Welcome.

ASPE’s Business Book Reports

*The Black Swan:*
*The Impact of the Highly Improbable*

By Nassim Nicholas Taleb
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The Black Swan: The Impact of the Highly Improbable

By Nassim Nicholas Taleb
Nassim Nicholas Taleb

@nntaleb
Why did we pick this book?

- Taleb gives critical “macro” insights
- Great critical thinking primer for business
- Helps you understand how to navigate uncertainty

Great book for anyone interested in critical thinking, product strategy, navigating the market
The book’s main themes

- Biggest impacts come from unpredictable outlier events
- History is “cumulatively recursive”
- You don’t know and can’t explain
- In business, your best shot comes from trying as many ideas as possible and optimizing scalability
Key points up front

• Nassim is a philosopher who espouses the empirical, but values dignity and aesthetic even more
• Themes are rooted in Nassim’s observations of ignorance and hubris, even (especially) by the learned
• Neglect of hard-to-grasp realities is dangerous
Nassim’s background

- Lebonese – his society has had a tough time and he observed many irrational human tendencies
- Philosopher at heart, who went into business at Wharton
- Early specialist in derivatives
- Early interest in odd probabilities and everyone’s seeming ignorance of the real nature of risk
On History

- It makes sense in retrospect – not in advance
- History doesn’t “crawl,” it “jumps”
- The driver – “God knows”
- Clustering and categories
- “The highly improbable consequential event”
Black Swans

- Purported not to exist until travels to Australia
- It is a rare outlier
- It has extreme impact – disproportionate to any logic
- It is retrospectively explainable and predictable
Scalability vs. Gravity

- The best and worst advice – “idea jobs” vs. those subject to gravity
- Designing a shoe vs. making it
- Mediocristan vs. Extremistan
- Collective sum; “bell curve” dynamic vs. disproportionate collective effect, “accidents”
The Bell Curve

FREQUENCY

IMPACT

IMPACT

Real Training. Real skills, real world, real results.
The turkey: “1001 days”
Themes of part 1

• We focus on pre-selected segments of the seen and generalize to the unseen
• We behave as if black swans don’t exist
• History hides black swans; we don’t see everything that’s there
• We focus on ("tunnel") a few well-defined sources of uncertainty
Themes of part 1

• Our default mode of reasoning was well-adapted for prehistoric African plains survival
• The world now is exponentially complex
• Sources of black swans have multiplied, yet that causes us to “tunnel” even more
• Human nature is to simplify: the utter opponent to understanding the black swan concept
More good points from part 1

• We aren’t well-adapted to the non-linear
• We favor the highly visible
• The surprise that you very badly want to happen
• Short-term goals over long-term results
• The pool of starving artists is much larger than the pool of starving accountants: scalability vs. gravity
More good points from part 1

• “In real life you don’t know the odds; you have to discover them”
• Distance yourself from primates: train yourself to spot the difference between the sensational and the empirical
• “Prediction, not narration, is the real test of our understanding of the world”
The scandal of prediction

• Information is bad for knowledge
• An experiment: Pick a question and frame it in terms of “98% probability”
• The 2% margin of error usually turns out to be 15, 30, or 1000% true margin
• The “doctor problem” – know-how vs. know-what (doctor or reporter?)
Part 2
More on prediction

- The “expert problem”
- Things that move vs. things that don’t move
- Predictions from authorities are well-documented and able to be studied
- Events are outlandish
- The un-fitness of complicated approaches
- Anchoring: lowering anxiety about uncertainty
Reasoning fallacies

- Variability matters – not as much as the prediction itself
- Behaving based on averages
- “Don’t cross a river if it averages four feet deep”
- Equating near- and far-term futures
- Misunderstanding the random variables
The deception of history

• The past’s past, and the past’s future
• Overestimation – misfortune and risk
• You get plenty of negative confirmation from history, but also plenty of illusions of knowledge
• There are plenty of practical measure we can take against future/past blindness
So...what should you do?

- Be human! And be prepared
- Don’t prioritize small, steady gains in the face of huge risks
- Distinguish between positive and negative contingencies
- Don’t be precise AND local (narrowminded)
- Seize anything that looks like opportunity
- Beware of precise plans by governments
The way things really work

- The “Matthew” effect
- Riches and reputation
- Language and the lazy selection of words
- The contagion of ideas
- Nobody is safe!
- Nobody is threatened with complete extinction either
Concentration

- Globalization and banks too big too fail
- Nodes on a network
- Electrical networks
- The internet
- (Nassim wrote this in 2007)
On the bell curve

- “A great intellectual fraud”
- The headwinds in deviations
- Gaussian distribution vs. Mandelbrotian (scalable) distribution
- 80/20 = 50/01
- The larger the sample size, the less dispersion of the observed average
- The love of certainties
Fractal vs. Gaussian

• The nature is the same regardless of scale
• This has huge implications for consequence
• Beware precision
• A fractal world doesn’t play by Gaussian rules
• Things are possible (greater than 0% probability) although they never happened in the past
• Mandelbrot domesticates some black swans into gray swans...but not all
Two ways to approach randomness

- Premises over models
- Courage of ignorance over models
- Broadly right vs. precisely wrong
- Sophisticated craft vs. poor science
- Bottom-up vs. top-down
- Minimal theory vs. broad modeling
- Black swans vs. ordinary fluctuations
Nassim is...

- Very aggressive with exposure to positive black swans, very conservative when under threat from one
- Shallow with aesthetics; not shallow with risk/return
- Worried less about advertised risks; more about vicious hidden ones
- Worried more about “safe” blue chip stocks than about speculative ventures
“Imagine a speck of dust next to a planet a billion times the size of earth. The speck represents the odds of your being born; the planet the odds against. So stop sweating the small stuff. Stop looking the gift horse in the mouth – remember that you are a black swan.”
Thank you!

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