



Epsilon Theory

HAVING NICE THINGS AGAIN #1 | BY RUSTY GUINN

The Acrobat and the Fly

No, nothing makes sense, nothing seems to fit
I know you'd hit out if you only knew who to hit
And I'd join the movement
If there was one I could believe in.
Yeah, I'd break bread and wine
If there was a church I could receive in,
Cause I need it now
To take the cup
To fill it up, to drink it slow
I can't let you go
And I must be an acrobat
To talk like this and act like that,
And you can dream, so dream out loud,
And don't let the bastards grind you down.

— U2, *Achtung Baby*, "Acrobat" (1991)



It's no secret that a conscience can sometimes be a pest
It's no secret ambition bites the nails of success
Every artist is a cannibal, every poet is a thief
All kill their inspiration and sing about their grief
Over love
A man will rise
A man will fall
From the sheer face of love
Like a fly from a wall
It's no secret at all

— U2, *Achtung Baby*, "The Fly" (1991)

Maybe because of their popular appeal, or the fact that our society can't abide a person like Bono with unapologetic *earnestness* about his beliefs, or because of the band's retreat into musical

weirdness and emergence into arena bombast, U2 has been treated rather uncharitably by modern commentators. But at their best, U2 were mesmerizing. Stylistically, I prefer *Unforgettable Fire* or *War*, and for sheer songwriting genius, *Joshua Tree* remains one of the greatest albums ever recorded.

But where art about making art (e.g., *La La Land*, *Birdman*) can sometimes veer toward self-indulgence, *Achtung Baby* reaches a different kind of peak. It is raw and self-critical, with no attempt at final redemption. I mean, it is melodramatic as all hell, which is kind of the concept of the whole album, but if its arc carries any absolution for the artist, it is that hypocrisy is the universal result of art and not some unique moral failing. *Every artist is a cannibal, every poet is a thief.*

But in the end, neither the artist's cannibalism nor the poet's thievery invalidate their art. *You can dream, so dream out loud, and don't let the bastards grind you down.* There's a narrow lesson in this that goes like, "You can still read *Ender's Game* even though Orson Scott Card once ate a Chick-fil-A sandwich." But there's a bigger lesson, too: if you go around looking for hypocrisy in your enemies, you'll always find it. Doing so will always feel good. Doing so will rarely get you closer to truth, beauty or love.

I was recently explaining to a friend and former colleague what I write about on *Epsilon Theory*. They asked me if it was a behavioral investing blog, and I wasn't sure how to answer.

In a sense, yes, of course *Epsilon Theory* is a behavioral investing blog. We believe that humans and the stories they tell heavily influence, and sometimes determine asset prices. And we write about that. But when most people say "behavioral economics" or discuss investment strategies that account for investor behaviors, what they usually mean is "cognitive biases." Yes, we write about those things, too.

But except in the way that all human activities are influenced by the way that our brains evolved to process information, *Epsilon Theory* isn't really about cognitive biases. That isn't because we don't believe in those biases. Quite the contrary. Instead, it is a recognition that our biased brains are riding on meat puppets that spend most of their time interacting with other meat puppets. Our brains are rarely tasked with drawing conclusions from raw data. Most of the things that matter to us and our lives are social. That means that the stimuli that reach us, the basis for our judgments and opinions, are usually the outputs of other compromised brains, processed through established cultural and social structures.

It is intuitive that understanding and mastering our own biases should mean not only being aware of innate evolutionary impulses, but also understanding how they manifest in social behavior. This is what Ben meant when he wrote about acknowledging our own vulnerabilities to the introduction of memes and Narrative in [This is Why We Can't Have Nice Things](#). We like to think that we operate from internally coherent, epistemologically sound ethical, social and political frameworks. You don't. I don't. We don't. We're making it up as we go along and we all know it.

It is rarely possible to divorce ourselves completely from the ways in which our human brains are wired to respond to society that is increasingly aware of the ways in which other human brains are wired to respond. We cannot pretend that it doesn't change anything that companies like Tesla and

Salesforce now seek to foster rabid audiences and stabilize their stock price through targeted social media engagement strategies — what we write about on these pages as Missionary activity. We cannot pretend that it doesn't change the priors that drive how we build investment portfolios that standing governments consider markets to be utilities for maintaining public order and assent, and actively employ communications strategies to establish Narrative around fiscal, monetary and trade policy.

And so it is that in our investing lives, and in our public, political lives, it is very difficult to refuse to play the game. Ours is a Narrative-driven world, and surviving in it means doing more than understanding how our biology predisposes us to cognitive biases. It means understanding how our engagement with social structures and with one another creates new biases and pitfalls altogether, a kind of special susceptibility to brutal logical fallacies. Many of these are so-called ecological fallacies, discussed in an ET [note from 2013](#) that still reads very well.

Ben wrote recently that the memeification of information — the transformation of Emails into *Emails!* or Lyme disease into *Lyme disease!* — is a big part of why we can't have nice things. I want to suggest to you that it is possible to have nice things again. **Real conversations with other people that result in real outcomes.** Perhaps even a move back in the direction of Cooperative Games from the Competitive Game we are in today. I argued in my [essay from last August](#) that this would require a critical mass of well-intentioned people willing to give up on, to lose, non-existential battles. I also warned that you wouldn't like my advice. In the interest of providing you with yet more unsolicited advice that you won't like, allow me to outline the four Competitive Game equilibrium-enforcing strategies I think we must give up if we're going to make ourselves and our thinking less vulnerable to memes, abstractions, tribalism and Narrative.

Know in advance that in a Competitive Game, each of these four is a dominant strategy. To wit:

- The People Who Disagree with Me are Hypocrites
- The People Who Disagree with Me are Stupid
- The People Who Disagree with Me are Evil
- The People Who Disagree with Me are Controlled

If you give up using these strategies as I will recommend to you, you will lose. You will lose credibility. You will lose standing. You will lose popularity. People will believe you are losing arguments. People will believe you are less intelligent. People may believe you are less committed to ethics, morality and justice.

Wondering where you can sign up yet? Good. We're going to lose so much, you're going to be so sick and tired of #losing.

You're Too Biased to Measure the Impact of Hypocrisy on Credibility

Before we get too far, however, let's get one thing out of the way: the people who disagree with you really are hypocrites.

I don't know the people who disagree with you and I don't need to know. Hypocrisy has been the human condition since Adam proclaimed his holiness by blaming the apple eating on his wife (I mean, it was kind of her fault, if you think about it). But the game of find-the-hypocrite isn't really about finding gaps between the behaviors people condemn in others and the actions those people

take themselves. We all know those exist, and I hope you came here for meatier arguments than, “We’re all hypocrites, so live and let live, amirite?” No, the game is about how we go about *quantifying* that gap. Who is the bigger fraud, the bigger phony? It’s also about *why* we seek out hypocrisy in others.

You might think that this strategy would be played out by first looking for the worst actions and then aligning them with incongruous statements of condemnation. Turns out that isn’t exactly the case. Four Yale researchers in psychology published a [fascinating study](#) in 2017 on this topic. It’s a well-written, very digestible bit of research based on cleverly formulated questions. A rarity for such papers, I recommend reading the whole thing. It holds a few interesting insights:

- People attribute more moral value to condemnations of bad acts than to claims of good acts.
- People will forgive admitted actions that don’t jive with values, but they won’t forgive bad acts that conflict with condemnations of bad acts.

In other words, what people hate about hypocrisy isn’t the immoral act, or even the gap between values and actions. It’s the intentionally **false signal** from moralizing about the act. And while the paper doesn’t suggest this directly, it is my belief that this aversion is one reason why excessively strong signaling or moral condemnation, when coupled with even suspicions that someone may be acting in conflict with those signals, is so distasteful to many of us. You’ve heard of **virtue signaling**, I presume.

The gulf between a false signal and simple conflict between values and action may seem like a distinction without a difference, but it isn’t. It *matters* that our anger about hypocrisy is not the response to a moral failure, but to a failure in ideological signaling. That means that it is an opportunity to assault the credibility of those signaling.

It just so happens, of course, that credibility is one of the most important social signals we send, and one of the ones that matters most in Narrative-driven political, financial and other social and civic markets. The mechanisms of credibility within social capital are so pivotal to influence, wealth generation, capital formation, new lead generation and popularity in general that signaling “I am a credible person” becomes for many of us an objective unto itself. We may complain about Missionaries and their attempts to influence us, but we would all be Missionaries in a heartbeat if we could. For those who have read my piece exhorting us to [Make America Good Again](#) (and to stop worrying about being great), you won’t be surprised to learn where I come out on this issue. Those who have built on the sands of [cringeworthy credibility signaling](#) may come to a different conclusion.

One of our most potent weapons for winning the credibility game — or so we perceive — is seeking out and identifying hypocrisy in others. We are attracted to assaulting hypocrisy for two reasons. First, it acts as a credibility signal for us. It tells others that we are players in the great game. It tells others that we care about logical consistency and other Good Things. Second, it acts as a credibility reducer for our opponent. It challenges and reduces their believability and standing, and seeks to insinuate that they care less about intellectual honesty and logical and moral consistency. In effect, it is a force multiplier for our arguments, because once we establish that another party has made hypocritical statements, we can summon that spectre again and again to relieve us of the need to dispute further arguments on their merits.

There's just one problem with this: **we are hopelessly prone to bias in our assessments of others' hypocrisy.** Why? Because our anger about hypocrisy doesn't begin with systematic, objective observation of moral failures or flawed reasoning under our value system. It begins with our selective observation of moral, philosophical or intellectual condemnations made by others — and guess what? We tend to pay a little more attention when someone condemns someone we like or something we believe in. In other words, when someone expresses a criticism of us, our friends, our allies and their behaviors or actions, we are simultaneously inspired to diminish that person's credibility to protect our ego, **and** to search for actions that conflict with their condemnation. It's like handing a three-year old a club and telling him that other boy over there took his favorite toy.

It's an overwhelming bias that seems so obvious and non-partisan in its pervasiveness when you step back to view it with as much dispassion as any of us can muster. It's why the political right quickly finds every example of a preening Hollywood numbskull moralizing about some progressive social justice issue right before they end up in TMZ for abetting the abuse of young actors and actresses. It's why the political left is lying in wait for any Bible-thumping family values Republican politician to get caught in an ethics scandal. It's why there are millions of people still penning gotcha pieces on the hypocrisy of Bill Clinton supporters who criticized the moral failings of Donald Trump and why millions of people are still writing pieces on the hypocrisy of Donald Trump supporters who had criticized the moral failings of Bill Clinton. Claims of hypocrisy aren't about morality. Claims of hypocrisy are about ideology.

But *Hypocrisy!* the meme isn't about either of those things. It's about *credibility*. And *Hypocrisy!* the meme is warm, wet garbage. In those rare moments when we are honest with ourselves, we know that the reason we accuse others of hypocrisy rarely has anything to do with a good-faith belief that it justifies devaluation of their opinions or arguments which would often stand on their own merits. Likewise, research tells us it has next to nothing to do with any moral objection on our part. No, we do it because we know that those we disagree with will use this same technique at every opportunity to devalue us and those we agree with. We know that not responding in kind makes us vulnerable.

I saw a [lovely anecdote](#) recently from Ethics and Public Policy Center fellow Pascal-Emmanuel Gobry recently, which expresses a similar idea somewhat more succinctly:

My high school best friend's dad was one of the most talented jazz guitarists of his generation. When my friend was a kid, he asked his dad if he could teach him to play guitar. The dad was of course thrilled. "I'd love nothing more in the world, he said. But first, you'll have to learn music notation and music theory and chords. Then I'll teach you to play."

My friend, being a wiseass, retorted, "Paul McCartney never learned any of that stuff, and it didn't stop him." My friend's dad, being a wise man, replied, "Yeah, but you're not Paul McCartney."

Yeah, in the *Bible* Jesus calls people broods of vipers and whitewashed tombs. And Paul, and the Prophets, and saints, used salty language. Yes, there are times when such language is called for. But the reality of original sin means the odds of you using this language out of pride overwhelm the odds of using it because of the necessities of speaking love in truth.

You're not Paul McCartney.

Whatever social structure or biological impulse evolved in us to make us respond the way we do to hypocrisy makes us uniquely unsuited to routinely rely on our detection of it as an indicator of anything other than our own bias. Neither you nor I are Paul McCartney (unless you are Paul McCartney, in which case, hello, thank you for reading and what is the weird chord in the second half of the third verse of "Let It Be" when you sing "Mother Mary" because I've been trying to figure out what's happening there for 20 years).

I should be clear about the narrow point I am making, and the point I am certainly not making. From a moral and ethical perspective, there is no particular reason why being biased should prevent us from holding one another accountable for dishonesty, hypocrisy and other flaws. If we only spoke up about injustice and error when we had no dog in the fight, we would comprise an ugly society indeed. But I hope that you can see the difference between the impact of bias on the justifiable use of it as an argumentation technique and the justifiable reference to it in good faith efforts to improve our own behavior or of those who we love, trust and want to grow us with as humans.

Being a Hypocrite Doesn't Make You Wrong

Even if we can play a mean left-handed bass and believe that we are capable of being even-handed in using accusations of hypocrisy as an element of our political and social engagement, it doesn't take long to recognize that doing so is frequently counterproductive to the whole point of that engagement in the first place. It's pretty simple. If what you care about is being *considered* right and winning those arguments, then the *hypocrisy!* meme is the right tool for the job. If your objective is to get to a better policy or portfolio outcome, then it isn't.

The next time you're looking to bring this tool out in an argument or disagreement, ask yourself: does this person's false signaling really devalue the argument he or she is making? The data he or she is using to support it? Or is it just a tool I would use to discredit this person so that I don't have to bother with the whole debate? It's a bad, biased heuristic.

Consider Warren Buffett, the investing world's moralizer-in-chief. Here he is on leverage.

Once having profited from its wonders, very few people retreat to more conservative practices. And as we all learned in third grade — and some relearned in 2008 — any series of positive numbers, however impressive the numbers may be, evaporates when multiplied by a single zero. History tells us that leverage all too often produces zeroes, even when it is employed by very smart people.

Here he is [in 2003](#) on derivatives:

No matter how financially sophisticated you are, you can't possibly learn from reading the disclosure documents of a derivatives-intensive company what risks lurk in its positions. Indeed, the more you know about derivatives, the less you will feel you can learn from the disclosures normally proffered you. In Darwin's words, "Ignorance more frequently begets confidence than does knowledge."

Guess who sold protection on a bunch of munis starting in 2007, not entirely different in scope, although admittedly in scale, from similar trades that sunk AIG around the same time? Guess who, according to [research from AQR](#), has historically generated his returns through effective leverage of 1.6-to-1?

For someone like me, who is convinced that randomness would almost certainly produce a Buffett or two through sheer chance rather than skill, applying the *hypocrisy!* meme is tempting. I am envious of his reputation, and I hold the good-faith belief that people who follow what Buffett does are focusing on things **that don't matter**. I believe that the people who follow what he says about index funds place too much emphasis on costs and too little emphasis on getting the right **level** and **sources** of investment risk. It is so easy for me to justify why it isn't just correct, it's the *right* and *moral* thing to do to throw this guy under the bus for hypocrisy, to try to reduce his influence.

Except he really is an incredibly thoughtful investor with innumerable traits I wish I had, wisdom our world would be worse without, and perhaps the keenest insight into the role of temperament in the success of the investor we've seen in the last 50 years. The Competitive Game strategy says to seek to diminish him — to make ourselves the Fly. To kill our inspiration to sing about our grief.

But that's just the meme talking. The fact that Buffett's views on leverage and derivatives are insanely hypocritical don't change the fact that he has a tremendous amount of investment wisdom to share.

Letting Ourselves Off the Hook

Maybe the worst harm this tick has in store for us, however, is the doubt it sows in us. You and I are both hypocrites. There's a fine balance between internalizing the moral importance of honesty, consistency and forthrightness on the one hand, and not internalizing the *hypocrisy!* meme in ways that would cause us not to champion causes and values we believe in simply because we know we can't live up to them on the other. This is a real danger.

In many cases, our hypocrisy is just growth. When I was 23, I put myself at odds with some genuinely nice and thoughtful people I worked with and for. Why? Because I was an arrogant ass who knew that no one could build and code a model as quickly and efficiently as I could, and because I knew that my skills in this area were creating all the company's value. Except that wasn't true. *Of course* it wasn't true. I was a stupid kid with no concept of the value of different people and skills. Should I let this moral failure keep me from teaching young analysts today that modeling is a commodity skill? That their real value in an organization will come from cultivating trust, honing temperament, identifying business drivers that matter and becoming better communicators?

In some cases, what looks like hypocrisy is just the reality of a world of contradictions. I've written and, yes, moralized about the things investors waste time on, and the things they should focus on more. In these pages, I've condemned bad behaviors, like focusing too much time on picking stocks, on picking funds, on fees over other costs. And yet, like many who agree with me on these topics, I still spend far too much time doing each. I've spent days trying to figure out if my largely systematic framework for selecting U.S. stocks for our wealth management business is missing something on consumer brands. I've spent more time thinking about General Mills and Colgate-Palmolive than I have about things that I know will have greater long-term impact on financial markets and investor outcomes. But I know that these things are important to my clients, too. I know that it matters to them to understand what they own, and why, in a very qualitative sense. And if it matters to them, it matters to me. The hypocrisy that seems so clear in others is not always so cut and dry when we apply it to ourselves with all the details. Our life and work are complicated.

We are complicated, too. Today I relish the trappings of my Texas identity, but it wasn't always that way. It took me five seconds to decide where I would go to college when the opportunity to escape a

small town in southeast Texas presented itself more than 20 years ago. While I can't imagine harboring that sentiment now, there's a part of me that can't figure how much of that reformed identity is affectation, a resistance to things I didn't like about living in the northeast, or an authentic expression of my values. We're all complicated, conflicted, growing and changing, and there's no nobility in allowing the *hypocrisy!* meme to cause us to withdraw from figuring out our own small issues, or helping our communities and societies figure out the big issues.

This isn't some weird attempt to present hypocrisy as moral, or something we should be more or less prone to forgive or criticize. None of that. It's awful and you should stamp it out wherever you see it whenever you have the standing with someone to be influential. It is about how you will respond to the tick, the meta-meme of *hypocrisy!* that seeks to shut off people you would learn from, deepen your falsely held belief in your tribe's moral superiority, and short-circuit your own brilliance out of false-humble feelings driven by knowledge of your own hypocrisy.

Now because by reason of those daily sins of which I have spoken, it is necessary for you to say, in that daily prayer of cleansing as it were, "Forgive us our debts, as we also forgive our debtors;" what will ye do? Ye have enemies. For who can live on this earth without them? Take heed to yourselves, love them. In no way can thine enemy so hurt thee by his violence, as thou dost hurt thyself if thou love him not... In this he is as thou art: thou hast a soul, and so hath he. Thou hast a body, and so hath he. He is of the same substance as thou art; ye were made both out of the same earth, and quickened by the same Lord. In all this he is as thou art. Acknowledge in him then thy brother.

— Saint Augustine of Hippo, *St. Matthew's Gospel*, "Sermon on the Lord's Prayer"

The most painful realization of all in a world awash with Narrative, of course, is that the people who disagree with us are not especially hypocritical or contradictory. It is that they are our brother. Our sister. Made out of the same earth. And probably every bit as smart, upstanding, independent-minded and, yes, flawed as we are.

When we stop telling lies about why we disagree and start telling this truth, we can grapple with the uncomfortable fact that our brothers and sisters saw the same facts and came to different conclusions. As Narratives force us into ever narrower bands of acceptable views on markets and politics, the speech we must tolerate becomes more uncomfortable, and will feel more extreme. It will also feel more contradictory. Friends, if you would end the Competitive Game, if you would triumph over tribalism, you must learn to tolerate some hypocrisy — in yourself and in others. You must embrace the Acrobat and not the Fly. How?

Dream out loud, and don't let the bastards grind you down.

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