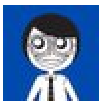
Twitter Thread by Kostas ■■■ ■ ■



Kostas ■■■ ■ ■
@itsKostasWithK

The Baltimore Stockbroker Parable

How one stockbroker managed to achieve a 100% success rate in predicting stock movements

/THREAD/

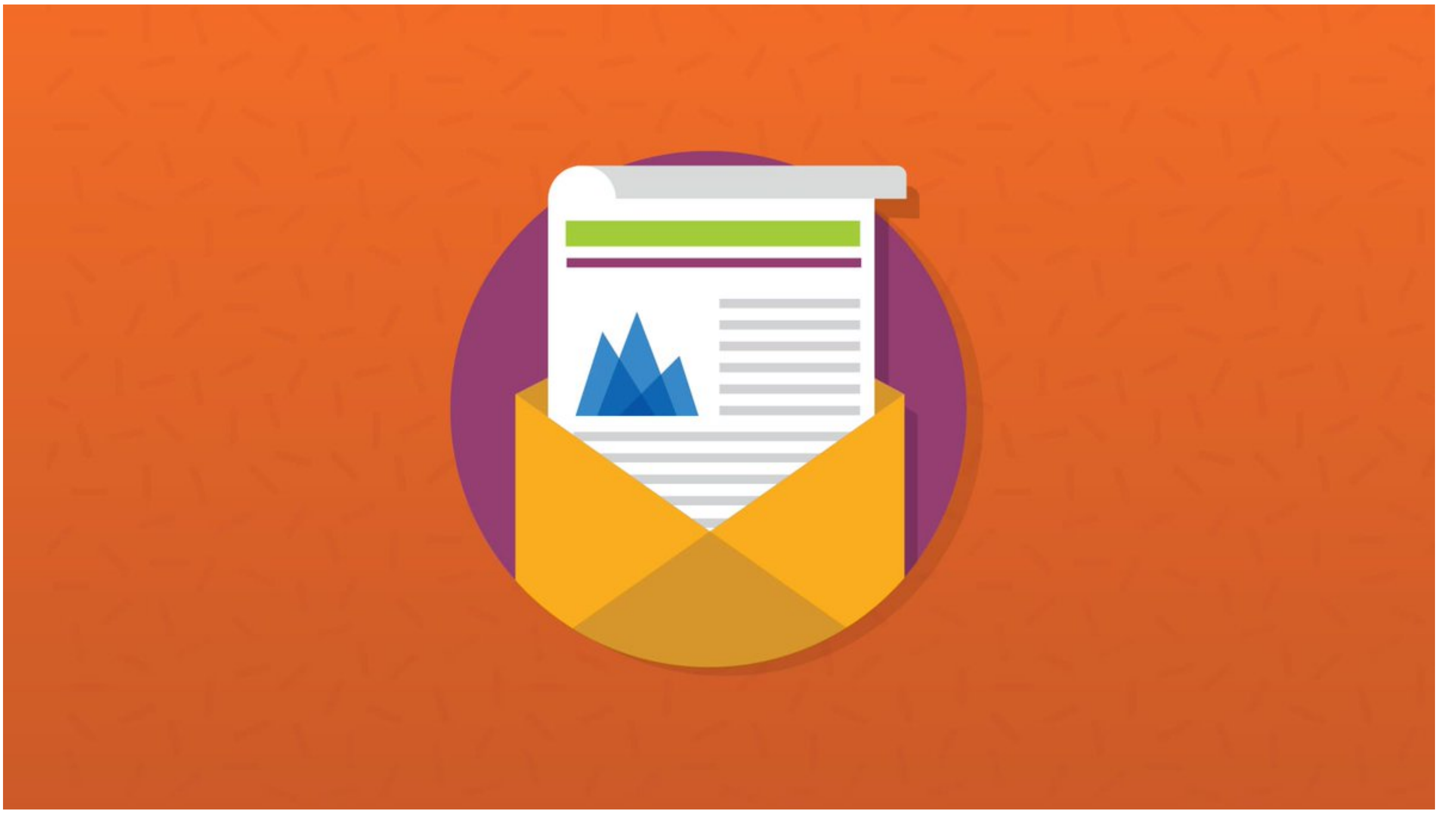
1/ One day you receive an unsolicited newsletter from a stockbroker in Baltimore.

It contains a tip that a certain stock will soon rise sharply.

A week passes, and as he predicted, the stock goes up.

2/ The next week, you get another newsletter from the stockbroker, this time with a tip about a stock that will fall.

And next week, the stock craters.



3/ Ten weeks go by, and each week you receive a tip about a stock that will go up or down.

Every time the prediction comes true.

4/ On the 11th week, you get a solicitation to invest your money with the Baltimore stockbroker for a hefty commission, justified by his successful predictions.

That sounds like a great deal, right?

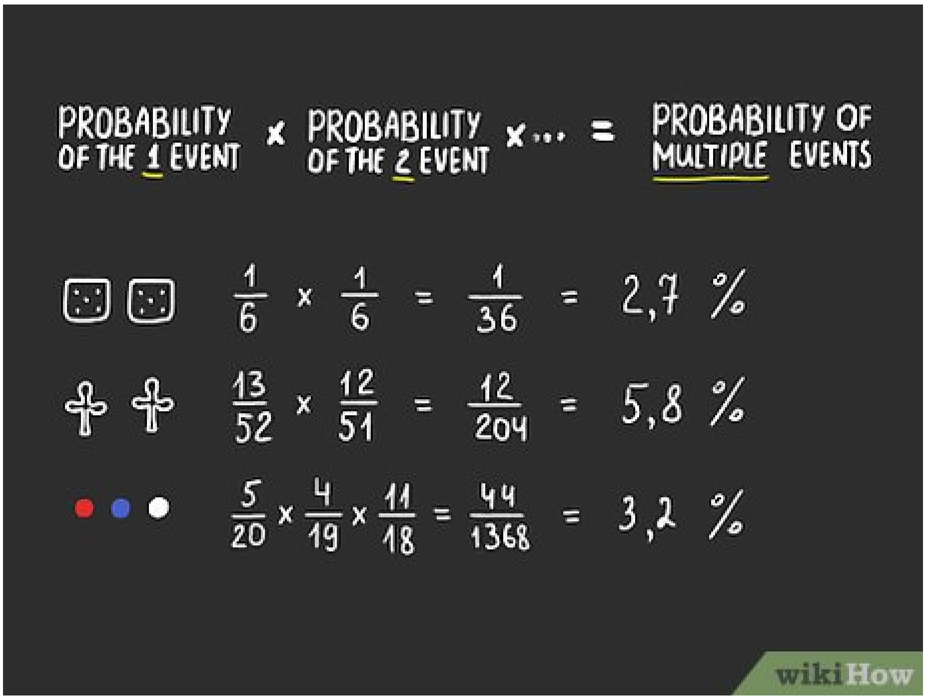
5/ This stockbroker seems to know what he is doing.

It is incredibly unlikely that a complete buffoon with no special knowledge would have gotten 10 correct stock predictions in a row.

6/ In fact, you grab a pen and paper and compute the probability of him getting 10 correct predictions in a row.

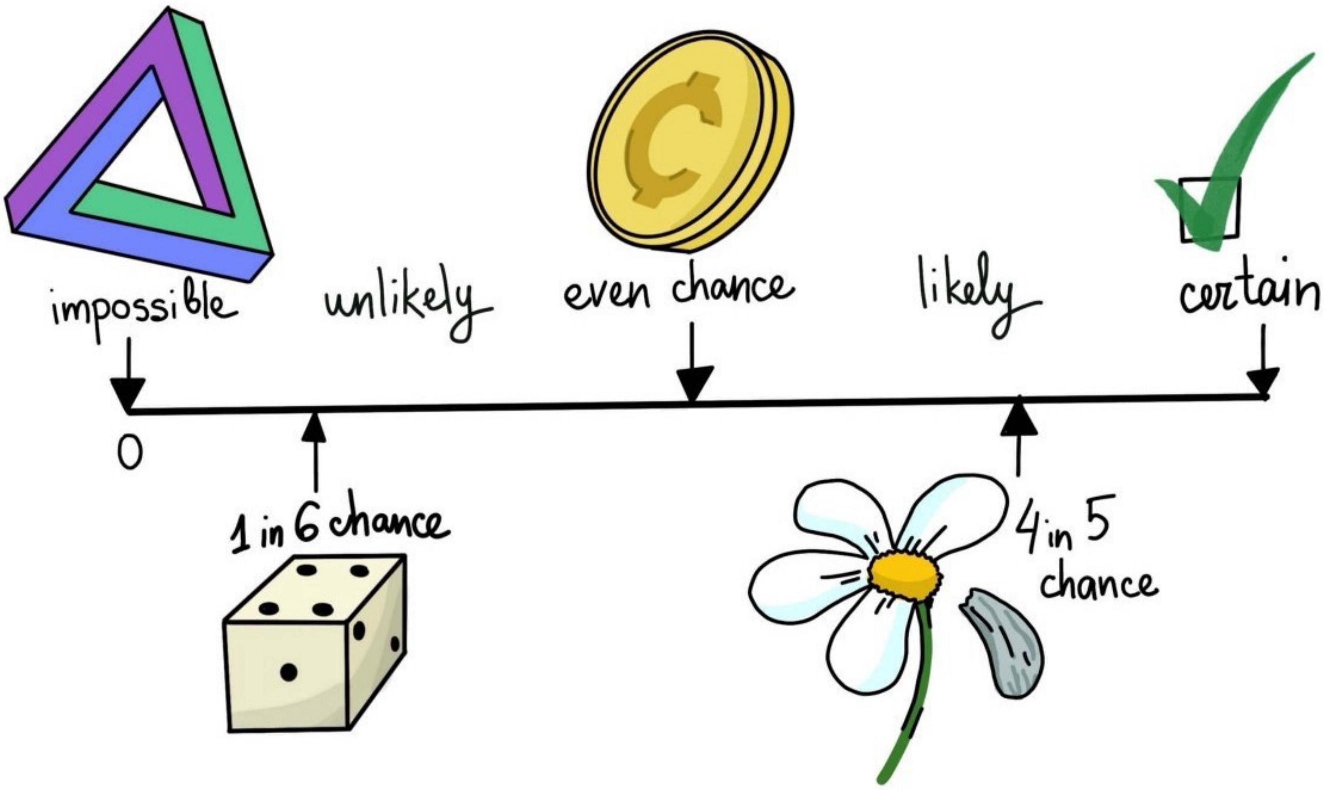
For a 50-50 chance of being right or wrong, and 10 picks, the calculation is (1/2) in the power of 10.

This comes down to 1/1024, less than 0.1%.



7/ This is so minuscule, that you think that this guy can't be so lucky and he must be the real deal.

But things look different from the stockbroker's side.



8/ In the 1st week, you weren't the only one who received the newsletter.

He sent out 10,240, half with the prediction the stock will rise and half with the opposite prediction.

The 5,120 who received the incorrect prediction never heard from him again.

9/ This continues every week.

The recipients that got the correct prediction, receive another newsletter.

Half the recipients get the "correct" prediction and half of them the "incorrect".

10/ After 10 weeks, there are 10 "lucky" people who received 10 correct predictions in a row.

Ten people who think the stockbroker from Baltimore is an investing genius.

Ten people from whom he expects to collect hefty fees.

11/ The closest this parable came to reality, was in a 2008 reality TV show.

A British magician, Derren Brown, pulled off a similar stunt, mailing various horse-racing picks to thousands of people, eventually convincing one that he had created a foolproof prediction system.

12/ However, this parable is alive and well in the financial industry.

When an investment firm launches a mutual fund, they often maintain it in-house before they open it to the public.

13/ This practice is called incubation.

Typically, these firms incubate dozens of funds at the same time, experimenting with different strategies and allocations.

14/ The funds that show great returns are quickly made available to the public, with detailed documentation of their performance.

The ones that fail, are thrown into the trash can, and the public never notices they even existed.

15/ However, once the public starts investing in these successful mutual funds, they do not maintain their excellent performance.

Instead, they offer the same mediocre returns as all the other mutual funds in the market.

16/ So how do all these affect your investment decisions?

It means you would be better off resisting the temptation of the hot new funds with the excellent track record and incredible returns over the past couple of years.

17/ Instead, follow the unsexy financial planning advice.

Stop looking for the stock magician with the golden touch and put your money in a low-cost index fund and forget about it.

https://t.co/l9sb5X2z2F

> Jack Bogle, the Father of Indexing
>
> How John "Jack" Bogle's creation impacted investors more than Bill Gates, Steve Jobs, and Warren Buffett combined
>
> /THREAD/ pic.twitter.com/4wPi8x3cXn
>
> — Kostas \U0001f468\u200d\U0001f4bc \U0001f4c8 \U0001f4b8 (@itsKostasWithK) January 8, 2021

18/ When you put your life savings into the new hot fund with the eye-popping returns, you are like the person who received the newsletter from the Baltimore stockbroker.

You have been lured by the impressive results, but you don't know how many chances they had to get them.

19/ The same applies to all the internet gurus, who tell you how good they are because they suggested buying $AMZN 15 years ago.

But they never tell you how many predictions they have made.

/END/

If you liked this thread click below and retweet the first tweet, and follow to stay updated.

https://t.co/a0k6jzZ6wg

> The Baltimore Stockbroker Parable
>
> How one stockbroker managed to achieve a 100% success rate in predicting stock movements
>
> /THREAD/ pic.twitter.com/xCRL6CfxBu
>
> — Kostas \U0001f468\u200d\U0001f4bc \U0001f4c8 \U0001f4b8 (@itsKostasWithK) January 23, 2021

For more educational threads on financial independence and investing for beginners see below for a collection of threads ■■■

https://t.co/6o3A2IQCMs

> List of Educational Threads on Financial Independence and Investing for Beginners#FinancialIndependence #financialeducation #financialfreedom #investing
>
> 1/ Financial Freedomhttps://t.co/8j5KG5ioFK
>
> — Kostas \U0001f468\u200d\U0001f4bc \U0001f4c8 \U0001f4b8 (@itsKostasWithK) January 3, 2021