

## LUCRI ALPHA NEWSLETTER NR 39

23 April 2024

Dear Lucri friends,

In this newsletter, we discuss several diverse topics such as hyperinflation, real intelligence, real investments and the role that probability needs to play in your investment process. We look at feedback from the Lucri year-end and revisit the simple portfolio. In line with previous April letters, Freddie Fiat and Pat Productive are comparing their investment results.

### On a lighter note

John's friend: "I just got a puppy for my little brother."

John: "It sounds like a fair trade...."

What should you do if you find a dog eating a dictionary? You take the words right out of its mouth...

Now for your regular teaching on nature: Where would you find a tortoise with no legs? Where you left it.

Why did the chicken cross the road, roll in a muddy puddle and cross the road again? Because she is a dirty double crosser!

### On a heavier note

We have a per capita recession in South Africa. Our population growth rate is currently between 1.5% and 1.6% per annum. Our economic growth rate (growth in GDP) was 0.6% in 2023. So, we are currently experiencing more than two successive quarters of negative growth per person in South Africa.

So, while we are narrowly avoiding a technical recession, we are right in the middle of a per capita recession.

### Quotes

Warren Buffett was asked the following question: "*What makes a brilliant investor?*" He answered as follows: "*You need to control your emotions. You also need to know what you know, and know what you do not know – and occasionally, you act.*"

*"Be content with getting rich slowly – be long term greedy, not short term greedy."*  
Warren Buffett

In his 2024 letter to shareholders, Warren wrote the following: "*Though the stock market is massively larger than it was in our early days, today's active participants are neither more emotionally stable nor better taught than when I was in school. For whatever reasons, markets now exhibit far more casino-like behaviour than they did when I was young. The casino now resides in many homes and daily tempts the occupants.*"

*“An investment said to have an 80% chance of success sounds far more attractive than one with a 20% chance of failure. The human mind cannot easily recognize that they are the same.” Daniel Kahneman*

Lucri agrees. The human mind is not too good at statistics. The majority of people are still being caught by silly advertisements and emotional attacks because they are not thinking for themselves.

*“The trick is to learn to not trust your gut feelings, but rather to discipline yourself to ignore them. Stand by your stock selections as long as the fundamental story of the company has not changed.” Peter Lynch*

*“Volatility is the price of admission. The prize inside is superior long term returns.”*  
Morgan Housel

*“It all comes down to interest rates. As an investor, all you are doing is putting up a lump-sum payment for a future cash flow.” Ray Dalio*

### **Hyperinflation in Germany around 1923**

People used wheel barrows to convey all the banknotes needed for a purchase at the market – which we know already. What I did not know, is that the chance that your wheel barrow will get stolen was much higher than the chance that the cash on the wheel barrow will disappear – because the wheel barrow had real value while the cash was basically worthless!

Please refer to the exchange rate of the German Mark to the pound. This explains why those on fixed income soon joined the poor – savings were wiped out and pension plans became worthless. One Pound was equal to:

Jan 1914 – 20 Marks

Aug 1920 – 310 Marks

Nov 1921 – 1040 Marks

Apr 1922 – 2200 Marks

Aug 1922 – 9000 Marks

Christmas 1922 – 35000 Marks

Jan 1923 – 227500 Marks

7 July 1923 – 800 000 Marks

23 July 1923 – 1 600 000 Marks

31 July 1923 – 5 000 000 Marks

20 Nov 1923 – 18 000 000 000 000 Marks

I know that history does not always repeat itself – but history often rhymes with the present and the future. We know about the depreciation of the Zimbabwe dollar.

Another current example is the deterioration of the Rial (Iran currency) to the US dollar.

### **Charlie Munger (1/1/1924 – 28/11/2023)**

In the previous newsletter, Lucri warned that newsletter readers will continue to hear from Charlie in future.

The following is a Lucri summary of an interview that a reporter had with Charlie:

*“Our investment style has been given a name – focus investing – which implies ten holdings, not one hundred or four hundred. The idea that it is hard to find good investments, so concentrate in a few, seems to me to be an obvious idea. But 98% of the investment world does not think this way. It’s been good to us.”*

*“You have to learn all the big ideas in the key disciplines in a way that they are in a mental latticework in your head and you automatically use them for the rest of your life.”*

*“Much of what is taught in modern corporate finance courses is twaddle.”*

*“You have to know accounting. It is the language of practical business life. Double-entry bookkeeping was a hell of an invention. And it is not that hard to understand. But you have to know enough about it to understand its limitations – because although accounting is the starting place, it is only a crude approximation. Just because you express the depreciation rate in neat numbers does not make it anything you really know.”*

*“How do these super-smart people with all these degrees and higher mathematics end up doing these dumb things? I think it is explainable by the old proverb that to the man with a hammer every problem looks pretty much like a nail. They have learned these techniques and they just twist the problem so it fits the solution – which is not the way to do it.”*

### **Real Intelligence**

With all the talk nowadays about AI, it struck me the other day that we are not talking enough about RI – real intelligence, or authentic intelligence – the kind of intelligence I like much more! You instantly recognize RI when you encounter it. Charlie Munger clearly had an abundance of RI, and was always ready to share and teach. In his own words, it is his duty to remove ignorance and stupidity, starting with himself every day! Charlie referred to RI as uncommon sense – as he rarely encountered it!

### **Measurement of investment success**

Investment success or failure should NOT be measured by the outcome only, as you can get lucky or unlucky. It must always be measured by your investment process, and the probabilities that were in play.

For example, if someone is willing to give you 2 to 1 odds on the tossing of a coin, and you lose the bet – you still have a successful longer term proposition assuming the bet can be repeated many times. Your investment process was sound with the

odds firmly in your favour. If you walk through life, disciplined to only proceed with investments where the odds are strongly in your favour, you will surely enjoy success. You only need to repeat the action a few times before you will enjoy gains. Your investment process was sound – you may be a bit unlucky, but you will still come out on top after a few repeat investments of this quality.

Listen to Charlie on this topic: “*You may rise slowly if you are unlucky, but you are sure to rise!*” In the example where a coin is tossed, there are a winner and a loser. While it is a good example to illustrate odds and probability, it is a bad example of true, beneficial investment. In successful investment, it is highly likely that all parties involved will be winners. A finite, win-lose short term bet is not real investment. A true investor will not take part in this kind of betting. The person with RI are looking for infinite, long term win-win opportunities while searching for an extra-ordinary investment opportunity. Mathematical probabilities will play an important role in true investment – but the outcome will only be known over a period of many years and someone does not need to lose in order for you to win.

### **The simple portfolio**

Please refer to newsletter 38 for a discussion on the simple portfolio. Over the first three months, the R100 000 investment has grown to R109 943. The calculation is as follows for 22 April 2024:

$7.228 \text{ brk.b} \times \$410.09 \times 19.18 \text{ R/\$} = \text{R}56\,852$

$528.11 \text{ STX500} \times \text{R}100.53 = \text{R}53\,091$

The two components add up to R109 943. Now, a three month period is way too short to provide us with any conclusions – but you are welcome to test this against your own portfolios and check whether you could achieve almost 10% growth in rand over the past three month period. We shall return to the simple portfolio in future.

### **Freddie Fiat and Pat Productive**

We introduced the two characters mentioned above in newsletter 27.

Readers may recall that Freddie thought to himself last year: “Let’s see if Pat can beat my R9749 interest that I shall earn in the new investment year.”

Over the past year, Freddie could invest at 8.78%, taking his portfolio from R111036 to R120 785. He earned R9749 in interest before tax.

Let’s take a look at the portfolio performance of Pat over the past year, measured on 22 April 2024:

Name	Share count	Price per share in cent 22 April 2024	Capital value (Rand)	Dividend received past year per share (cent)	Dividend received past year in Rand	End value dividend included (Rand)
British American Tobacco	92	55600	51152	5282	4859.44	56011
Lewis	688.17	4380	29265	418	2792.95	32058
Nuworld	884.69	2800	24771	125.3	1108.51	25880
Coronation	377.71	2980	11255	165	623.22	11878
			116443		<b>9384</b>	<b>125827</b>

Pat had a reasonable year, with the total value increasing from R 114832 to R125827 over the past 12 months, but the severe price decline of British American Tobacco was a strong head wind.

It seems that Freddie was correct – he received R9749 in interest before tax versus the R9384 in dividends before tax that Pat received.

After three years, the scorecard is as follows:

Total interest that Freddie received: R 20 785

Total dividends that Pat received: R 26 643

Capital value in total for Freddie: R 120 785

Capital value in total for Pat: R 125 827

So, for the first three years, the total dividends received by Pat is outperforming the total interest received by Freddie. Over the past year, however, Freddie outperformed on interest received versus the dividends from Pat.

On total capital value, Pat is ahead of Freddie as expected, but the outperformance is due to dividends only. The capital growth was slightly negative.

With the interest rate cycle now close to a peak or already at a peak, Freddie is enjoying a tailwind. Freddie visited his local bank branch and decided to invest the R120785 at 9.25% for the next 12 months. He is therefore ensuring a future interest inflow of R11172.

Pat decides to buy additional BTI shares at R556 each with the R9384 earned via total dividends. After brokerage cost, Pat could add 16.71 BTI shares to his portfolio. The total BTI share count now increases from 92 to 108.71.

With interest rates being relatively high currently, Freddie Fiat is compounding interest quickly – but it is not fast enough to beat Pat Productive overall.

After another year of high interest rates that Freddie could now lock in with a fixed deposit, we shall do the comparison again.

Lucri still expects that Pat Productive will eventually outperform on total capital value, and that the total dividends received by Pat will most likely also outperform the interest earnings of Freddie.

### **Feedback from the Lucri year-end**

Over 2023/2024, from 17 March 2023 to 1 March 2024, 76 out of 86 portfolios enjoyed positive Alpha, representing a success rate of 88%. This is lower than the 95.7% of last year (2022/2023), but higher than the 81% of 2021/2022.

The total portfolio count also reduced slightly from 92 to 86. There are two main reasons for this: Lucri has stopped accepting any new investors, and Lucri also reduced investors that are using platforms with two factor authentication.

Looking back at the past year, the S&P 500 index in America appreciated with 31% before dividends had been added. Value investors like Lucri had a hard time beating the S&P 500 index – only a few Lucri portfolios could beat the American market.

On the other hand, the JSE all share index appreciated only 0.3% over the same time period. With net dividends included, the index could not exceed 3% growth. So, for South African portfolios, it was too easy to beat the index – exactly the opposite described above. The victory in South Africa therefore felt a bit empty – there was no competition.

The stark difference between the market performances in South Africa versus America is almost scary.

### **Lucri housekeeping**

Please always remember to tell me via SMS, WhatsApp, Telegram or e-mail when you move cash in or out of your account.

All comprehensive Lucri communication is only via e-mail. If you send an e-mail to [streicher.simonj@gmail.com](mailto:streicher.simonj@gmail.com), I promise to answer in a few days.

Kind regards and enjoy “Pat Productive” investing,

Simon Streicher