EPISODE 61

Ted Seides: Much More Than a Betting Man

[INTRODUCTION]

[0:00:05.8] Benjamin Felix: This is the Rational Reminder Podcast, a weekly reality check on sensible investing and financial decision-making for Canadians. We are hosted by me, Bejamin Felix and Cameron Passmore.

Our guest today was Ted Seides. He is the host of the Capital Allocators Podcast, which some of you may have listened to. I don't know what you'd call him, a classically impressive guy. Studied at Yale and then did his MBA at Harvard. Ran a hedge fund, what would you call it? A fund of funds? Protégé Partners.

[0:00:37.8] Cameron Passmore: Yeah. Maybe he was trained under David Swensen, the legendary manager at Yale, so impressive pedigree education and experience. Then famously, made that bet with Warren Buffett in 2008 whether or not the pool of hedge funds were BPSV500. He was on the hedge fund side, so I think most of our listeners will know how that bet turned out. That certainly put him on the map at notoriety.

[0:01:05.8] BF: That's right. If you don't know who Ted is, many of the other endeavors, you'd certainly know of the bet.

[0:01:11.0] CP: We talked about that and he was so insightful. This whole active versus passive world is not as black and white at certain levels of wealth. He took a very nuanced discussion around which I thought was incredible.

[0:01:26.9] BF: He shed a lot of grey light on that black and white view that it's very easy to take on the active-passive discussion, which is not something that I expected to feel after the conversation. He definitely made that happen.

[0:01:40.4] CP: He's a nice guy, well-spoken, he was very courteous and we talked for a while after. It was a good conversation.

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[0:01:47.3] BF: Yeah. As we mentioned on one of the recent episodes, we've gotten more diligent with posting episodes and putting links and useful information on the rationalreminder.ca website. If you have anything to say about this episode after you've listened to it, we'd appreciate it. Instead of sending us an e-mail, as much as we appreciate those, head over to the rationalreminder.ca website and comment on this episode's post.

[0:02:12.2] CP: I agree. Love to see you there. Enjoy our conversation with Ted Seides.

[EPISODE]

[0:02:22.4] CP: Ted, welcome to the Rational Reminder. We're so happy to have you join us. I've been a regular listener of your podcast Capital Allocators for a long time. I really enjoy them, and especially the insights that you give us into great minds in this business.

[0:02:38.9] Ted Seides: Well, thanks Cameron. Thanks Ben. Thanks for having me.

[0:02:41.7] CP: You started your career working with David Swensen, who was famous for managing the Yale endowment. In a recent article, you said that David Swensen plays a different game from those in public markets and Yale has much less – I think it's less than 25% of his portfolio in public markets. Can you talk about what you learned and what lessons you learned from David that have carried you through your career?

[0:03:06.6] TS: Well, sure. I learned a lot. He wrote it all up in a book. At the time he wrote the book, I felt like I knew what was going to be on the next page. If you were distilling a lot of what I learned into something that's broadly applicable, I would say the core of how David approached the investment problem, which is pervasive, is he developed a certain set of beliefs about investing. Then he was incredibly good at communicating those beliefs to his constituents, which is his board, his team. Then being very creative about what strategy he was going to use to tie into those beliefs.

For David, a lot of it was in the book. It's an endowment of the long-time horizon that leads to an equity orientation and diversification and he didn't think you are truly diversified in a 60-40 to asset portfolio, so he diversified across other things that look like equity-oriented assets. Then when you really get into the weeds a little bit, what David possesses that very, very few

investors of all types do is just an extreme discipline in being able to stick to the plan and being able to communicate in such a way that encourages everyone around him to stick to the plan.

Then beyond that, there are all kinds of nuances that go into the process of implementation through manager selection. I was just fortunate to start my career working for an absolutely brilliant guy and a great teacher and investor.

[0:04:36.6] BF: Fascinating. As you're talking, I've got more questions popping into my head, but I do want to follow a little bit of the structure that we have in mind. You started Protégé Partners, which was focused on investing in and seeding small hedge funds. Obviously, between your experience of Yale and Protégé Partners, you have quite a bit of experience selecting managers, because that's a lot of what you were doing. If there is one, what do you think is the most important criterion when you're selecting a manager?

[0:05:04.1] TS: Yeah. I mean, I don't think it's fair to distill any complex decision that into a single criterion. If you were breaking it down, and I'd even used the framework I just mentioned about with David. Start with a set of beliefs. The particular investment problem we were trying to solve was just focused on hedge funds. If that's your investable universe, what set of beliefs do you have? For us, they were a few-fold.

The purpose of investing in those assets, or that asset class was to try to generate equity-like returns with less risk than the equity markets. We thought and this again was just something that I had transferred over from a subset of what was happening at Yale, the best way to do that was actually to invest in smaller funds, because hedge funds inherently oftentimes are capacity constrained strategies. Certainly felt that way 20 years ago or so.

That framed the beginning of the set of beliefs that we had about how we were going to implement. Then when you get into that implementation, which is really the core of your question of what's the most important criteria, well there's probably three different buckets; what strategy the manager is pursuing, the structure or the deal between the LP and the GP and then of course, the people.

Now if you could take a corollary of something that Warren Buffett said about companies and industries, if you don’t have the people right, everything else doesn't matter at all. In fact, and

some cases can be worse for you. There's a lot of criteria that you could create that might comprise characteristics of a manager that outperforms over the time. Some of those have to do with alignment and structure and making sure that incentives are aligned as a GP and NLP. A lot of it has to do with training and horsepower and insight. Some of it is just innate skill and drive.

What's gotten more and more difficult over the years is that there are many, many more people who fit into that set of criteria, then end up outperforming and what's become an incredibly competitive marketplace. There are actually very few that possess all those kinds of criteria and still have in an organizational structure behind them, the right kind of capital behind them that allow them to at least be structured to succeed in outperforming.

You come to that last piece of having extreme discipline, there is an element that you simply can't compromise on anything. Something that well, we really like this person, but the strategy is a little bit out of favor. We don't like the value, the underlying valuation of high-yield today, but it's a distressed debt manager, whatever it is. Trying to play through that playbook of having your set of beliefs, understanding a strategy that makes sense to implement those and then having extreme discipline to stick to it is the framework we use to approach that.

[0:08:01.8] BF: That makes a lot of sense. When you think about public equities, which I know they're different things, but think well, public equities, you have market beta. If you're unable to go and find an active manager, you can just take market beta and call it a day. When we're talking about hedge funds or alternatives may be in general, you can't really do that. Do you think that it's – is it something where if you don't have the ability to go through a process like you just explained, or have your own process that you think is better, if you don't have something like that, is it worth pursuing the risk premiums in alternative asset classes at all?

[0:08:36.1] TS: Generally speaking, I think the answer to that is no. There's a lot of subtle currents that you mentioned, right? If you compare 10 or 15 years ago to today, you now have a proliferation of products that you can invest in that comprise risk factor. There's the basic risk factors that we know about in quality and yield and size. Those things didn't actually really exist 15 or 20 years ago. If you wanted to get exposure to small cap value and you didn't like growth, the only way to do that was in a hedge fund, if you could short growth. There are a lot of other ways you can just get the exposures today.

Where that has taken the industry, it is people's definition of what adding value means has changed, because there are more alternatives or as you said alternative beta. Take it from a QR, which was probably the first to mass proliferate different types of products. I'd had a ongoing conversation over time with Cliff Asness about once you know that there's an alternative beta in a strategy, is that strategy likely to be attractive going forward? We could think of a merger arb is a great example.

You now can buy a mutual fund. You can buy an AQR product that give you exposure to all the mergers. When merger arb was really interesting was when not that many people understood it and knew about it. By the time people understand it enough to commoditize it, most of the time that alternative beta is not an equity-like expected return, it’s something less. I think the successful hedge fund strategies is true of private equity as well. Most of the alternative categories are difficult to buy cheaply and get the kind of returns that people have sought in them for the last –

[0:10:33.8] BF: That's a fantastic answer to the question.

[0:10:36.4] CP: Yeah. It prompts so many questions. I'm really curious how, like Charley Ellis was on the investment committee at Yale, is that correct?

[0:10:45.2] TS: Yeah.

[0:10:45.8] CP: He's famous for writing *Winning the Loser’s Game* book, which is an indexer’s almost bible, I think you could say. Can you talk about conversations and how these kinds of conversation would happen when you got such two different worlds?

[0:10:59.1] TS: Sure. I mean, and it's a great question. I think to some extent, Charley's opinion has changed since – I mean, I first met Charley in the early 90s when I worked at Yale. I've had a few endowment chief investment officers on my podcast. Scott Malpass from Notre Dame and Andy Golden at Princeton University and Jim Williams at the Getty Foundation, who have been in their seats for 15, 20, 30 years.

Most of the people in those seats pursuing these strategies, all will tell you that there are only a few dozen pools of capital that are properly structured to pursue these and succeed. It requires an army of people, a small army of people, a small army of talented people. It requires a governance board that fully understands the investment strategies and has the patience to pursue them through difficult times. I think that's right. I think that it's for me, sitting outside of Yale, I can't possibly do what Yale would do.

Let me give you one recent example of that, relatively recent example. I have a friend who has been subject to due diligence from one of these institutions. Was talking to him recently about how the process was going and he said, "Yeah, I think it's going well." He said, "We just had our sixth meeting. They were here for eight hours." Which I said, "Oh, where are they doing it?" "Well, we visited a company with them. They walked through our positions. They updated." Most people don't have the time to dedicate to that type of due diligence. Most people don't have the opportunity to get in that type of depth. By the way, this institution may not even invest with this manager.

[0:12:57.8] CP: Amazing.

[0:12:58.7] TS: To put some color on the depth and the quality of research that some of these endowed institutions put in the problem, I think there's a reason why the returns of say, the top endowments and foundations are better than others pursuing these types of strategies.

[0:13:15.5] BF: When you think about that, think about that level of due diligence and the process that's involved with picking a manager, allocating to a manager. Once that decision has been made, how do whether it was a good decision or not? How do you know that you're getting the outcome that you expected?

[0:13:31.0] TS: Well, the first thing you go in knowing is that you will absolutely have the data to figure out if that was a decision, probably in 30 or 40 years. You know that you can't do that quantitatively, right? That lends you to determining what's the appropriate process to create, so that you can make a decision if you need to make a change. That starts with having some type of hypothesis about why you're investing that's not tied to short-term returns.

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It might be tied to disprovable hypotheses about the underlying investment strategy. It might be tied to your beliefs about the most important people that are there and how engaged they are. It might be tied to a quality of a team. In some instances, it might be tied to the pursuit of an idiosyncratic innovative investment strategy that you're fully cognizant, may go away at some point in time, or that inefficiency arbitrage may go away.

In different situations, you can have different hypotheses. Then through recurring ongoing due diligence and meeting with people over time and talking to people about what's happening in their portfolios, you're sure of consistently retesting and pushing on a hypothesis, knowing all along that there's a lot more noise in the short-term results than there is signal. Of course, that's different across asset classes.

To give you one example in the hedge fund space where I spent a lot of time, there is, Soros talks about reflexivity. There is reflexivity in hedge fund organizations from investment returns. If the hedge fund is not performing well, they could lose good people to other organizations, which makes it more difficult for them to perform all in the future. They tend to be more dynamic organizationally, than say, a long-only value manager who has very low turnover in their positions. In different asset classes and different strategies, you may have to think about time horizons a little bit differently.

[0:15:35.3] CP: A lot of our listeners are retail investors. Do you think the average retail investor saving for retirement should consider an allocation to hedge funds?

[0:15:46.1] TS: Mostly, no. Mostly, they should not. I say mostly, because there are some interesting changes in dynamics in what's happening in the hedge fund landscape that might allow retail investors with the right kind of access to access some good funds. Let me put a little more color on that. What's happened particularly in the last 10 years is a significant concentration in the hedge fund industry. It’s the large firms are getting bigger and bigger and are effectively hoovering up talent that wasn't able to sustain itself at a small firm.

The reason that that's relevant is that some of these large firms, and you could – you may know some of the brand names, or places like Citadel and Millennium and D.E. Shaw and Two Sigma and Lone Pine. Lone Pine is not quite the right example. Viking is a good example. These large

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firms have continued to perform to their investors' expectations and they are now mostly 30 to 50 billion dollars in assets.

If a retail investor has access to a large manager and believes that the market for talent is efficient, or is increasingly efficient in the hedge fund space, which I believe it is, they may be able to get an allocation that's quite different from what they'd be able to get anywhere in the public markets and understand they're not necessarily going to know a lot about what's going on, but there are a lot of really, really smart people that do. That's a little bit of a dangerous strategy, but if you knew what I know, I would say if you're able to get access to some of the very, very successful talented hedge funds today, that actually might be a good way to go.

Now somewhere along the way, you need to have access to someone who's paying attention to what's happening there, because sometimes these organizations can change. It's a bit of a risky strategy, but we're also talking at a time where most people look at public market valuations in the equity and bond markets and wonder if just the underlying betas will allow them to meet whatever their liability requirements, or spending for individuals or institutions. If that's the case, that's the reason why some of these talented hedge fund managers have continued to grow, because you need to find another way to make a buck, if the easy, simple passive way isn't going to get you there.

[0:18:17.3] BF: Access has to be – it has to be restricted I think by definition, right? There's only so much alpha that can go around.

[0:18:23.3] TS: Yeah. Yeah, it's hard. I mean, I think the default to the answer to that question, the default is no. The default is the average retail investor probably should not be investing in these strategies. I think there are exceptions and sometimes the exceptions can be big, but it's not something I recommend for my parents.

[0:18:40.1] BF: It's a great way to put it. You gained quite a bit of notoriety, or whatever you want to call it with your bet with Buffett. If you Google your name, maybe your podcast comes up more than the bet now. After the bet with Buffett, it would be easy to label you as someone that does not believe that investing in index funds is a good thing, just because of the side of the bet that you were on. What do you think about indexed funds?

[0:19:02.6] TS: I think, it's funny that you said that. It would be easy to label me that way. That really is based on a perception of someone making some assumptions that may or may not be correct. I have always thought that index funds are a terrific tool for most investors. I say most, because most investors do not know why they might be beating the market. You have this wonderful opportunity to just join the market and pay next to nothing for it.

As I mentioned earlier, it's not clear to me that just doing that will be a great outcome for a lot of people for the next 5, or 10, or 20 years, but it may be the best alternative for people who don't otherwise know that they're pursuing a strategy that's likely to beat the market, because for sure, all these other strategies are expensive. No, I'm a huge fan of index funds and always have been, but I made a particularly bet at a particular point in time, so people can make their assumptions they want about what I think.

[0:20:05.3] CP: Given that there's only so much alpha to go around, I assume there's very little fee compression in the hedge fund world, or is that a false assumption?

[0:20:12.2] TS: It is a really interesting question today, because the hedge fund world has very much become a binary setting of the haves and have-nots. For the industry as a whole, there is fee compression. For a long time, I would say that the industry fee look liked a 1.5% management fee and a 20% incentive fee. For most of the participants in the hedge fund industry, the fees are lower than that today and continue to come down.

Now I say it's binary, because there have been a few recent examples of larger funds that in order to restrain their asset size, have been increasing their fees. One of the ones I mentioned earlier, D.E. Shaw earlier this year, I don't remember the exact numbers, but I think they went from 2 and half and 25 to 3 and 30. It was a mechanism that they were trying to use, so that their clients could self-select, they wanted to restrain their asset size.

[0:21:07.1] CP: Would this be also in the institutional world? Didn't matter who the client was?

[0:21:11.4] TS: Didn’t matter who the client was.

[0:21:12.7] CP: Wow.

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[0:21:15.9] TS: When investors of all types are absolutely willing to pay for real alpha, and when it exists, people will pay very richly for it and are happy to do so.

[0:21:27.3] BF: Which is exactly what you'd expect if the market is – if that market is efficient. If you have consistent alpha, you will raise your fees and people will pay.

[0:21:34.6] TS: That's one plausible outcome.

[0:21:37.0] BF: Right. Yeah. You mentioned your parents, if you had to tell your parents, or if you do tell your parents how to invest their money, what do you tell them?

[0:21:42.8] TS: Well, my parents don't listen to me when it comes to investing anyway. They're older, so it's pretty traditional. I had an uncle who passed away a couple years that was the chairman of Capital Group in California, the wonderful mutual fund company. My parents have always had their equity allocations invested with Capital. I was very comfortable for them, because there was a personal familiarity to it. It was very comfortable for me, because it's a wonderful organization and terrific way to get exposure.

My parents have had some mix of a stock bond portfolio through Capital's funds. As they've gotten older, they shift more and more towards bonds. I mean, it's a fairly simple asset allocation and a fairly straightforward path to try to get them what they need as they're now retired and living off of those savings.

[0:22:29.8] CP: You live in a country where indexing is absolutely exploding with the popularity of Vanguard and iShares, much more so than we're experiencing in Canada. Do you have concerns about too much the market becoming indexed?

[0:22:41.9] TS: Not anytime soon. I've had this conversation with Charley Ellis and a bunch of other people. People can go back and forth on what percentage of the market needs to be active in order to have efficient price discovery. If you asked Charley, he says 10%. Other people think we're close to that point.

Passive per se in terms of investment allocation isn't troubling. What is troubling is the ramifications that has on the governance of the underlying companies that will drive the returns.

You could imagine if you have 95% passive investors that corporate executives could do whatever they want, because their shareholder base would never turn over. That's a real problem.

We have some problems in the US relating to the short-termism that is set up in incentive structures in an executive compensation and how managers are paid and all kinds of things that have not been addressed for a long time.

There are some people starting to, or at least starting to try to address that. In terms of actual size, my hunch is that there's still a very large universe of dollars that should be a natural audience for index funds in the US, but are still in some more active strategy, mostly owing to that history and tradition and less the conscious decision that a low-cost alternative is better for that person.

[0:24:08.2] BF: You just answered the question that I want to ask, but I can ask you and dig into a little bit more. In the states less so than in Canada, there's still a ton of assets invested in public equities in actively managed mutual funds with high fees. I agree, there's probably alpha in hedge funds if you know where to look. In public markets, it's a bit more dicey. Why do you think people are still investing in that stuff?

[0:24:33.1] TS: If you want to be really aggressive, there's probably some percentage of money that is not financially literate to understand these trends. I have no idea how to put numbers on that. That's the skeptical end of it. I think that the US market for index funds is actually quite different from most other markets around the world, in that say the S&P 500 is very diverse with a lot of global leading companies.

If you were to look in, say emerging markets, there are a lot of countries where the index is dominated by a very small number of enterprises and they tend to be either state-owned enterprise, or a utility. They're not the dynamic companies in the economies. Just an active strategy to not be forced to own certain concentrated names makes a lot of sense in a lot of countries around the world. In the US, it's just less the case. I mean, there are concentrations, or there's concentration and technology that's really driven the S&P 500 in the last 10 years or so, but there's just – it's just a dynamic diverse economy.

I think that's one of the reasons why index funds make a lot of sense in the US and probably make more sense in the US. I don't really know the composition of the Canadian economy, but I know there's a lot of energy and there's a lot of minerals and mining. The question is you want all your assets exposed, not only to those sectors, but those are the sectors by definition that are going to drive the economy. You could be working in some other part of the Canadian economy. If you had all your money in the same drivers of GDP and that softened and the country starts doing worse, are you more at risk of getting laid off? Is the banking sector more at risk because it's lending to real estate that's owned by people in that sector? The more concentrated economy is into a certain sector, the less diversification you get by investing your personal assets in that sector as well.

[0:26:34.9] CP: You've been around very wealthy families and hedge fund managers that also have very high levels of wealth. I'm curious your observations as to how wealthy people behave and how they decide to invest their money as their wealth level increases.

[0:26:52.1] TS: I think there’s a lot of different ways to answer that. There's a difference between people who have money and that people who acquire money over time. The one thing that's consistent across those people is, once they have some comfort of financial flexibility, they do what they want. There's a line that Charley Ellis, as we mentioned earlier, taught me a long time ago. He said, money makes people more so, or money makes people more of what they already are.

Someone who's generous might become more generous. Someone who is greedy might become more greedy, because there's less resistance and people treat them a certain way, but they just have the flexibility to do what they want. In terms of how they invest their money, I watched this very carefully in the hedge fund industry, you do see people as they generate a lot of wealth, often get a little bit more conservative.

Most people that have substantial amounts of wealth that wasn't inherited made it by taking significant risk. Once they make it, they don't necessarily continue to take significant risk with it. People may diversify. They may get a little more conservative in what it is they were doing. That's some of the effect of how you see people change with different levels of wealth.

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[0:28:12.1] CP: You mentioned concerns about market beta going forward and I agree, evaluations are high. That's a bit scary. If you talk to someone with I don't know, 200 million dollars to allocate today, in broad terms, what would you be telling to do?

[0:28:25.9] TS: Well, I think that conversation has – I've been involved in this exercise with a good friend of mine in the last couple of years. That conversation has to start with who's the person, what are they trying to accomplish, how they want to get there? That doesn't mean, hey, I need this money for my living expenses, certainly at that size of wealth. Some people with 200 million dollars desperately want to make 2 billion. Some people with 200 million desperately don't want to lose 20 million and get to a 180.

Depending on what their objectives are, dramatically colors the strategy. If you had a pool of capital that had a lot of duration to it, because there wasn't a lot of spending in that size, I would be quite equity oriented. You can start with a baseline of different market exposures that you want access to in the public markets. Then as I'm managing that capital, I'm going to lean on relationships with managers that I've had over the years that I think are truly exceptional and invest capital with them and then constantly be looking for something interesting new and different.

[0:29:28.1] CP: Interesting. Through this conversation and other conversations that I've had recently, the importance of relationships, if you're seeking something more than market beta, the importance of relationships has come up repeatedly, which I find very interesting.

[0:29:40.6] TS: Yeah, I think that's right. Long ago when I started in this business, it really felt like a relationship business. Then it got away from it for a while, because Wall Street – certainly, the hedge funds space, Wall Street came in and effectively intermediated. They had capital introduction groups whose job it was to match buyers and sellers. After a while, there were so much of that activity that it gravitated back to relationships again.

Yeah, I think that having the right networks to be able to access and find great investment ideas is pretty important. It's one of the reasons why where we started some of these large endowments have been able to perpetuate returns, because they have long histories of being demonstrated to be a very long-term, very supportive and very critical investor. The managers who have benefitted from that over a long period of time are more than happy to refer to them

the people they think also meet their high standards. That is a network of people that the vast, almost nobody else has access to.

[0:30:46.4] BF: Amazing. Yeah.

[0:30:48.2] CP: On a recent podcast, we talked about how the last 10 years of the returns in the US market were so – outside the expected realm of possibility, it was an extreme event. This is also the same time period where you had your famous bet we talked about earlier with Warren Buffett. Can you talk about how that – how you look back on that bet and how that bet might have affected you personally?

[0:31:12.0] TS: Oh, sure. Those are two different things. I mean, there's an investment side and then there's a personal side. On the investment side, I think anytime you're involved in markets, or anytime you're involved in any decisions, you want to try to get better at making decisions. I went into the bet with a certain hypothesis that didn't really have to do with hedge funds being superior to the market. They're quite different. They're really apples and oranges. It's not hard to recall what happened in 2008 in the public markets. This bet started in January 1 of 2008.

I went into the bet thinking, "Boy, with the valuation as high as it was on the S&P 500 and most everybody fairly complacent that that is a long-term trend that will just continue, you pretty much want to be invested anywhere else." That Warren saying, "Oh, hedge funds couldn't beat the market was just a bad bet." This was my hypothesis, because he was picking the S&P at a historical all-time high.

Whether it was hedge funds, or treasury bills, or real estate, or farmland, it almost didn't matter. I would have taken that bet against the S&P 500. Now as it played out, that was the wrong bet. It looked really good for about a year and a half and then the fed came in and the S&P over that 10-year period, despite starting at a historically high level, had historically average returns.

Then you look back and say, okay was I wrong? Did I miss something? Did you miss that the market is always going to recover itself? At one point, I called Warren and I said, "Yeah, I'm trying to figure out my own decision process here. When we started the bet, my partners and I had said, we thought we had – I don't remember what the number was. An 80% or 85% chance of winning and you said you had a 60% chance of winning. Now when you talk about it, you

make it sound like it was a fait accompli, that because of the fees you were always going to win. Do you remember why you said 60%? Was it because the market was rich?" He said, "No, I don't really remember."

He didn't have a robust thesis. He was just plying it to hope to make the point that fees in hedge fund world are expensive. I came out of it saying, I actually still don't think it was a bad bet at the time. There was one outcome, it ended up being a bad outcome. It was over a long period of time. I tried to write that up. When you write something up, people give you all kinds of flack for it in public, but that's fine.

Personally, it's been incredible, right? I had never met Warren before. I've spent a lot of time with him. It was this interesting platform to be able to talk in some nuance about these kinds of issues and all kinds of issues. All kinds of neat things happened from the time I spent with Warren, everything from Jack Bogle showing up at his annual meeting, that actually came out of one of the dinners I had in Omaha, to a few other pretty niche-y cool things that you never could have anticipated. Some terrific friendships came out of it. I guess, there's some infamous name recognition, which is fine, but I didn't really care about one way or the other.

[0:34:30.8] CP: What a great story. Thank you for sharing.

[0:34:32.9] BF: All right, so valuations are high again. Would you make the bet again now?

[0:34:38.7] TS: I got asked this a lot over the last couple of years and I said I would not make the bet again, but let me explain why. I wouldn't make the bet again, because I don't think the odds of winning are as favorable as they were now or 12 years ago. I don't think the markets priced any differently, but hedge funds have changed a lot.

The assets managed in these hedge fund strategies is a multiple of what it was 12 years ago, so the competition is higher. You have the impact of all of this proliferation of ETFs and factor-based products and what that does to the markets. You have a movement of quantitative investing and that's really making it difficult for fundamentally-driven investors to short stocks and be successful.

There are a lot of dynamics that would lead me to believe that the expected return on a long short equity hedge fund, a similar long-short equity hedge fund is going to be lower going forward than it was. Then there's this one factor that's the easiest to describe and the most impactful on hedge fund returns that very few people talk about, which is simply the nominal level of interest rates.

The bet started short-term rates, or maybe – I don't remember what it was, about 4%. Today, they're close to zero, and that is a 4%, maybe 3% annual difference in performance, just because of the short rebate on the way long-short funds are constructed. That's a very meaningful detriment to hedge fund returns in the current environment. I think that it's probably 50/50, if you had a good hedge fund portfolio versus the market for the next 10 years. I would never make what I thought was a 50/50 bet in public with Warren Buffett.

[0:36:17.2] CP: Okay, got it. I just want to shift gears for a bit. We share with you the same podcast producer in Mat Passy and you told us earlier that that is thanks to you making the introduction to our common contacts. Shout out to Mat. Can you talk about the impact that your podcast, the Capital Allocators has had? Is it been a surprising experience? What has come of it?

[0:36:39.7] TS: Sure. Well, it's been really terrific and again, big shout out to Mathew. Many of the investment podcasts that people listen to are produced by him and he really does an extraordinary job and makes all of us seem much better at this than we actually are.

I started the podcast as a way to connect more broadly with people I knew in the investment community, in a way that I was able to when I was only focused on hedge fund strategies. That's been a lot of fun. I just have a great passion for connecting with both people and ideas. Those two can go together, but are also quite separate.

It's been personally, that's been very rewarding. I think there's been a pleasant surprise and you mentioned it in Google searching my name. I assumed that no matter what, the bet and having lost the bet to Warren would be part of my public legacy, and I wasn't going to be able to do anything about that. I was not expecting that doing a podcast would broaden people's at least knowledge of me and what I've done.

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In particular, like I mentioned, when you write something that you think is thoughtful and you put it out in public as I did a few times relating to the bet, people mostly still would see me as an arrogant hedge fund guy. They'd make the same assumptions that Ben talked about earlier about, "Oh, you must love hedge funds. You must hate the index fund. You must think this is terrible for everybody." People make all kinds of assumptions.

When you're on a podcast, you're interviewing people, you're putting yourself out. It's your voice. It's your thoughts and ideas. That's been rewarding, because I've been around the industry a long time and I thought I knew lots of people, but the breadth and quality of the people I've been able to connect with just from having done this has been really extraordinary. It's been a real gift personally and professionally.

I've been pleasantly surprised by the amount of goodwill it generates. On my show, I do the interviews. I think I'm not the – I do maybe 5% or 10% of the talking. It's the people who come on who do all the heavy-lifting. Yet because of the audience, all kinds of – almost every single guest gets some at the least, dozens and dozens of positive e-mails from friends and in many instances, some positive business development, or otherwise. That's been just terrific and building up and I called building up goodwill on my personal balance sheet.

[0:39:05.5] CP: When you think about how you spend your time, obviously the podcast takes a lot of time I'm assuming. I know ours takes quite a bit of time to prepare for. When you think about how you spend your time, what do you wish that you could do more of?

[0:39:17.5] TS: I think we all wish we had more time. I think I'd love to find a way to sleep more. Probably not what you had in mind. I have been engaged in a bunch of different things without one full professional activity for the last couple of years. That's allowed me to do the podcast. I've been working with a friend of mine helping him kind of oversee his portfolio. I've been always thinking about what bigger thing might I find to do next.

I've actually done this at a period of time where I feel I've had a tremendous amount of time. Maybe it's the opposite. Maybe the way I'd like to be spending more of my time now is to be more deeply focused on investing, or with an investment management firm. That's probably the direction I'm headed and hopefully can bring the podcast alongside.

[0:40:03.9] BF: Very cool. As you move into that potentially next stage, how do you define success for yourself?

[0:40:09.2] TS: I'm always reminded of a dear friend of mine who I went to business school with. She tells me that on the day we graduated, I said to her, I wish her all success in the world, whatever that means to her. I don't remember saying it, but it resonated so strongly with her that she remembers. For me, the most important barometer of success is my personal happiness and fulfillment. That takes all kinds of forms and family and relationships, professional engagement.

A newer one is deep authenticity and trying to be very true to myself and the people that are around me. There's always some measure of financial success, which I define as an absence of having to worry about whatever it is the future. I certainly had some success at Protégé and then life circumstances change, and so I still have much of the same worry that many people do, but it would be nice to get to a point where I didn't have to worry about that. Then the last one, the one I've been focusing more on in the last few years is ensuring a high volume of quality connection with other people.

[0:41:17.2] CP: What a great answer. I must say, Ted, I echo what you're saying about the podcast. This experience of interviewing and getting a chance to meet you is an example of that. We started this podcast inspired by the guys with animal spirits.

We have a mutual friend in Barry Ritholtz, who we met through podcasting. It's been an amazing a year, a little bit more than a year for Ben and I and I really want to say thanks to you for being willing to join us on our podcast. Hopefully, you keep up your podcast for a long time, because I am a huge fan of it. Thanks Ted very much for your time.

[0:41:49.9] TS: Thanks, Cameron. I really appreciate it.

[0:41:51.1] BF: Thank you, Ted.

[0:41:51.6] TS: Thanks, Ben.

[END]

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