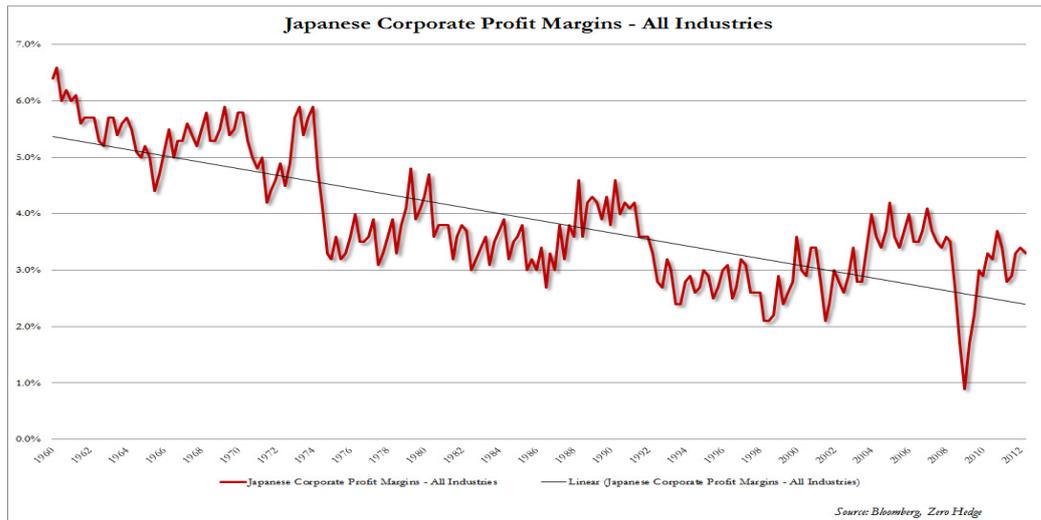


Source: Federal Reserve Economic Database & Season Investments, LLC

In simplistic terms there are some people that believe these record profit margins are not sustainable and this makes the overall market expensive whereas if these profit margins are sustainable one might be able to argue that the market is not expensive.

I think Taleb is suggesting that a country that goes from “Mediocristan” to “Extremistan” might very well see a sustainable increase in profit margins. I believe America has done just that because when I first started as a trainee fund manager back in 1986 we still talked about Inland Steel, Bethlehem Steel, GE and Exxon whereas in 2015 those companies are far less important.

I’m writing this in the week where the bankruptcy of Daichi Chuo Kisen (a Japanese shipping line) made headlines in Japan whereas I don’t think America even has any shipping lines that would make headlines. This highlights the extent to which Japan remains in “Mediocristan” with low profit margins.



As much as I admire “Extremistan America” and worry about “Mediocristan Japan”, I would not like to give the impression that this automatically means that I am recommending investing in American companies. As a value investor I still intend to stick with the core elements of a value philosophy. In other words I am unlikely to invest in a company like Apple because I worry that the franchise it has built might not last very long and therefore I feel it is outside of my circle of competence. It is important however that I try to think about how my investments might be threatened by companies that do come from an “Extremistan” world. The world of media is a good example of an industry that has been transformed by the emergence of companies like Facebook. It is not that long ago that I would have considered newspapers as a potentially interesting investment but I was wrong.

In conclusion I just want to reiterate my original point of how much I am looking forward to seeing Taleb because I think he is one of the most influential commentators of our day and I hope his talk will introduce more people to the worlds of Extremistan and Mediocristan.

## **BANKING INQUIRY**

I have watched recordings of a number of witnesses at the banking inquiry and I have tried in particular to watch witnesses that were connected to Anglo Irish Bank. There are many things that I could comment on and I might decide to do just that in a later opinion piece but for the time being I am just going to comment on one particular quote. The quote comes from Fintan Drury a former director of Anglo and it goes as follows

*“there wasn’t an analyst, there wasn’t a fund, there wasn’t any form of commentator who was, on a consistent basis, saying, “There’s a problem with Anglo Irish Bank.”*

I have highlighted this quote because I would regard myself as one of the analysts at one of the funds (when I worked in Setanta) that was trying to understand Anglo and in hindsight I feel that I was misled. I was consistently told by Anglo that they were a low risk lender that would only lend to a property developer once they had an anchor tenant committed to a lease (Marks & Spencer being the example that they used). Based on the information I was given there was no way I could have said "There's a problem with Anglo Irish Bank" so I feel Fintan Drury is trying to save his own reputation because he should have been one of the first to say that "there's a problem with Anglo Irish Bank".