THOUGHTS FOR THE WEEK

INVERT, ALWAYS INVERT

January 26, 2024

Some of the Bay Area's best hiking lies just over the Golden Gate Bridge in Marin County. From the peak of Mt Tamalpais, down to the shores of Stinson Beach, through the winding valleys of Muir Woods, Marin rarely disappoints adventurers.

The unique climate can reward hikers with *cloud inversions* – when the mix of cold and warm air in the valleys *inverts*, leaving a layer of clouds sitting below a mountain summit. The boundary between clouds and the surrounding bodies of water blurs, and you can often times see the tips of the tallest buildings in San Francisco poking through a mass of white and grey mist.

"Man muss immer umkehrer."

- Carl Gustav Jacob Jacobi, a 19th century German mathematician

This quote loosely translates from German to English as, "Invert, always invert."

Jacobi wasn't referring to the aforementioned meteorological *inversion*. Rather, he was referring to *inversion* as a way of thinking – a "mental model" – that involves solving an unknown problem by *inverting* a known solution. Or solving the problem *backwards* instead of *forwards*.

For example, if you wanted to know the secret to living a long life, the *forward* way of thinking might be to eat healthy, exercise, reduce stress, and surround yourself with loved ones.

Alternatively, you could *invert* the problem. Instead of asking yourself, "What leads to a long life?," you could ask, "What leads to a short life?", and avoid doing those life-shortening-things.

For example, by not smoking, your life expectancy increases by a number of years. If you don't jump out of planes for fun, a skydiving accident is one less thing to worry about. Or, as Charlie Munger advocated, "The only thing I want to know is where I'm going to die so I never go there."

Sadly, Charlie went "there" late last year, but the value of *inverting* lives on.

When counseling clients on their investment needs, we often times find ourselves *inverting*.

A common question: What's the key to successful investing?

The *forward* way of thinking might be to invest with a very long-term time horizon in assets that have attractive long-term expected returns.

Agreed. But easier said than done!

The *inverted* way of thinking would be to ask, "What leads to *unsuccessful* investing?" and avoid doing those things:

- **Paying high taxes and fees** erodes the compounding process. We try to minimize taxes by investing in assets with tax-favorable return streams – deferring capital gains and income realization where possible — and prefer to allocate capital to investment strategies with no or low additional costs (eg, expenses ratios, manager fees, carried interest, etc). Some amount of taxes and fees are unavoidable in prudent asset management, but we do our best to minimize them.

- **Unforced errors** can eat away at investor returns. These mistakes often manifest themselves in the form of panicked selling during periods of market duress. We recommend holding ample cash reserves and investing with no or low leverage. This typically gives investors time to *ride out* bad markets…rather than *react* to them. Selling becomes a *choice* rather than a *necessity*, reducing the probability of making an unforced error.

- **Overconcentration** means holding too much of your wealth in too few assets. This doesn't always lead to "unsuccessful investing," rather it increases a portfolio's volatility – the highs can be higher and the lows lower. A more diversified basket of stocks, bonds, and cash can lead to a lower, slower grind to wealth accumulation than a more concentrated approach, but it can also reduce the probability and magnitude of wealth deteriorating events.

Inverting comes in handy in your personal life, as well. The "right" things to do to foster a happy marriage might be a bit mysterious, but most of us can easily spot the "wrong" things. And there's no "right way" to raise your children, but there are obvious choices you want to avoid.

Successful investing, and successful living, are just as much about avoiding mistakes as they are about making great decisions. When forward thinking starts making your aspirations feel distant or your questions unanswerable, remember, "Invert, always invert."

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Mike Burbank's Awards:
2017-2022 **Barron's Top 1,200 Financial Advisors: State-by-State** (formerly referred to as Barron's Top 1,000 Financial Advisors: State-by-State) Source: Barrons.com (Awarded 2017-2022). Data compiled by Barron's based on 12-month period concluding in Sept of the year prior to the issuance of the award.

2013-2020 **Financial Times 400 Top Financial Advisors**
Source: ft.com. Data compiled by the Financial Times based the following time periods:
Awarded 2013-2020; data 12/31/12 - 6/30/19

2019-2020 & 2022 **Forbes Best-In- State Wealth Advisors**
Source: Forbes.com (Awarded 2019-2020 & 2022). Data compiled by SHOOK Research LLC based 12-month time period concluding in June of year prior to the issuance of the award.
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