Analysis

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The Long Game

Key take-aways

- Being successful in investing over time is about ensuring a win on those points that really matter and stepping up when the odds of losing are small compared to the odds of winning. It also requires mental fortitude when the market is panicked.
- Investing is also about risk control: not risking too much on a single trade, or betting on a single outcome, such that an error could permanently nullify you from the game. This requires a superior risk framework gleaned from history, analysis and M&G Investments has long prioritised the key components of risk consciousness, anchored valuations, and a team-based approach.

I have always enjoyed games, and anecdotally observe that many of my colleagues share the same fondness. The sentiment is widespread in the investment management community; Warren Buffett and Charlie Munger are keen Bridge players, while several hedge fund managers have made an appearance at the World Series of Poker. Perhaps that's a peculiarity of competitive personalities, but given their popularity, I think most people enjoy playing games of some variety, even if for no other reason than a bit of fun.

Games provide a controlled environment convenient for experimenting: with strategy, tactics and simulating different plays. More technically, competitive games are interactions humans have with other humans that involve a strategic element; meaning my decisions are contingent on your decisions and your decisions are contingent on my decisions. Consciously or not, we are all playing games all the time.

There are many iterations of games: opponent games, multi-player games, finite games, infinite games, etc… but for purposes of this article let us draw a distinction between games where there is a single play against a clear opponent (a tennis match) versus the long game of navigating a bunch of smaller games that make it up. If a single tennis match is an example of the single-play game, then managing a successful tennis career as a professional sportsman would be the long game. Quick-witted readers might rightfully point out that the long game is simply the sum of individual single-play games over time. And yes, that is technically accurate, but the way one would "play" to win a given match could be different (sometimes vastly so) to the way one would play if you were optimising for the best overall outcome over the span of a career. To illustrate the point, a professional tennis player with a wonky knee would make a very different decision if a shot could compromise his game for the season vis-à-vis a casual player who enjoys the Sunday match with the gang.

Statistics offers an edge in both short and long games

The popular board game Monopoly is a nice playground to observe outcomes across various strategies. As a kid, I remember being attracted to the high-profile properties of Jan Smuts Ave and

Eloff Street, owing to the high rents commanded by the navy boulevards. I'm sure many readers would welcome the nostalgia of recalling the moment when an opponent finally landed on your fully developed navy neighbourhood. But I also remember opponents often getting lucky around these expensive streets and not landing on them as much as I would have liked. The expensive properties would often bankrupt an opponent or two, but somehow it was not sufficient to beat all opponents. This was no coincidence.

Source: www.vice.com

The figure depicts the Monopoly board (left) alongside a heat-map (right) reflecting the frequency with which counters land on individual properties in a typical game. The more a property is landed on, the closer to red it is coloured on the heat-map. What is striking observing the heat-map is how clearly divided the board is (along the diagonal running bottom left to top right – from the "Jail" to the "Go to Jail" squares) between properties that are frequently landed on and those that aren't. As was hinted at, the expensive neighbourhoods (and the cheapest) are the least landed on properties on the board. The most landed on properties are the orange and red neighbourhoods because of where these streets are located relative to the "Jail" square.[1]

The single square most landed-upon in the game is Jail because there are so many ways to get there.[2] Jail then puts you one roll away from the orange streets and two rolls away from the red streets. Despite having an element of luck (by rolling the die), the trajectory around the board is simple statistics. Winning the game is more closely tied to securing the right real estate – orange and red streets – or if you can't do that, to prevent opponents from securing them. If you were to take up Monopoly competitively, you would not want to own the navy boulevards over the orange avenues. Statistics is enough to see you through to the top spot in most games.

But a successful long game requires more than statistics - Strategy is crucial

Robert James (Bobby) Fischer, the Eleventh World Chess Championship winner, had a remarkable career. Widely considered a chess prodigy, he was largely self-taught on his way to becoming a grand master and ultimately securing the championship. Fischer learned the game of chess at the age of six and played what some people dub the "game of the century" at the age of 13. He was a top-eight player by the age of 15.

[1]The most landed on property on the original South African board is Hoffman Square. A player is 1.6x more likely to land on Hoffman Square that they would be to land on Eloff Street over the course of a typical game.
[2]Two cards that send you there; roll doubles three times; and a Go to Jail square

Bobby Fischer is well known for a great number of accolades and personal peculiarities, but he is not as well known for the strategic intent with which he approached his chess career. Robert James Fischer played one of the greatest bait-and-switch long games in the history of the chess championships. How? He always played the same sort of game: regularly opening with the same move (pawn to king 4). He ran the same playbook for the 16 years he was on the public chess scene, until he played the most important match of his career: the 1972 World Chess Championship against then-defending champion, Boris Spassky of the Soviet Union.

After conceding the first two games of the match (actually forfeiting the second game by not arriving to play on the day), Fischer does something completely novel in the third game, surprising Spassky, who then reacts poorly. Fischer plays a move totally out of character and without precedent for the first time in his 16-year career, completely flipping his playbook on its head. All the study of Fischer's previous games in preparation for the match now largely moot, Spassky puts up a weak defence, ultimately conceding the Championship to Bobby Fischer.

Fischer's crushing defeat of Spassky might have played out over 21 games in 1972, but the strategy was 16 years in making and meticulously executed. Imagine the preparation that went into the study of his new strategy, and not revealing that in play until the fateful moment of the championship – that's the long game if ever there was one.

Investing is the long game

> "The less prudence with which others conduct their affairs, the greater the prudence with which we should conduct our own affairs."
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> — Warren Buffet

Optimising for the long game is about ensuring a win on those points that really matter. It is also about not letting an error permanently nullify you from the game – think a professional sportsman who risks a debilitating injury to make the point.

Investing is a long game, not risking too much on any individual trade such that if you are wrong, you're out of the game. It is also about capitalising on the moments that really matter and stepping up when opportunities are hugely asymmetrical and the odds in your favour. Having liquidity and the mental fortitude when the market is panicked can be a source of tremendous advantage. For this you will require a superior risk framework that is effective before the event that yields opportunity.

M&G Investments has long prioritised the key components of risk consciousness, anchored valuations, and a team-based approach. Over 25 years, these foundations have consistently helped us serve our clients well in the long game. □

Aadil joined M&G Investments in July 2013 as an Equity Analyst. In August 2018 he joined a global equity hedge fund in London, before returning to M&G Investments in January 2020 as Head of Equity Research. With 15 years' investment experience, Aadil's qualifications include a BCom degree (Hons, cum laude) from the University of Pretoria and a Masters in Finance degree from INSEAD. He is also a CFA charterholder.