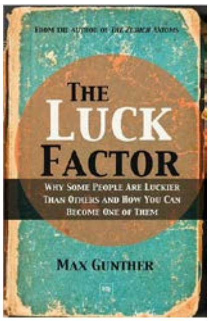
The Luck Factor



Why some people are luckier that others and how you can become one of them

By Max Gunther

One of the books that I learned a great deal from many years ago when I was first learning investment was a book called *The Zurich Axioms* by Max Gunther. I still reread this book from time to time to refresh myself with the insights into investing in this book. Interestingly, the copy that I own does not list any other books by Max Gunther and for years I assumed that was the only book that he had written. However, one day I made a search and found some of the other books that he had written. Among them was a book called *The Luck Factor*. As it happened, I was at that time reading a book called *Little Bets* which mentioned another book called *The Luck Factor* by Richard Wiseman. The latter is a recent book but Max Gunther's book had been written in 1970s and I thought it would be interesting to read it.

The Luck Factor is an easy to read book that is actually in four parts:

The first part is a general introduction to the book and gives a broad definition of luck: events that influence our life and are seemingly beyond our control.

The second part deals with Speculations on the Nature of Luck: Some Scientific Tries, specifically The Randomness Theory, The Psychic Theories and The Synchronicity Theory.

The third part deals with Speculations on the Nature of Luck: Some Cult and Mystical Tries, specifically Numbers, Destiny and God, and Charms, Signs and Portents.

The second and third parts of the book make very interesting reading. Max Gunther explains each of the tries in a way that is sympathetic to its believers and each is illustrated with many personal anecdotes about people he has come in contact with over the years in his search to understand luck.

The fourth part is called the Luck Adjustment and deals primarily with what he calls the five components of the Luck Adjustment. This was by far the most interesting part of the book for me because, in it, Max Gunther distils everything he has learned about what makes some people lucky and other people unlucky under five headings:

- The Spiderweb Structure
- The Hunching Skill
- Audentes Fortuna Juvat
- The Ratchet Effect
- The Pessimism Paradox

I was surprised to find, as I read these last five chapters, just how applicable most of them are to investing and speculating (trading). Here is a brief description of the key ideas:

The Spiderweb Structure

The basic idea here is that the luckiest men and women tend to be those of us who, over our lifetime, have formed many friendly contacts with other people. At the time that we form a contact with other people we will generally have no idea where that will lead. However, if we did, it would of course not be luck when some good fortune emerged from that contact. Luck occurs when something good happens to us as a result of us having made many contacts over our lifetime and one of those contacts is the conduit through which luck finds its way to us.

The Hunching Skill

A hunch is a feeling that we have from time to time that might seem to us a bit like knowledge, but which we feel nevertheless is something that we should not trust as we would with a confirmed fact. What Max Gunther found was that lucky people have a tendency to trust their hunches whereas unlucky people rarely do so. However, it is not all that simple. Not any hunch will do. What lucky people seem to have is an ability to formulate accurate hunches. Even more important, they have great faith in their hunches and act on them, as more timid and unlucky people would not.

What I found even more interesting was Max Gunther's observation that the ability to generate sound hunches was a skill that can be learned. In order to do this there are three rules:

The first rule: Learn to assess the database

One of the key ideas about a hunch is that we don't really know what our feeling is based on. However, it will be based in some way upon the knowledge we have about the general area covered by the hunch. What we can do is to ask ourselves whether we may have, at some time, collected those facts and whether they are likely to be reliable. However, there are two problems to be avoided which Max Gunther lists as corollaries:

Corollary one

Never trust a hunch about someone we have just met.

Corollary two

Never regard our hunch as a way of avoiding the hard work in researching the situation.

The second rule: Never confuse a hunch with hope

This rule concerns a situation in which a hunch is something that you want very badly to believe to be true. These hunches should never be acted upon without further research.

The third rule: make room for hunches to grow

The idea here is that we must learn to trust our hunch is by listening to our feelings, respecting them and considering them carefully. Max Gunther regards this as the most important of the three rules. This rule also has two corollaries:

Corollary one

Don't smother a hunch by over analysing it.

Instead we must learn to focus on we how we feel about the situation. As you think about your hunch ask more and more questions of yourself about how and why you feel the way you do rather than trying to analyse the situation only in a strictly logical way.

Corollary two

Collect soft facts along with hard.

What Max Gunther means hereby soft facts are feelings or impressions that we have about the situation. Those of us who habitually confine our analysis to hard facts are at the opposite pole in dealing with hunches.

Audentes Fortuna Juvat

This is a Latin aphorism meaning *fortune favours the bold*. What Max Gunther is found in this area is that as a general rule lucky people tend to exhibit boldness. On the other hand the least lucky people tend to be the most timid ones. He offers some rules for how to develop the required degree of boldness:

The First Rule

Be always ready to examine and embrace lucky opportunities when we find them.

The Second Rule

Know when we are being bold and when we are simply acting rashly.

The Third Rule

Don't insist on having complete advance knowledge of any situation we are about to enter. It is rare that we can have all the facts. When all the facts are obvious it is usual that we have already missed the opportunity.

The Ratchet Effect

Max Gunther describes a ratchet is a device that preserves gains. What he means here is that allows us to move forward boldly but without slipping back so far that we are wiped out financially. Investors and speculators will recognise this is what they call money management or the disciplined exercise of stop losses. In other words we act now on hunches, but as soon as the situation seems to go wrong we quickly get out before the losses grow out of control. This implies a zigzag process where we undertake a series of risks quickly cutting our losses in those that do not work out while we wait for the few that we allow to build into huge successes. Max Gunther sees two obstacles that unlucky people never overcome, but which lucky people have moved beyond:

The first obstacle

It's too hard to say “I was wrong”.

In explaining this Max Gunther refers to the characteristic commonly exhibited by born losers: an overwhelming need to prove their own brilliance. The born losers will persist with a losing situation far beyond what is reasonable. Lucky people will have jumped out of the situation as soon as they perceived that it was not working out.

The second obstacle

It's too hard to abandon investment.

In this respect Max Gunther sees an investment as consisting of money, love, time, effort, commitment, or a combination of any of those. These investments become defined in our mind as being part of us and we tried desperately to protect them.

Max Gunther goes to some lengths here to emphasise to as that the ratchet effect does not imply that the lucky people are fickle or capricious. They do not seek to change for the sake of change itself or because they have become bored with the situation. As far as luck is concerned Max Gunther finds that only two useful reasons for making a change

A clearly defined piece of good luck has turned up and we see it boldly.

The situation has gone wrong or has met with bad luck.

The way the ratchet works is that lucky people enter attractive ventures that might have otherwise scared them away, but their potential losses are limited by their ability to cut and run when bad luck intervenes. At the same time their potential gains are unlimited.

The pessimism paradox

This is an intriguing idea. We are properly been brought up to believe that lucky people are those who are optimistic. We attach pessimism as a label to those who are unlucky and never see opportunities. However, Max Gunther puts it to us that the truly lucky people tend to be pessimists. As an example he evidences a commodity speculator whose mantra was: “Out of every four trades I'll lose money on three of them”. He believes that the use of pessimism by lucky people is associated with two Cardinal Law's, which interlock rather than being exercised on their own:

Murphy's Law: “If something can go wrong it will.” It is easy to see how this ties into the ratchet.

Mitchell's Law: “Life is slippery like a piece of soap. If you think you have a good grip on it, you are wrong.” Again, this is a fundamental way of thinking that ties back to Murphy's Law and the ratchet.

The way Max Gunther puts these together is "Murphy's Law counsels us not to depend too much on luck, for things are as likely to go wrong as right. Mitchell's law counsels us not to depend too much on our own control over events, for that control is less good than we sometimes like to think. Both laws say: never enter a situation without knowing what we will do when it goes wrong."

Interestingly Max Gunther sees these two pessimistic laws as having an optimistic corollary: "If something goes right don't argue, or to put it another way: when good luck pulls you sideways, let go.”

Conclusion

I found *The Luck Factor* to be a valuable discussion of the idea of luck and how we can use it to better succeed in our lives. To fully understand Max Gunther's ideas the review above is no more than a sketch map. I would recommend that readers who find this subject interesting may be well rewarded by reading the book in its entirety. To my knowledge it is not available in Australia, but I had no trouble finding it on Amazon.