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Challenging Conventional Wisdom

PROFESSIONAL FIGHTING AND INVESTMENTS

Having recently watched the much hyped cage-fighter, Conor McGregor, lose to a really average, heavier opponent. I was once again struck by the similarities between professional sport (in this instance, fighting) and investments. I believe the careers of Floyd Mayweather and McGregor can teach us a lot about investing hype, market commentators and how we should manage our investments.

Floyd Mayweather could be a Value Manager

For those of you who don't follow boxing, Floyd Mayweather retired recently as an undefeated boxer and has the distinction of being a champion in five different weight divisions. Of more relevance to readers of Moneyweb, his fights generated more than $1,300,000,000 in pay-per-view TV revenue. He was regularly ranked as the highest paid athlete in the world and has amassed a significant personal fortune. He was also widely criticised, especially in the latter parts of his career when he really started becoming commercially successful and economically powerful in the boxing world. His (winning) style of fighting was considered by his critics to be "ugly", boring, uncomfortable and not fun to watch. Mayweather had learned over his career how to fight in a particular style that was low risk, aimed at wearing his opponent down over time, and focussed on winning over 12 rounds. He had a legion of critics but when you analyse his results it is difficult to argue that he wasn't very effective.

Mayweather's career reminds me a lot of Value fund managers and the significant criticism they attract when they are going through a dry spell. As a method of managing money, Value is not for the fainthearted. You often have to buy investments that many "experts" would avoid. The Value sector is not made up of fun, flashy, fashionable and exciting companies. Mostly, companies that excite Value managers are boring, unloved and rarely popular. This means that people investing with Value managers very often have an uncomfortable journey for long periods of time but eventually the results speak for themselves. The best example of this journey is when Warren Buffett was lambasted by the "experts" during the Dot-Com boom when he avoided Internet businesses because he could not find value in their shares. Critics said he was a dinosaur, had lost his touch, should retire and did not understand the new world order. When the Dot-Com bubble burst, investors lost $5 trillion, many businesses collapsed completely. Needless to say, Buffett was proved correct as his ugly, unloved, boring companies continued to thrive and reward investors.

For the last 18 months, Value managers in South Africa have been on the receiving end of massive criticism from armchair critics and talking heads who don't actually manage large pools of money themselves. If we consider resources (mining) shares in South Africa as an example, many "experts" have been telling anyone who will listen that Value managers have been completely wrong to be in the sector when "anyone" could see that they were bad investments. Admittedly some Value managers have made significant losses that are unlikely to be recovered but good Value managers are starting to show great results for their investors again. As an example, according to Morningstar, over the 12 months ended 11 March, one of the top performing funds in SA is Investec Value with a return of more than 28%. Over the last three years, you would have earned more than 14% per year from this fund. Admittedly, there are funds that have returned more for investors over 3 years but watch this space, the Value story is not finished yet.

Conor McGregor – man of the moment but is he a long term proposition?

Conor McGregor, the world's most popular cage fighter and current world champ was defeated recently by a journeyman, Nate Diaz, who has won a few more fights than he has lost over his career. Diaz fights in the welterweight category, which is two categories higher than McGregor's customary category. The difference equates to more than 11kg, and in the fighting world this is significant, like a Labrador taking on a Great Dane. McGregor is popular because he is brash, flashy and glamorous. So how did he get beaten by Mr Average? There are a few reasons, Diaz knows his strengths, remained consistent, had a solid methodology to win the fight, had longer term focus to win the fight in the in the latter rounds and avoided unnecessary risks. McGregor, when faced with a heavier, stronger opponent realised that he did not have a gameplan suited to the big time. He was so arrogant that he felt he could jump two weight categories in one go without needing to learn how to adapt his strategy.

The McGregor story reminds me of investors chasing "the next big thing" when they find a new fund manager (especially in the hedge fund space) that has delivered a few good sets of results with smaller amounts of money. The fund manager wins a few awards, gets some glowing reviews in the media and is suddenly flooded with new money to manage. It is remarkable how many of these fund managers flounder like Conor McGregor. They do not give themselves the chance to learn and adapt their craft as they grow in size and eventually Mr Average starts to make them look foolish. In this instance Mr Average is the stock market index and it is remarkable how many times the index beats the "next big thing" over longer periods of time.

For investors, there are some lessons here: avoid hype and don't chase the current flavour of the month. If you are uncertain, don't be afraid of backing Mr Average. Buying the index is often your best strategy. Rather be consistent, use a solid methodology and maintain a long-term focus, in other words be happy to miss out on a few McGregors because you are planning to be a Mayweather and win over your entire investment career.