

Taking a leaf on investing from Darwin

Pulak Prasad's book reframes the quest for long-term investing success from a focus on tools to one on desired outcomes



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INVESTMENT professionals know that there is no substitute for hours of in-depth textbook study, combined with an equal helping of hands-on experience.

Self-taught investors, however, can develop significant knowledge and skill sets for their own investing success even without the formal rigour of a professional designation or related university degree. A third group of investors, less inclined to investment theory and practice, may stop at foundational concepts such as risk and return, the benefits of compounding, and the impact of taxes.

These three groups are well served by, respectively, high-priced textbooks, detailed investment guides, and retirement planning guides. Pulak Prasad, star asset manager and founder of Singapore-based Nalanda Capital, has written a timely and practical guide for the middle group. The book, *What I Learned About Investing from Darwin*, is also a potent reminder to investment professionals that all the technical skills in the world are no substitute for good perspective and strategy.

Prasad treads the well-worn path of other (and perhaps better known in North America) star investors such as Peter Lynch, whose classic guide *One Up on Wall Street* directed readers to invest in companies they know – in particular, those with abundant compound growth potential.

He leverages Lynch's well-supported wisdom with examples from his India-focused fund, but with far greater attention to investment theory and analytical techniques.

This level of detail may overwhelm investors who lack a strong grounding in theory and practice, but it is essential to Prasad's claim that too many professional analysts rely on a false precision that provides answers unrelated to this fundamental question: "Is this company a good long-term investment?"

He does not reject the analytical tools but, rather, rejects their unbridled use as they hinder analysts' abilities to identify companies that provide superior compound growth and downside protection. He thereby provides an indispensable reminder to chronically underperforming active managers.

Evolution meets investment

Prasad also does not shy away from detailed commentary on analytical techniques. Instead, he uses a folksy style like Warren Buffett's to relate each point to real-world examples, often from his own portfolio at Nalanda Capital. Doing so helps the narrative flow, which is much better than in many textbooks – another reason for investment professionals to pick up the book.

He highlights his points through well-chosen examples from evolutionary biology, including, but not limited to, works by Charles Darwin. Each chapter begins with a well-chosen quote from Darwin and from Buffett, who is also liberally referenced throughout the book, and concludes with a summary of the main points.

Prasad's ability to draw parallels between evolutionary theory and investment theory emphasises the concepts that are most likely to lead to long-term success and market outperformance.

For example, in his second chapter, he cites an evolutionary biology experiment conducted in Siberia, in which wild foxes were bred for a "tameness" gene that would make them more like domestic dogs. The experiment began in 1959, and by 1963, it had



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produced a tamer fox.

But the genetic modification also produced other pet-like changes in the animal, such as "floppy ears, a piebald colouration, and a shorter snout", as well as a shorter reproductive cycle.

Prasad draws a parallel between the scientists' focus on a single desirable trait and his own favoured investment metric: return on capital employed (Roce). He explains that Roce is likely to be associated with other favourable corporate qualities, such as stellar management, exceptional capital allocation, strong competitive advantage, and capacity to innovate and grow a company.

By choosing the primary metric with the most explanatory power, the associated secondary metrics (floppy ears or stellar manage-

ment) are likely to be attractive. Most analysts are misguided in their use of earnings before interest and taxes (Ebit), or its related measure, Ebitda (which includes depreciation and amortisation), because those measures can obscure other financial issues.

Prasad's focus on Roce is an initial screen around which, in the following chapters, he methodically builds his case with additional financial and evolutionary theory, illustrating each with colourful examples.

By the book's conclusion, he has reminded us that the detailed knowledge and refined techniques we acquire through study are not an end in themselves, but a means to an end. His perspective is one that draws on experience and demonstrated success, and one

that investors would do well to emulate.

It is also a perspective that may become more valuable in the future, as algorithms and artificial intelligence are used to attain financial ends. After all, more and faster spreadsheets will not help if they do not focus on the best metrics.

Tripping at times

The book is clearly written and well-edited, with only occasional missteps. Examples include Prasad's claim of a zero per cent return for an investment that goes bankrupt. That would be a minus 100 per cent return rather than zero per cent. And there is also his awkward attempt at humour in suggesting that younger readers may not know what a bookshop is.

Also, some of his advice seems to lack context. For example, he "detests any debt" on company balance sheets, but public companies with no debt (or even with less debt than they can bear) and without dual-class voting structures may be prime candidates for leveraged buyouts. This strategy is a fine potential exit for many active managers, but one seemingly at odds with the author's "buy and hold forever" strategy.

These quibbles, however, are small. For amateur and professional investors alike, the book reframes the quest for long-term investment success from a focus on the tools we have to a focus on the outcomes we seek.

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