

The Narrative Machine: Investing in a World of Tall Tales, Big Games, and Giant Cons | Ben Hunt

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What started as an entirely laudable effort to keep capital markets from collapsing became an entirely problematic effort to turn capital markets into political utilities. — Ben Hunt

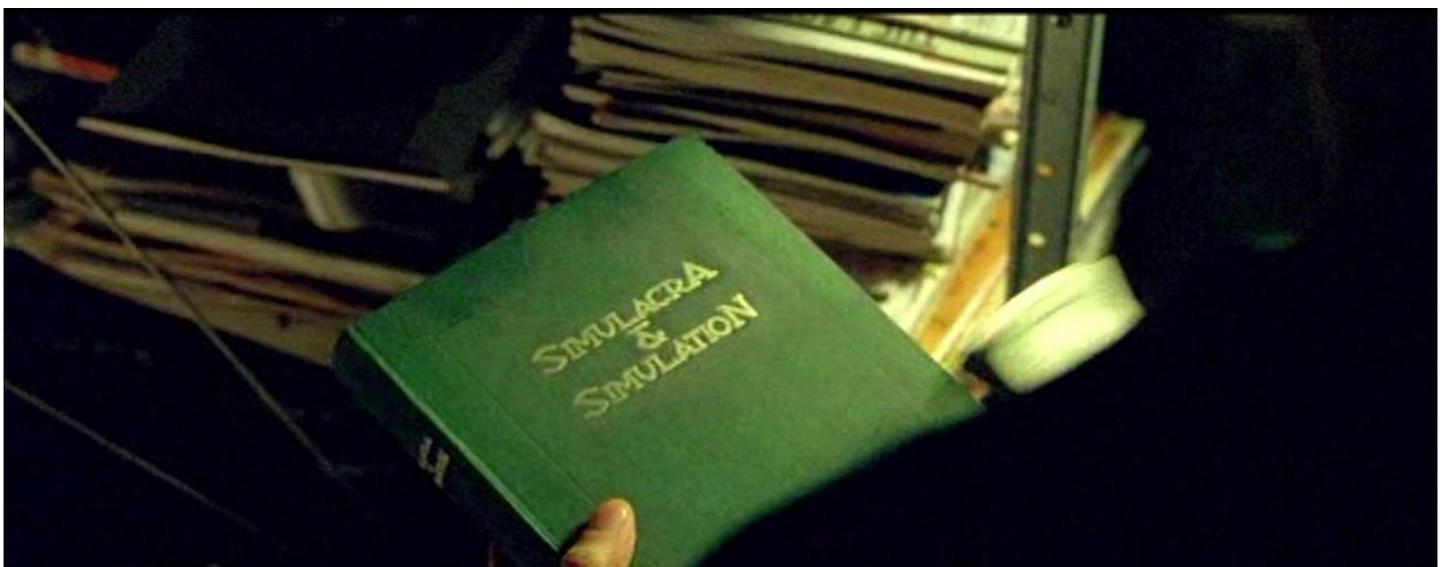
INTRODUCTION

Ben Hunt is the CIO at Second Foundation Partners, a consultant for large institutional investors, and the author of Epsilon Theory, a newsletter and website that examines markets through the lenses of game theory, history and nature. Over 100,000 professional investors and allocators across 200 countries read Epsilon Theory for its fresh perspective and novel insights into market dynamics. In prior positions, Ben has managed a billion-dollar hedge fund and served as Chief Strategist for a \$13 billion-dollar asset manager. He has a Ph.D. from Harvard University, was a tenured Political Science professor, and has co-founded three technology companies. Ben spends lots of time on a family owned farm, which inspires many original ideas on the parallels between human and animal behavior.

WHY DO I CARE?

What I find most interesting about Ben's work is his attempt to wrap his arms around narrative. I'm still unclear about whether or not he believes such a thing can be quantified or how monolithic it is. It seems to me that he is relying upon a metanarrative that is based on a period from the 1950's and 60's of media centralization that no longer exists. In fact, I feel like part of the challenge we face today as investors is that there is no coherent narrative like there was even 20 years ago. In this sense, trying to understand what the "narrative" is requires bridging an epistemological gap for investors that has widened over the decades. Not only must we try and figure out what all the competing narratives are, ascribe to them varying levels of importance, and process them, but we must also account for "narratives unseen" (i.e. narratives working in the background of our minds which we are unconsciously aware of and which influence our perception). For example, when I hear Ben explain what the narrative for Bitcoin is, I must say that I don't find it relatable. This idea that buying bitcoin is like getting a tattoo on your arm (i.e. that you are a bad ass or a rebel) may be accurate, but it is only accurate for a very small group of people in my view.

So, long story short, I'm not convinced that this endeavor is anything other than a fool's errand, and yet, the attempt may be well worth the effort. It seems that Ben's central point is that simply by engaging these themes we can become more aware of how we are being played. Let's see!



THREE-BODY PROBLEM

You did a series of interviews in 2018 where you discussed the problem of complexity in social systems like the stock market. I'd like to explore that here:

Abstraction — Q: Is value investing dead? Q: How long has the quality narrative persisted? Q: Is objective value no longer real? Q: Was it ever real? Has this always been a hall of mirrors? Q: How do we invest?

RISK MANAGEMENT

I want to be long volatility and short abstraction. — Ben Hunt

Profound Agnosticism — Q: How do we manage risk in this world?

MinMax Regret — Q: What do you mean when you talk about MinMax regret?

COMPETING NARRATIVES

Metanarrative — Q: Have you considered the possibility that your narrative about the power of narrative is itself a narrative that was handed down to us as a result of the period of media centralization during the 50s, 60s, and 70s, where it was possible to monopolize narrative so that there was one "narrative" about inflation, stagflation, Soviet Russia, etc.?

Behavioral Algorithms and Social Media — Q: How do you address the fact that there are many, many more individual narratives, and that those narratives are increasingly tailored to our existing biases? Q: What does this mean? Q: Does this dampen the creative destruction of narratives and does it make existing narratives more powerful?

Narrative Momentum — Q: Is there a momentum factor to narratives?

Bleed Factor — Q: Is there a "bleed factor" to narratives or trends?

Algorithms — Q: What do you mean when you talk about algorithms in human terms?

Systems of Social Control — Q: What do you think about systems of social control and self-censorship? Q: How does this relate to all the white male shaming stuff? Q: Who is this really targeting?

Natural Language Processing (NLP) — Q: How do you use this technology in your investing and at Epsilon?

Now what I DO think is advisable, though, is to react to event risk once it actually happens. What I DO think is advisable is to have a plan for what to sell and what to buy. What I DO think is advisable is to measure the dynamics of event risk as it happens and is converted into market-moving narrative, and use that as the trigger for the plan. — Ben Hunt

Let's Explore Some

- (1) Rise of White Supremacy
- (2) Globalization
- (3) Inflation vs. Deflation
- (4) Silicon Valley "Bad" (especially Facebook "bad")
- (5) Privacy vs. Security vs. Connectivity/Free 'Stuff'
- (7) China Global Partner → China Frenemy (China Model) → China Enemy
- (9) Role of Government (Bullish on Government)
- (11) Terrorism/Patriotism
- (12) Isolationism vs. Indispensable Nation
- (13) National Debt (90's vs. Today)
- (14) Climate Change
- (15) Running Out of Oil vs. New Saudi Arabia

Bitcoin/Crypto Narrative — I think there's an interesting angle to consider with respect to Bitcoin that incorporates the great financial crisis and the increasing levels of indebtedness and wealth inequality that have made it practically impossible for millennials or younger to become wealthy or even join the upper-middle class.

The capacity to save has been shattered. Traditional notions of return on capital or dividend investing have disappeared. Financial markets and products are seen as a "scam."

The narrative of bitcoin as both an escape from a soul crushing job market and simultaneously as revenge against those who created the conditions.

- Profound disillusionment with the "system." Millennials feel abandoned by it. This is a rational response and provides a sense of control and identity that is partly generational.
- Millennials feel bitcoin can be a way to claw back wealth deemed unfairly taken by boomer/older generations.
- Bitcoin is seen as a way of escaping wage slavery.
- Clear supply schedule has changed the way these people view money. Ownership of bitcoin is defined by #/21 mill, stackingsats movement, etc.
- Acceptance that life is a Ponzi and bitcoin is no different. New buyers not seen as victims but as new, fellow acolytes.
- Bitcoin replacements as being seen as undue attempts to restart and hamper the so-called revolution.
- All of this being compounded by the fact that mainstream culture now holds wealth and consumer spending above all else, despite it being inaccessible to most people.
- Bitcoin also provides a sense of belonging and hope to many who feel left behind by the recovery.

The image shows a screenshot of a Twitter thread on a dark background. At the top, a tweet by Matthew Haywood (@wintercooled) from July 14, 2019, at 4:31 AM, has 107 retweets and 522 likes. The tweet text is: "1/ Younger generations can't afford to buy property because previous generations have bought up all the plots in order to store their wealth outside of fiat. No worry, these generations will buy up the new Bitcoin 'digital real estate' instead, getting in before old money does." Below this are four replies from the same user, dated July 14, 2019. Reply 2: "2/ Real estate supply is limited by habitable landmass. Bitcoin supply is limited by software. Unlike real estate, you can buy fractions of the digital 'real estate' and transfer it globally for pennies. There's no permission required to buy in and it's a market open to everyone." Reply 3: "3/ I can't see the young today being interested in buying stock either. A company they can't verify the annual reports of versus a digital asset that they can verify." Reply 4: "4/ Bitcoin as digital gold is a great analogy but unfortunately the wider public don't understand why gold is valuable in the first place. Many more think they know why real estate is: competition to buy limited resources drives up price." Reply 5: "5/ Perhaps 'Bitcoin is digital real estate' is a stretched analogy, but Bitcoin really is far more accessible and understandable to the young, who have been priced out of the actual real estate market and will be looking for a way to secure their future wealth." Below the replies is a tweet by Neil Woodfine (@rwoodfine) with a laughing face emoji: "Haha millennials are so irresponsible buying avocado toast when they should be diligently saving their wageslaved fiat to pump my inflation-driven property market bubble." Below that is another tweet by Neil Woodfine with a laughing face emoji: "Bitcoin has no intrinsic value." Below the tweets is a tweet from Squawk Box (@SquawkCNBC) with a video player. The video shows a man in a suit and tie speaking in a legislative chamber. The video title is "REP. MCCARTHY ON LIBRA" and the subtitle is "BITCOIN, LEADER. >> LOOK, I LIKE BITCOIN." The video is from CNBC and was posted on July 16, 2019, at 8:30 AM.