# The Tim Ferriss Show Transcripts
# Episode 109: 5 Things I Did To Become a Better Investor
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**Tim Ferriss:** Hello, my friendly little magwai. This is Tim Ferriss and welcome to another episode of the Tim Ferriss show. Routinely what I normally do is interview someone and dissect their excellence. In other words, I have a world class performer of some type and I deconstruct the routines, the habits, the influences, the favored books and so on that have impacted them and helped them to perform at the highest level imaginable.

Whether that is in entertainment, law, finance, music, chess, you name it we cover a lot of different fields because you find commonalities. Every once in awhile I do an episode like this one, which is intended to be very short and I call them "inbetweeinsodes," and that's normally when I riff on a particular topic. This time I'm going to talk about investing because I've had a lot of people ask me about it so I'm going to talk about the five or so things – might end up being six, I'm not sure; depends on how you count – that I did to become a better investor and some of my thoughts on investing. I should put out a few caveats beforehand and provide a little context. So No. 1, I make no claims to be the best investor out there.

There are many, many thousands of people who are supremely capable and better than myself. I will say, however, that I've been able to develop a skill set in specifically early stage tech investing whereby I have been able to generate about 10X than I have in publishing, or more than 10x and I've been able to – very important point – cash out enough positions that I've earned in real dollars in real bank accounts as much as I have in publishing. So that I would consider a success.

They're still small numbers compared to what many hedge fund icons and so on produce on an annual basis, of course but I think there are some lessons that I've been able to adopt and adapt for my own personality, my own weaknesses, my own life that may be helpful for other people out there listening. I've also had the opportunity to interact with many different styles of investors. So for instance, you have Chris Sacca, who will end up most likely being the most successful venture capitalist in history, at least having the most successful fund in history.

He's been on the podcast so you can listen to that episode, as well. I've had a chance to interact with a lot of very, very skilled hedge fund managers who, by definition, are good at hedging. They're good at not only participating in bull markets but also bear markets and are good at covering their exposure. So that, I find, just as a concept in and of itself very fascinating. That chess game is very, very interesting; we'll get to that.

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And then, of course, I've had a chance to interact with people who are kind of buy and hold, ore even index investors, and people who are very good at it. Then you have value investors along the lines of, say, Buffett who I've actually also had the chance to ask Buffett a question or two at the Berkshire Hathaway shareholders meeting. There's a blog post on that. If you search Warren Buffet and my name, that will come up.

But let me just try and keep this simple. I'm going to go through the steps that I took and how you can apply them, hopefully for some increase in competence, confidence or just the pure realization that you shouldn't play in games you aren't prepared to research and win.

So first off, a basic concept that I'd like to push out there, and this was shared with me by other people in the hedge fund world that I think makes a lot of sense: how do you invest and win? Well, you have to have an advantage. There may be exceptions but there are always exceptions so I'm not going to cover all of them. The advantages you could have could be informational; that means you have information other people do not and that gives you a decided advantage. In Silicon Valley, living in San Francisco and participating as I do in the startup scene, I have an informational advantage. That is my primary advantage in picking stocks, as it were; in this case early stage startups.

Let's say you don't have an informational advantage. You could have an analytical advantage. That means you're better at reading the charts, doing technicals, or even crunching numbers. Maybe you have PhDs; maybe you have algorithms that help you to take data that is available to other people but make better use of it. Renaissance Capital would be a good example of that, and there are many others; some folks at D.E. Shaw, for instance, blah, blah, blah.

Then you have behavioral. Behavioral is a very, very I think under discussed element. People are keen to get to the how-to and they want the recipe for investing. But just because Warren Buffett can use it doesn't mean you can. And by behavioral, just as one example, if you read *The Making of an American Capitalist* about Buffett, there's a story of his daily routine of how we would go to the office, come home from the office and then walk up stairs to read annual reports. I'm roughly paraphrasing this; I might be getting a few details wrong. At one point, he came home and I think his son was just splayed out on the stairs, completely wiped out and was in pain.

He stepped over his son, went up to the office and later came down – maybe a few minutes afterward – and said, "Are you okay?" Alright. He has a hard wiring and an ability to divorce emotion from life which includes financial decisions so that he doesn't succumb to what you might call Mr. Market, the manic depressive who will have all the wrong instincts ad not do what Buffett says, which is be greedy when others are fearful and fearful when others are greedy. Easier said than done.

So behavioral. Do you have a particular personality type or temperament that allows you to make better decisions? That's it. So those are the basics; those are the three. The first

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step is to read about different styles of investing. I should also point out defining the term investing can be a little tricky. For me, I subjectively define it as allocating resources to improve my quality of life.

What that means personally for me, again, I could have an investment that returns an incredible annualized compounded interest, like 20 percent. But if it keeps me up every night with insomnia and sweaty palms, it is not necessarily a good investment. Oftentimes, liquidate those or avoid them altogether. Because if I am sacrificing my present day quality of life, especially if it's for longer periods of times – years and years – for a speculative future cash out, that is an extremely dangerous proposition and a gamble.

I am investing to improve my quality of life, and that is how I think of capital and resource allocation; time, energy, etc. I'll go into that another time. So start reading about different and conflicting styles of investment. This is to, in some ways, try to spot patterns so you can identify people who embody your strengths or weaknesses.

Again, looking through the lens of informational advantage, analytical advantage, behavioral advantage; who could you emulate potentially? Number of books, and if you don't have time to read these books; guess what, you shouldn't play because you're going to get your fucking face ripped off. I'm not a professional financial advisor so everything in this is my own experience and opinion. Get professional advice before making any financial decisions, blah, blah, blah. But if you can't make the time to do this, consider putting your cash in a mattress or just putting a bunch of stuff in no load index funds and just forgetting about it. Or use something like Wealth Front, which I'm an investor in, meaning I own equity in Wealth Front itself.

But coming back, Buffett. Let's look at Buffett first. There are two ways to read Buffett that I really enjoyed. The first is *The Making of an American Capitalist.*

Some would say read *Snowball. Snowball* is also very good. I just enjoyed the perhaps more brutally honest assessment of the unauthorized biography, but they're both very, very good. *The Making of an American Capitalist* is a very good look at Buffett. Secondly, read his annual letters. If you search the annual letters of Warren Buffett sent to shareholders of Berkshire Hathaway, you can find a paperback collection that is worth its weight in gold.

Next, let's look at a very sharp contrast. There is a fantastic book called *More Money Than God,* and it's about hedge fund managers and the history of hedge funds. There are some incredible personalities in this book with extremely diverse styles of investing. It is a fantastic read. It's along the lines of, I would say, *Liar's Poker* in its readability and I think *Liar's Poker* is another great book to read, so I'll bring that up next.

So *More Money Than God,* must read. Next, *Liar's Poker* and *Flash Boys.* You could really read either one of them. *Liar's Poker* put Michael Lewis on the map, covers Solomon Brothers among many other things, bond trading and I think it covers mortgage

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backed securities. Then you have *Flash Boys,* which is about high frequency trading. Both of these make it clear that if you expect to read barons and then go compete against professionals who do this with nearly infinite resources, that you are on a fool's errand. So you wouldn't necessarily – hopefully – bet on yourself if you sat down with, say, the ten best poker players in the world. You wouldn't bet on yourself.

If you were thrown into a golf tournament with the best golf players in the world, you would not bet on yourself. So if you get thrown into the stock market with sharks and brainiacs and teams of PhDs and computer scientists and so on with infinite resources, would you bet on yourself?

The answer should be 999,999 times out of 100,000 no. So these are two good reality checks. They're fun reads because Michael Lewis is amazing, but they show you just what happens behind the scenes. So for instance, the anecdote that stuck with me in *Liar's Poker* was that at one point, there was a guy at Solomon Brothers, the equivalent of I think his name is Fat Tony, who's the character and caricature that Nassim Taleb uses for street smarts who would say put – I'm making this number up – $10 million into a particular type of bond, and he'd say it's going up. And it wouldn't go up, and his colleagues would mock him. Then he would put $500 million or $1 billion in, and the entire market would freak out.

All the market participants would think that he knew something he didn't, and then they would drive it up. And he would say, "See? I told you it was going up." This is not an uncommon type of tactic. So those are two good reality checks so you have a healthy fear of death in you when you step into any of these markets.

Next, to give you perhaps some confidence after that has deflated you, is a very underrated book. And I think it's underrated partially because of the title, and I know how that feels because I wrote a book called *The Four Hour Workweek.* This one is, *You Can Be a Stock Market Genius,* by Joel Greenblatt. And again, I'm not a professional investor guy so excuse me if I misspeak, but it's effectively event based investing and I will let you look into this. It's a surprisingly advanced book, so I would say it's probably for intermediate and advanced investors who have some track record or mileage on their investing.

But again, the purpose right now is not to immediately jump in and start spending money; it is to read about different styles. Event based, meaning a merger or a disaster; an event based approach to investing I find just intrinsically fascinating. So that one is a good one to check out, and I'm probably not doing it justice but *You Can Be a Stock Market Genius,* great book.

I'm going to give one more and then we're going to get to the buy and hold type books that I think have a lot of compelling logic in them for a lot of people. But before that, *Money: Master the Game* by Tony Robbins is also a compilation. You have people from PIMCO, you have people like Ray Dalio, very famous hedge fund manager, Carl Icahn, etc. who are interviewed by Tony who is extremely good at deconstructing best practices.

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I found that book very compelling, and whether for the novice or professional I think there are gems in this. It's a long book but there are gems in there. I did a two-part interview with Tony about money and finance. If you want to check that out, just go to fourhourworkweek.com, click on podcast or, quite frankly, just search Tim Ferriss/Tony Robbins podcast and it'll pop right up.

Next we have one by Daniel Solin, S-O-L-I-N, *The Smartest Investment Book You'll Ever Read.* You could also read stuff by Bogle or, say, *Random Walk Down Wall Street* by Burton Malkiel. These really contain a compelling logic for a very large number of people, a very high percentage for those of you people listening to this, following an index approach to investing.

I will leave it at that. It's a very quick read and I think a worthwhile [read to offset some of the irrational enthusiasm and optimism and fight that you'll have in you reading, say, *More Money Than God.* Because easier said than done, what these guys do. They're the professional athletes, the Michael Jordans of the finance world. So read *The Smartest Investment Book You'll Ever Read.* The title may not deliver but it is a smart investment book, at the very least.

So those are some of the books. Now, I'm going to point out on in particular, so this is the next step, which is *What I Learned Losing a Million Dollars.* I think it's very important to offset all of these success stories, ands there are some tragedies in failures in the books that I just mentioned but to read a book about losing money specifically. *What I Learned Losing a Million Dollars* was introduced to me by Nassim Taleb in his books. We've also discussed it in person.

*The Black Swan,* amazing book, *Antifragile,* great book; both of them have enormous implications for life but also finance, of course, since Taleb was in a former life, though he might still have some participation in derivatives trading, which is a whole, separate subject. *What I Learned Losing a Million Dollars* gets into the psychological, gets into the practical and it gets into cognitive biases and fallacies in particular when you start attributing failure to bad luck and success to skill. It underscores, I think, a number of issues that are inherent in investing and that are common failure points when you're working with financial advisors. I'm sure many of you listening have been asked, what is your risk tolerance? Would you be comfortable in a quarterly decrease of 5 percent in your portfolio, of 10 percent in your portfolio, 25 percent in your portfolio?

And you pretty much just cover your eyes and throw a dart, make a guess and check a box. I have yet to meet anyone who has accurately been able to predict that. And I would say 99 plus percent people vastly overestimate it. I've spoken with some very high level wealth managers and I've asked them what the average was. They say most people say 15 percent. And I said when their portfolio starts dropping, when do they actually freak out? These are high net worth people but 5 to 10 percent, okay? So I think that it pays, in some cases, to take a very conservative approach to assessing your risk tolerance. Chance are

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you're going to freak out a lot sooner than you expect you will, and that has to be factored into a lot of your decisions.

So you've read about the different styles, you've read about losing money. Now it's time to pick an area, pick a timeline and pick tentative rules.

What I mean by that is you've read about many different people investing in many different ways, based on your personality, based on the amount of capital you have to play with, and based on what timeline you think best suits all of those things. Are you going to hold for a day as a day trader? Are you going to hold for two months, three months? Are you going to hold for three years, 30 years? What is the timeframe?

Then you have tentative rules. What I mean by that is simply criteria; criteria for investment and also criteria and triggers for buying and selling. Because a fundamental, I think, error that I certainly have made many times is thinking that choosing the stock and buying it is game over, meaning you've done your job and now you can just sit back and enjoy the spoils. But the reality is, and of course you can use all sorts of weird instruments to make this much more complicated but you haven't made your ROI until you sell, until you liquidate in some fashion.

Of course, you'd use it as collateral for other things like revolving lines of credit; blah, blah, blah but we're not going to get into that. So knowing when to sell and having a plan for selling is just as important as buying in the first place. So people might say you make your money in real estate or stocks when you buy; that's why it pays to be a value investor because you're buying below book value. So even in a worst case scenario, you can do pretty well. And I would agree with that but you can still make massive mistakes if you haven't decided, like a good poker player, when you're going to walk with your chips.

So that's it. You're picking an area, one or two maybe, then you're picking timeframes and then you're picking tentative rules like I did in the world of startups. What's next? Are you going to go out and spend a bunch of money, make a bunch of bets? Well, yes and no. I would suggest one of two approaches; you could do both. That is one, I highly, highly encourage you to paper trade.

What does this mean? This means you're virtually trading. You're not going out and putting real money into bets, yet. You can approach this two different ways. You can either say I have a hypothetical portfolio over two years; I like to think of it kind of as an MBA and we'll come back to that. So let's just say an MBA costs $120,000 over two years. So you decide to take $120,000 of your hypothetical portfolio and invest it over two years.

You could do that for two years. If you're investing for life, what's the rush? But in that case, you would pick stocks, decide how frequently you're going to invest, for instance, if you've chosen stocks, and see how well your criteria works. Let's say that you have a two year hold period. That's your time that you're planning on holding investments. So

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you place a bunch of bets in the first quarter or two of this hypothetical MBA. Again, it’s not real money. This is on paper.

Then you track those investments. You should know when you’re inclined to sell or think you would have sold or bought more, for instance, had you been allowed to. And then after two years, you can look at the results and assess, in fact, how you would have done over that period of time. Now, of course if you have a 30 year time horizon, this is very difficult. There are ways to get around that. For instance, you can back test. You can also do Monte Carlo simulations but we’re not going to get into that. I guess they kind of overlap.

But if you’re looking at startup investing, for instance, and because these time horizons tend to be pretty fast and you can have subsequent rounds of funding that indicate, at least on paper – and this is dangerous – that the value has gone up. So for instance, if you’re interested in startup investing, you’ve read all these various books and you would add another book to that which is *Venture Deals,* by Brad Feldon and Jason Mendelson so you understand deal structure, super important.

Then you could go to AngelList. And full disclosure, I'm an advisor to AngelList. I also have a massive syndicate on AngelList. But you go to AngelList and you could look at the startups that are being syndicated. And again, you have this $120,000 over two years. You could place bets, see how much self control you have. See if you spend it all too quickly. And then track that over the subsequent months, year, etc. and note how many die; in other words, how many shut down. Or how many acqui-hires; larger companies acquire the companies but they’re really just soft landings. You as the investor might not get anything back, especially if you don’t have preferences, or favorable preferences.

So AngelList, very helpful for that. If you want to see the deals that I've picked, you can check them out: Angel.co/tim. I think I have 40 to 50 deals total since 2007. You can check nearly all of them out, and my criteria and whatnot if you want another data set.

So that’s Angel.co/tim. And there are lots of very good Angel investors on AngelList. Okay, how would you back test? If you’re like, you know what? I want to get started sooner. I don’t want to wait two years. I don’t want to wait a year. What do you do? You could, for instance, go back and look at – and you can just Google this – Tech Crunch 50, or Tech Crunch Disrupt Finalists, winners and runners-up from 2009, 2010, 2011. Just look at the article that lists them, the five or six companies. Watch the pitches as they were given that year, and then place your bets. If you had to place a bit on one of them, or you could even take a more conservative approach and look at two different Tech Crunch 2009, 2010.

Look at the four to six finalists in both cases and say if you had to invest in one to three companies, who would you invest in? Because startups tend to live fast, die fast, you will be able to probably figure out which are dead, which are kind of the walking dead like zombies who are probably not going to exit well but they’re kind of limping along, and

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then which ones did really well. So you could try to back test that way, and do it pretty quickly.

The other way that you could do this, and the way that I approached it and this is why I introduced the concept of a real world MBA. If you want very specific details on how I did this, just Google Real World MBA Tim Ferriss and I go into great detail on a 2,000 word post of this. I pined after going to Stanford Business School, decided instead that I would take the money I would have spent, $120,000, and spend it over two years on startups.

Very important assumption I had was that I would lose all of that money but that the skills and relationships that I developed over that two year period of time, just like in an MBA program, would more than compensate for that cost. So I viewed it as tuition. I did not expect to make an immediate return on investment over the two year period. I was viewing it just like an alumni network and skill sets from classes in an MBA program.

But I was playing with my own money. That is how I got started in 2007, and big thanks to Mike Naples Jr. for helping me with that and the many people who have helped me along the way in my education, like Chris Sacca and Naval Ravikant, who is the CEO of AngelList, as a side note. But that’s how I got started. I made some very small bets in the early stages; made some massive mistakes and in that way cut my teeth in the real world. Because the way you respond playing Mike Tyson punch out is very different [00:30:00] from how you respond when you have Mike Tyson actually punch you in the face.

That is how I have developed my skill set. But I expected to lose that money; it is extremely important that you understand that. Because it gave me a psychological freedom and the ability and confidence to make decisions that I otherwise probably would not have had if I had felt committed to making that money back very, very quickly. And for all the hits that I've had, the Twitters and the Ubers and whatnot, the whole time – and Uber, of course hasn’t exited yet – Evernote, you name it – Shopify would be another one – the average hold time for me from my first contact and first paperwork to liquidation was seven to ten years. It’s not as short as you night thing. So that is how that happened.

Those are my two recommendations; paper trade or consider, if you have the financial cushion to so; you have to be able to afford losing it, real world MBA. Hopefully this is helpful for you guys. It seems kind of wordy to me but I'm doing my best, here.

Last but not least – this is a super important step – is you need to have regular check-ins with yourself and practices so that you don’t forget the point and lose the forest for the trees. What I mean by don’t forget the point is, it is extremely easy to focus purely on the metrics, the compounded interest, the financial ROI, the amount of money in the bank account, the valuations on paper. And many of those things could be making you utterly fucking miserable. I have found that in the past, and then I've liquidated various positions. You could say I'm losing money because they later went up but that is very rarely the case if you compare it to the starting point.

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Although, that's been true with options. I suck at options. Maybe somebody can teach me how to be better at that. So there are a number of resources that I find very helpful. One is *The 80/20 Principle*, and the book is by Richard Koch; I'm not sure if that's how you pronounce that name but I will choose that version; K-O-C-H. Another is *Less is More; an Anthology of Ancient and Modern Voices in Praise of Simplicity.* Fantastic anthology and seems very self-serving. But the *Four Hour Workweek* is really a collection of lessons, parables, principles that I collected for precisely this purpose, so that may also be worth a read or revisit.

If you guys want to hear more of this kind of thing, let me know; I could have investors on the podcast. I know a lot of good investors. And if you want to look at how I was thinking about investing in 2008, 2009, which hasn't changed all that much, quite frankly, you could search Rethinking Investing, and then my name, Tim Ferriss.

There are two long blog posts, part one and part two, about this. So *Rethinking Investing*, and I think it's *Common Sense Investing for Uncommon Times*, something like that. I appreciate you guys listening. I'm not the best investor in the world but I've been able to make it work for me. And I've been able to generate more of a return than I ever thought imaginable. And I have played in other areas and done decently well, not just startups; so real estate, for instance. For me personally, I decided that I wanted to take – and I'm sure I'm going to do this principle – the concept "no justice." So maybe I'll have Nassim Taleb on the podcast at some point. But I have decided that for me, I don't have the time or I don't want to dedicate the time to develop an approach like some of these incredible asset allocators like Swenson of Yale, for instance.

I just don't have the bandwidth and concentration. It's not a good personality fit. However, I can take a barbell strategy approach which is something Taleb talks quite a bit about where I am either being – and there's much more nuance to this so read into it; get *The Black Swan,* get *Antifragile.* But I am taking either hyper, hyper conservative approaches; cash, cash-like instruments, etc. that are, say, 80 to 90 percent of my portfolio, and then a small percentage – 10 to 20 percent – are hyper, hyper aggressive; early stage startups. For some people, that might be options.

I do not play moderately conservative or moderately aggressive. That is my choice; it should not necessarily be yours. And for many of you, it is the entirely wrong approach. But for me, this barbell approach has really allowed me to sleep well at night, especially when there are binary decisions where I am doing a lot of homework, then investing in something like startups where I can't change my mind.

In other words, I'm not watching a stock ticker wondering should I buy more, should I sell; should I buy more, should I sell every moment of every day, which I know is my masochistic tendency. So as in many things, know thyself. That applies to investing as well as everything else; skill acquisition, learning, happiness in general, relationships. But I appreciate you guys listening and if you want more of this stuff, just let me know at TFerriss, T-F-E-R-R-I-S-S on Twitter or Facebook.com/timferriss, two Rs, two Ss on

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Facebook. I'll be doing plenty of Q&A on Facebook and might have some investors pop in. so like the page, check it out and as always, thank you for listening.

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