January 27, 2022 (/podcast/185)

Episode 185: Lighting your Money on Fire with Thematic ETFs (/podcast/185)

As we all know, not all investments are equally exciting, but on today's show, we make the case that you should not put your money into an ETF just because it is trending. A thematic

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Episode 184: Robin Wigglesworth: The Story of Index Funds (/podcast/184)
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Episode 183: Market Efficiency Myths and Misconceptions

ETF is a fund that offers the opportunity to invest based on a particular theme, such as climate change or artificial intelligence. The concept behind investment themes is that they ostensibly offer investors the opportunity to participate in potentially disruptive trends with the idea of earning excess returns. The problem we find with these ETFs is that as the markets they are based on attract more attention and an influx of entrants, everybody's per-share earnings get reduced. By the time a themed ETF becomes investable, it experiences a mean reversion of prices and media sentiment, in contrast to the attractive returns shown in its backtested index. This means that while thematic ETFs are good business for the ETF providers, they do not create value for investors on average. Toward the end of our show, we invite Wes Gray from Alpha Architect to talk about their change from index to active ETFs and more. Wrapping up, Wes along with Robin Taub join us for a lively round of Talking Cents. Tune in today!

RR #185 - Lighting your Money on Fire with Th...

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Key Points From This Episode:

- Shows, updates, and an introduction to our guests for today. **[0:00:27]**
- Discussing themes of harnessing inner dialogue in Ethan Kross's *Chatter.* **[0:06:17]**
- This week's news: BlackRock hits $10 trillion in assets under management. **[0:12:12]**
- An introduction to the history of thematic ETFs and their appeal. **[0:13:12]**
- The reduction of the per-share earning of entrants into exciting industries. **[0:16:35]**
- How more new share issuance dilutes the earning per share of businesses in that investment theme. **[0:17:50]**
- What the extent of overpricing in a market will depend on. **[0:20:37]**
- The connection between overconfident investors and bubble-like asset prices. **[0:21:48]**
- How specialized ETFs make the providers money but do not create value for investors on average. **[0:21:48]**
- What factor mix you get when you invest in thematic ETFs. **[0:29:39]**
- Reasons for why people would invest in thematic indexes. **[0:31:08]**
- The large behavior gap typical of thematic ETFs. **[0:35:35]**
- Why Wes Gray is switching from an index to an active implementation for his ETFs. **[0:39:33]**
- How investors should weigh active versus index

implementations when choosing a fund. **[0:41:44]**

- Why Cathy Wood pulled her filing for a Bitcoin futures ETF. **[0:44:25]**
- Wes's feelings about facilitating a Bitcoin product. **[0:45:48]**
- Whether the SEC will approve spot crypto ETFs. **[0:47:17]**
- Wes's thoughts on the 'shovel selling' aspect of his business. **[0:48:45]**
- If there is a tax advantage to ETFs or mutual funds in Canada. **[0:53:22]**
- The tax benefits of Wes's move to Puerto Rico. **[0:56:00]**
- Robin Taub and Wes join us for this week's Talking Cents segment. **[0:58:50]**

Read the Transcript:

Ben Felix: This is the Rational Reminder Podcast a weekly reality check on sensible investing and financial decision-making from two Canadians. We're hosted by me, Benjamin Felix and Cameron Passmore, portfolio managers at PWL Capital.

Cameron Passmore: Welcome to Episode 185. I have a show recommendation for you. I don't think you've watched Ozark yet.

Ben Felix: Oh, I have. I have.

Cameron Passmore: Oh, you have. My mistake. But if have

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you seen Season Four yet, it came out on Friday.

Ben Felix: Started watching the first episode.

Cameron Passmore: The season is so good. Unbelievable cliffhanger. I can't say anything because I'll blow it for people. But wow, what a great, it's such a shame. It's only seven episodes. It's such a shame we're going to wait another, what, 18 months for the next season to come out. But boy, is it good, Ruth, what a character.

Ben Felix: Honestly, I've never been able to pay attention to Ozark. It's we've played all the episodes on the television with us in the room. But I can't say that we've watched them. I couldn't tell you a single thing about the storyline.

Cameron Passmore: Real? I get so into it. It's almost a Breaking Bad good for us.

Ben Felix: I have not found that. I found it's very good background noise, but it's I'm on my laptop or my wife's reading a book or something.

Cameron Passmore: Well, you have to pay attention because there's a lot of storylines going on.

Ben Felix: Yeah. No. I have not been doing that for sure. On the podcast today, we have a bunch of people on. It's fun. We had Wes Gray from Alpha Architect join us to talk about, I don't know, the ETF business a little bit, Bitcoin ETFs a little bit, bear change from index to active ETFs, a whole bunch of inside baseball type stuff, but definitely with some important takeaways for individual investors.

Then at the end of the episode for our normal Talking Cents segment that Cameron and I do together, we had Robin Taub and Wes on at the same time. Robin Taub was a recent guest, and she was such a perfect fit to do Talking Cents with just based on her book is about teaching kids about money.

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Afterwards, we're like, "Ah, we should have done Talking Cents."

Then I think your computer crashed or something and just we couldn't do it. Anyway, we rescheduled for her to join us to do a Talking Cents segment. Then it just happened that this was a day we could get Wes on, too. We did with everybody. It was fun.

Cameron Passmore: She turned the tables on us with our own deck of cards.

Ben Felix: Right. It was good.

Cameron Passmore: It's fun. In other news, the 22 and 22 Reading Challenge update. There'll be a whole new website or page on our website that launches February 10th, which is a Thursday. As we said last time, we will have a special guest join us for that launch. In the meantime, keep track of the books that you've read, that you can upload them to the site. Angelica says it's really cool.

We're supposed to see it this week, I think Ben, get our first glimpse of the site, the gamifies reading. Just a note, I've had a few people reached out saying like, "Yeah, 22 and 22 is catchy. But it's a bit much like enough with the 22 books this year. Can I do it with just five books?" Absolutely. It's a reading challenge. You do what you think you can do. We're going to figure out rewards or badges or who knows where it's going to go.

We're brainstorming ideas now. I also heard Sandrine told me today that they're planning to have a vote. I think it's going to be on Instagram, Twitter, and in the community, where people get to vote on what will be the next book that I read. I'm not sure where this is going to go or where the ideas for the book will come from, but something to keep an eye out for.

for.

We also had some feedback last week that our audio levels are off on YouTube. I think Matt Gambino, our video specialists has made some adjustments to that. It should be better listening experience this week. If not, please put the comments out there. Upcoming guests next week, Andrew Hallam's joining us again. We talked about his newly released book, Balance: How to Invest and Spend for Happiness, Health and Wealth.

Ben Felix: That was a fun episode to record. I enjoyed that conversation.

Cameron Passmore: It was very good and very important book. Then two weeks after that Ayelet Fishbach, from the Booth School at Chicago, and author of the phenomenal book, Get It Done: Surprising Lessons from the Science of Motivation. Then two weeks after that, in five weeks time, Gerard O'Reilly who's the co-CEO, and the chief investment officer of Dimensional Fund Advisors will be here.

Ben Felix: That'd be good.

Cameron Passmore: Should be very good. Want to highlight in the store, we get lots of stock ready to ship. As we said in the past, we take no margin on this. We just cover a bit of the shipping which is free in North America and pretty cheap around the world. You can check the store out on the Rational Reminder website. Every order gets a free pair of socks. In case you haven't seen pretty cheap prices, the Talking Cents Card, they're 30 bucks; t-shirts at 25. Super soft hoodies are 45. Duke's 22. Love to get some stuff out there.

Ben Felix: Couldn't see it on camera. But Wes was wearing his Rational Reminder shirt.

Cameron Passmore: He sure was. As always, you can check out Rational Reminder on Instagram. I'm on there as well. I

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out Rational Reminder on Instagram. I'm on there as well. I don't think you're on Instagram.

Ben Felix: I think Angelica was going to make one for me because we had an issue where I was being impersonated on Instagram for a while.

Cameron Passmore: Oh, yeah.

Ben Felix: It was the sole thing. The Rational Reminder community, somebody in there works for Facebook or something and helped us resolve the whole ... it was quite the incident. I think they're going to make an account for me so that that is less likely to happen, I guess

Cameron Passmore: That's a good idea.

Ben Felix: I won't be behind it.

Cameron Passmore: You're not the biggest fan. CP313 or #rationalreminder on Peloton. I'm on Good Reads. We're both on Twitter. We're both in LinkedIn. But I think you've delegated that responsibility as well.

Ben Felix: Yep. Never logged in again.

Cameron Passmore: Of course, the exploding community. It's just unbelievable what's going on over there.

Ben Felix: Yeah. It's up to, I think, around 6,200 people in there, but it's great. The discussions in there are fantastic. I'm active there.

Cameron Passmore: You're very active. Anyways, anything else to add?

Ben Felix: No. Let's go ahead to Episode 185. Welcome to Episode 185, of the Rational Reminder Podcast.

Cameron Passmore: Okay. For this week's book review, you may have seen it. A lot of people are recommending it. It's a may have seen it. A lot of people are recommending it. It's a book called Chatter: The Voice in Our Head, Why It Matters and How to Harness It by Ethan Kross. It's a book I saw. It was recommended by Adam Grant. It sounded interesting. It was simply phenomenal. Ethan Kross is a professor of psychology at University of Michigan. Get this for a cool gig. He's the director of the Emotion and Self-Help Laboratory also at the University of Michigan.

Chatter is the voice that's in our head. It's the audio track that accompanies you wherever you go. No matter what you're doing, the voice is always there. It's always playing. If you remember, when Brian Portnoy joined us, I think the first time he talked about us as humans are the only species that can actually ... Our mind can go to the past or the current or to the future, and back and forth. We can switch memories to imagination all in an instant.

It's that voice that's going in your head as you're doing all of this. While that chatter can be a great benefit to you, it can also cause all sorts of problems and challenges and can certainly drive some people crazy. This book is about helping people realize ... Firstly, you've got this inner voice, how to control it, and get this, even how to have that voice become a coach for you. How to capitalize on, he says, this gift that you have.

Clearly the challenges that it can cause are ... You can have self doubt and anxiety, you can make up all kinds of stories. When it's in our head, these are narratives that can go unchecked in our minds. To be very mindful of that, it can also get in the way of forming goals and get in the way of certain accomplishments we may want to do. As he talks about in the book, it can really be self-sabotage a lot of people.

But he says the challenge, and what you really want to do is

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to turn the tables on your inner voice and have it help you identify solutions. If there's pain in your inner voice is to take the energy of that pain to impact change on you, and enable it to become a coach for you. He says that you can absolutely change that voice from being an inner critic to being an inner coach. He gives some actual strategies.

At the end of the book, there's a whole litany of strategies of what you can do. But he said it's really important to get inside your head, be thoughtful about what's going on, to be introspective about what's going on with these voices that this can actually lead to a more fulfilling life. He says some of the things you can do ... I've actually been more aware of this as I listened to the chatter. But some of the things that you can do is to zoom out, try to get a global picture of these voices going in your head.

He also suggests try to use your own name in the voice or use a third person that's watching the chatter going on, or to try to be a fly on the wall. He gives all kinds of examples like this. Another real cool part of the book that something you've talked about, especially with your move is the benefit of having experiences that deliver "Ah." Something that's awesome. He highlights especially nature, being around trees.

He also says your child's first steps. He says all of these things can help reduce the chatter, calm the chatter and help you refocus your mind. He says the experience of "Ah," which is especially when you're in the presence of something vast, such as forest or the ocean, this makes you feel smaller. Therefore, the chatter and your voice in your head actually shrinks. Get this being by the ocean actually causes people to think that there is more time available to them.

People who spend more time in these awesome environments are more humble and more balanced, and

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actually give more credit outside influences to the success. Interesting, I mean Wes talks about this later, how he's changed his lifestyle would have been neat to ask him some of these questions. But we feel smaller when we gain control of our inner voice. Another one of the benefits of nature, get this, children who are not regularly exposed to nature have a 50% more chance that they'll experience depression and anxiety when they're adults.

Ben Felix: Wow.

Cameron Passmore: How's that for a wild statistic.

Ben Felix: That is wild.

Cameron Passmore: Another thing about calming chatter, too, is he talks about the power of rituals. By having rituals in a structure, it enables your mind to focus on the task at hand, not organizing your world to be able to do the task at hand. That's why a lot of people need a lot of structure and order in their lives. Anyways, phenomenal book. There's a whole list of things that you can do at the end of it. Highly recommend it.

Ben Felix: It's very interesting. Andrew Hallam talks about that, as well about time perception, and about how new experiences and being in nature alter your perception of time. As we've known humans can't extend their lives indefinitely. We can increase the perception of the length of our lives by having new experiences and being outside.

Cameron Passmore: Hey, talked about how you ... You'll remember the experiences for your life. But you'll remember the stuff you bought. You have more life in your life.

Ben Felix: Right.

Cameron Passmore: Interesting. Quick story, new story I came across actually this morning. Blackrock became the

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Episode 100: Prof. Kenneth French: Expect the Unexpected (/podcast/100)
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Episode 99: Andrew Hallam (Millionaire Teacher): How to

first public asset manager to hit $10 trillion in assets under management, that incredible?

Ben Felix: That's a lot of assets.

Cameron Passmore: I mean, I remember I think at 5 trillion was a lot. Now it's 10 trillion. They added 104 billion US of ETFs in Q4 of 2021. A quarter, 169 billion to all their long-term assets, including ETFs and Q4. Active strategies, including alternatives contributed over 60% of 2021 organic growth. Not just a passive ETF shop by any stretch.

Ben Felix: Fee growth or growth?

Cameron Passmore: In fee growth assets. Long-term fee growth assets. They now manage $2.6 trillion in actively managed funds, and ETFs and hedge funds.

Ben Felix: Unreal.

Cameron Passmore: Ten trillion is the new trillion. Anyways, on to your main topic on thematic ETFs.

Ben Felix: Yep. As everyone knows, not all investments are equally exciting. I guess we talked about this with our good companies, good investments, maybe this is similar but a little different. Recently, stuff like crypto has been a big one, blockchain, marijuana. Maybe a couple years ago, cloud computing, electric vehicles, clean energy, robotics, a lot of the ARKK stuff. I think ARKK has funds for a lot of these things.

But so does iShares and other companies, too. Artificial intelligence is another one. These are all current exciting themes that you can get products for. But the theme of themes though is not new. If you go back in the '60s, it was electronics. They didn't have ETFs back then. But everyone was clamoring for small cap high priced electronic stocks, without a whole lot of fundamentals behind their businesses.

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In the '70s was different, the nifty 50, but same idea. Everyone is willing to pay really high prices for these specific types of companies. It's biotech in the '80s. Internet stocks in the '90s. These are just broad categorizations. I'm sure that there were more hot themes within each of those decades. Those are just the big ones. But there are similar examples going back hundreds of years. This is not a new phenomenon by any means.

Cameron Passmore: The mutual fund industry, as well all through the '90s and, well, all the way through in Canada for sure.

Ben Felix: The concept behind these themes, these investment themes, is that investors can participate in potentially disruptive trends or innovations with the idea presumably of earning excess returns, in excess of the market or an excessive risk taking, or whatever. S&P describes their thematic indexes as offering access to a series of technologically enabled, often disruptive industries, generally referred to an aggregate as the fourth industrial revolution.

Cameron Passmore: Who doesn't want that?

Ben Felix: It's pretty exciting. Now, I think that if you're excited about an investment, if you're not expecting pain from an investment, it's probably not a good investment. The collective excitement of investors has a tendency to drive up stock prices. I think exciting new technologies or industries or themes are common focal point of that investor excitement. I used to read about this stuff in books about the past, and like I mentioned, all the ones from the previous decades, but I've been working in this field for not that long.

I mean, less than a decade collectively, or almost a decade collectively. But I've lived through some of these now. I mean,

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crypto, we'll see how that goes. But marijuana stocks have gone full circle. Electric vehicles, clean energy alone leave me a lot of this crazy high price behavior. I mean, marijuana stocks, because that one's gone full cycle, it's easy one to talk about. But back then everyone was going to get rich, and everyone was talking about, and everyone is investing in it. Everyone wanted to put a little bit in their TFSA or whatever.

But that didn't work out too well. That was a short cycle. Some of these can last a lot longer.

Cameron Passmore: Now there's marijuana stores everywhere around us.

Ben Felix: Yeah. We'll talk about that big market idea. But think about ... There's a finite amount of profit or earnings for marijuana businesses, and not even publicly listed ones. We were just talking about retail marijuana stores. There's a finite amount of profit to go around. You look at the amount, the number of retail storefront businesses. They're slicing that profit up. That pie of profit, they're slicing it up thin.

Cameron Passmore: Every one of those is another slice of the pie, because that pie can't change.

Ben Felix: The pie stays roughly the same. The pie is what it is. Every new store is just taking a piece of it. I mean, it's competition. It's business.

Cameron Passmore: Yep.

Ben Felix: This is one of the challenges with exciting new industries is that they're exciting. They attract entrepreneurs, and they attract investors who want to invest in entrepreneurs and fund the businesses. But it reduces the per share earnings of all of these entrants into the new exciting business. I mean, the marijuana storefronts is a great example. But it happens with public securities, too. Maybe electric vehicles is another current example that's fairly obvious.

There's tons of companies like that. But they're all slicing up one pie thinner and thinner. The more issuance, the more new share issuance for new businesses or capital raises from existing businesses that just dilutes and dilutes and dilutes the earnings per share of the businesses in that investment theme. This, of course, idea was formalized in the 2003 paper by William Bernstein and Rob Arnott that we've talked about a bunch of times called earnings growth at 2% dilution.

The dilution is bad, basically. If there's a lot of new share issuance, the economic growth of a country or an industry or whatever, is going to lead the earnings per share growth, because of the dilution, because of the dilution from share issuance. Now, I think the problem for investors is that most entrepreneurs and most investors don't think like this. They don't think that all of these new businesses in the investment theme or sector or whatever, are slicing the pie thinner and thinner and thinner.

The entrepreneurs and investors are looking at this thinking, if I'm the entrepreneur, I think that I'm going to start a business that's going to be successful. In a big industry, look at look how big this pie is. Imagine how big my business could get. But they think that they're going to win. They think that they're going to be the winner and capture a big piece of this pie. But unless they have some big competitive advantage, they're going to face competition.

Then investors, like you think whether it's VCs or retail investors or whatever, they're not looking at the company saying, "Geez, that looks like a bad investment, because this piece of profit pie is getting sliced up so thin by all the new entrants." They're looking at and thinking "I'm going to pick a winner." I think the effect of that is you get high prices,

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Episode 72: Interest Rates, Optimal Asset Location, and Reverse Mortgages (/podcast/72)
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Episode 71: Dave Nadig: Everything that you could ever know about ETFs (/podcast/71)
Nov 7, 2019

because entrepreneurs think they're going to be winners, so they command high prices for their businesses.

Investors are willing to supply capital because they think they're going to pick a winner. You end up with high prices. High prices make an investment theme more enticing to investors. It's like, "Oh, geez, look at electric vehicle stocks. Look what they did last year. I want to invest in that now after their performance." But eventually what happens is investors learn about the market, the actual size of the market as opposed to the potential size, the level of competition, the earnings per share of the companies and eventually prices tend to ... I mean, we've seen this cycle many times historically, prices tend to fall and they often fall a lot, especially if they got really high.

Now this isn't just me opining. I got most of those ideas from Brad Cornell. Who's been a guest on the podcast and Aswath Damodaran. They had a paper in 2020, The Big Market Delusion: Valuation and Investment Implications. We talked about this concept of Rob Arnott and also with Brad Cornell in past episodes. They explained in that paper that the extent of overpricing in a market will depend on the degree of overconfidence exhibited by entrepreneurs and investors, where more overconfidence leads to higher prices.

The potential size of the market where a larger potential market leads to higher prices, the degree of uncertainty about the future profitability of the market, where greater uncertainty leads to higher prices due to an amplification of the overconfidence effect, and the perception of winner take all markets. Where again, if it's perceived to be a winner take all market overconfident entrepreneurs and investors will assign higher prices to securities.

In the Cornell and Damodaran paper, they give examples of ecommerce in the 1990s, the online advertising industry from

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2015 to 2020, and cannabis stocks in 2018. As people would probably recognize those were all huge markets, but with intense competition, extremely high prices and an eventual sobering drop in prices. We talked about Jose Scheinkman in a recent episode. I love his paper on overconfidence.

2003 paper, Scheinkman and Wei Xiong titled Overconfidence and Speculative Bubbles. It's a great paper. If you can get through it, it's mathematically painful to remind people, or if people have listened that episode. They explained that paper that because of the costs of short selling, overconfident investors will tend to have more of an impact on prices than pessimistic investors. Overconfident investors will be willing to pay more than their own assessment of a stock's fundamental value to buy it because it gives them the option to sell to an even more overconfident investor later.

The result of that overconfidence is bubble-like behavior in asset prices, which as we know, doesn't tend to end well for investors. I think this is ... Scheinkman makes a note of this in a lecture that he gave it's especially problematic for naive investors who maybe don't know a whole lot about asset pricing or expected returns or how to assess these things on their own.

He says in his 2013 lecture, this is a quote experts that wish to signal their familiarity with new technologies have a tendency to exaggerate their value, and in this way, generate over optimism among naive investors, that over ... This is no longer the quote, the over optimism among naive investors is something that financial product providers are happy or even eager to cash in on. This is where the idea of thematic ETFs comes in.

You got all these overconfident people willing to pay high prices for some perceived big market. If your Y-shares or Horizons there may always have stuff to meet whatever

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Horizons there may always have stuff to meet whatever thematic need attendees or profit opportunities. I mean these are big markets on themselves. There's a 2021 paper, really good paper, by Itzhak, Ben David, and three coauthors Competition for Attention in the ETF Space. They find in their paper that specialized ETFs, which are typically concentrated portfolios with high fees, focused on trendy themes.

They find that they're launched just after the peak of excitement and often the peak of returns related to popular investment themes. They find in the paper that specialized ETFs do not create value for investors on average, delivering a negative 4 factor alpha of about 6% on average in the 5 years after inception of the fund, not of the index, but of the fund. I'll talk more about that in a second. Before the fund inception, the authors of this paper find the index is used to create the specialized index funds tend to have had very positive performance.

It's slippery. But it makes sense economically for the fund provider. They create an index based on a popular theme with high recent past returns, positive media sentiment, high prices, all that kind of stuff. They built an ETF to track that index, keeping in mind that they're back testing the index. They're saying, "Look what this index just did," but given that we know ex-post that it has done well. Then they create an ETF to launch this positive back test thematic index.

They find this paper that leading up to thematic ETF launches, the securities in the indexes tend to have been increasing in relative price, makes sense. They use book to market and media sentiment. But pre-launch, like I was just mentioning, the indexes are not investable. These are back tested conceptions that index manufacturers think are going to sell. Then after the ETF launches, and the index actually becomes investable, the stock valuations tend to come back to Earth.

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We'll put a chart in the YouTube version of this. That's a pretty good chart from the paper. The media sentiment also tends to decline. That's also in the chart. I mean, it's crazy. It's mean reversion of prices and media sentiment after the theme becomes actually investable, as opposed to just a back-tested index. The thematic indexes also tend to contain stocks with more positive skewness, which is that's the lottery ticket idea ...

Cameron Passmore: Yep. Make sense.

Ben Felix: ... where typically they do poorly, but sometimes they do extremely well. That could be interesting if somebody wants lottery like payoffs. I mean, hey, we saw that with ARKK Innovation ETF.

Cameron Passmore: They do want the lottery like payoffs. They just don't want the ...

Ben Felix: Some people.

Cameron Passmore: They just don't want the opposite. They don't want the left tail.

Ben Felix: Yeah. Well, I mean, if you won a lottery like payoff ...

Cameron Passmore: Who doesn't want to win a lottery?

Ben Felix: ... you expect to lose on average with a lottery. They want the ... You're right they want the right tail. Yeah. I'm still on the same paper. They find that within ... This is interesting. Within the specialized ETFs, the ones holding stocks with the highest pre-launched returns, compared to the other ones, the other specialized ETFs, and media sentiment, perform even the worst ... They performed the worst post launch, which further supports the idea that the issuance of specialized ETFs occurs near the peak evaluation of the underlying securities. That's predictive of poor future performance.

The more exciting it is, the worse it probably is as an investment. Now, one thing that's interesting to think about is that people don't look at that. I mean, it's the big market delusion idea. People don't look at this and think "I'm going to lose my money by investing this thing." That's not what they think.

Cameron Passmore: No, because there's often compelling stories by in these two, right?

Ben Felix: Yep. They're thinking about the right tail. They're thinking about the big market. But they're not thinking about how thinly that market is going to be sliced. The authors of this paper, they took analyst forecasts for earnings as a proxy for investor expectations. They just say, "We're going to assume that investors believe what analysts are using as forecasts." They find that portfolios of specialized stocks display significantly higher long-term growth forecast in the period leading up to the ETF launch.

The stocks are going into these thematic indexes. Analysts also think that they're going to have extremely high future growth. But then after launch, the stocks in these specialized ETFs tend to experience a downward revision in growth expectations. The forecast error is measured by the realized earnings per share minus the analyst's long-term growth forecast at the time of launch. They look at where did they forecast at the time of launch versus where the earnings actually end up in real life.

There's a big negative gap, which is statistically significant, and economically large. This again, of course, is consistent with strong over optimism in expectations around the time of launch. Again, it's that big market idea, "Oh, look, this is

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going to be huge. It's going to be huge." The market will be huge, but your slice might not be. There are 50 other companies thinking the same thing that maybe aren't in your index. Or even if they are, the prices you're paying are so high that it's not going to matter regardless.

It's like ... Robert I'm going to talk about this when he was on our podcast that every EV stock, at least back when he was talking about, every EV stock is priced as if it's going to be the dominant share of the market. Okay. The data from this paper support the hypothesis that the providers of thematic ETF, ETFs launch products based on themes where investors hold optimistic beliefs, make sense. Thematic indexes, on which the thematic ETFs are based consist of high price stocks with strong media sentiment, and optimistic analyst forecasts.

All of which tend to decline around the time that the ETF tracking the index launches and it actually becomes investable. It's just a story, "Look at these past returns. Look at this." Then all of a sudden, "Oh, it's gone." Another question that I think is worth investigating is factor exposure. Okay. We've got these thematic ETFs through the factor investing lens. Let's take the Fama/French 5 factor model in the paper. I'm going to refer to. They use that plus momentum.

Six factor model, what factor mix are you getting when you invest in these thematic ETFs? This is a paper called Betting Against Quant Examining the Factor Exposures of Thematic Indexes by David Blitz. He used the thematic indexes from MSCI and S&P as a sample. He finds that thematic indexes tend to have lots of idiosyncratic risk measured by their volatility ratio. Of course, that's risks that could be diversified away in a more diversified portfolio.

They also tend to be tilted towards small cap stocks with high prices, weak profitability, and little more mixed, but generally aggressive investment. Of course, that factor mix empirically is horrendous in terms of expected returns and risk adjusted returns. I mean, if you look at companies like Dimensional and Adventus, they're intentionally excluding those types of stocks, not including them, which is interesting, too.

Because if you're a Dimensional or Adventus, everyone starts with the market. The market is there. If you want to get rid of small cap growth, low profitability, high investment stocks, who are you going to sell them to? Who would want to buy those? Apparently, thematic investors would, which is funny. Let's have some other ideas for why people would invest in these thematic indexes. Like, "Okay. We know these things are pretty bad in terms their expected return profile."

But he says, "Some people might not believe in factor models," or maybe they don't know about factor models, I guess that could be an alternative interpretation there. Let's say if someone doesn't believe in the value premium, or believes value investing is dead, then yeah, there's no expected returns reason not to hold a small cap growth, low profitability fund. If you don't believe in asset pricing models, then it's irrelevant to you.

Or if you believe that the premiums have reversed, then maybe this is a good thing, maybe you want this small cap growth, low profitability, positive premium that you imagined to exist in the future. The other possibility is that these relatively concentrated portfolios, because you're getting a bad factor exposure mix, but it's also a concentrated portfolio. You're going to have an error. You're going to have an alpha that's not explained by the factor exposure.

It's possible that even though the factor exposure on these things is so bad, you're going to have this big alpha, because the security selection is so good.

Cameron Passmore: That's a good point.

Ben Felix: That's possible. But remember, the data that we talked about from that other paper were pre-launch, that's true, pre-launch on the back-tested index, you do have big positive alphas. But post-launch on average, that other paper found a four-factor Fama and French and Carhart four-factor alpha of negative 6% on average. You get the positive alpha in the back test. But not in the live fund, which isn't great.

Another possibility that we talked about a little earlier in the segment is that people want that lottery like pay off. People want ... Sure you're going to lose on average, but you might knock it out of the park. That's well-documented. Barber and Odean have a couple pretty famous papers from 2007 and 2020 and there are lots of other papers like that, that people don't necessarily want standard payoffs.

Then the other big one is Chasing Past Returns and Buying Attention Grabbing Investments. Sorry. That's the Barber and Odean reference is attention grabbing investments. People are more likely to invest in stuff that they hear about if it's in the news, or if it's because it had large or small, extremely positive or extremely negative returns. If they saw it on TV, if they saw Elon Musk tweet about it, they're more likely ... If it was promoted to them on their Robin Hood app, people are more likely to invest in that stuff. That could be another reason people invest in thematic ETFs.

Then the final possibility is that there are nonfinancial benefits to owning the stocks in the indexes, I need to belong. Or if you feel good about the investment, need to belong is interesting, because like ARKK, there's a subreddit with 16,500 people. I checked how many people were in there before we started recording. It's a community around it. You invest in the ARKK funds, and you're part of the ARKK community and everyone's talking about their returns or how they're changing the world with our investment or whatever they're talking about.

That's worth something to some people. I think a lot of them are maybe hurting right now. But that's a different story. Thrill-seeking is another one. People sometimes just like to gamble. I guess that ties into the skewness comment. But if you're satisfying a need with meeting a thrill-seeking desire then, hey, who am I to tell you you're not getting a good risk adjusted return from that if it's satisfying a need. Now that that paper that we're just talking about is titled Betting Against Quant: Examining the Factor Exposures of Thematic Indexes.

Now what does that title alluding to? It's alluding to the fact that quantum investors are typically investing in stocks with low prices, not high and robust profitability, not weak and conservative investment, not aggressive. They're taking the opposite side of those trades. That's something that you can do low cost systematically. It's theoretically sound and empirically persistent positive differences in expected returns, as opposed to negative for the thematic stuff.

But like I mentioned earlier, to build those portfolios, quant investors need to ... I need somebody else to overweight the small cap growth, low profitability. It seems that's the thematic investors doing that. One of the worst parts about this is we can talk about how bad thematic indexes do post-launch and how bad thematic ETFs do. But that aside, the behavior of investors in these things is even worse. Morningstar has their Mind the Gap report where they compare time weighted and money weighted returns for various types of investments.

Now, to be fair and upfront about a bit it, the Mind the Gap report does not have thematic as a category, but they do

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have sector. The gap for sector funds is the largest gap of any fund classification other than alternative. Alternative is the biggest. But the behavior gap for sector funds is significant. It's negative 3.4%, I think. That's the difference between the investor return and the fund return.

I don't have the data. But I'm willing to bet that thematic funds would be even worse, or at least as bad as sector funds. Morningstar also did this blog post on their blog looking at ARKK, Cathie Wood's flagship, ARKK, A-R-K-K fund. This is data as of November 2021. ARKK Innovation had delivered a five-year compound return of 41.3%.

Cameron Passmore: Wow.

Ben Felix: Impressive, right? But the average ARKK investor with the money weighted return measurement had earned only 9.9%.

Cameron Passmore: That was as of November. I would think now, those numbers may be dramatically different.

Ben Felix: On both sides, probably. Yeah. I don't know how the gap would have changed but the time weighted returns definitely come down. That's a big behavior gap. That's historic performance, or it was at that time, but the behavior gap is ginormous. Fund companies have this massive incentive to create market products that cater to attention grabbing investment themes. Why do they have an incentive? When you look at the fees like Cathie Wood's ARKK ETF, 75 basis points.

The Horizons Marijuana Life Sciences index ETF fee of 75 basis points, management expense ratio of 85 basis points which includes admin costs and taxes. I mean, look, use Horizons as the example their total return index ETFs, where you get the broad market, they're almost free, or iShares, or whatever. The margin is in these thematic ETFs. If you can hit on themes that people are excited about and pick up some assets then, hey, in one of the papers I read, it talks about how the AUM, the Assets Under Management of thematic ETFs are relatively low.

But they make up about a third of the fee revenue for the ETF industry.

Cameron Passmore: Wow. Really?

Ben Felix: Yeah. I mean, think about it's like the Blackrock thing. The active and hedge fund stuff for Blackrock is making a massive contribution to fee growth.

Cameron Passmore: For sure.

Ben Felix: Of course. I mean, it's not coming from their total market index ETFs basis points. Anyway, thematic ETFs are lighting your money on fire, to put it gently. It's good business for the ETF providers. But if you're jumping on a thematic bandwagon, I think you should expect to lose money in the short-run, even though sometimes that doesn't happen. But that wasn't just like ARKK had the fantastic performance. But it wasn't just ARKK. Small cap growth, low profitability as a class had phenomenal performance over a short period of time.

It can happen that you'll have a good short-term outcome. But long-term, the expected returns are terrible. Most of the time in the short-run also can be terrible. You can't buy a back test. You can feel good about it, but you can't actually invest in the back test. All right. That's it.

Cameron Passmore: Awesome. All right. Thanks. Let's go over and welcome Wes Gray to the podcast. Wes Gray. Welcome back to the Rational Reminder podcast.

Wes Gray: Thanks for having me, gentlemen. Happy to be nere.

Cameron Passmore: You guys being Alpha Architect recently announced that you're switching from an index to an active implementation for your ETFs. What are the advantages to going active?

Wes Gray: For us, it's basically bombing a lot of costs that we don't want to deal associated with maintaining index and then the additional compliance of having an index and putting up walls internally. Frankly, just didn't make any sense to us. Then now that all the tax rules are all harmonized across ETFs, it's all good. I think we're one of the few shops to actually start off active, moved index for tax reasons.

Then now we're moving back to active because tax doesn't matter, but we save more costs. Yet our underlying process is literally exactly the same whole time. It's just all legal stuff.

Cameron Passmore: Interesting. Is that what changed, the tax treatment of active?

Wes Gray: Yeah. Yeah. What happened is, in the old days, a lot of the initial providers like Vanguard, WisdomTree, they had a different act of relief down here, which allowed them to basically do custom baskets, just without any recourse. Then what happened is when we launched, even though everyone did it, it was understood. Technically, in a relief, you're not supposed to do custom baskets. Then once that was brought to our attention, and it was like, "Hey, technically shouldn't be doing this, even though we understand that other people are doing it until they harmonize the rules. You should probably do something else."

We're like, "Okay, great." We went blew 50 grand on switching to index just for tax. Now, I think it was 2019 they did that, the unifying ETF rule down here, where they said, "This is crazy. There's 20 different rules for everyone out there. Let's just harmonize it across the board." People like Alpha Architect don't have to blow 50 grand just because they're not Vanguard. Hey, let's make it equal. Now that it's equal, we can go back to active because we don't really benefit from being indexed.

As you guys know, we're not an intense marketing shop. Index has benefits, because you can market your back test, it's easier to get on big wirehouse platforms. There's definitely some uses for it. But those users are just not that useful to us.

Cameron Passmore: How should investors weigh the active versus index implementations? Just thinking this through as an investor when they're choosing a fund?

Wes Gray: It really depends, and this probably marginal, to be honest. But so whenever you're an index fund, or an active fund, you always have an option to not disclose what is going to be in your basket. Even though we self-indexed, technically tell for six more days from now, anytime we do a rebalance, we don't go out to the world and say, "Hey, here's our new index."

What we do is we say, "Hey, we are going to post up our new index in two days from now. But tomorrow, we're going to actually maneuver to our new index." Then we're going to announce what the new index is. We've always been able to trade to our index, which is what active people do. We've always operated like that, whether we're called index or called active. But generally what happens is with index funds more broadly, especially like big, famous ones like S&P, they'll throw up what they call a forward looking basket.

It's basically saying, "Hey, here's our index to the world. Then tomorrow, you would go implement executions to trade to that basket." There's big arguments about, "Well, is that increase impact cost? Does it actually improve liquidity, what have you?" I don't really know the answer to that. But from an actual nitty-gritty implementation perspective, we do the same thing, regardless of who's active or index based.

Cameron Passmore: You're just as systematic as you were before, rules based as before?

Wes Gray: Yes. Yes.

Cameron Passmore: Does it feel different than how you're managing at all, or it really is?

Wes Gray: No. Not really. I mean, the one thing you get though is the problem with being indexed is you're very beholden to the rules hard and fast, like period. And anytime you do something, if it's any change, even if it's "deminimish," you're going to have to document that, put that in your compliance manual. It's a huge pain. Where obviously, if you're active, the nice thing about it is you don't have to deal with this extra compliance burden.

Wes Gray: Let's say, "I don't want to rebalance tomorrow, because for whatever reason, some crazies going on. I don't have to." Whereas if your indexed, you can do that. But the bar to be able to make that call is a lot higher, because has to be the power went out in the world or the market's crumbling. You're going to have to defend that decision every single time, basically. Whereas if I'm active fund, and I want to change my rebound state, I could just wake up tomorrow and say, "No. We're doing it tomorrow. Not today." It's a lot nicer from a flexibility standpoint, I would say.

Cameron Passmore: Very interesting. Switching gears a bit, Cathie Wood's ARKK last year filed for a Bitcoin futures ETF using your white label platform, but then they pulled the filing. What's the story there? What happened?

Wes Gray: There's a lot of things going on there. But basically, behind the scenes, accessing the futures and getting a FCM to facilitate was essentially incredibly onerous. I'm not going to say they were gouging. Let's just say the pricing for some of the stuff in the end I'm not sure it made sense to launch a product because the intent is you want to launch products that are obviously going to be good for the clients in the end after cost and after all the brain damage.

But if you're going to get gouged, at some level, you just say, "You know what? Fine, we're patient. We'll wait." I think it was a mix of that. Then I'm not going to speak to their own personal business issues and circumstances. But maybe there was other things related to that. Because if you guys pay attention to recent performance, but sometimes you need to shore up the ship before you go on another adventure. Imagine that was part of the calculus at some level as well.

Cameron Passmore: Huh, got shored up the ARKK.

Wes Gray: Yeah. Yeah. Got shore up the ARKK. There you go. I like it.

Cameron Passmore: There was an April Fool's joke back in 2018 on the Alpha Architect blog about launching a crypto ETF. How do you feel about potentially facilitating a Bitcoin product for real?

Wes Gray: I just want to be clear that we have Alpha Architect, which mission is empower investors for education and all those products that I put my own money into, and I have no problem getting other people invested, all full stop. Then we have ETF architect, which is a shovel selling business where the mission there is how do we help people access ETF market and deliver the best product they can for their client base.

I have no problem as a shovel salesman. If you have a dream, and you have a market segment, and we can help you get to that market and deliver that in the most cost efficient, affordable way possible, even if Wes won't personally put all of his capital into this fund, all good. It's just a different mentality. I don't know, man. I'm just old school. The Bitcoin thing just feels like sentiment driven mania, degenerate gamblers everywhere, where there's with no regulation, I got no problem with it.

But I just like to count cash flow, money. For me, I just can't wrap my head around it. I'm not offended by people that are into that stuff. It's just not something that I personally want to do as an investment. But I understand that there are other people that highly demand those investments. If we can facilitate, we will.

Cameron Passmore: Do you think the SEC will eventually approved spot crypto ETFs?

Wes Gray: I just don't know. I think it's a long ways off. Because the main issue and challenge was off, obviously, with the crypto markets is they're totally unregulated. You need to maintain a fair and orderly market. But it's very easy in crypto to buy and sell to yourself. It just generate volume. You can do all the old scams. That the reason they put all the rules in back in the '20s and '30s, you could still do all of that in crypto markets and no one even knows.

Until there's some semblance of a fair and orderly marketplace there, I understand both sides. I know why people are pissed, why they won't do. But I also understand for regulatory standpoint, who would want to be caught dead doing that and launching product where it's unclear, what's going on behind the scenes, I would say.

Cameron Passmore: Do you think ... Because we have spa products in Canada, or the Canadian regulators nuts or what?

Wes Gray: I don't know if they're nuts. But I think the minute you open it up into the US market, whether it's good or bad, we lead and we have so much more capital that will come to market. It's one thing have three, four, five billion. But down here, you could get 100 billion in one of these things. I'm not smart enough to be Gary Gensler.

But I've heard that guy talk and I'm just impressed, honestly. If you read his background, I just have to put a lot of trust and faith that someone like that is probably knows what he's doing, and who am I to judge at some level?

Cameron Passmore: I'm curious about the shovel side of your business. Can you talk about what's going on there? What trends you're seeing, talking about the demand for these services?

Wes Gray: Yes. ETF manufacturing services are white hot right now. It used to be people that wanted to come into the market to launch a new thematic or do what have you. But now that we've got a lot of clarity on the tax down here, because the tax bills are passed us and are people they settled that, "Hey, the ETF thing is not going to get blown up." Now what we're seeing is conversions basically.

As you guys know, DFA was the lead sled dog on doing that. I think what's happened is a lot of mutual fund companies are like, "Oh my God. This free cash flow is amazing. But no one really digs that, let's just wait," and then DFA dropped. Everyone's like, "Ah, now we have to have an ETF strategy," because if they're doing it, we don't have any more excuses and say, "Well, DFA's not do it. That's why we have to do it."

Mutual fund conversions are huge right now. We're in the middle of a ton of talks. Hedge fund conversions, you could do that. Then another big one is SMA conversions. We've actually already done this and we're talking a lot more on fund offices and IRAs, where you can take as SMAs. As you have a bunch of accounts that have individual securities with low basis, you can actually use those to seed an ETF. As you guys are aware, once you get it into the ETF structure, it's much easier to manage your taxes, essentially.

We're starting to see a lot of migration of RIAs down here, essentially moving a lot of their business and managing it through a white label ETF, basically.

Cameron Passmore: Once you do that, other people can purchase that ETF correct? It's no longer your own private SMA.

Wes Gray: It's not your own private SMA. The trade off there, if you're doing this as an advisor is you're going to gain access to the tax efficiency, obviously, but you lose the scarcity and proprietariness of it, because now your clients can buy it, but so can everyone has a TD Ameritrade account. You obviously, to the extent you had something that was super limited scalability, or there was issues with capacity, obviously, probably don't want to do that in an ETF.

Because a lot of people have tried and we've actually asked on behalf of a lot of huge mutual funds that have capacity constrained strategies. You can't realistically do it in an ETF. There's no way around. This is what it is.

Cameron Passmore: How does it work? If it's the example you just gave with an IRA taking an SMA and stick it into an ETF, if there's not a ton of volume on that, how does that work with the authorized participants? It is the creation redemption process still smooth?

Wes Gray: Yeah. It's a little bit different in Canada. In Canada, the only way you can leverage the tax efficiency of an ETF is you need natural volume, because then as you get a redeem, you pull out the pro rata basket where you dump low basis on AP. Then obviously, on the crate, you get new updated basis. If you trade by appointment, that's not very useful for you as a Canadian ETF. It's different in the state.

In the states, we have what they call a custom rebalance capability, which means you don't have to do pro rata baskets. If I want to redeem or crate, it doesn't have to be the exact basket we're currently on. I could literally take your portfolio and trade it for cash and it's all good. You could trade for anything. Even if you never trade a single share in a US ETF, you can't guarantee anything, but you can almost guarantee 100% tax efficiency, because at any given moment, I can do a custom rebalance and just dump out basis, and then accept in new basis, essentially.

Cameron Passmore: Geez, wow.

Wes Gray: It's very different than the Canadian market. As you guys know, we're involved with folks up there, it stinks because it'd be nice if they just followed our rules down here, because then you get the same benefits. But up in Canada, there's really a huge monopoly benefit, where if you have a ETF that's already out there and has a ton of volume, not only do you get potential liquidity benefits, but you also get a massive tax benefit over other counterparts in the Canadian market, because they just don't have the capability to do custom rebalancing, which stinks and is unfair, but it just is what it is.

Cameron Passmore: I want to keep going on this Canada bit, just because you got knowledge there. Is there a tax advantage, like you mentioned for larger ETFs maybe? But in general, is there a tax advantage to ETFs or mutual funds in Canada or can there be?

Wes Gray: From the perspective of a Canadian investor?

Cameron Passmore: Yeah.

Wes Gray: There are some advantages. You guys probably know more about this than I do. I mean, one of the advantages is it's a Canadian Security. God bless US government, but if they can take your money, they will. If you have a lot of US assets, and the US government deems you subject to a state tax, they might go knocking on your door in Canada, and that's a good reason if you're a really rich person, you might want either structure or avoid US assets. That's reason number one. You got to be careful.

Then some other reasons are having to do with withholding tax on dividends. I think there's a treaty like US funds, it's not that hard to get back access to the withholding tax. Then international is more of a pain. But to the extent at the fund level, you're able to pull in a lot of the withholding tax, which we do, a lot of firms do. You can minimize that impact, because we're already going to collect it at the fund level. It's less of an issue.

But a lot of fund companies just withholding taxes like, "Oh, that's your problem." My understanding is that you basically can never get that if you're trading through an ETF in the US that owns international securities. You have to punt on that component. There's definitely some issues with Canadian investors owning US ETFs. But you guys obviously probably know that a lot more than I do.

Cameron Passmore: What about in the US, the ETF has a pretty significant tax advantage over a mutual fund in the US for a US investor. Is there anything like that in Canada? If you're Canadian owning an ETF, do you have an advantage over a Canadian?

Wes Gray: I think so to the extent that, let's say you're doing a momentum strategy, for example, that has massive turnover.

momentum strategy, for example, that has massive turnover, and to the extent you have a Canadian ETF that's in Canada that can't obviously use custom, create redemption, but where's there one in the states can, to the extent you're willing to subject yourself to that state tax risks that we're talking about there. If you're mega rich, it might be a problem.

But as long as you're not mega rich, but you're still taxable, and you're willing to deal with the currency issues, I do think there's probably is a pretty substantial tax benefit, even to a Canadian investor to owning US vehicles, because you implicitly get to take advantage of the fact that down here, for whatever reason, our capital gain distributions are usually going to be zero, or that capability is going to be limited in the Canadian market.

Cameron Passmore: Right. Yeah. It makes a lot of sense. Last time you're on, Wes, you just moved to Puerto Rico, which I think was for some pretty interesting tax benefits for you. Can you talk about that? Has the move been worth it?

Wes Gray: Yeah. Yeah. I mean, I always tell people, I feel like it's the greatest arbitrage of all time. It's not for everybody. But the basic logic for why I did it is my wife and I were looking for an opportunity to give our kids something unique, adventurous, and original. Were like, "Hey, let's go move to Chile and learn Spanish or just do something different." Then as I kept digging, because we're so buried in the weeds on esoteric tax stuff, I always knew about Puerto Rico.

I was like, "But wait a second. I don't need to change passport. They have this insane tax benefit. It's effectively going to different country." They speak Spanish here. I pitched my wife and she's like, "Well, yeah, that sounds a lot better." Yeah. We moved down here last May. I love it, honestly. Great weather. The people are super cool. I covered a functional and Spanish at this point. It's easy for me to a functional and Spanish at this point. It's easy for me to manage business and our team through the Internet, what have you, plus I've really good teammates.

Honestly, I'm just getting away at this point if I'm actually in person. It's been wonderful for me, in particular, maybe not for everyone. But yeah, if any of you listeners are interested or want to talk about, I'm happy to oblige. That's easy.

Cameron Passmore: How long do you plan on staying there?

Wes Gray: Honestly, I plan on being here for indefinite future. My wife's actually up in Philly, get her house ready to be sold. Unless there's ... Maybe when I hit a cat five, and my roof blows off, and I'm blown away out to sea, I might have a different tune. I survived hurricane season this last year. It wasn't that bad. I've been in hurricanes before. I used to live in Japan. I love it.

Low tax, low cost living, great people, great food, tons of entrepreneurs down here. It's right next to the beach. Honestly, I just ... I don't know why more people aren't moving down here to be frank, but I'm not other people. I think it's an arbitrage opportunity personally. But the market's spoken. There's not too many people crazy enough to move their whole family down to Puerto Rico and do it.

I don't know if it's a heavy status quo bias or maybe the market's efficient and I'm just missing something. It could be a possibility as well.

Cameron Passmore: Interesting. Well, thanks for joining us Wes. Can you stick around for the Talking Cents part of the podcast?

Wes Gray: Sure. Of course.

Cameron Passmore: All right. Let's move to the Talking Cents segment of this episode. Wes, we're going to welcome back a past guest, Robin Taub. Robin, welcome to the show.

Robin Taub: Thanks for having me back.

Cameron Passmore: This is the first time we've ever had four of us doing this. You suggested off here that maybe you could pull some cards since you have a deck of these as well. I've got one to kick off, which I'll throw to you guys. I've got a quote for you from Ralph Waldo Emerson. The quote is, "Money often cost too much." What do you think this means, Wes?

Wes Gray: I have no idea. But I imagine maybe it has something to do with people focus on it too much. That's all they put their whole life and time into is money and not their family, their relationships, and that kind of stuff. That'd be my guess.

Cameron Passmore: It's good answer. Robin, what do you think?

Robin Taub: I agree with that. That if you focus too much on money for the sake of money, that you'll pay the price in other areas of your life.

Cameron Passmore: I was also thinking times like now where we have some volatility going on in the markets that what's happening your portfolio could often cause some of your mental space these days. That's another cost. Ben, any other thoughts?

Ben Felix: Oh, I think Wes totally nailed on the first go.

Cameron Passmore: All right. Robin do you have a card ready? Or you're going to pull another one.

Robin Taub: I do. I do.

Cameron Passmore: Fire away.

Robin Taub: An investment in knowledge pays the best interest, Benjamin Franklin. What do you think that means?

Ben Felix: Cameron, you go first.

Cameron Passmore: I completely agree and people know how passionate I'd be I'm about reading. I just love learning and knowledge. I completely agree. You guys?

Ben Felix: For most people, at least for a large portion of our lives, human capital is most valuable asset. Definitely agree that investing in education pays good interest.

Wes Gray: This is easy for me because I use that in one of my pitch decks. I lived in Philadelphia for a long part of my life. I love Ben Franklin. Our firm mission is to empower investors through education. I am all in on that quote, because I think it's a great one. I can't disagree with old Ben.

Robin Taub: Yeah. If I may, I think I even say on the back of my book cover that teaching your kids about money will pay dividends for years to come. It's not interest, its dividend. But still, it is a wise investment.

Cameron Passmore: Okay. I've got one for you guys. When you think about saving money, which phrase resonates more with you? You only live once, or plan today for a better tomorrow, Ben?

Ben Felix: Well, I mean, I think realistically, it's a balance. But in general, I'll pick the "You only live once," if I'm making a money spending decision.

Robin Taub: I think I've become a little more on the yellow side, I think because of COVID a bit. You got to grab these opportunities while you can to travel or to do something or to have a little bit of fun. I mean, as you say, balanced against prudent planning, but the best laid plans can go out the window. Yeah. I'm a little bit more about seizing the moment now.

Wes Gray: For me, I'm in transition. I'm a depression baby born in 1980, used to be on food stamps, and I was broke my whole life. By nature, I have to save money, because I feel like it's decided to do that. But now that I actually got somebody, I'm moving towards the yellow phase of my life, and I'm slowly trying to not be such a cheap bastard and enjoy some things in life. But it's a challenge.

Cameron Passmore: Robin, you have another card to pull?

Robin Taub: Sure. Would you prefer to be responsible for others, or have others responsible for you?

Cameron Passmore: Wes, go ahead. I think we had this one last week. Hey, Ben, we pulled this one randomly last week.

Ben Felix: Did we?

Cameron Passmore: A couple weeks ago. I think so.

Wes Gray: Yeah. I mean, for me, I just cannot stand what people have to do stuff for me. I'm definitely in the first camp, personally,

Robin Taub: I think for me, sometimes I feel like I have so many responsibilities, for my investments, for my kids, for my business, for my employee, it just feels a little much. Sometimes I just wish that somebody said to me, "Don't worry. We're looking after all of it for you." I don't know. Maybe just because it feels like it would be nice to offload some of it sometimes. Although probably when it came down to it, it would be pretty hard to hand the reins over to somebody else.

Cameron Passmore: It's interesting. In our business, sometimes we can feel responsible for people that are here.

But as the team matures, you can see them taking over. The creation of the enterprise overtakes everybody. As the collective that's taking care of everybody, which is an interesting shift that's happened over the past few years I've observed. Ben, anything else to add?

Ben Felix: I much prefer to be responsible for other people than have other people be responsible for me. Recently, our water heater broke, and then our well froze, and we had no water, no heat for a couple of weeks. It was minus 30 here. Yeah. But we dealt with it. My parents found it after the fact. I just didn't mention it to them. They felt guilty for not having helped, because I didn't tell them. But I just wasn't interested in relying on other people, I guess.

Cameron Passmore: You guys want to do another one?

Robin Taub: Sure. You want me to choose one or you want to?

Cameron Passmore: No. Go ahead.

Robin Taub: This is a good one. If you could try any job for just one month, what would it be? I know.

Cameron Passmore: Go ahead.

Robin Taub: I'd love to be either a backup singer, or a roadie for a really great band. Probably backup singer would be my number one job I'd love to do, in a cool soul or R&B band.

Cameron Passmore: Yeah. I'd love to be the lead guitarist for a band.

Robin Taub: There you go.

Cameron Passmore: It'd be so much fun.

Ben Felix: We had this one recently, and I said that I'd be a carpenter. I think I still stand by that. I did that every summer for a few years in high school and love to try it out as a full time job.

Wes Gray: Yeah. I have to go with the rock star routine. Yeah. I always want to be like a drummer. I never want to be a singer because it seems I can't sing. I get embarrassed, but drum roll I saw it'd be cool. Sit in the back. Just go crazy back there. Three out of four for going on stage, that's pretty good

Cameron Passmore: You guys can form a band.

Robin Taub: Yeah.

Wes Gray: Yeah.

Robin Taub: Probably one of those fake ones. Remember that game? That was garage. I forget what it was called.

Cameron Passmore: Yeah. The Rock Band.

Robin Taub: Rock Band. Yeah. I don't even need to be the lead singer. I'd be really happy just to be one of those backup singers.

Wes Gray: We got Cameron.

Robin Taub: Oh, cool.

Wes Gray: He can be a lead.

Robin Taub: Okay.

Wes Gray: I'll be in the back doing drums and you can be backup singer. I think you got some going here, man.

Cameron Passmore: Yeah. Ben could be the lead singer.

Wes Gray: There you go.

Cameron Passmore: Since a regular viewer of the podcast and a good friend sent a video on the weekend. A cover by a band he knows of the Doobie Brothers China Grove, and there's this guy in the front right hand side that's playing the lead rhythm guitar, I guess, playing the chord, just like I said to James. I said, "Man, that's real. I'd love to play." I don't need to be doing all the riffs up front. But to be the cool dude playing the Stratocaster on the side, that'd be alright.

Robin Taub: Yeah. I guess I just have to live vicariously because my son is in an actual band. He's the bass player. I'm 20 feet from stardom, just like that movie. I don't know if you've seen it, but it's a fabulous movie.

Cameron Passmore: Anything else? You guys want to do another one?

Ben Felix: We've done a lot. I think we're good.

Cameron Passmore: That's good. Well, Robin's been great to have you. Wes, so great to have you join us this week. It's been a lot of fun.

Robin Taub: I look forward to listening to this episode, Wes.

Wes Gray: Yeah. Yeah. You got it.

Robin Taub: Thanks, guys.

Wes Gray: Good chatting.

Ben Felix: Thanks. Thanks, Robin.

Books From Today's Episode:

The Wisest Investment — https://amzn.to/3BWQfZw (https://amzn.to/3BWQfZw)

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Robin Taub — https://robintaub.com/ (https://robintaub.com/)

'Earnings Growth: The Two Percent Dilution' — https://www.researchaffiliates.com/documents/FAJ-2003-Two-Percent-Dilution.pdf (https://www.researchaffiliates.com/documents/FAJ-2003-Two-Percent-Dilution.pdf)

'The Big Market Delusion: Valuation and Investment Implications' — https://www.tandfonline.com/doi/full/10.1080/0015198X.2020.1730655 (https://www.tandfonline.com/doi/full/10.1080/0015198X.2020.1730655)

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'Betting Against Quant: Examining the Factor Exposures of Thematic Indices' — https://papers.ssrn.com/sol3/papers.cfm?

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