

The Disciplined Investor Podcast – Guest Interview Summary

Guest: Jack Schwager

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Summary

Trading Edge and Manager Performance

Andrew and Jack discussed the importance of having a trading methodology with an edge, beyond just risk management. Jack shared insights from his interviews with successful traders, emphasizing that human emotions often lead to worse decision-making than random chance. They also touched on the fact that most fund managers underperform the market, with Jack citing studies showing around 85% of managers do worse than the S&P.

Self-Awareness in Trading Success

Jack and Andrew discussed the differences between the S&P 500, which has minimal transaction costs and fees, and other managed funds. They explored the theme of self-awareness in trading success, noting that successful traders often maintain journals to track their emotions and moods, which can reveal patterns between their psychological state and trading performance. Andrew emphasized the importance of understanding one's limitations and avoiding over-leverage or under-leverage in trading.

Algorithmic Trading and Human Expertise

Jack discussed the evolution of trading, highlighting how algorithms have replaced human traders in high-speed, keyword-based trades. He noted that while algorithms excel in rapid reactions, humans still have an advantage in complex scenarios requiring nuanced interpretation, such as understanding jurisdictional differences in mergers and acquisitions. Jack shared an example of a trader who adapted to the rise of algorithms by focusing on areas where human expertise remains valuable.

Market Efficiency and Trading Opportunities

Jack and Andrew discussed the evolution of market efficiency and its impact on trading. They explored how traders can capitalize on market inefficiencies, particularly in areas like tax rules and bond ratings. Jack shared remarkable stories of traders who started with small accounts and grew their investments to half a billion dollars over a relatively short period,

highlighting the potential for exceptional returns in trading. They also touched on how increased transparency and market efficiency might limit future opportunities for traders.

Jack and George's Book Collaboration

Jack discussed his collaboration with George Coyle on a new book project. He explained how they met through a mutual acquaintance and decided to work together after George sought Jack's feedback on some articles. They divided the workload, with Jack writing commentary on George's chapters and George handling the research and interviews. The book is similar in style to Jack's previous Market Wizard books, and they worked on boiling down long interview transcripts into shorter sections.

Market Wizards' Future and AI Impact

Jack and Andrew discussed the future of the "Market Wizards" franchise, with Jack expressing his willingness to pass on the torch to George if he wishes to continue the series. They also talked about the impact of AI and algorithms on the financial markets, noting that while AI's effects are still not fully understood, algorithms have been influencing markets for some time. Jack shared his accidental entry into the financial industry and what keeps him engaged, emphasizing the ever-changing nature of markets and the requirement for creativity.

Market Timing and Investment Strategies

Jack and Andrew discussed market cycles and investment strategies, with Jack sharing insights from his book "Market Sense and Nonsense." Jack emphasized that the best time to invest long-term is when recent market performance has been poor, citing data showing that periods of low returns tend to be followed by higher returns. He expressed skepticism about the "this time is different" narrative often used by investors, including recent claims about AI. Jack also criticized the efficient market hypothesis, noting that many self-proclaimed experts have unverifiable track records.

Risk Management and Market Efficiency

Jack discussed the trading records of two successful traders, noting one had no down months in 11 years and another had only minor losses over 15 years. He emphasized that while the efficient market hypothesis is incorrect, most investors should act as if it's true due to the statistical advantage of low-cost index funds. Jack shared that Bruce Covner's advice "know where you will get out before you get in" has been a significant influence on his risk management philosophy, as it captures 95% of risk management in one sentence and helps maintain objectivity when entering trades.

Government Market Trends and Book Release

Andrew and Jack discussed the potential impact of government involvement in markets, with Andrew expressing concerns about state-owned enterprises and government ownership. They agreed that while this trend might not continue beyond the current administration, it's a significant development to monitor. Jack also mentioned that his book, tentatively titled "Market: The Next Generation," is scheduled for release next summer around June or July.

Video Games in Trading Insights

Jack discussed his observations from interviewing younger traders, noting their short-term trading orientation and the increasing involvement of video games in their lives, which was a new theme compared to previous interviews. Andrew shared his experiences with early video games and expressed interest in writing a blurb for Jack's book. Both agreed to stay in touch for future collaboration.