Are you a 'results-oriented' investor? If so, you're making a big mistake, says top poker thinker

Alex Rosenberg | @AcesRose
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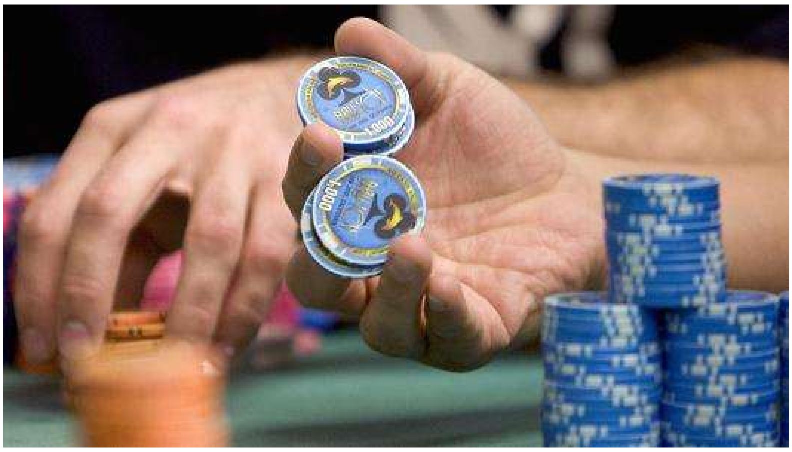

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Put yourself in the following scenario.

Some time ago, after carefully considering a situation and thinking methodically through your options, you decided to take a substantial risk. Unfortunately, it didn't work out, and ended up costing you dearly. As you castigate yourself, trying to figure out what you could have done differently, a colleague comments that you are engaged in "results-oriented thinking." Would you take this remark as praise, or as criticism?

It might depend on what you and your colleague do for a living. While "results-oriented" has a hearty, laudatory ring in many business and investing contexts, it is a common criticism among poker players, as poker coach and writer Tommy Angelo pointed out in a recent phone interview with CNBC.

"In professional poker, results-oriented-ness is something that you want to experience less of — it is considered to be a flaw," said Angelo

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"You might make a really bad play and it comes in well and, because you won, you think, 'I made a good play.' Bad plays happen to win sometimes, and good plays happen to lose," Angelo said.

But of course players shouldn't continue to make unwise bets simply because, for instance, the final card made their hand the winner one particular time.

Yet Angelo observes that the culture of finance "is all about results-oriented-ness — they use the phrase like it's a positive thing. As if, if I return 30 percent, it doesn't matter how I played."

Both poker and investing involve using generally imperfect information to make decisions that stand to be the source of either monetary losses or gains. Another similarity is that for investors, outperforming one's peers involves some combination of making better decisions than them and being luckier than them — the same things it takes to beat opponents in poker. So it stands to reason that experts in the one discipline could have something to teach experts in the other.

When it comes to the interpretation of results, Angelo thinks investors may be making a mistake.

"When investors are talking among themselves, and they're talking about 'How can I improve my game?' or 'How can I get better?'; getting rid of results-oriented-ness should be part of that conversation."

After all, in investing, as in poker, a true professional is trying to make the best possible decisions at all times.

In assessing a prior move, technically the question one ought to answer is along the lines of: "Given all the information I had at the time, was my decision the right one? If I made my decision in each of the universes I could have been living in at the time, with each containing different hidden past events and different unknowable future events, what would the result have been in each? If I assess all of the decisions I could have made and all the universes I could have been living in, and set the appropriate probabilities, which decision on average has the best outcome — with 'best' up for me to define as I see fit?"

Unfortunately, employing such a technique is often impossible, not to mention difficult. So instead, it is common to perform the shortcut that psychologist Daniel Kahneman terms "attribute substitution." When trying to assess the wisdom of a prior decision, rather than attempting to answer the difficult set of nested questions laid out above, we lazily choose to answer an easier one: "How did it work out when I did it last time?"

Of course, this is not to suggest that actual information regarding results is irrelevant. The trouble, for poker players and investors alike, comes in figuring out how to get beyond knee-jerk reactions in order to milk it for critical insights.

"Be process-oriented on short time scales, results-oriented on long ones," advises Aaron Brown, managing director and head of financial market research at AQR Capital Management. "The trick is to know what is short and what is long in terms of your area of risk-taking and strategy."

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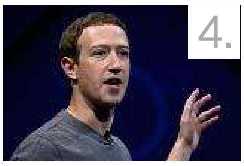

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investors and poker players — but adds an important caveat.

"Quantitative investors think like poker players," he wrote in an email to CNBC. "In poker and quantitative investing, you're making lots of bets with small edges. Therefore it takes very large drawdowns before you question your strategy. Poker players and quantitative investors need the strength to stick to their strategies through the noise of frequent large upswings and downswings."

Ironically, results-oriented thinking happens to be more common — as well as more sensible — among investors who are less reliant on data.

"Qualitative investors and traders tend to make fewer bets with larger edges. Even a single loss is worth exploring for potential lessons," Brown wrote. These individuals "need to be constantly learning."

That is to say, it's not necessarily a mistake for those who make a small number of high-conviction decisions to carefully consider what a specific outcome might tell them about the strength of their process.

So far, so good. But one frequent misstep comes when those making the secondary investment decision of which manger to entrust with their money rely too heavily on results.

"Too many investors chase funds with good three- and five-year track records," Brown wrote, when asked for an example of results-oriented thinking at work. This is especially unfortunate given that "three- and five-year performances tend to revert."

In Angelo's view, the refusal to let rather irrelevant results influence future decisions is just one skill that investors can learn from those who coach poker players.

"A lot of what I offer is just awareness," Angelo said. "Awareness is the most important thing that a trader would need to know if they're going to succeed in the long run. They can't just expend energy on making their 'A-game' better — they also need to lop off their 'C-game,' and the discipline that takes is huge."

For online poker players and computer-based traders alike, Angelo starts by offering an easy tip: Get up and walk a circle around your chair every five or 10 minutes.

"If somebody did nothing but that, I think they would make more money, because they'd be less likely to fall into that trance state where they're not necessarily conscious of the emotional decisions they're making," Angelo said.

In his long-awaited "Painless Poker," Angelo imagines that seven people "reeling in poker pain" are transported to a seminar in which Angelo shows them how to ease the negative emotions they experience playing the game.

"All of the pitfalls that poker players suffer from, and that traders also suffer from, are covered in great detail in the book by way of characters talking about them," Angelo told CNBC. "It's not about trading directly, but there's a lot in there that could be related to trading."

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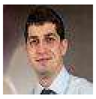

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