Demetri Kofinas:	00:00:00	Today's episode of Hidden Forces is made possible by listeners like you. For more information about this week's episode or for easy access to related programming, visit our website at hiddenforces.io and subscribe to our free email list. If you listen to the show on your Apple Podcast app, remember, you can give us a review. Each review helps more people find the show and join our amazing community. With that, please enjoy this week's episode.
Demetri Kofinas:	00:00:31	What's up, everybody? I'm Demetri Kofinas, and you're listening to Hidden Forces, where each week I speak with experts in the fields of technology, science, finance, and culture, to help you gain the tools to better navigate an increasingly complex world, so that you're less surprised by tomorrow and better able to predict what happens next. My guest this week is legendary value investor, Howard Marks, who serves as the co-chairman and co-founder of Oaktree Capital Management, a leading investment management firm responsible for over $120 billion in client assets. Our conversation centers on the subject of cycles, their origins, and impact. Howard shares his philosophy on risk management, asset bubbles, contrarianism, and what he calls second-level thinking, something that has allowed him to outperform his competitors and beat the market time and again, over the course of a career that has spanned five decades, encompassing the most turbulent and iconic periods in modern finance.
Demetri Kofinas:	00:01:39	We also explore how markets and the economy have changed over the last 50 years, how the drivers of a secular bull market in finance may already have come to an end, and how a new normal, characterized by low returns on capital is unleashing political and social forces that have yet to be appreciated, let alone priced into financial assets. Finally, I ask Howard what he sees as the greatest challenge facing the next generation of investors, what skills he believes they will need to survive the current cycle and thrive in the next. With that, let's get right into this week's conversation.
Demetri Kofinas:	00:02:23	Howard Marks, welcome to Hidden Forces.
Howard Marks:	00:02:24	Thank you, Demetri. Glad to be here.
Demetri Kofinas:	00:02:26	You've written two books, correct? This is your second?
Howard Marks:	00:02:29	Yes.

Demetri Kofinas:	00:02:30	Your last one was called "The Most Important Thing," and I was telling you that it probably should've been called the 19 or 20 Most Important Things. I don't remember how many there were, but you've written this second book, and it's about one of those things, which are market cycles. I suppose the first appropriate question is what is a market cycle? Then, why did you decide to write a book about it?
Howard Marks:	00:02:50	Well, there is no standard definition, because a cycle is a continuous thing. Generally, we think of it in terms of a sine wave, and it doesn't really formally have a beginning or an end, since it is continuous, but you could say that a market cycle might be from a low to high and back, or from a high to a low and back, or from a midpoint to the high to the low and back. Anyway, a market cycle is a period of time that includes both rising and falling. I guess that's the best answer.
Demetri Kofinas:	00:03:20	Well, you use the metaphor of a pendulum swinging in your book. Why did you use that metaphor? How is it an apt metaphor, and how is it different?
Howard Marks:	00:03:29	For some reason, I find it easier to think of a pendulum when I think about psychology, because psychology in the market really consists of people swinging from one extreme to the other and then back, and for my way of thinking, it fits better than a sine wave. Investors swing from greedy to fearful, from optimistic to pessimistic, from euphoric to depressed, from credulous to skeptical, from risk tolerant to risk averse. Those swings are the result of some cycles and the cause of others. There are several cycles, all of which operate at the same time, all of which have effect on each other and back. Understanding where we are in the cycles, what's causing them, gives us some idea of what the future holds.
Demetri Kofinas:	00:04:27	It's a continuous, dynamic process. You know, there's been a lot of work done in recent decades around this theory of emergence. It's used a lot for neuroscience, and really complexity theory, and markets are very complex. Do you think of these cycles in similar fashion, that they are emergent phenomena? The way I think about it, when I read your book, for example, with the pendulum analogy, is that, because you also make the point that, unlike a pendulum, which is predictable in the speed and duration of the swing, in markets, you don't actually know when the pendulum is going to turn back. It also turns back ... One of your partners at Oaktree says the air comes out of the balloon faster than it goes in.

Demetri Kofinas:	00:05:05	The way that I think about them, in terms of emergence, is that you have all these different markets that have all these different pendulums. There are pendulums in every different market, and each pendulum has within it another pendulum, because there are smaller cycles within cycles, and so you've got an infinite number of variables knocking into each other, and out of that emerges a price.
Howard Marks:	00:05:24	I see.
Demetri Kofinas:	00:05:25	That seems like an infinitely complex thing to do, which I think speaks of the artful nature of investing.
Howard Marks:	00:05:30	Well, as you know, when I was finishing my first book, I had lunch with Charlie Munger, Warren's partner, and toward the end he said, “Now, just remember that none of this is meant to be easy. Anybody who thinks it's easy is stupid.” I never try, in my books or memos or speech, to simplify investing. It's extremely complex. If I were to convince you that it's simple, I would be doing you a disservice. It is complex, and that's why most people have to take a very measured approach to what they're doing.
Howard Marks:	00:06:07	I think that one of the points I try to make in the book is that if you say to the average thoughtful person, “What is a cycle, a market cycle, an economic cycle, et cetera,” I think they would say, “It's a series of events that follow each other, one after the next, in a consistent pattern of up and down.” That's okay, as far as it goes, but it's not enough, because what they miss is that they are events where the first isn't merely followed by the second. The first causes the second. Once you understand that, I think you've gone a good way to understanding cycles.
Demetri Kofinas:	00:06:42	In other words, what you might be saying, if I understand correctly, is there's a popular misconception by the public, perhaps, that when a crash happens, they ask, “Well, what happened? What caused the crash?” But the crash was preceded by a boom. You can't have a bust without a boom.
Howard Marks:	00:06:56	Exactly, exactly, I think that's very important. There is a certain symmetry to cycles, just as there is to pendulum swings, but these things are not mechanical, and they're not pursuant to the laws of nature. They're pursuant to the laws of psychology or emotion and, as a consequence, they are not regular. As you say, things inflate over a long period of time and then tend to deflate rather quickly when people lose heart. Some cycles have a modest amplitude. Some have a great amplitude. When you

have a great amplitude, then it's reasonable to expect a greater bust, but not necessarily.

Demetri Kofinas: 00:07:35 In that sense, because you know during the Greenspan era, in particular, there was this idea of the great moderation, that we've tackled the market cycle. We've tamed it. Are cycles a feature, not a bug? Are they endemic to human societies, to markets with human participants in them? In that sense, is that driven by the psychology and emotions of fear, greed, envy?

Howard Marks: 00:07:58 I think entirely. I think we'll stop having cycles ... Well, there are two possibilities, either when people aren't involved or when people stop being emotional. I don't think either of those will ever happen, but the point is, for example, you look at the market. The market returns, let's say, about 10% on average per year. Well, why doesn't it just go up 10% every year? Why sometimes 12 and sometimes 8 and sometimes 15, sometimes 5, and sometimes up 30, and sometimes -10. The answer is the involvement of people.

Howard Marks: 00:08:32 Ben Graham, who was Buffett's teacher, who wrote the seminal book, called The Intelligent Investor, said that, in the long run, the market is a weighing machine, ascertaining the merits, but in the short run, it's a voting machine, in which all it does is record swings in popularity. The point is that the reason we have cycles is that, when things are going well, the positives are overestimated and excesses are created, which take it to unsustainable levels, from which it then has to correct, and it doesn't go back to fair. It goes back to overly depressed, from which it will correct again, and thus we have cycles.

Demetri Kofinas: 00:09:14 There are two things that that makes me think about. One has to do with what you said about emotions, and the other one has to do with this idea of second-level thinking. With respect to emotions, I'm curious. You said you don't think that we'll ever get to a place where people don't have emotions. Are superior investors less emotional, or are they simply better able to govern their passions? I would ask that also in the context of bearish and bullish biases, which are something else that you've talked about.

Howard Marks: 00:09:39 I think that people make mistakes because of their emotions. They get excited when things are going well, and they buy too much at high prices, and then they get depressed when things are going poorly, and they sell too much at low prices. I was taught buy low, sell high. Human nature tends to get us to buy high, sell low, so that's clearly a mistake.

Howard Marks:	00:10:01	In order to not succumb to the common error, to over-exaggerate, to oversimplify, you have to resist those emotional swings. Obviously, in theory, there are two ways to do it: either not be emotional, or be emotional, but have your emotions under control. I think that the first is the easier one. Those of us who are, by nature, unemotional have an easier time. We look at the crowd, and it's clear to us ... I put myself in that category. It's clear to us what they're doing wrong.
Howard Marks:	00:10:34	Now, their error is not necessarily corrected the next day, so they can be wrong, and it could go on for a long time, but the point is the unemotional has a great remove and is able to see what's going on. Being emotional, but controlling your emotions should work in theory, but I think is much more challenging. One of the most frequent questions I get is can you teach yourself to be unemotional? I think it's very challenging.
Howard Marks:	00:11:01	Your second question was about second-level thinking, and people say, "How can I teach myself to be a second-level thinker?" In theory, these things can be taught, but in my first book, The Most Important Thing, discussing second-level thinking, I said it's like the basketball coach, who says, "I can't coach height." All the coaching in the world won't make a basketball player taller, and it won't make an investor unemotional.
Demetri Kofinas:	00:11:26	Let's delve into those a little bit more. We'll get into second-level thinking, because I have a great sentence that I want to quote from your book, but with respect to emotions, so you're saying that it's pretty much something that you're born with. You can cultivate it a bit. I have another question, which is what about experience? I've found that, as I've gotten older, I've gotten much cooler. Some of that's hormonal, I'm sure, but it's also experience. After you've been through a crisis ... The more you've been through one, the cooler you can get at handling that. How much of a role has experience played for you in making you a more level-headed investor over time?
Howard Marks:	00:11:58	I think it's a great help. I think it's helped me. I think it can help many. As with so many things in life, the key is not to merely experience things, but to learn from those experiences. After you've gone through a few cycles, and you've watched how the crowd gets excited at the highs and throws caution to the wind and forgets about prudence, then you can say, "Well, now I understand what a bull market is about and the error in it." I think you have to either learn from experience or learn by reading other people's experiences. Santa Anna said, "Those

who are ignorant of the past are bound to repeat it," and I think this is a perfect example.

Demetri Kofinas: 00:12:42 This brings up a question about risk management, because it shows again the qualitative nature, by which you need to assess the environment, the cycle that you're in, and where you are, which also is an interesting paradox, because you can't predict the future, but at the same time, you need to be able to have some sense of where you are in a cycle, which you can't really know, because it's a fractal. I mean, you'd have to zoom out and see the whole picture, and you can't.

Demetri Kofinas: 00:13:05 There's this great line in your book where you write, well, defining what risk is. You say, "Risk is primarily the likelihood of permanent capital loss, but there's also such a thing as opportunity risk, the likelihood of missing out on potential gains. Put those two together, and we see that risk is the possibility of things not going your way." I mean, that's one of many great quotes in the book. I really love that. Can you explain that a bit? Then, explain to me, how do you implement that, as an investor? Then, how do you scale that for a company?

Howard Marks: 00:13:36 In the investment academia, risk is defined as volatility, the possibility that asset prices will fluctuate wildly, and that returns will fluctuate between positive and negative. That fits the academic's needs for his thought process, but I don't think it's the way life is in the real world. For most people, the risk that matters is the risk, as you say, primarily of permanent loss. Secondarily ... By the way, there are many forms of risk. Well, there are really three. One is the risk of permanent loss. One is the risk of missing opportunities that arise. The third is positioning yourself, so that you can survive the inevitable fluctuations.

Howard Marks: 00:14:25 If you think about it, when we talk about permanent loss, most things in the world that go down, then recover, and go down, and recover. There is this cycle, both in economies and in the fortunes of companies, and thus, in stock prices. They tend to go up and down. Some people say, "Well, I'm going to be a long-term investor. I'm going to buy and hold, and I'm indifferent to fluctuations."

Demetri Kofinas: 00:14:50 Or price.

Howard Marks: 00:14:51 Or price. If you think about the market cycle, you have an underlying upward secular trend. The market tends to go up over decades and so forth, and you have fluctuations around the trend. It's tempting to say, “I'm not concerned about fluctuation, and I will not have permanent loss, because there will always be a recovery from the declines.” That's true, as long as you hang in there, but one of the emotional things that goes on is that people tend to overestimate their ability to hang in when the going gets tough.

Howard Marks: 00:15:28 Again, you think about that economic pattern, and I dwell on it so much in the book, because I think it's so important. I mean, the emotional pattern. The point is, we should like things more the lower the price goes. Buffett says, “I like hamburgers. I eat more hamburgers when they go on sale.” My wife goes to the sales. She buys more during the sales than she does in the non-sale period. We all should do that. In microeconomics, there's a demand curve, which shows that the lower the price, the higher the quantity demanded. That's the way it should be, but if you think about what I said at the beginning, about the effect of emotion, the point is, as prices go lower, people regret their past mistakes. They rue their losses. They tend to sell out, because they feel stupid, and they're afraid of further losses at just the moment they should be buying.

Demetri Kofinas: 00:16:25 They see the decline in price of the asset, which they already bought, as a slight against that asset, as opposed to an opportunity to buy more of it.

Howard Marks: 00:16:34 Exactly, exactly, and so in economics, there's the term Giffen good, G-I-F-F-E-N. It's a good that is paradoxical to the laws of supply and demand. Maybe women's handbags are an example.

Demetri Kofinas: 00:16:45 Snob goods.

Howard Marks: 00:16:46 Snob goods, and then if you turn it around, clearly people only buy stocks, because they feel good about them. Then, when the price falls in half, then they feel stupid and disillusioned, and they become more likely to sell. If their premise was right, and it's always challenging to know whether your premise is right, you should like it much more after the price has halved, but most people find it impossible to do that.

Demetri Kofinas: 00:17:13 A few things that come up there when you're talking. One of them is contrarianism, right?

Howard Marks: 00:17:16 Yes.

Demetri Kofinas: 00:17:17 Because you need to be able to be ... not just contrarian, but to be comfortable with being a contrarian, which aren't mutually inclusive. Also, I wonder, when you're speaking, and I was thinking about this while reading the book, in those moments where the classical, there's blood on the streets, that's when you buy, is the reason why most people sell in those moments because they never had a fundamental conviction about the value of what they had purchased?

Howard Marks: 00:17:42 I think many had a reason in mind. Maybe they didn't have conviction. Of course, some people buy things because their brother-in-law bought it, and it went up, and they're jealous of his success, and they want to participate. Some people buy without knowing anything. Back in the dotcom bubble, the first of my memos that was really successful was called bubble.com on the first day of 2000. I said in there, "People buy things where not only did they not know what the company did, but in many cases, they didn't even know the name." They knew the ticker, you know? They bought it.

Howard Marks: 00:18:16 Clearly if you buy things where you don't know the name, you don't know what they do, you don't know the merits, how can you possibly do the right thing when the stuff hits the fan and when the going gets tough. The other thing is ... You see, this is why we've been dancing around this question of second-level thinking. This is why second-level thinking is so important, because if we roll the tape back, and we listen to your question, you said things are down, but most people can't buy there, can't bring themselves.

Howard Marks: 00:18:48 Why are they down? They're down, because people are depressed, and they've swung to pessimistic and to fearful. If most people have depressed prices by selling fearfully they, by definition, can't turn around and become avid buyers. That's why the average investor, or the below-average investor, who is riven by these emotions, is fated to do the wrong thing at every turn.

Demetri Kofinas: 00:19:26 In the Most Important Thing, you write, in describing second-level thinking ... There are a number of sentences in recurrence actually, so you make the point redundant. "It's a good company, but everyone thinks it's a great company, and it's not, so the stock's overrated and overpriced. Let's sell." I feel like there's a lot there to unpack in that sentence.

Howard Marks: 00:19:45 Sure. Well, you left out the first part.

Demetri Kofinas: 00:19:46 Okay.

Howard Marks:	00:19:47	The first part is that the first-level thinker says, “This is a good company. We should buy the stock.” The second-level thinker may say, “It's a good company, but it's not as good as other people think.” That is, the price has been driven on their optimism to a price, which is excessive, given the fundamentals, so it's a compelling sale, same company, just looking at it superficially and simplistically, or deeply.
Howard Marks:	00:20:17	Now, there are so many moving parts in the world, that it's hard to be precisely right in valuing things, but I think things have intrinsic values that we can strive to understand and assign. As I said about what Charlie said, it's not easy. I think the vast majority of investors, A, have no idea how money is made safely. They think you make money in the market by buying and having things go up. They don't know what makes things go up dependably, and so they can't invest an intellectually solid way.
Demetri Kofinas:	00:20:55	When you say dependably, what you mean is understanding the fundamentals, the absolute value, as opposed to the relative value, which is the momentum of what everyone else is doing to bid up the stock.
Howard Marks:	00:21:04	Exactly, but I belong to a school of thought, which is called value investing. Value investors look at a stock or a company or a building or a bond or whatever it may be, and they try to assign an intrinsic value, and then they look to see if they can buy it at that value or less. That's safe investing. If you can buy it at much less, that has a lot of potential. If something has an intrinsic value of X and you're paying 2X, even if the company is a good company, that is unlikely to work. It all goes back to intrinsic value, and I think rather few people understand the importance of value and how to derive it.
Demetri Kofinas:	00:21:48	You made another point there, which is about if you can get it for even less than less, get it.
Howard Marks:	00:21:52	Right, right.
Demetri Kofinas:	00:21:54	That's what you would refer to as margin for error, right?
Howard Marks:	00:21:57	Mm-hmm (affirmative), yes.
Demetri Kofinas:	00:21:57	How important is margin for error in the way that you manage risk?
Howard Marks:	00:22:01	Well, margin for error is very important because, you see, we invest to take advantage of the knowledge we believe we have

and on the basis of the things we believe to be true, but we may be wrong in our assumptions, and anyway, the day-to-day fluctuations, the external events, the random events, all the other things that go on in the world, may cause the outcome to be less favorable than we had predicted. I think one of the important things for being a successful investor is that if things don't go the way you had hoped and planned, you're still okay. In order for that to be true, you have to have margin of safety.

Demetri Kofinas: 00:22:49 The opposite of what you were saying about, well, it's a great company. Just buy the Nifty 50 stocks. If you buy IBM, it's a great company. You're going to be fine. Turns out, that's not true. Price matters.

Howard Marks: 00:22:59 Right. Well, look, as a kid, my first summer job at Citibank in the Investment Research Department was 50 years ago this summer. The bank was what was called the Nifty 50 Investor. They bought the stocks of the 50 best and fastest growing companies in America, under the premise that, A, nothing could go wrong with these companies, because they were bulletproof, and B, if you paid a price that was a little high for the intrinsic value at that time, it would grow so fast that it would grow into its price and make you money. The official dictum was that there's no such thing as a price too high.

Howard Marks: 00:23:34 If you bought those stocks the day I arrived at the bank and held them for five or six years, you lost almost all your money, in the best companies in America. Then, in '78, I switched to investing in high yield bonds, so called junk bonds. Now, I'm investing in the worst companies in America, and I'm making money steadily and safely. If you can lose a lot of money in the best companies and make money in the worst companies, then it can't be true that the secret to good investing is buying high quality assets. That's when I concluded that it's not what you buy. It's what you pay.

Demetri Kofinas: 00:24:12 Then you say ... There's another great quote of yours, like I said, you have so many, where you said you looked into the dictionary when you were investing in junk bonds, and you looked to see what is the definition of ... Was it the D rating or whatever the credit rating was, and it does not have the attributes of a desirable investment or something like that?

Howard Marks: 00:24:29 Right, yeah, that was actually Moody's Manual, where they publish all their bond ratings. Of course, everything was published on paper in those days, and it was a big book that sat on the shelf, because it had information on the bonds of every company outstanding. They said, “Fails to possess the characteristics of a desirable investment." Now, if when we get through with this interview, we go down to the street, and I show you my car, and you need a car, and I have a car I want to sell, and I say, "Demetri, would you like to buy my car?" Hopefully, there's a question you would ask me before you say yes, and that is, "What's the price?"

Demetri Kofinas: 00:25:06 Or let me see the car.

Howard Marks: 00:25:09 Well, but the point is you can't intelligently make a decision about whether something's a good buy, until you know the price. Moody's was saying that if a bond has questionable creditworthiness, it's not a good buy, regardless of the price, and that can't be right, if you think about it. That is the kind of thinking that gave way to the junk bond era, which started 40 years ago, in 1978, and has transformed the investment and financial world.

Demetri Kofinas: 00:25:46 Let's go back a little bit to what you were saying with the Nifty 50 stocks, and the same thing was true of the Tech Bubble in the late '90s and 2000s. There is a different between a market that's overvalued and one that's in bubble territory, right?

Howard Marks: 00:26:01 Right.

Demetri Kofinas: 00:26:02 You've talked about this idea of bubble thinking, and being able to identify when there's bubble thinking. That seems, A, very qualitative to me, very fuzzy to try to figure that out. How do we know if we're in a bubble, and how do you go about trying to figure that out?

Howard Marks: 00:26:15 Well, a bubble is an extreme form of a bull market, and you're right. It is fuzzy, and it is qualitative, but I think these are things we have to assess. If when the price is higher than the intrinsic value, if that produces danger, then you would not say that every asset that is selling above its intrinsic value is equally dangerous. The danger is proportional to the degree to which the price exceeds the intrinsic value. We have to have an idea how it's a mistake for things to sell above their intrinsic value. How big is the mistake that's being made today?

Howard Marks: 00:26:57 Most people would say that today's stocks are selling a little on the high side. The average P/E ratio, price/earnings ratio, for the postwar period is about 16, and today they're selling at about 19. That's a little high. Back in 2000, it was 32. That was a bubble. That's the difference. Is it a little overvalued, or is it extremely overvalued?

Howard Marks:	00:27:20	You can assess these things in two ways. One is quantitatively. You can look at the valuation indicators, just like I mentioned about P/E ratios, yields, yield spreads, what we call capitalization rates/ratios on real estate, enterprise values, EBITDA multiples on private equity. You can look. There are quantitative measures, but there are also, as you indicate, Demetri, important qualitative measures.
Howard Marks:	00:27:46	For example, I believe that it's fair to say one of the characteristics of a real bubble is the belief that there's no price too high, like people did about the Nifty 50 in 1968 and about the techs, Internet, and eCommerce stocks in 1999-2000. They say, "This is such a great thing that there's no price too high." Well, if that kind of thinking, if no price too high thinking is dominating the market, then there's every reason to believe that things are selling too high on too much optimism, relative to their intrinsic values, and that they're dangerous.
Demetri Kofinas:	00:28:32	Do you feel that there's a difference, a structural difference, today investing than there was when you started out? Because interest rates have been taken down to zero. All this quantitative [inaudible 00:28:42] occurred, and it's created a fog in the landscape of trying to discover the value of assets.
Howard Marks:	00:28:50	Well, I don't think there's a huge mystery about what the risk-free rate is. It's somewhere around 2% or 1.5% or something like that. I think that the question is, where are rates going? Are things priced fairly, relative to the risk-free rate? Questions like that. To me, one of the biggest things that has changed the investment environment is that, you're sitting at dinner, and you say, "How many home runs did Hank Aaron hit?" You pull out your phone, and 10 seconds later you know.
Howard Marks:	00:29:27	There's no such thing anymore as not knowing something. When I started, there was all kinds of stuff that not everybody knew. It was possible to work hard and find out stuff that others didn't know. There was no Regulation FD from the SEC. You know, there's something called the Reg FD, and it means that companies have to give everybody the same information. That was not the law, so you could have a knowledge advantage.
Howard Marks:	00:29:58	When I started in high yield bonds 40 years ago, there was no performance history. There was no pricing place, where prices were reported, transactions were reported. There was clearly no understanding of the merits, since Moody's said what they said. They had a pejorative nickname, junk bonds; 90% of investment organizations had a rule against investing in them, so clearly you could get a bargain.

Howard Marks:	00:30:23	Today, everybody knows everything. A lot of these biases ... What's the last time you heard somebody say, “Well, young man,” as they said to me, “I'm sure you can make money doing that, but it wouldn't be proper.” Everybody will do anything today to make a buck, especially if it's legal, so the investment industry has moved a long way to what's called efficiency. In an efficient market, where everybody knows everything, and everybody is highly motivated and intelligent and computerize and so forth, it's hard to find bargains, and it's hard to beat the market. I believe that this is the process that has made investing harder.
Demetri Kofinas:	00:31:01	There are fewer information asymmetries, and there are fewer scruples-
Howard Marks:	00:31:05	Well, that's right.
Demetri Kofinas:	00:31:06	Around what you can invest in and what you can't invest in.
Howard Marks:	00:31:08	Well, but I would summarize on the scruples by saying there are fewer biases.
Demetri Kofinas:	00:31:12	Fewer biases.
Howard Marks:	00:31:12	You know?
Demetri Kofinas:	00:31:13	Fewer hang-up’s.
Howard Marks:	00:31:14	Right, it's biases or, as you say, hang-up’s that keep people from making good decisions. That's one of the things. The economists talk about something called perfect markets, which is their equivalent of our efficient markets. One of the requirements for a perfect market is that if there's a given asset, you are equally willing to buy it or sell it, and you're equally willing to hold it or hold a substitute for it. That is to say, you're not biased. In the old days, people were biased. Today I think people are less biased in the ways I'm discussing, so this is among the things that makes investing hard.
Demetri Kofinas:	00:31:55	Is that change reflected or driven or a driver of the growth of the financial industry as a proportion of GDP in the last however many decades? I mean, when you started, it was obviously a much smaller industry. It's grown a great deal. Has that growth allowed for more competition and for some of these inefficiencies to be identified and taken advantage of by market participants?

Howard Marks:	00:32:20	The short answer is yes, but you have to ... This is, again, second-level thinking. You say, disequilibria, be taken advantage of by investors. Yes, but when investors find an inefficiency and take advantage of it, they also drive it out of existence. The increased knowledgeability of the investment world has made it more efficient and has tended to drive out inefficiencies and make it harder to outperform.
Demetri Kofinas:	00:32:50	Is that, in keeping with the theme of cycles, has that, that 40 year or so bull market in finance ... Is that a cycle? Is that a cycle that has reached its zenith, perhaps, in 2008? I don't know what the numbers are, since 2008, but I assume it's pretty much flatter or gotten a little bit smaller as a percentage of GDP.
Howard Marks:	00:33:10	Good question. I do think that over the ... Let's say, the period I was exposed to, '68 to '08. I think there was a big upswing in the role of investing and finance, relative to the economy overall, and then, of course, those activities took a real knock in '08-'09, and maybe some people left the business, or fewer people were going in.
Howard Marks:	00:33:35	Nowadays, kids getting out of school want to be entrepreneurs and go to Silicon Valley and create new companies. I think, perhaps, the profitability of investing has come down a little bit, as it has become harder to outperform, certainly in the hedge fund world, for example. Back in '08, when the banking and finance world was suffering, I wrote in one of my memos that it wouldn't be such a terrible thing if the smartest kid in the class became a doctor and cured a serious disease, as opposed to going to a hedge fund to try to make a lot of money.
Demetri Kofinas:	00:34:08	Well, that was going to be another question I was going to ask you, which is, if we're at a place where finance will decline as a proportion of the economy, is health care possibly one of those areas that's going to grow? Is that because of something else, which I think is something fascinating to discuss and, I think, underappreciated by the public, which is the role of structural demographics and the secular stagnation argument? A, what do you think about that secular stagnation, and B, does that have any relationship to what you think might be some of the winning sectors of the future?
Howard Marks:	00:34:37	Well, I don't consider myself a futurist, but I spend more of my time trying to understand the markets today than I do guessing at what's going to go on in the economy tomorrow. As for the secular stagnation argument, what I would say, Demetri, is that coming out of World War II, there was a lot of hunger. There was a lot of room for growth. There was a lot of appetite,

especially with the enormous population fill-up from the baby boomers.

Howard Marks: 00:35:06 Then you add to this, massive increases in productivity and technology, and the combination produced a period of unusually high growth, culminating in the '90s. You could see it in the stock market. The stocks are said to go up at about 10% a year, but in the '90s, they went up at 20% a year, both through the fundamental strengths, but also through excessively positive psychology.

Howard Marks: 00:35:32 Economic growth is slower now than it used to be. Maybe we were moving from a period of under-performance to full performance on the economy. Once we're at full performance, it's going to be hard to grow above trend line from there. My guess would be that economic growth in the next 30 years will be less than it was in the second half of the 20th century. Then, of course, we have complications, such as globalization and automation adding to the complexities.

Demetri Kofinas: 00:36:06 How much of a role do you feel ... I mentioned the demographics. That's obviously going to play a role, no question about it. In fact, it would be a great time to talk about Japan. I think that would be a fascinating corollary to examine and look for maybe lessons and examples, but obviously the population. The population growth, as well. We're going to have a much larger number of people that live in the world and perhaps fewer room for growth. That's debatable, of course. Then, there's also the debt, the tremendous growth in debt, and that has created this lopsided distribution of those who own capital and those who don't have it. I think all of those things feed into this growth argument, and they also, I think, feed into the low return expectations on capital. How ... I don't know how you want to tackle that. That's kind of a ...

Howard Marks: 00:36:49 It's a big question, if in fact it is a question.

Demetri Kofinas: 00:36:51 It is. It is. There are many questions buried in there somewhere.

Howard Marks: 00:36:55 Yes, right, but first of all, the population of the world is growing rapidly, but not every place. The developed nations are suffering a low birth rate and, in most cases, not replacing. You know, if you have a man and a wife get married, and they don't have two children, then they're not replacing. In many places, they're not.

Howard Marks:	00:37:17	The undeveloped parts of the world, like Asia and Africa, have high birth rates, so there's every reason to believe that the population of the developed nations will shrink, relative to the population of the undeveloped. Of course, the large populations in the undeveloped create cheap labor, which make the undeveloped countries able to benefit from the outplacement of work from the developed.
Howard Marks:	00:37:47	This is a serious question. When people rail against our loss of jobs, part of it, a small part of it, is because jobs began to be done in China and India, which used to be done in the States, after we globalized. Of course, that's not the biggest single problem. The biggest single problem was automation. U.S. manufacturing, I think, has doubled since the late '70s, but now employs a third less people. If you can double the output with a third less people, that means that if you had an increase in productivity, the number of people employed would be triple what it is today.
Howard Marks:	00:38:25	These are all problems. I'm far from being smart enough to know what the solution will be. I think that in the next 10 years, we're going to see a lot of discussion of universal basic income and government guaranteed jobs. Look, we're already seeing it in the campaigns of the left. Right now, in the Democratic Party, there are people who want to take over the Party, who espouse ideas like this. We'll see where that goes, but a lot of it is the effect of globalization on the one hand and automation on the other.
Demetri Kofinas:	00:39:01	I agree with that. That's something that we would expect to see in our politics. I think a lot of the volatility that, perhaps, we haven't been seeing in financial markets, is showing up in politics, in populism now on the right in Europe and the United States, and certainly on the left with these ideas of universal basic income. I'm not particularly optimistic about that, because I think you'll agree that work is about much more than just money. It's about meaning, right?
Howard Marks:	00:39:23	Right. When we pay people to sit on their porches, they're not going to get the meaning that they got from work. Even menial work, I think, produces more self-satisfaction than just getting a check.
Demetri Kofinas:	00:39:39	Well, interestingly, Madison and Jefferson spoke about this in The Federalist Papers, which was that they were concerned about people not having a stake in the country. That was why they wanted to have people devote to be landowners, one of the reasons. They wanted people to actually have a stake. They

were worried about some of these rebellions and mutinies and mobs that they had seen in Europe. I think that speaks to that point, as well.

Demetri Kofinas: 00:40:01 Let's go back to this thing about Japan, because this came up when I was thinking about a question I want to ask you, which is, are we in a bubble, right? Of course, that is the question, but when I was thinking about that, I was thinking, well, it doesn't really feel like we're in a bubble. I mean, some of the stuff that I remember from ... I certainly think I would say certain areas I see bubble thinking, like in cryptocurrencies, but what we saw in the late '90s, I don't feel like we see now.

Demetri Kofinas: 00:40:26 Then I was thinking about Japan. Japan went through two noticeable peaks after '89, where the market dropped, if I am recalling this correctly, dropped approximately 50%. I don't know what the sentiment or psychology was in Japan at the time, and I wonder if it was comparable to what it was in '89, and I wonder if future peaks in financial markets, if we can judge them or expect that they will exhibit the same level of euphoria that is normally characteristic of a bubble.

Howard Marks: 00:40:55 Sure, and I have a definite answer, and that is maybe, but because we never know, because emotion and psychology are unpredictable.

Demetri Kofinas: 00:41:04 Sure.

Howard Marks: 00:41:06 You know, this is an important topic. Anybody who came into the financial world in the last 20 years, they saw the Tech Bubble burst in 2001, and they saw the global financial crisis in '08 or '09. All they've seen is bubbles bursting. I think there's a tendency to believe that every elevated market is a bubble, and every correction is a crash. It doesn't have to be, because we can have moderate highs, which correct moderately. I think right now that that's much more likely.

Howard Marks: 00:41:48 If you look at ... First of all, the Tech Bubble was clearly concentrated in one small segment of the economy, where things were taken to ridiculous extremes, where people were buying things on the assumption that nothing could go wrong and that no rules applied. Forget profits. Even if it didn't have any revenues, you could still invest in it wisely at a very high price. That's clearly dangerous bubble thinking, but that was a small segment of the economy.

Howard Marks:	00:42:16	In '07-'08, there was a much broader phenomenon. It was economy wide. What were the things that went wrong that gave rise to the global financial crisis? Well, number one, a very, very high level of leverage, and the banks were permitted to take their assets to 32 times their equity. If your assets are 32 times your equity, and your assets decline in value by 4%, then you have no equity left. That was very dangerous, and that's really why we had a meltdown. High leverage is equal to susceptibility to a meltdown, and today the financial institutions, and I think most of the financial world, is not as highly levered. Funds, entities, certainly banks are not so highly levered today.
Howard Marks:	00:43:06	Number two: The real building block of the crisis was the subprime mortgage. It was enormous in size. It was completely not understood, and there was no there, there, you know? I mean, I want to lend you money, so you can buy your house. I'll lend you money at 5% if you show me your W2 or at 7% if you refuse to do so. You say, “You know, I'd rather pay 7%.” Well, clearly, you must not have any income.
Demetri Kofinas:	00:43:38	NINJA loans.
Howard Marks:	00:43:38	Clearly ... Yes, or we used to call them liar loans.
Demetri Kofinas:	00:43:42	Liar loans.
Howard Marks:	00:43:43	There's no analogy that I can see to that now. There are some things where behavior is loosey-goosey, but there's nothing as fraudulent as that. You put together the leverage, the emptiness of the mortgages and mortgage-backed securities, and then wide deregulation of the financial sector, and that's how you got a bubble. I don't see anything comparable today. Psychology is clearly not euphoric today, and that's a good thing, when you're assessing risk.
Demetri Kofinas:	00:44:16	Right. It sounds a lot like what Gillian Tett said when she was on our show. She called it the Great Ooze, that it's going to be just this slow deflation, as opposed to a pop.
Howard Marks:	00:44:27	Maybe.
Demetri Kofinas:	00:44:28	Yeah, maybe.
Howard Marks:	00:44:29	Maybe.
Demetri Kofinas:	00:44:29	That's the only definite thing you can say.

Howard Marks:	00:44:31	Yeah, I mean, we can talk about what we believe. We can talk about what we think is most likely, but one of the biggest mistakes you can make in the financial world, in the economy or in the markets, is to think you know what's going to happen.
Demetri Kofinas:	00:44:44	Well, this probably would be a good time to ask you something, which is, again, in the book you talk about investing as being a reshuffling of lottery tickets in a jar or marbles, depending on distribution. I think one of the common things that I've learned is that really good investors tend to have a probabilistic distribution of outcomes. How do you, A, gather the information you need, in order to determine what the probability distribution is, to the best of your ability? Then, B, how do you dynamically change those probabilities as they change, and then how do you deploy, how do you make changes to your strategy in real-time, in order to take all that into account? I want to embed this within the larger point about cycles, which is that you want to know when you want to tilt into the wind or when you want to tilt against it.
Howard Marks:	00:45:35	You know, one of the things I'm happiest with is the subtitle of the book, which is Getting the Odds on Your Side. You just said, “We never know what the future holds.” I believe that very strongly. If you look around, there aren't a lot of people who have been successful at investing on the basis of macro predictions for the economies, currencies, rates, markets. Most of the people who have been very successful as investors, it's because they could tell a cheap stock from an expensive stock. Of course, I oversimplify, but it's really hard to make nonconformist predictions for the economy or the macro, which turn out to be exceptionally correct.
Demetri Kofinas:	00:46:24	That has to do with the complexity of a global economy, right?
Howard Marks:	00:46:26	Yes, complexity-
Demetri Kofinas:	00:46:26	They are just way more variables.
Howard Marks:	00:46:28	And randomness in the world, you know? I think one of the important things for people to remember is that this is not science. There is no schematic diagram. You walk in the studio. You turn on the light switch. Lights come on, every time, because that's how these things work. In the book, I quote the physicist, Richard Feynman, who said, “Physics would be much more difficult if electrons had feelings.” The point is that markets and economies are nothing more than aggregations of people, and people have feelings, and so the way a market is going to work is unpredictable. Sometimes you throw the

switch, the market goes up. Sometimes you throw the switch, the market goes down. Sometimes the company has or reports a good quarter, the stock price goes up. Sometimes it doesn't change at all. It can even go down, if they announce an earnings gain which was less than people expected and impacted enterprises. It's really hard to invest on the basis of a forecast for the future.

Demetri Kofinas:	00:47:34	I was going to say, markets are non-deterministic-
Howard Marks:	00:47:38	I think that's right.
Demetri Kofinas:	00:47:39	Is I think what you're saying.
Howard Marks:	00:47:40	Yes, I think that's right. One of the things I say, and I said in the first book, was that we never know where we're going, in that sense, but we sure as hell ought to have an idea for where we are. Where we are tells us something about the future probabilities. It doesn't tell us everything, but it tells us something. In a world which is not deterministic, knowing something beats the heck out of knowing nothing.
Howard Marks:	00:48:01	Now, you used my favorite analogy, which was the lottery tickets in the bowl. Investment performance is nothing other than pulling a ticket from the bowl. There are black tickets and there are white tickets. There are winners and losers. Even when they're mostly winners, you can get a loser. Even when they're mostly losers, you can get a winner. That's why the outcome is not knowable. It's uncertain. It's beset by randomness, but yet we know that the distribution of tickets in the bowl between, let's say, winners and losers, highly influences the outcome. It determines the expected outcome, which doesn't always happen, and is highly influential on what we should do.
Howard Marks:	00:48:52	We should increase our bet, we should buy more lottery tickets, when there are more winners in the bowl than usual, and we should decrease our buying of lottery tickets when there are fewer winners in the bowl than usually. What determines the makeup the tickets in the bowl and, I think, mostly where we stand in the cycle. When the news has been good, and prices have risen, and people are euphoric and greedy and buying, and valuations are above average, it makes sense to think that there are fewer winners left in the bowl than usual, and vice versa. When people have been depressed, the news has been bad, there's been massive selling, valuations are lower than historic, it makes sense to believe that there are more winners in the bowl than usual.

Howard Marks:	00:49:49	These are things we can know, in my opinion. These are things that help us to understand whether this is a good or a bad time to increase our bets in the lottery. Yet, none of them have anything to do about the future. They're just based on observations of the present.
Demetri Kofinas:	00:50:12	This touches on a few really great things that we haven't had a chance to discuss yet. One of them is the role of history. Basically, we could think of it scientifically as a sample size. We have a sample of past events. There are people that have tried in the past ... LTCM was a famous example ... to make investment decisions about the future, based on past occurrences, and saying that, well, if this has happened only so many times in so many years, it's only so likely to happen in the future, which actually goes against probability works, which is something's future probability of occurring isn't based on how often it's happened in the past.
Howard Marks:	00:50:47	Well, it may.
Demetri Kofinas:	00:50:48	It may, but it-
Howard Marks:	00:50:49	I mean, the point is that if the past experience represents a large and unbiased sample from the universe, then we can attach importance to history, but in the investment world, people say, "Well, it really hasn't happened in the last 10 years, so I don't think it's going to happen." Ten years is a very small sample.
Demetri Kofinas:	00:51:12	To your point, though, if you have a coin, a coin has two possible outcomes. If you flipped a coin a hundred times, and you don't know anything intrinsically about the nature of the coin's probabilistic function, you're going to assume that you're safe to keep flipping it, and you're going to get heads, but in fact, the next time you flip it, it's 50% likelihood to go tails.
Howard Marks:	00:51:30	That's right. Well, that's why it's extremely important to understand the nature of the process we're investing in, and since people don't understand these things, especially probabilities. You flip a coin 10 times, and it comes up heads 10 times. There are certain people who say, "Well, this is obviously a coin that's biased towards heads, so I'm going to bet on heads." There are certain people who say, "Ten heads, the next 10 have to be tails." Neither of those people understands probabilities. The answer is, if you flip a fair coin, it has a 50% probability of being heads and a 50% probability of tails, regardless. Why? Because the trials are independent, but I go

back to saying, you have to understand whether or not it's a fair coin.

Howard Marks: 00:52:16 Markets are not coins. When the market is elevated in its cycle, it's a coin which is improbable to come up the way you want. When the market is depressed, the outcomes are biased toward favorable. In the book, I have some graphs where I show my notion of when the market rises and falls in its cycle, the distribution of expected return shifts from left to right. This is my way of representing that.

Demetri Kofinas: 00:52:50 The coins can become more or less fair, right?

Howard Marks: 00:52:53 Oh, yes.

Demetri Kofinas: 00:52:53 They change. That's the point about that you have to be able to update the probability distribution, the tendencies of whatever you're doing. How do you then incorporate history, because history's important, right? I mean, you've talked about it in the book. I mean, you quote Galbraith a lot in the book, who's obviously a great financial historian and has imparted a great amount of wisdom. How do you incorporate the lessons of history in your financial decisions, when you understand that history isn't a roadmap to the future?

Howard Marks: 00:53:21 Right, well, you know the theme, Demetri, that I think guides the book more than any other one thing, is a quote that's attributed to Mark Twain. He may have said it. He may not have said it. He said, “History does not repeat, but it does rhyme.” We cannot use what has gone before as an ironclad rule, but there are some things that tend to repeat or rhyme.

Howard Marks: 00:53:47 We discussed, at the beginning of this interview, the fact that the amplitude, duration, speed of a cycle is different from one to the next, so are the causes and so are the effects, but there are generalities, which I think do rhyme from cycle to cycle. Number one: There are some things that I would say are part of the origin of every strong market boom, things like too much optimism, too little risk aversion, too much money around, and too much willingness/eagerness to invest it. When those things are all true, the market is probably going to go to a dangerously elevated level.

Howard Marks: 00:54:46 The other things that repeat are that when the market is elevated in its cycle, the probability distribution of future outcomes shifts to unfavorable. When the market is depressed, the distribution of possible outcomes shifts toward favorable.

These are the things that we can know. When the market will turn, how far it will go, what will make it turn ... These are things we can't know. I use the word tendencies over and over in the book. We can understand, given where the market is, in its cycle, given the factors that have got it there, we can understand what the market will tend to do in the coming months and years.

Demetri Kofinas: 00:55:34 Based on those tendencies, as you understand them today, have you been positioning yourself more aggressively or more defensively or Oaktree, your portfolio?

Howard Marks: 00:55:44 In recent years, I would say more defensively. We are not stock investors. We are credit investors, fixed income investors. With interest rates so low, people have been eager to try to achieve, shall I say, high returns in a low return world, which has led them to engage in pro-risk behavior. That means that they're investing in lesser quality companies. Their due diligence, their demand for margin of safety is not so strong. They're making more generous assumptions. They're willing to live without some of the protections that they enjoyed in the past.

Howard Marks: 00:56:23 If these things are true, and I think they are, then that means we should be more defensive than on average. We've had a mantra for a few years now: Move forward, but with caution. Move forward. Invest. We invest every day. We try to be fully invested, but when I say with caution, we are a cautious firm, so with caution means even more caution than usual, and I think that's appropriate today.

Demetri Kofinas: 00:56:50 Do you think that investors ... You know, it's interesting, because a number of investors, some of them famed investors, have had to close their funds, because they've just had too hard a time investing in this environment. Is what you're saying another way of saying that people have not yet become accustomed to what might be a new normal, where a safe return or a reasonable return on capital is not 10% or 8%; it may be closer to 5%, and because of that, they're taking risks that they would not take, let's say, in a future cycle, if people were more accustomed to this, and that that is what is making you defensive?

Howard Marks: 00:57:27 Yes, that's a good part of it. Let's use your example. It used to be that you could make 10 safely. Now you can only make 5 safely. People are doing things now to make 8 in a 5% world.

Demetri Kofinas: 00:57:40 Because they don't realize they're in a 5% world, or they're in denial.

Howard Marks:	00:57:43	Well, I don't think they're in denial. I think that they need the money. When you look at the average U.S. pension fund or university endowment fund, they need about 7.5 or 8% to make the numbers work. They can't say, "Well, in this environment, you can safely make 5. We're going to settle for 5," because then they'll consume their endowments, so they say, "We need 8 in a 5% world," so they take increased risk, and they do things that they wouldn't have done when the safe return was 10, because they didn't need to take risky actions. I think that that is one of the things, pro-risk behavior, the pursuit of high returns in a low return world, is one of the things that I think compels some degree of caution today.
Howard Marks:	00:58:28	I'm not saying to get out of the market. I'm not saying to not be in the market. Somebody on one of the TV shows said last year, "Marks says it's time to get out." I said to him, "There's only two things I would never say. One is get out, and two is it's time." I'm never that sure, and I'm certainly not that sure today, but I would moderate my aggressiveness today.
Howard Marks:	00:58:51	Investors face two main risks. Every investor faces two main risks, whether they're aware of it or not. The main risk, and everybody knows it, is the risk of losing money, but the second risk, which is a little more subtle, is the risk of missing opportunities. At any point in time, we have to say, "Which of the two risks should I be worried about more today?" You can prevent either one. If you say to me, "Howard, I want to invest, but I don't want to lose any money. I want to be absolutely sure," then, I say, "Okay, we'll put you all into treasuries, T-Bills. You can't lose any money, but you miss all the opportunities."
Howard Marks:	00:59:34	If you say, "Howard, I want to be 100% sure that I don't miss any opportunities," then I say, "Okay, no T-Bills for you, and then your whole portfolio is exposed to the risk of permanent loss." You can prevent one risk or the other risk, but avoiding that risk puts you firmly exposed to the other, or you can compromise, but you can favor one over the other.
Howard Marks:	00:59:59	Think about yourself, your age, your financial situation, your aspirations, what your job pays, how many kids you have, your psyche. You should have ... Every listener should have an idea, even if it's only subjective and qualitative, of what their normal risk posture should be, based on the things I enumerate. That's question number one.
Howard Marks:	01:00:23	Question number two is where should we be today, relative to your normal risk posture? I would say that I would somewhat favor defense. We are fully invested at Oaktree, but our

portfolio embodies a strong insistence on defense. When the market goes up, that means you don't go up quite as much. I think that's the right posture for today, given the description that I gave you.

Demetri Kofinas: 01:00:52 You mentioned pension, pension funds. We have a huge problem in unfunded liabilities in this country, and not just in this country, but in the Western World, generally. Considering all the stuff we just discussed, how serious do you think that looming crisis in unfunded liabilities is, and do you feel that our political system is up to the challenge of dealing with it?

Howard Marks: 01:01:18 I think it's very serious. The problem resides in what are called defined benefit plans. Defined benefit plans are pension plans where every employee is promised a pension, which is a function of his terminal salary, multiplied by years worked. I worked at Citibank for 17 years, and I now already am receiving a pension equal to 34% of my last five years' average salary, 2% a year, defined benefit.

Howard Marks: 01:01:51 When I sit here today, and I get my monthly check from Citibank, I haven't been there in 33 years, it seems almost nutty. It seems overly generous that they're giving me money today for not working there. Well, guess what, everybody else caught onto that. Most corporations have closed their defined benefit pension plans. Governments have not.

Howard Marks: 01:02:15 The big, open and growing defined benefit pension plans are state and city, for the most part, and they put in this much money today. They're going to have to pay you that much money when you retire. The difference will be made up by further funding and investment returns. They need a return. It's called the actuarial assumption to get this much money to be worth that much money X years out. Today it's about 7.5%. You can't easily and safely make 7.5% today. Most funds, even if you ... State and city funds, even if you assume 7.5%, they're underfunded anyway. It's going to be a big problem, when it arrives, when these funds pay out the benefits.

Howard Marks: 01:03:11 Now, a lot of states and cities have tried renegotiating or restructuring their pension funds. There's been some success. Some states and cities have gone bankrupt, in part, to escape these obligations, and they will continue to do so. Illinois, which is one of the less funded plans, insisted on a mandatory restructuring, and the Court said, “No, you can't do that, because the state constitution says that they can't escape their pension obligations.” It is going to be a big problem. Your second question was, can we solve this politically? Right now, no.

Demetri Kofinas: 01:03:48 No, definitely not right now.

Howard Marks: 01:03:49 I mean, you don't hear any discussion of this. You don't hear any discussion of the perilous funding situation of Social Security or Medicare and Medicaid. They're all heading for trouble. The math is inescapable, but nobody's doing anything about it. This is when 30-40 years from now, when we're in the soup, people are going to look back, and they're going to say, "What was that generation doing, in the early part of the 21st century, about their debts to us?"

Howard Marks: 01:04:22 In fact, what are we doing? What are we doing? We are borrowing money, at the federal level and other levels, to spend. Part of the tax cut that was passed in December was a decision to increase the deficit, increase the debt, to give it out as tax cuts. It's a matter of generational equity. The current generation is borrowing to have more stuff today, more spending, lower taxes, et cetera, and they're going to put the burden on the future generation. There's a lot of questions about fairness with that. I remember, when I was a boy, there were debates about whether it's proper for nations to have permanent national debt, proper. It seems nobody's worried about that anymore.

Demetri Kofinas: 01:05:17 Mm-hmm (affirmative), quite the contrary. In fact, there are schools of thought that take the view that public debt doesn't matter at all. I don't know if you're familiar with some of these ideas, but they do seem somewhat ludicrous. Again, they have some of these qualities of bubble thinking, you know?

Howard Marks: 01:05:29 Yes.

Demetri Kofinas: 01:05:29 Impossible ideas, that it doesn't matter simply because the Government has the capacity to print the money, to make good on the nominal debt level.

Howard Marks: 01:05:37 Yeah, well, some do and some don't. The nations of Europe ... Greece would've avoided it's suffering as an austerity, if they would've just printed more money, but there's no more drachma around, so they couldn't. Other countries can print the currencies, but the World may not accept them without severe devaluations. It happens, right now, that the U.S. can print more money. It's the reserve currency of the world, the dollar, and people accept them without severe devaluations. Is that going to be without limitation? It's not clear.

Demetri Kofinas: 01:06:11 When you say that, do you mean that it's unclear whether the dollar will maintain its hegemonic posture in the next decade?

Howard Marks: 01:06:18 And its value.

Demetri Kofinas: 01:06:19 And its value, obviously.

Howard Marks: 01:06:20 Right? Yeah.

Demetri Kofinas: 01:06:20 Well, that's directly related to this pensions crisis, right?

Howard Marks: 01:06:22 Right, sure.

Demetri Kofinas: 01:06:23 Because all these things, the pensions, the debt, these things would all come to a head. Another exogenous factor is climate, right?

Howard Marks: 01:06:30 Yeah, well, climate's going to get us all. I think the climate is not going to change the fortunes of the U.S., relative to Europe. We're all going to suffer probably from what's going on with climate, but the countries that behave with less discipline, they may bear some effects. The point is, right now, the Englishman will take a dollar and give us, I don't know, let's say 75 pence for it. Will they always do that? Or will there be a time when they give us 40 pence? That's what's called devaluation.

Howard Marks: 01:07:05 Weimar, Germany, coming out of World War I, was judged to have certain debt to the rest of the world that they couldn't pay, so they took a thousand mark note, and they put a rubber stamp on it, a million marks, and they said, "Here, you've been paid off." Can they get away with that? These are all open questions, but we've gone quite far down the road from the little subjects we started on, but these are cosmic questions that nobody has the answer to and, in my opinion, nobody's doing anything about it.

Demetri Kofinas: 01:07:37 Mr. Howard Marks, I greatly appreciate you taking so much time. I think I've taken more than enough of your time today. I want to thank you very much for coming on the show.

Howard Marks: 01:07:45 Thank you, Demetri. It's been a pleasure.

Demetri Kofinas: 01:07:48 That was my episode with Howard Marks. I want to thank Howard for being on my program. Today's episode of Hidden

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