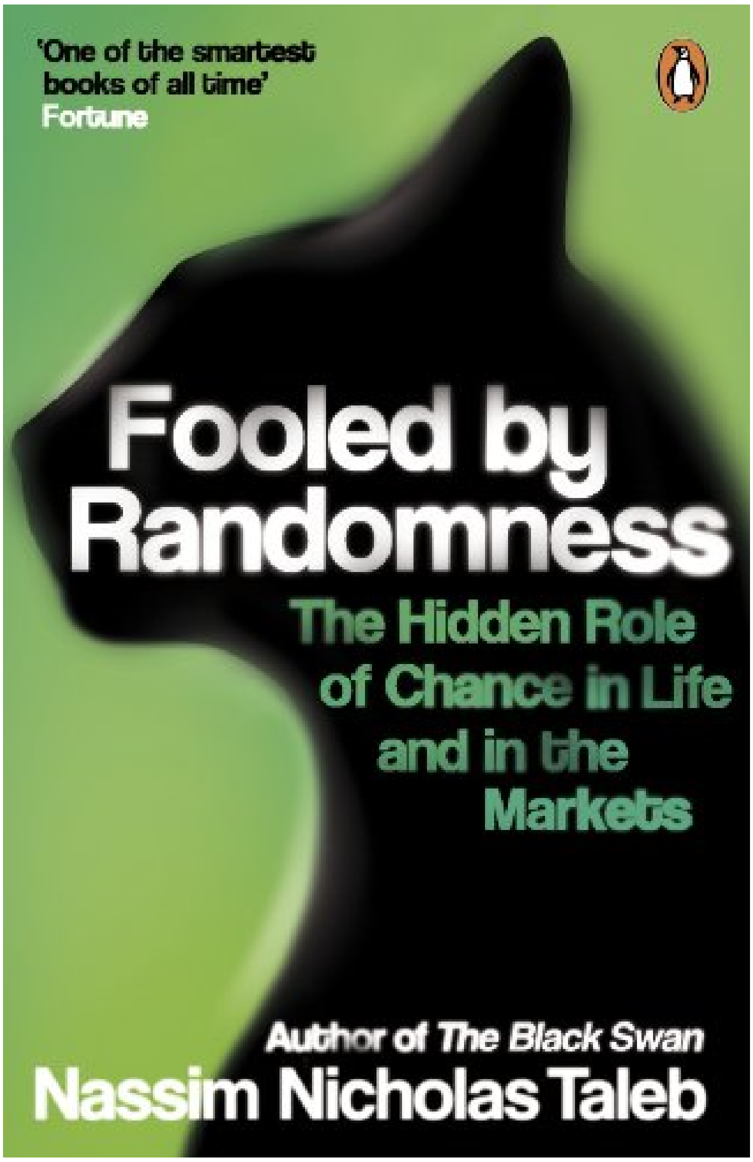
Fooled by Randomness: The Hidden Role of Chance in Life and in the Markets



Par Nassim Nicholas Taleb

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Par Nassim Nicholas Taleb : Fooled by Randomness: The Hidden Role of Chance in Life and in the Markets before purchasing it in order to gage whether or not it would be worth my time, and all praised Fooled by Randomness: The Hidden Role of Chance in Life and in the Markets:

Description :

Prsentation de l'diteurEveryone wants to succeed in life. But what causes some of us to be more successful than others? Is it really down to skill and strategy; or something altogether more unpredictable? This book is the word-of-mouth sensation that will change the way you think about business and the world. It is all about luck: more precisely, how we perceive luck in our personal and professional experiences. Nowhere is this more obvious than in the markets we hear an entrepreneur has vision or a trader is talented, but all too often their performance is down to chance rather than skill. It is only because we fail to understand probability that we continue to believe events are non-random, finding reasons where none exist. This irreverent bestseller has shattered the illusions of people around the world by teaching them how to recognize randomness. Now it can do the same for you..comIf the prescriptions for getting rich that are outlined in books such as The Millionaire Next Door and Rich Dad Poor Dad are successful enough to make the books bestsellers, then one must ask, Why aren't there more millionaires? In Fooled by Randomness, Nassim Nicholas Taleb, a professional trader and mathematics professor, examines what randomness means in business and in life and why human beings are so prone to mistake dumb luck for consummate skill. This eccentric and highly personal exploration of the nature of randomness meanders from the court of Croesus and trading rooms in New York and London to Russian roulette, Monte Carlo engines, and the philosophy of Karl Popper. Part of what makes this book so good is Taleb's ability to make seemingly arcane mathematical concepts (at least to this reviewer) entirely relevant in evaluating and understanding everything from the stock market to the success of those millionaires cited in the aforementioned bestsellers. Here's an articulate, wise, and humorous meditation on the nature of success and failure that anyone who wants a little more of the former would do well to consider. Highly recommended. --Harry C. Edwards ExtraitChapter 1 Croesus, King of Lydia, was considered the richest man of his time. To this day Romance languages use the expression rich as Croesus to describe a person of excessive wealth. He was said to be visited by Solon, the Greek legislator known for his dignity, reserve, upright morals, humility, frugality, wisdom, intelligence, and courage. Solon did not display the smallest surprise at the wealth and splendor surrounding his host, nor the tiniest admiration for their owner. Croesus was so irked by the manifest lack of impression on the part of this illustrious visitor that he attempted to extract from him some acknowledgment. He asked him if he had known a happier man than him. Solon cited the life of a man who led a noble existence and died while in battle. Prodded for more, he gave similar examples of heroic but terminated lives, until Croesus, irate, asked him point-blank if he was not to be considered the happiest man of all. Solon answered: The observation of the numerous misfortunes that attend all conditions forbids us to grow insolent upon our present enjoyments, or to admire a mans happiness that may yet, in course of time, suffer change. For the uncertain future has yet to come, with all variety of future; and him only to whom the divinity has [guaranteed] continued happiness until the end we may call happy. The modern equivalent has been no less eloquently voiced by the baseball coach Yogi Berra, who seems to have translated Solons outburst from the pure Attic Greek into no less pure Brooklyn English with it aint over until its over, or, in a less dignified manner, with it aint over until the fat lady sings. In addition, aside from his use of the vernacular, the Yogi Berra quote presents an advantage of being true, while the meeting between Croesus and Solon was one of those historical facts that benefited from the imagination of the chroniclers, as it was chronologically impossible for the two men to have been in the same location. Part I is concerned with the degree to which a situation may yet, in the course of time, suffer change. For we can be tricked by situations involving mostly the activities of the goddess FortunaJupiters firstborn daughter. Solon was wise enough to get the following point; that which came with the help of luck could be taken away by luck (and often rapidly and unexpectedly at that). The flipside, which deserves to be considered as well (in fact it is even more of our concern), is that things that come with little help from luck are more resistant to randomness. Solon also had the intuition of a problem that has obsessed science for the past three centuries. It is called the problem of induction. I call it in this book the black swan or the rare event. Solon even understood another linked problem, which I call the skewness issue; it does not matter how frequently something succeeds if failure is too costly to bear. Yet the story of Croesus has another twist. Having lost a battle to the redoubtable Persian king Cyrus, he was about to be burned alive when he called Solons name and shouted (something like) Solon, you were right (again this is legend). Cyrus asked about the nature of such unusual invocations, and he told him about Solons warning. This impressed Cyrus so much that he decided to spare Croesus life, as he reflected on the possibilities as far as his own fate was concerned. People were thoughtful at that time. If Youre So Rich, Why Arent You So Smart? An illustration of the effect of randomness on social pecking order and jealousy, through two characters of opposite attitudes. On the concealed rare event. How things in modern life may change rather rapidly, except, perhaps, in dentistry. Nero Tulip Hit by Lightning Nero Tulip became obsessed with trading after witnessing a strange scene one spring day as he was visiting the Chicago Mercantile Exchange. A red convertible Porsche, driven at several times the city speed limit, abruptly stopped in front of the entrance, its tires emitting the sound of pigs being slaughtered. A visibly demented athletic man in his thirties, his face flushed red, emerged and ran up the steps as if he were chased by a tiger. He left the car double-parked, its engine running, provoking an angry fanfare of horns. After a long minute, a bored young man clad in a yellow jacket (yellow was the color reserved for clerks) came down the steps, visibly untroubled by the traffic commotion. He drove the car into the underground parking garageperfunctorily, as if it were his daily chore. That day Nero Tulip was hit with what the French call a coup de foudre, a sudden intense (and obsessive) infatuation that strikes like lightning. This is for me! he screamed enthusiasticallyhe could not help comparing the life of a trader to the alternative lives that could present themselves to him. Academia conjured up the image of a silent university office with rude secretaries; business, the image of a quiet office staffed with slow thinkers and semislow thinkers who express themselves in full sentences. Temporary Sanity Unlike a coup de foudre, the infatuation triggered by the Chicago scene has not left him more than a decade and a half after the incident. For Nero swears that no other lawful profession in our times could be as devoid of boredom as that of the trader. Furthermore, although he has not yet practiced the profession of high-sea piracy, he is now convinced that even that occupation would present more dull moments than that of the trader. Nero could best be described as someone who randomly (and abruptly) swings between the deportment and speech manners of a church historian and the verbally abusive intensity of a Chicago pit trader. He can commit hundreds of millions of dollars in a transaction without a blink or a shadow of a second thought, yet agonize between two appetizers on the menu, changing his mind back and forth and wearing out the most patient of waiters. Nero holds an undergraduate degree in ancient literature and mathematics from Cambridge University. He enrolled in a Ph.D. program in statistics at the University of Chicago but, after completing the prerequisite coursework, as well as the bulk of his doctoral research, he switched to the philosophy department. He called the switch a moment of temporary sanity, adding to the consternation of his thesis director, who warned him against philosophers and predicted his return back to the fold. He finished writing his thesis in philosophy. But not the Derrida continental style of incomprehensible philosophy (that is, incomprehensible to anyone outside of their ranks, like myself). It was quite the opposite; his thesis was on the methodology of statistical inference in its application to the social sciences. In fact, his thesis was indistinguishable from a thesis in mathematical statisticsit was just a bit more thoughtful (and twice as long). It is often said that philosophy cannot feed its manbut that was not the reason Nero left. He left because philosophy cannot entertain its man. At first, it started looking futile; he recalled his statistics thesis directors warnings. Then, suddenly, it started to look like work. As he became tired of writing papers on some arcane details of his earlier papers, he gave up the academy. The academic debates bored him to tears, particularly when minute points (invisible to the noninitiated) were at stake. Action was what Nero required. The problem, however, was that he selected the academy in the first place in order to kill what he detected was the flatness and tempered submission of employment life. After witnessing the scene of the trader chased by a tiger, Nero found a trainee spot on the Chicago Mercantile Exchange, the large exchange where traders transact by shouting and gesticulating frenetically. There he worked for a prestigious (but eccentric) local, who trained him in the Chicago style, in return for Nero solving his mathematical equations. The energy in the air proved motivating to Nero. He rapidly graduated to the rank of self-employed trader. Then, when he got tired of standing on his feet in the crowd, and straining his vocal cords, he decided to seek employment upstairs, that is, trading from a desk. He moved to the New York area and took a position with an investment house. Nero specialized in quantitative financial products, in which he had an early moment of glory, became famous and in demand. Many investment houses in New York and London flashed huge guaranteed bonuses at him. Nero spent a couple of years shuttling between the two cities, attending important meetings and wearing expensive suits. But soon Nero went into hiding; he rapidly pulled back to anonymitythe Wall Street stardom track did not quite fit his temperament. To stay a hot trader requires some organizational ambitions and a power hunger that he feels lucky not to possess. He was only in it for the funand his idea of fun does not include administrative and managerial work. He is susceptible to conference room boredom and is incapable of talking to businessmen, particularly the run-of-the-mill variety. Nero is allergic to the vocabulary of business talk, not just on plain aesthetic grounds. Phrases like game plan, bottom line, how to get there from here, we provide our clients with solutions, our mission, and other hackneyed expressions that dominate meetings lack both the precision and the coloration that he prefers to hear. Whether people populate silence with hollow sentences, or if such meetings present any true merit, he does not know; at any rate he did not want to be part of it. Indeed Neros extensive social life includes almost no businesspeople. But unlike me (I can be extremely humiliating when someone rubs me the wrong way with inelegant pompousness), Nero handles himself with gentle aloofness in these circumstances. So, Nero switched careers to what is called proprietary trading. Traders are set up as independent entities, internal funds with their own allocation of capital. They are left alone to do as they please, provided of course that their results satisfy the executives. The name proprietary comes from the fact that they trade the companys own capital. At the end of the year they receive between 7% and 12% of the profits generated. The proprietary trader has all the benefits of self-employment, and none of the burdens of running the mundane details of his own business. He can work any hours he likes, travel at a whim, and engage in all manner of personal pursuits. It is paradise for an intellectual like Nero who dislikes manual work and values unscheduled meditation. He has been doing that for the past ten years, in the employment of two different trading firms. Modus Operandi A word on Neros methods. He is as conservative a trader as one can be in such a business. In the past he has had good years and less than good yearsbut virtually no truly bad years. Over these years he has slowly built for himself a stable nest egg, thanks to an income ranging between $300,000 and (at the peak) $2.5 million. On average, he manages to accumulate $500,000 a year in after-tax money (from an average income of about $1 million); this goes straight into his savings account. In 1993, he had a bad year and was made to feel uncomfortable in his company. Other traders made out much better, so the capital at his disposal was severely reduced, and he was made to feel undesirable at the institution. He then went to get an identical job, down to an identically designed workspace, but in a different firm that was friendlier. In the fall of 1994 the traders who had been competing for the great performance award blew up in unison during the worldwide bond market crash that resulted from the random tightening by the Federal Reserve Bank of the United States. They are all currently out of the market, performing a variety of tasks. This business has a high mortality rate. Why isnt Nero more affluent? Because of his trading styleor perhaps his personality. His risk aversion is extreme. Neros objective is not to maximize his profits, so much as it is to avoid having this entertaining machine called trading taken away from him. Blowing up would mean returning to the tedium of the university or the nontrading life. Every time his risks increase, he conjures up the image of the quiet hallway at the university, the long mornings at his desk spent in revising a paper, kept awake by bad coffee. No, he does not want to have to face the solemn university library where he was bored to tears. I am shooting for longevity, he is wont to say. Nero has seen many traders blow up, and does not want to get into that situation. Blow up in the lingo has a precise meaning; it does not just mean to lose money; it means to lose more money than one ever expected, to the point of being thrown out of the business (the equivalent of a doctor losing his license to practice or a lawyer being disbarred). Nero rapidly exits trades after a predetermined loss. He never sells naked options (a strategy that would leave him exposed to large possible losses). He never puts himself in a situation where he can lose more than, say, $1 millionregardless of the probability of such an event. That amount has always been variable; it depends on his accumulated profits for the year. This risk aversion prevented him from making as much money as the other traders on Wall Street who are often called Masters of the Universe. The firms he has worked for generally allocate more money to traders with a different style from Nero, like John, whom we will encounter soon. Neros temperament is such that he does not mind losing small change. I love taking small losses, he says. I just need my winners to be large. In no circumstances does he want to be exposed to those rare events, like panics and sudden crashes, that wipe a trader out in a flash. To the contrary, he wants to benefit from them. When people ask him why he does not hold on to losers, he invariably answers that he was trained by the most chicken of them all, the Chicago trader Stevo who taught him the business. This is not true; the real reason is his training in probability and his innate skepticism.From the Trade Paperback edition.