

FOCUS ON

# THE STATE OF THE INDUSTRY

Continuing the series of discussions for their Swiss Strategies Think Tank, alternative investment specialists Dr Guenther Dobrauz-Saldapenna of PwC and Nils Beitlich of Credit Suisse chat with legendary US artist and noted political and economics thinker Henry Rollins. The trio discuss the state of the financial markets and value of a systematic approach, as well as the lessons fund managers can learn from rock bands.



## Dr. Guenther Dobrauz-Saldapenna

heads PwC Zurich's Asset Management R&C Services practice. Earlier, he practised with Deloitte and as an attorney. He was also Legal Counsel to a VC/PE firm and to a hedge fund group. He holds a Ph.D in investment law, an MBA degree, and is co-founder of the Swiss Strategies Group.

**GUENTHER DOBRAUZ-SALDAPENNA (GDS):** There is currently a lot of discussion as to what the actual state of the world economy is right now. Some believe that we are heading for a financial cliff with unprecedented consequences, others believe that we have actually already gone over and only hang in the air like some cartoon character thanks to government and central bank gimmicks and will be rushing into the abyss any moment now. Still others believe that by pulling together we have made it, and the worst is behind us although we will be facing an era of austerity for some years to come. What is your take on this? Where do we stand and where are we headed?

**HENRY ROLLINS (HR):** I am not a numbers person. All I can do is read the news and try to connect the dots. However, I do a lot of travelling to some fairly diverse destinations. What I see abroad is what I have seen in America. The money seems to be flowing upwards through everything from bailouts to loopholes in the tax code, breaking-up of unions, no overtime, fewer benefits, outsourcing, and so forth. The money goes to a few and there it sits, out of the economy not doing anything. The owners of the money, the mythical 'job creators' don't seem to do much but get wealthier. I have never seen the virtues of supply-side economics. Those on the demand-side create the jobs when they spend money. So, where are 'we' headed? You are fine, or at least good enough. However, there are other 'we's' in the world. Africa and southeast and central

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Asia, are going to have a tough time and there will be a lot of people who are not going to make it. I think the centre of Africa, parts of eastern Africa and western Mali, for example, will see a population fall off. Austerity is caused by the rich telling the poor to suck it up and get tough. I don't know how much tougher people should have to be in this short life.

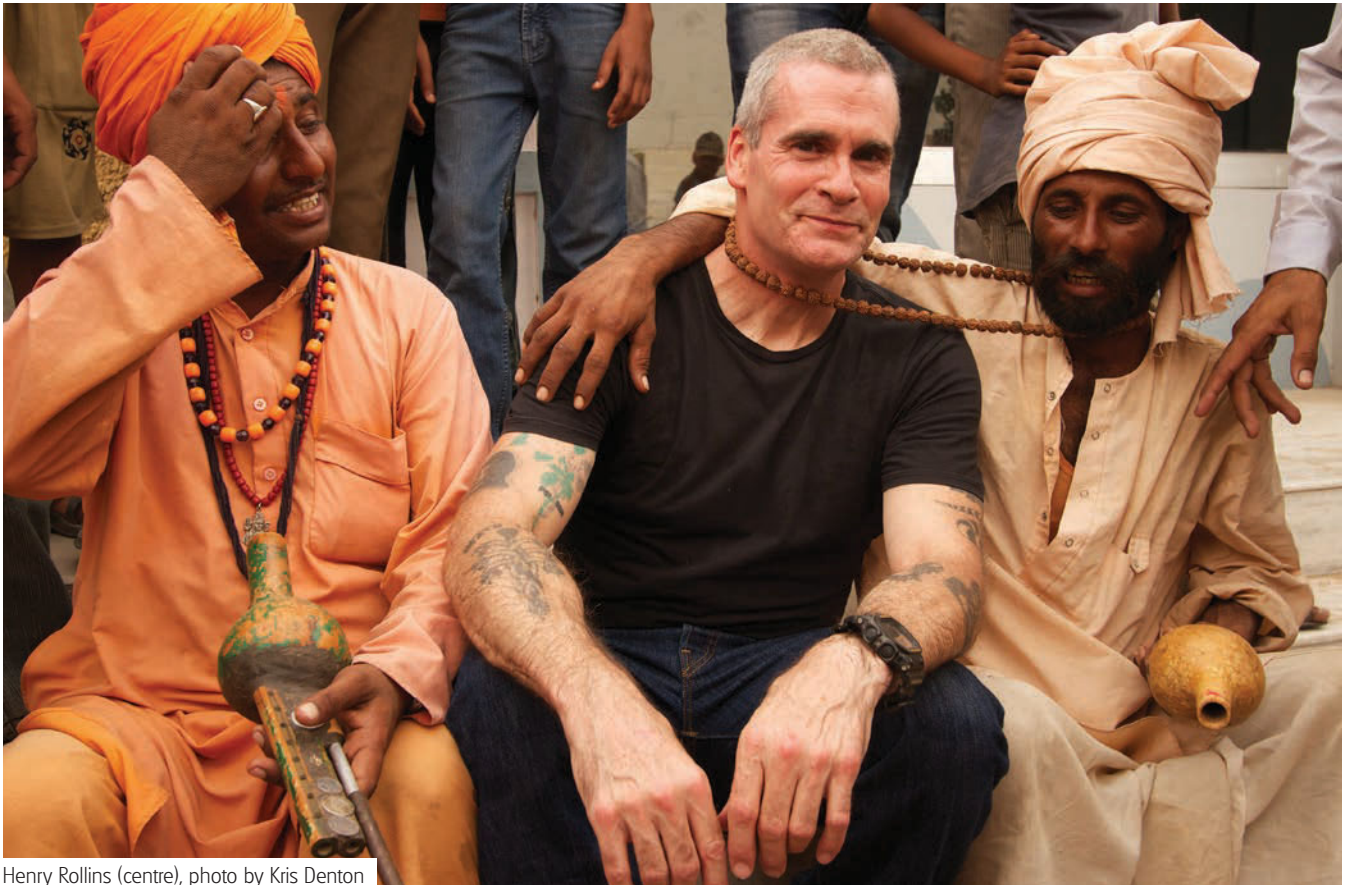
**NILS BEITLICH (NB):** How did we end up in all of this?

**HR:** Simple. The victors write the history books. The rich make the rules. Everyone else has to play by them. You have so much water and other resources and a world population that seems hell bent on proving Malthus to be correct. Humans keep breeding away while again, the money goes up the ladder and there are more people with less. They get by as best they can. The 'mess' is only solved temporarily when people seek to have their populations comport with geographical and ecological limitations – the money doesn't sit so still. I don't think the money is going to be moving anytime soon, so again, a lot of populations will be losing headcount.

**GDS:** Some believe that we suffer from a misallocation of talent based on a skewed incentive system – in terms of monetary rewards, social recognition and moral priorities – resulting in a disproportionately large share of some of our brightest people working in the financial sector rather than dedicating their time to innovation and service to people who may actually help to solve some of our most pressing problems. The counter argument is that it is financial warfare out there and war is the father of all things and in the end pays off. What is your take on this?

**HR:** My take on it is that if that is how the game is going to be played, then it is probably better to be on the winning side. It also lends itself to the saying that when all you have is a hammer, everything looks like a nail. If you see crisis as a revenue stream, you have plenty of people to kill and lots of territory to ravage. It makes sense, if you're a warmongering coward but





Henry Rollins (centre), photo by Kris Denton

hey, that's how some people roll. Again, the victors write the history books. For myself, I cannot carry that much contempt for my fellow man. I'm more on the hospital-building side of things; you know, the 'peace buck' that some people talk about.

**GDS:** Knowledge and information equal power, and in combination with determination and hard work provide the only valid and sustainable path to success. Unfortunately, rather than creating useful means of mass education which would be possible with all the technology available today, ever higher fences are erected and even the most basic principles of, for example, business and economics are shrouded in pseudo-complexity, which in turn creates and sustains an artificial elite. Through our Swiss Strategies Think Tank, we try to demystify some of the things and try to find new ways and solutions by going back to the basics and most importantly by initiating discussions and cross-disciplinary thought exchange. If you were given the chance to speak to the youth of the world and share with them what you've learned about business, investing and how to work with people to achieve great results, what would you tell them?

**HR:** I would tell them that the rich didn't get rich by being generous unless it was a photo op and they were going to get a return on the investment. I would advise that any school teaching them how to 'crack the code' will only get them so far. There is no way you would give your best information to someone who could one



**Nils Beitlich**

is head of Alternative Investment Research at Credit Suisse. Previously, he was a quantitative and qualitative research analyst with a leading hedge fund group that focuses on systematic trading strategies. Nils holds an MSc degree and CAIA certification, and is co-founder of the Swiss Strategies Group.

day come in and infringe upon your revenue stream. Basically, I would advise that they learn how economic structures and platforms work and then start thinking outside of the box with ideas that are not as static and are with the times, like Facebook for example.

**NB:** You've worked hard all of your life and as a result we hope that you've been able to put a little bit aside. We assume that you must appreciate the independence and freedom that comes from a certain level of wealth and disposable income. How do you protect this? Where do you invest in this environment?

**HR:** I have been very fortunate and am well off. Living in America, one would be advised to make as much as you can and stay low to avoid getting caught in the crossfire. I've always invested in bonds and very boring, slow-moving stocks and property. All of these have performed well for me. I don't spend money on stupid things like drugs or eighty pairs of shoes, so I protect my reserves by really not changing the way I live my life all that much. I work every day as I always have, but now I don't have to wonder if I can pay my bills. This allows me to work even more, which I enjoy.

**NB:** Our passion is early-stage venture capital investments and fully systematic trading strategies – the former for the sheer pleasure of working with incredibly passionate people on the cutting edge and indeed with the hope of eventually being part of the next big thing; the latter since we realise that people are flawed. They

are basically driven by fear and greed. This is also what usually destroys most good ventures, and on a larger scale upsets the markets. Systematic trading is based on the recognition of principles. Managed futures systems, for example, try to detect market trends that are in essence caused by human herd behaviour and follow them without emotion, reacting purely on the basis of algorithms and safeguarding the money involved by means of automatically set stops that prevent major losses. Having performed in front of the masses, you surely have seen how human beings react as a collective, singing and moving to the tune. We are by no means arguing for machine over man as a principle, but still in areas such as investments and financial markets we see some value in limiting the human factor and the ability to prevent fraud, as well as creating transparency. Do you see some value in this view?

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HR: I find the irony of that to be amazing, this idea of making things better for people by basically keeping them out of it. Thomas Jefferson repeatedly pointed out that humans are easily corrupted. Perhaps you have something there. In my country, some of the more scorched-earth profiteers seem to tie making money to brutal coarseness like they are schoolyard bullies. These are the ones with multiple divorces and a lot of anger, the fear and greed thing as you pointed out. Gordon Gekko said that greed is good. I think a lot of people agree. I think that they should read up on King Midas.

GDS: True alpha is most likely to come from dedicated, small teams using both the latest in technology and research while still being firmly grounded in common sense. As we know from innovation theory, disruptive technologies usually originate outside the established industries and are most likely to be discovered when specialist knowledge is applied in a cross-disciplinary way, or when experts from different fields collaborate to find new solutions. What's true for technology also applies to investment strategies. In recent years we've seen behavioural finance and pattern recognition segue into the professional investment arena. Similarly, concepts such as the Kalman Filter and Fourier analysis have become applied by systematic traders. Unfortunately, we see many young investment management teams with new ideas struggling to find people to back them. Again, that sounds very

much like what most bands experience when starting out. Having made it yourself, what would be your recommendation to new teams starting out? Do you agree with our aforementioned belief that the next great thing is most likely not going to come from the established players but is being put together this very moment by some dedicated youngsters with almost no budget in a garage?

HR: The Kalman filter, what I understand of it, takes into account irregularities and potential turbulence when making estimates of what is to be. This is not at all my area of expertise. I am just some guy. But it seems to me that we live in a time of great change and movement and with that comes a degree of uncertainty. I think this leads to innovation and allows younger points of view to supplement the more established economic environments. I believe that it is the younger innovators who will make a break with the past and perhaps, to a certain degree, change how the world does business. Perhaps these new methods will engender more peace and prosperity. The old ways are effective but are restrictive to the many who have in part been turned into expendable and easily replaceable tools of industry. The bands I have been in, my small publishing company and all the other things I do for the most part came out of a vacuum into reality by a lot of push, but not a lot of money. We had to be innovative, as we had no budget. Money allows you to succeed but it also can allow you to acquire a fat layer. I was more often than not in a position of being lean and mean and it has served me well. I am not interested in being mean but I like to stay hungry and keep pressing forward to the next thing. That's how I live my life. ■

