

## *Winning the Loser's Game*

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I have written about the fact that, despite an apparent understanding of basic investment principles, many people make repeated and persistent unwise investment decisions. More specifically, they make a large “number” of investment decisions. While we can attribute some of this to simple naiveté, I have found that people are more often driven by a desire to “win” at investing. Unfortunately, trying too hard to win the investment game leads inexorably to lost opportunities and lost wealth.

Charles D. Ellis is founder of Greenwich Associates, one of the oldest investment consulting firms in the U.S. He chaired Yale University's investment board during its emergence as one of the most successful investment funds ever put together.

In Ellis's 1998 book *Winning the Loser's Game*, he likens investing to tennis. With credit to the original study of Dr. Simon Ramo, Ellis observes that there are two games of tennis played in the world. There is the game played by pros and elite amateurs and there is the game played by the other 99 percent of us.

In pro tennis, about 80 percent of the points are “won”. That is, one player hits the ball in such a way that the opponent cannot hit it back. An ace; a passing shot; a forced error. Watch tennis on TV sometime, and you'll see what I mean. You win this form of tennis by attacking the game and your opponent. This game of tennis is a “winner's game.”

In the tennis everyone else plays, the vast majority of the points are “lost”. We double fault; we hit it into the net, trip over our shoelaces or simply miss the ball. On rare occasions, we knock a good one by somebody. You win this form of tennis by avoiding mistakes and by just keeping the ball in play. This game of tennis is a “loser's game.” If you try too hard to hit brilliant shots every time, you will lose the match.

Charles Ellis has been around a long time and offers these words of wisdom: Investing is a loser's game. I am sorry to break the bad news to you.

Until about the early 1970's, investing was a winner's game. An investor could gain an edge on the market by out-thinking and out-analyzing other investors. Individual investors accounted for 90 percent of the daily trading volume on the exchanges, and they had virtually no data to work with. A smart, hardworking investor could find gold among the rocks.

The pre-1970 era was the heyday of Benjamin Graham, whom some of you may know as the “father” of investment analysis and as one of Warren Buffet's heroes.

In the modern market, professional investors with large staffs and vast research budgets do over 90 percent of each day's trading volume. The 50 largest institutions do 50 percent of all trades in the market. So not only are individuals competing with professionals, the professionals are competing with each other in setting the market's direction.

Even these very smart people find it exceedingly difficult to beat the average return of the whole market. How would you do against Pete Sampras or Serena Williams?

Ellis advises an approach to investing that requires you to know where you are going with your money before you start investing it. I like to think of an investment program like a compass. You know where you are now and you know where you want to go. Find the compass direction that links the two and stick to it. Don't veer off onto shoals and into unknown waters. You will get where you are going with the highest degree of confidence by avoiding mistakes.

Mistakes include buying a stock that someone told you is "hot". Mistakes also include moving your money from one place to another repeatedly, chasing the most recent winners.

Every time you make another investment decision, you expose yourself to the risk of a mistake. Changing funds, buying and selling stock repeatedly, moving in and out of the market — every one of these decisions is more likely to lead to a mistake than to a success. Imagine you played tennis by trying to hit every single shot to within inches of the corners. Your opponent could just stand there and let you self-destruct.

By imploring you to avoid mistakes I don't mean that you should resign yourself to mediocre results. Rather, I mean that you should embrace the fact that a consistently applied plan that takes the whole picture into account will produce the best investment results over time. Time and patience are your allies, so let them work for you.

I will offer some thoughts over the next few months on how you can create an investment plan that will allow you to win the game.