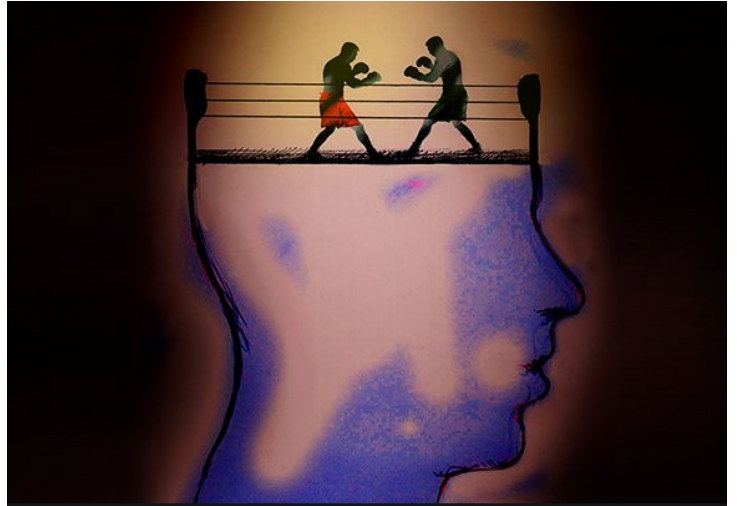




Binary thinking, What-Ifs and why it helps to disagree with yourself

"I feel I change my mind all the time. And I sort of feel that's your responsibility as a person, as a human being – to constantly be updating your positions on as many things as possible. And if you don't contradict yourself on a regular basis, then you're not thinking."

– Malcolm Gladwell



We live in a world of complex problems. Each day we need to make decisions which affect our lives and those of our clients and colleagues. We are also subject to the decisions of others – business leaders, governments, central banks and other role players in a global economy where singular decisions have far reaching implications.

Examples of these complex and divisive problems today include how a country manages their lockdown and re-opening of their economy, or how a central bank decides to manage its stimulus package to bail out companies and individuals. On a day to day basis we are also faced with complex problems around emigration, investing and financial planning. Within companies, the decisions to retrench staff or acquire competitors, and to make long term decisions in the face of huge uncertainty.

These topics and many others frame the question of how we deal with complex problems, and how we should develop a thought process to ensure we are making the best decisions.

The concept '*binary thinking*' relates to the idea that when faced with complex decisions as those illustrated above, we are prone to oversimplifying the problem to arrive at convenient answers. We do this to remove the anxiety such a complex problem might present for us.

This is false comfort. The trouble with this decision process is that we tend to place more emphasis on those facts we personally agree with and avoid the opposing facts which detract from our argument. This leads to conveniently simple, yet potentially misleading, 'yes or no' type decisions. For example: "*Should I take my money offshore now? Yes, I should, because this lockdown will kill our economy*". This is a current example that we are seeing quite often as anxieties are high. The convenience of using a single point of view to support a very important and complex decision excludes the wide spectrum of other pieces of information which should be considered at the same time:

- "*how cheap are South African assets and do they present a good opportunity, despite the lockdown. If I take my money offshore, I will miss this opportunity*"
- "*Is the Rand cheap? Am I taking money offshore at a bad time? Or is it the dollar which is expensive?*"
- "*Are global assets not overpriced? I would be selling low/buying high*"
- "*What is my ideal level of investment in South Africa relative to offshore and how does my current allocation compare?*"



This highlights some of the more practical questions we could use to test the decision we arrived at to start. However, there are also a second set of questions which relate to the numerous alternate outcomes which would be in direct conflict with your current view. These require more mental fortitude to consider properly. These are the 'what if' questions:

- "what if South Africa emerges from this lockdown in better shape than I expect, while the rest of the world struggles?"
- "what if it is proven over time, that the tough decisions our government is making today allow us to recover more quickly than other economies?"
- "what if global investors flock to SA assets because they offer an attractive yield?"

In doing this, you are taking the opposite side to your own argument and not just adding further testing to your existing argument. You are essentially disagreeing with yourself. This is a tough mental process to consider properly:

"But the test of a first-rate intelligence is the ability to hold two opposed ideas in mind at the same time, and still retain the ability to function or, in this case I'll say, the ability to invest. To invest well. To hold over time that which deserves to be held."^[1]

The upside is you are now faced with a more balanced view to the decision you need to make and are then able to make an informed choice. This may not necessarily change your ultimate decision, but it may temper the extent of what action you take and will also hopefully set out the facts on which the decision was made for future reflection.

By considering a much broader spectrum of 'what if's' we can also build better investment portfolios. This concept lies at the heart of diversification.

- "I may believe that equities are cheap, and I may also observe that they are cheap, but what if I am wrong?" In many cases equities today are cheap, but are they cheap enough given the issues?
- "Fund Manager X is exceptional, but what if their business cannot survive?" Many good fund managers don't deliver good investment returns, for other reasons.
- "Growth shares look massively overpriced, but what if these shares don't disappoint in future?" Growth shares are at their highest premium ever to value shares so one would naturally be a seller of overpriced growth shares.
- "South African property is a safe investment, but what if our economy suffers a prolonged recession?" (this question would have been useful a few years ago).

This internal testing of your assumed point of view can come across as indecisive, low conviction and fence-sitting. The investment industry encourages high conviction, definitive answers and decisive actions. What if this is wrong?

Being comfortable forming your own opposing views is a critical function when building investment portfolios. When binary decision making is all around us, as it appears to be today, we need to take caution, step back, and consider a broader range of scenarios on which to base our views. The answer is usually somewhere inbetween, in the uncomfortable grey area which exists between the yes and the no.

^[1] David Gardner, *The Motley Fool*



data provided by Reuters and Datastream

30 April 2020

		3m	YTD	1yr	3yr pa	5yr pa	10yr pa	5yr Vol1	10yr Vol1
LOCAL MARKET INDICES									
FTSE/JSE All Share Index (ALSI)	ZAR	-8.8%	-10.4%	-10.8%	1.1%	1.6%	9.1%	14.5%	13.4%
FTSE/JSE SA Listed Property	ZAR	-42.8%	-44.5%	-46.0%	-21.4%	-12.3%	3.3%	22.2%	18.6%
SA All Bond Index (ALBI)	ZAR	-12.1%	-11.1%	-6.2%	3.9%	4.7%	7.0%	8.3%	7.7%
SA Cash Index (SteFI)	ZAR	1.6%	2.2%	7.1%	7.3%	7.2%	6.5%	0.1%	0.2%
Balanced Benchmark	ZAR	-5.7%	-5.0%	-3.1%	4.3%	4.6%	10.1%	9.8%	8.6%
SA Inflation (1 month lag)	ZAR	1.6%	1.6%	4.2%	4.2%	5.0%	5.1%	1.2%	1.3%
GLOBAL MARKET INDICES									
Global Equity (Datastream World)	USD	-11.7%	-12.3%	-3.5%	5.6%	5.5%	8.3%	14.3%	14.2%
Emerging Markets Equity (Datastream EM)	USD	-12.5%	-16.6%	-11.7%	0.9%	0.3%	1.8%	17.7%	18.0%
Global Property	USD	-17.3%	-16.5%	-9.6%	2.3%	2.7%	7.0%	14.8%	15.2%
Global Bonds (Barclays Global Bond Index)	USD	1.6%	3.2%	8.0%	4.2%	3.0%	2.3%	5.3%	5.3%
Global Cash	USD	0.3%	0.5%	1.9%	2.0%	1.5%	0.9%	0.2%	0.2%
MAJOR INDICES BASED TO RANDS									
FTSE/JSE All Share Index (ALSI)	ZAR	-8.8%	-10.4%	-10.8%	1.1%	1.6%	9.1%	14.5%	13.4%
Global Equity (Datastream World)	ZAR	8.1%	15.2%	23.7%	17.3%	15.0%	18.7%	16.8%	14.7%
Emerging Markets Equity (Datastream EM)	ZAR	7.2%	9.6%	13.2%	12.2%	9.3%	11.6%	14.6%	13.2%
Global Property	ZAR	1.3%	9.7%	15.8%	13.6%	11.9%	17.3%	17.2%	14.5%
SA All Bond Index (ALBI)	ZAR	-12.1%	-11.1%	-6.2%	3.9%	4.7%	7.0%	8.3%	7.7%
Global Bonds (Citigroup)	ZAR	24.4%	35.6%	38.3%	15.8%	12.2%	12.1%	16.6%	14.6%
COMMODITIES									
Gold (US Dollars)	USD	7.4%	12.1%	32.9%	10.4%	7.6%	3.8%	13.0%	15.8%
Gold (Rands)	ZAR	31.5%	47.2%	70.2%	22.7%	17.3%	13.7%		
CURRENCIES									
Rand / Dollar	ZAR	-22.4%	-31.3%	-28.1%	-11.1%	-9.0%	-9.6%	17.1%	15.8%
Rand / GBP Pound	ZAR	-17.2%	-25.0%	-23.9%	-10.2%	-4.7%	-7.5%	17.4%	14.9%
Rand / Euro	ZAR	-21.0%	-28.2%	-25.2%	-11.3%	-8.5%	-7.5%	15.9%	14.0%

Spot Rates		30-Apr-20	Latest Quarter	1 Year Ago	5 Years Ago	10 Years Ago	20 Years Ago
CURRENCIES							
Rand/US\$	Rand	18.37	17.86	14.34	11.96	7.36	6.78
Rand/GBP	Rand	22.74	22.15	18.69	18.37	11.27	10.60
Rand/EUR	Rand	20.12	19.60	16.07	13.40	9.78	6.18
RATES							
Libor 6m \$	US\$	0.76	1.18	2.62	0.41	0.53	6.73
Repo Rate	Rand	4.25	5.25	6.75	5.75	6.50	11.75
Prime	Rand	7.75	8.75	10.25	9.25	10.50	14.50
All Bond Index Yield	Rand	11.64	11.23	9.44	8.23	8.60	9.74
COMMODITIES							
Gold (\$/oz)	US\$	1,704.81	1,612.10	1,283.06	1,180.69	1,179.85	275.25
Platinum	US\$	767.00	727.00	889.00	1,136.00	1,738.00	525.00
Oil (Brent Crude) \$	US\$	25.52	22.60	72.90	64.57	86.28	24.10
INFLATION							
SA Inflation	%	4.1	4.1	4.4	4.5	4.8	9.4

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