❖ Contrarian Research Report ❖

February 20, 2002

The Language of the Modern Investment Profession

The libraries of the world are filled with unread volumes written by philologists that compare the language of Chaucer with the language of Shakespeare. There are innumerable but unknown studies of the structured cadences of historical writers such as Gibbon and Macaulay. This is, then, merely a humble attempt to add another example to this storehouse of ignored work.

The English of the modern investment profession is perhaps unique in the history of language. English is the lingua franca of the business world. The language is probably more important to commerce than was Latin in the Roman world. This language is characterized by unusual structural elements.

Modern Investment English relies heavily upon the use of the conditional tense. A declarative sentence must always be qualified by a clause. An interesting but nonetheless unanswerable question is whether or not this type of English can actually corrupt human thought. However, before discussion this question it is necessary to provide clear examples of the use of Modern Investment English.

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Given the space constraints of an essay, the best way to proceed is to translate several passages from so-called classical English into Modern Investment English. A well known and much admired example of English prose as used in Winston Churchill's speech on the miracle of Dunkirk delivered in the House of Commons on June 4, 1940. The most famous passage is from the conclusion of the speech:

> We shall go on to the end, we shall fight in France, we shall fight on the seas and oceans, we shall fight with growing confidence and growing strength in the air, we shall defend our island, whatever the cost may be, we shall fight on the beaches, we shall fight on the landing grounds, we shall fight in the fields and in the streets, we shall fight in the hills; we shall never surrender, and even if, which I do not for a moment believe, this island or a large part of it were subjugated and starving, then our Empire beyond the seas, armed and guarded by the British Fleet, would carry on the struggle, until, in God's good time, the new world, with all its power and might, steps forth to the rescue and the liberation of the old.[*]

Modern Investment English would avoid any use of an absolute as opposed to a relative term. Moreover, flourishes are generally understood to detract from a message. Speech should at all times be measured and moderate. It must be hopeful yet avoid any remark that might be interpreted as a promise. Thus translated, the Churchill speech would read as follows:

> We propose to fight in a wide variety of locations. We have no intention of surrendering at the current time. However, if we do surrender, we should be able to transfer some part of our populace to Canada, Australia and New Zealand. These nations, rich in resources and natural beauty, would potentially offer our people a splendid alternative lifestyle. There is also the possibility that we might receive some help from the United States but this is not reflected in our current conservative assessment of the situation.

This is hardly an exhortation to battle. Nonetheless, the translated words betray no sense of panic or of peril. Since the sense of peril is a state of mind, the absence of a sense of peril is interpreted as the absence of peril. Such a view is not at all far-fetched. In economics, an important statistic is the index of consumer confidence. If this figure demonstrates that people believe their financial circumstances to be good, then these will be good.

[*] Incidentally, Microsoft Word finds this passage grammatically objectionable, yet another example of Modern Investment English as encoded in generally used software.

The art of Investment English can only be mastered with practice and with some degree of difficulty. Let us therefore try another translation exercise. The following excerpt is from the same Churchill Dunkirk speech delivered in the House of Commons on June 4, 1940.

> I have myself full confidence that if all do their duty, if nothing is neglected, and if the best arrangements are made as they are being made, we shall prove ourselves once again able to defend our island home, to ride out the storm of war, and to outlive the menace of tyranny, if necessary for years, if necessary alone.

The reference to fighting alone is a comment upon the very real possibility that the French government would surrender which, in fact, actually happened two weeks later. The preceding phrase stating that we shall once again defend our island home is a pointed yet also oblique reference to British history. Modern Investment English also makes use of history but prefers to reclassify the study of history as a science instead of a social science. In order to accomplish this, statistics are blended with history. This use of statistics is an important tool of Investment English. Thus translated, the Churchill speech would read as follows:

> We are now making arrangements to defend the British Isles from invasion, which, although not perfect, should be more than adequate. The War Office has just completed a study of wars in which this country has participated since the War of Jenkin's Ear in 1739. This 200-year study establishes that the wars are not generally of long duration and that the military situation begins to improve, on average, nine months after the outbreak of the war. Of course, this war is almost exactly nine months old so that an improvement in our fortunes appears imminent.

The obvious historical reference would be that Britain had not been successfully invaded since William the Conqueror in 1066. Yet, this statement is tantamount to saying that Britain could be successfully invaded. It would be far too negative. It is the type of statistical outlier that skilled practitioners of Investment English would exclude. A 200-year study should be acceptable to most of the target market.

The combination of statistics and history as a means of predicting the future is endorsed by no responsible historian. If a long statistical series established a type of physical law, then the Pharaohs would still rule Egypt, a Shogun would rule Japan, Istanbul would still be called Constantinople and this essay would be written in Latin. History is infinitely variable.

In order to master our use of Investment English we must try one more translation exercise. This is yet again an excerpt from the same Churchill Dunkirk speech.

> We must be very careful not to assign to this deliverance the attributes of a victory. Wars are not won by evacuations.

Such a phrase could never be used in Investment English. It is a sober assessment of reality. It requires translation in the following manner:

> The withdrawal from Dunkirk has dramatically shortened the supply lines of the British forces and conversely increased the supply lines of the German army thereby placing additional burdens upon the enemy.

This translation is an extraordinary example of the manner in which Investment English permeates thought. The central theme of Investment English is the discovery of a positive rate of change. A shortening of supply lines must liberate resources. It is the military equivalent of a writeoff. Similarly, a writeoff is evidence of a reduction of expenses. If a reduction of expenses occurs, this should serve to increase profit. Thus, it is viewed as if it were an increase in profit. In order to have profits, one must first eliminate losses. Thus, the reduction of losses is a positive development that merits an increase in share price.

We are now ready to apply investment English to everyday experience. Let us commence with unemployment statistics. Let us note, as actually has happened in recent weeks, that the number of persons filing initial claims for unemployment insurance has remained almost unchanged at roughly 370,000 persons per week. This level has persisted for 5–6 weeks. Thus, it is argued that this is tangible evidence of an improvement in the economy. After all, if the economy were not improving, then the number would increase.

The economy may well improve and this essay pretends to no such knowledge of the subject. However, the aforementioned reasoning is ludicrous. The number of persons in the work force is finite. Therefore, even if every single person in the work force were to become unemployed, the number of persons filing for initial claims would eventually decrease if for no other reason than that every person that once was employed would be no longer employed.

A much more reasonable view would be to study the dismissal rate in relation to the natural labor force absorption rate. Hence, if 370,000 people become unemployed each week, the economy must create 19.24 million new jobs each year to avoid permanent labor displacement. Some positions are created by the natural rate of retirement, death and disability rate of the work force. However, this is almost always at least balanced and generally more than balanced by the rate of young persons entering the labor force. This is especially true of nations with growing populations and almost all populations grow.

According to the Statistical Abstract of the United States, there are slightly in excess of 600,000 new jobs created each month in a normal economy. This would correspond to 7.2 million new jobs created each year, or a 5% new labor absorption rate in an economy such as that of the United States with a work force of something like 140 million persons. There can be no reasonable expectation that 19.24 million displaced persons can be absorbed by the existing employed portion of the work force. Therefore, a weekly new claims figure for unemployment insurance of 370,000 persons can only be viewed as very alarming, and by no conceivable stretch of the imagination can this be viewed as a sign of coming prosperity.

The reason that it seems plausible to maintain that a constant weekly unemployment claims statistic is a sign of an improving economy is because the language actually corrupts thought. No further deterioration in a statistic devoid of any context is a notion that is simply applied to the larger economy. Employment is a basic economic statistic. Thus, no further deterioration is an employment statistic must imply no further deterioration in the economy.

Conversely, even an economy at full employment will have some unemployment claims as workers are displaced from failing industries and absorbed by growing industries. Thus, a weekly claims figure of even 200,000 should not be viewed as an instance of economic ill health. There is a natural labor velocity of change that is essential to an economy that can respond to market forces.

Comparison outside of proper context or misuse of the term rate of change are only some of the pedestrian uses of Investment English. Let us observe the use of the term extraordinary in modern investment parlance. Extraordinary is a synonym for unusual and it has come to mean in modern investment parlance items that are unusual and should be disregarded. The use of the term extraordinary charge might just as well note: “Please disregard this entry.” The term extraordinary charge has evolved from the former use of the term extraordinary loss, since one may disregard a charge. It is more difficult to disregard a loss since the loss term is less ambiguous than the word “charge.” Would such entries be disregarded if these were called "unanticipated diminution of shareholder capital"? There must be a limit to the degree to which shareholder capital can be diminished by writeoffs without fatal consequences to a given firm. After all, a firm must possess some capital.

A writeoff is an intriguing term. It is defined by Webster's dictionary as "to reduce the book value of" an asset. The word has a sterile character. It is a mere accounting entry. It is therefore much preferred over the more correct term, which is capital allocation error. Webster's dictionary defines an error as "an act that through ignorance, deficiency or accident departs from or fails to achieve what should be done." A writeoff is merely a more statistically correct form of book value accounting. It has nothing whatever to do with error. In the course of the past two decades, it is beyond question that American corporations have written off hundreds of billions of dollars of assets. Yet, curiously, no mistakes have been made.

Rating organizations have adopted the new investment terminology. Standard and Poor's reports earnings for the S&P 500 on an operating basis, which, of course, excludes writeoffs. This is to say the operating earnings are the normalized earnings. These are the earnings that would be reported if no mistakes were made. It is upon this ideal and no other scale that an equity share is to be valued.

The notion of a writeoff has encouraged the use of another term that is not actually a writeoff. This is the term non-cash expense. That is to say that an expense that does not entail the immediate outlay of cash is not to be regarded as an expense. For example, stock options and stock grants are a non-cash expense, which is to say that these are not really expenses. The issuance of a salary can be presumably halted at any time. The issuance of shares is unfortunately an infinite or perpetual right to share in the profits of a company. Its value must be very large since it is perpetual. In fact, although the market value of options or shares can be calculated at any time, this does not accurately measure the surrender of profits by the existing holders of shares to the new stockholders.

If the issuance of shares to management were to be called "perpetual compensation" as opposed to non-cash compensation, the issuance of shares might be considered as a very significant expense. However, expressed in the phraseology of Investment English, this is not actually an expense.

Companies and their accountants and attorneys are not the sole practitioners of Investment English. Investment English is a universal language. It is a form of modern Esperanto.

Investment managers and investment consultants have made innumerable contributions to English etymology. The most interesting, and probably the most dangerous, is the use and abuse of the word risk.

Webster's dictionary defines risk as "the possibility of loss or injury." It is synonymous with peril. Therefore a risky asset is attended with danger. Incidentally, as an example of the degree to which English has evolved, one might consult the 1944 edition of the Oxford English Usage. That volume maintains that English has no such word as risky. It is supposed that it derived from the French risqué and, as such, is an undesirable Gallicism. The Cassell French dictionary has two meanings for risqué. The first is identical to the English hazardous. The second is doubtful as in the French "une plaisanterie risqué" which means a doubtful joke.

Modern Investment English has reinterpreted the term or perhaps redefined the term. Risk is volatility of market price. The large degree of daily volatility in the price of an asset entails a high degree of risk. However, since a critical presumption of Modern Investment Theory is that markets are efficient, it follows that this risk would not be assumed unless it was attended by a higher reward. Thus an investment that entails great risk does not entail a doubtful outcome, it actually entails an unusually rewarding outcome. Therefore, the highest reward will belong to those who can tolerate extreme price volatility.

This notion, more than any other, is responsible for the rise of Nasdaq as a legitimate investment option for savings. In fact, this most volatile investment has become so legitimized that the Nasdaq 100 Exchange Traded Fund has a much higher daily trading volume than the S&P 500 Exchange Traded Fund. The distinction between the two indicies is not very important since the S&P 500 includes within itself many of these Nasdaq 100 shares. Enthusiasm for the Nasdaq type company might be somewhat muted if the technology firms that largely populate the index were called office equipment companies, which was the former conventional usage.

Since portfolio managers are evaluated in relation to these so-called benchmarks, an extension of the risk term is the risk of under performing an index. Hazard or danger is not defined by the ownership of these overvalued and usually unprofitable equities. On the contrary, there is residual or deviation risk if too many of these shares are *not* owned. Risk is reduced by owning as many of these shares as possible. Since mathematical expression of this notion can be found in any modern textbook on investments, readers of this passage should know that it is seriously intended and not simply "une plaisanterie risqué."

Modern Investment English is a very complex subject and most difficult to master. Mastery of the language requires years of practice. This poor attempt at a study of this vast field cannot possibly serve as an adequate tutorial. However, some useful advice for beginners would be to commence the daily practice of data interpretation, which, in modern investment parlance, is data exclusion. Many losses, many investment mistakes are caused by premises or assumptions so laughable or idiotic that these cannot be easily replicated. These are therefore extraordinary and should be excluded from any proper loss calculation. The student of Modern Investment English should endeavor to engage in this practice on a daily basis. Beginners seem to prefer EBITDA calculations that exclude interest, taxes and depreciation, which are real expenses that must ultimately be paid. Years of toil with such terminology are required before one can aspire to interpret national economic data.

In the coming months and years we shall hear more of Investment English. The language has corrupted thought in a most thorough manner. It will entail consequences to accumulated wealth that are very profound as well as very unpleasant. After all, it was Churchill that also said:

> Now this is not the end. It is not even the beginning of the end. But it is, perhaps, the end of the beginning. [**]

[**] Speech at the Lord Mayor's Day luncheon at Mansion House, November 10, 1942.

