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Podcast Transcripts: Dan McMurtrie

Brandon Beylo (host):

This is take two with Dan McMurtrie of Tyro Partners. One of those issues we covered is the whole topic of inverted shorts. Which I think is such a fascinating idea, where you're trying to look for ideas on the long side by inverting what you would normally consider to be a good short. So let's start there. And, talk to us about how you came about the inverted short process and maybe what that looks like in your investment style today with some recent examples if you can give any.

Dan McMurtrie:

Sure. So, I mean, I think timing is a really loaded word in investing because people associate it with a lot of ideas they consider to be bad. But timing is ultimately a major part of the job. And when you're going and doing fundamental research on a name, you know, you need to have a reason, why are you doing the research right now? Why are you proposing that your firm take a position? Why are you taking a position? And I think that, you know, I was brought up a value guy. I consider myself a value investor, but I do think that that doctrine gets taken a little too far. And there's a little too much dogma in that field. And it's one of these... I really embrace timing as a concept, but I think it's important to think about timing as observing what's happening in the present, not predicting what will happen in the future. Those are very different things.

Dan McMurtrie:

And so from that perspective, I think a lot of people can understand it better because what you're really trying to figure out is, "What's going on in fundamentals and what's going on in price?" And there's a great Paul Tudor Jones quote that my friend Necker Value was posting recently on Twitter about how, with all of the data that's available now, people are obsessed with needing to explain every possible thing. And sometimes price is a good indicator. I'm not all the way to where Paul is but, I do think that there is a lot you can learn around timing if you actually think about it and think about what is useful and not useful. And really what are you trying to achieve? Whether you're trying to chief risk management, et cetera.

Dan McMurtrie:

And so for us, the big thing I think... The muscle group that we've really built out over the last five or six years since we launched the fund is first, really learning and building really a practice of buying more when a thesis gets confirmed. And understanding that even if a price is higher, if the situation has changed, the risk reward may be better.

Dan McMurtrie:

And so a lot of times we basically the way our process works is our research process is unrelated to our trading. Our research process is something that has to happen in order for a security to be tradable for us. If we don't understand the business that the security represents, we are not going to

touch it. And it's really not because I think trading is not profitable. I know plenty of very profitable traders who don't know the... You know, it's like the green lumber thing that Epstein Pleb talks about. I know a lot of guys make a lot of money trading who don't know anything about what they're trading or know very little. But I do not have the stomach nor the trading style to do that. So I need to understand an enormous amount about what I'm trading and about who I'm trading with in order to trade.

Dan McMurtrie:

So our research process comes first. Things that make it through our research process. We're trying to think about, "Under what circumstances would we go long or short, and what incremental pieces of information will change the distribution of a future outcome?" So the big mental model there is basically the Monty hall problem, which some people well maybe familiar with from freshmen statistics. Which is, you know, game show, there are three doors. And I think there was a car behind one, and there's like a goat behind another for some reason, something like that. There's like two bad doors. And there's a good door where you win something. And what happens is you select a door, and then the host would open one of the other two doors and ask you, "Would you like to stick with the door you chose, or pick the other door?" And the statistically correct answer is to always pick the other door.

Dan McMurtrie:

Because if you go back to your initial pick, if you select the other door, you actually are getting the cumulative probability of two doors rather than one door. And that's very counter-intuitive. And it's counter-intuitive because you assume you know something about the door that you picked, right? And you go, "It hasn't changed, I had a reason to pick that." And that's very indicative of a cognitive bias where your brain will backfit and make you believe you have logic for a decision even if you have no basis for the decision. So one, when there's a clearing event or some type of catalyst, right? Or incremental piece of information that takes downside for a company off the table. The risk reward, even if reward is lower, the risk can drop dramatically, making the risk reward much better, and you can justify a much, much larger position.

Dan McMurtrie:

So for me, a core position should be 4 to 7% of the portfolio. And we tend to wait in the positions. But if the stars kind of align and we see everything happening and we get confirmation we'll go up to 10% at cost, and we'll let those run up to about 20% of the portfolio. And we're very particular about... Having 1, 15, or 20% position on is very different than having 4, right? So we got to pay attention to what else is in the portfolio. We built this muscle memory around, when the downside gets taken off the table if the upside is still there, you need to be increasing the position. And that's really hard to do. It's something that Julian Robertson talked a lot about and a lot of great investors have really mastered, but it's a very, very hard thing to do. Especially if you come from a value school.

Dan McMurtrie:

Now, taking that a step further, when you're looking at a short idea, there's a lot of people who want to focus on the timing of when do you put that short on. But it's a lot more important to think about when you take the short off. And a lot of times when you take the short off, you need to pay it attention to something that's been called, the 180 principle. There was a guy who was kind of an OG Twitter person who has handles Dasan, D-A-S-A-N. And he has a great blog that I think is still online, about what he calls the 180 principle. And basically ideas that if you're selling along, you should probably

short it. Or if you're covering a short, you might to go long it. Now I don't think that's a hard and fast rule.

Dan McMurtrie:

It's not binary. But it's very important to pay attention to short theses, especially popular short theses where there's a lot of positioning in the name. Because similar to the long side when something happens where all of a sudden the company can't go bankrupt anymore, or something like that, you want to buy. There's a similar thing on the short side which is, there are shorts that everybody looks at and they go, "This is overly promoted. This is this, this, this, this, this." And you may realize that there's actually only one outcome that takes the stock lower and any other outcome, including nothing changing, will take the stock much higher. And this is something where most of the things we do to make money are basically ways we lost money in the past.

Dan McMurtrie:

And so we found that a lot of the things, well I don't know a lot, but a good percentage of the things where my initial knee-jerk reaction is basically look at something and say, "That's preposterous." If I force myself to look at it a little further I'd realize that while there might be a good short thesis there, at some point, it's kind of like tennis and I'm swinging the racket when the ball's not on my side of the court. It's like, yeah, I eventually want to swing the racket, but I want to swing it when the ball's coming to me. So a great example of this is a company called Celsius Holdings. And they're an energy drink maker, and it has kind of a troubled history. They were a supplement company based out of Boca Raton, Florida. And so if you've ever shorted stocks, I think Jim Chanos has referred to Boca as the world's largest unfenced penitentiary, which I always think is hilarious.

Dan McMurtrie:

We bought a position in Celsius Holdings, essentially because we believed the short thesis was correct. What was now obsolete. They had a digital business that was not growing very rapidly. And we had disclosed in our thesis that we thought it was a ripe target for a short activist piece, because there were so many scandalous little details. And then you add endorsed and published on it. And I called in and I'm friendly with them. And I basically said, "I disagree and here's why." And friendly conversation, it was fine. And he's not religious about it. He was like, "Okay, that's interesting." But as I was mentioning before, I think that a lot of analysts have this C+ problem where you end up allocating a lot of time where there's work to do, rather than necessarily where there's the most money to be made.

Dan McMurtrie:

And that can lead, especially on the short side, to you really anchoring to the most complicated histories of companies. And that can lead to a loss of perspective on what really matters to the stock. And so we always try to make sure we're aware of all that stuff. We really want to boil it down to what's actually relevant here to the actual trade. So Celsius is a great example of something where, the short thesis essentially became obsolete. And that's what we'd call an inverted short. And so we'd like... A lot of the research we're doing is around understanding the thesis in terms of... Or the hypotheses, not around the thesis, the hypotheses for a company. One of the potential bull cases, bear cases. And it changes over time. I mean, the market environment changes a lot. Last two years obviously consumer trends, everybody's lives have changed.

Dan McMurtrie:

We're sitting here doing this on zoom. And so we just, we want to be very open-minded. We want to have things tagged out in terms of, what might change or what's important because, sometimes you have a bad business. Another good example of a company like this was American Eagle, which started their Aerie brand. And it was growing, growing, growing, growing, growing, and nobody cared. And then, you know, we love these setups where you have kind of a business that people don't care about. Especially if it's the main brand where they have a smaller business, it's becoming a bigger and bigger part of the business. And there's usually a point where the short has been working, right? And people think that we're going to work and it continued to go down. And that's actually the exact point where the growth part of the business is becoming a material enough part of the business to move the top line in aggregate.

Dan McMurtrie:

So we pay a lot of attention to that and we're modeling that. And we try to kind of create systems that alert us at some point in the future when we should look again. And so that's kind of the basis of our process, is trying to understand what the hypotheses are for a name. What are the key road signs? Whether we're in potential future state A, versus potential future state B versus D. Rather than trying to predict things. But we're really trying to think about it in terms of downside. So we want the incremental information to take downside off the table so that we don't need to necessarily bet on a tail outcome. And what we're really looking for behaviorally is situations where people think things are going to be over forever, are going to be perfect for forever.

Dan McMurtrie:

Whenever people are making really strong, absolute, permanent left or right tail statements, that's an indicator that work should be done. Because if that's even slightly wrong, or becomes wrong, the returns are pretty tremendous. And so I think there is as much to be learned from studying when to exit shorts, as there is from looking at when to put them on. Because often shorts that are no longer good shorts are actually fantastic longs. And just by the mathematics of long versus short, the return profile of buying things that are no longer good shorts tends to be very, very good. Particularly if you're there at the beginning of that move, because these things tend to really push themselves. So there's a lot of people like to pyramid into their trades and, for good reason. But that ends up in situations where people are really heavily short something where even a light breeze can send a stock up 50 or a 100 percent.

Dan McMurtrie:

And if that's going to happen where all of a sudden that's going to lead to it being included in indexes and the business is actually doing well. And especially if it's evolving from a bad business to a better business. That's how you can get gray cost spaces and things that you want on for multiple years. And so that's something we pay a lot of attention to, and we're really looking for things that we think are obvious. And a big part of that is just trying to make sure that you are both having runs at names where you're zooming in really close. And also where you're zooming out and saying, "Okay, high level, wow it actually matters here." And it's tough if you're... I mean, I think this is something people will struggle with as they go from analyst to PM. Is they're so used to needing to exclusively zoom in to deliver that information to the PM, that they don't necessarily develop the muscle memory of zooming out and saying, "What really matters here?"

Dan McMurtrie:

And so I think, especially in the era of infinite information, avoiding that C+ problem, paying attention to really extreme tail outcomes that are embedded in the name, and really being salient about the

framing of what's going on and what actually matters, is really important. And, an old Boston mentor and friend of mine, partner of mine, Miko Keith at 12th street asset management, used to say, "Price simplifies." And I'm really a believer in that. I think especially with the inverted short concept, that works really, really well. And I think on both sides of that trade, of a short, you're really looking for what occurs that makes this incrementally a better risk reward, not necessarily what is a good risk reward to make a prediction bet. And so, when we're looking at... At the beginning of our process, when new things are coming into our orbit, we're really trying to think about how, if we play out how this investment might go, what is our ability to change our bet size if we're right or wrong?

Dan McMurtrie:

And the best bets are things where you can be really, really small until you know you're right, or have no position until you know you're right. And you can put a big position on once you know you're right. The worst trades are always the ones where you have to put a lot of risk on and be an event where you can't transact, and then there's going to be an outcome. And it's really psychologically hard, right? Because what you're saying there is you're going to miss a lot of gaps. And I do think that particularly in the value of school, there... In special situations people are trying to do Joel Greenblatt type stuff. And I'm a huge fan of Joel and everything around that. But there is a bias of, or at least a fear or bias, or however you want to say that of missing those big gaps up or down.

Dan McMurtrie:

And... But when you look at many of the greatest longs and shorts of all time, if you miss the first 50 or a 100 percent day, you actually still made a very good amount of money, but you also made it with far less risk and generally far less volatility as well.

Brandon Beylo (host):

Right.

Dan McMurtrie:

And so I think going into events, if you're being a little objective about it, you probably can only risk some small percentage of your max position, depending on how you size positions. But post event you might be able to put on a very large position because your downside is really, really capped and that's tricky. And so that, when you think about it that way it also changes how you think about the concept of circle of confidence and things like that. And so that goes back to why we really want to do the research upfront is, I want to have done that zoom in work so that I have a good view on how to frame the trade and thinking through, what's the next step?

Dan McMurtrie:

What does this get me to that? Because I think a lot of times when people are frustrated with, "Why is this evaluation multiple low?" They're not thinking through it like a game that's played multiple times. And so the issue is, yes you might be right on the next three months, six months, twelve months, but does anything the company... can the company do anything in the next year that can validly change the bare case for the terminal value of this business?

Brandon Beylo (host):

Right.

Dan McMurtrie:

That's usually the issue, right? Value trap means there's some value traps where there's shrinking and it's just a problem and that's bad. But there's other businesses that perpetually have low multiples because people just don't believe that there's a terminal value. Or they're high flying names and people think the terminal value is very, very high. And so then they're willing to take more cashflow duration risk on that name.

Dan McMurtrie:

And so we think a lot about how does what's going to happen in the next quarter a year, two years, three years, influence what people are going to think of the long-term? And then you need to understand, okay, does management in the company understand that? Are we aligned on that? Does their capital allocation actually foot with that? Because if you're going to be at a low multiple, because people don't believe in the terminal value, you can, if you disagree, you can just buy back a ton of stock. There's things you can do to make that advantageous. But again, it's also not clear in those situations, whether your return as an equity holder will actually come prior to some incremental information that changes that opinion. And so even if the company is sucking up stock for years, all the return might come in year 3, 4, 5, 6 of that process, not in years 1, 2, 3, you know?

Dan McMurtrie:

And so, we just try to think about that. We're trying to understand, who's trading the security, what's going on in the business, where the opinions, who's bullish, who's bearish? Our people interpret the information. And when we find something where there's an extreme opinion set, and one incremental piece of information can massively change the perception and the mechanism by which people are interpreting information. That's really when we want to be maximal long. And of course on top of that we want to buy something at the right price or shorted at the right price base. And we're going to have all the normal stuff on top of that. But we have a really big focus on the behavioral element of investing. Who else is at the table? Why is something happening? We don't find the concept of Mr. Market very useful. Like I want to understand who is short list and why? Who is long list and why?-

Brandon Beylo (host):

So when you say... When you say you don't find the... I'm sorry to cut you off. When you say that you don't find the concept of Mr. Market useful, what do you mean by that? And maybe you were about to go into that and I just cut you off. So again, I apologize.

Dan McMurtrie:

Sure. So I just think that there is an... I'm going in complete reverse about what I said about Walter Jones. I think there is an explanation for most things that are going on. And I just don't think the caricature of irrational people is useful. I think by allowing that thinking in your firm and your team, I think there's something inherently arrogant about it. And there are a lot of really smart people. I mean, there's something like 270,000 active CFA's all with MBAs every year, ton of people online, everybody works for the company, the founders. I mean, there's no such thing as having an outright information edge. You can have a contextual information edge. But most of these companies people are talking about, there's at least 200 people in the company, plus their families who know all of the realities of what's happening. All this stuff's getting leaked online now because you know, people are talking more online. And so, not like M and PI, but I mean just people are constantly on clubhouses or things, debating every element of a business, go to market strategy, all this other stuff.

Dan McMurtrie:

And, but contextual information edge is a very real thing. And so you need to understand why... So I think basically there's, I believe in kind of the form of market efficiency of, no free lunch. Meaning you need to understand... You can't just say Mr market's drunk and depressed right now or something. I need to understand why are people not owning the security? So, great example right now is China. Where you've had the Chinese government take several actions just to scare the living shit out of people in the US. But if we're being really blunt about it, it's mostly white guys who have no China experience, or if they have any China experience its because they flew to Shanghai, which is very different from-

Brandon Beylo (host):

Or they read a substack piece.

Dan McMurtrie:

Right. And they are beginning to conflate some isolated regulatory actions that are, in my opinion, very consistent with the party's actions over the last 20 years. With the party's willingness to destroy their access to capital markets.

Dan McMurtrie:

Those are... that's a big, big, logical jump. Now on the other hand, because that is a meme. And because it is memetically spreading very effectively and price is reinforcing it. If you lose money in Chinese equities right now, you are going to be asked questions by your stakeholders that you cannot really answer. So, even if you know President Xi, you're not going to have a real edge here. It's just very complicated. And so you're not going to be able to make an investment based upon facts. And so there's uncertainty and the uncertainty becomes price it's priced in. And so the reality is that there's scenarios in the market where... Look, if you're running a mutual fund or you're running a mega platform, something like that. It makes sense to just get out of these names because you need to preserve your business more than you need to preserve returns from those individual securities.

Dan McMurtrie:

And I know that there are other good businesses elsewhere in the world. It's not about being right on every individual name. You don't need to play this games. It's very rational for people to just to say, "China's un-investible." But as we're seeing right now, that means that the uncertainty and that opinion and the agency costs are being priced into securities. The opposite can also be become true. Well, what often happens now is I think the vast majority of the market is basically mandate driven investing. A lot of the smartest people I know, their our lives revolve around plus minus versus a very particular benchmark. And it doesn't really... They know an enormous amount of the securities, but they only have the real ability to tilt things up or down versus bench. And if something in the bench starts moving significantly and they don't have a position, they risk a serious under-performance and it's kind of inexcusable.

Dan McMurtrie:

Yeah. And so, I think that might be part of what's happened in healthcare and biotech this year, is that modernize and names like it have been such large contributors to returns that almost everything else has basically had to be sold to keep up with those names. You saw some of the things happening with Tesla. That's before you get into index, addition, deletion. And a bunch of other kind of games being played there. So I really want to understand what's going on from those people's perspectives. It's not reasonable to assume that the people at fidelity are just depressed or were manic or something like that. They're usually very level headed and they understand exactly what's going on,

but they have constraints, right? And they have agency costs and other things. So I'm really trying to... I think of the market as a network of incredibly smart people, all of whom have very nuanced constraints.

Dan McMurtrie:

And what I want to understand is what other people's constraints are and incentives are and how those things work. And then you can process information from that perspective. And when you figure out a constraint is about to be added or removed, that's when you get a big price point. And that's you know, you can go back to the Saurus breaking the bank of England. That was a constraint based trade. A lot of the greatest investments of all time were constraint based trades. Sometimes you don't know exactly where the constraint is. Sometimes you can't time it. But if you know it's there, you know it's getting removed. That's what's going to drive price. Or from a different perspective, there's a risk. You could say, agency costs is a risk, and it is a risk.

Dan McMurtrie:

And so you're choosing to take that particular risk in exchange for out performance. Or just absolute returns. And so I believe your job as an investor is essentially to select which risks to take in order to drive returns. It's not to... I just don't believe in the idea of riskless profits or things like that. I mean, even if you are doing high-frequency this, this, this your risk is that your system breaks or your rescue is something like that. There's always a particular type of risk you're taking to generate returns. Now the risks can be almost a zero, almost a 0% probability of occurring. But I think you're always choosing what risk you're willing to take for what return very simply. And my job is to identify risks which are mispriced and take those risks. So essentially you're selling insurance.

Dan McMurtrie:

I mean this goes back, you can mathematically foot this up with kind of Miller Modigliani and put call parity and things like that. So it's not an original idea. But I don't think it's fully appreciated if you think about the market as a increasingly interconnected network, how that happens. Because I think the big thing is one, not necessarily passive, but mandate driven, investing, combined with everybody talking is really changing how the market works.

Brandon Beylo (host):

Yeah. No, it's one of those things where, I'm always hesitant to even think that I have an edge. Whether it's in a security or whether it's in an industry or whether it's in anywhere, just because of the Michael Mauboussin calls it, the collection.. Or the, "Wisdom of the crowd." Where I think long-term investors, and this is something that cliff Sosin even described on how to balance long-term ism while at the same time, not using it as a scapegoat for under-performance basically.

Brandon Beylo (host):

And there's kind of this dichotomy you have to, you have to go between saying like, "Oh, Mr. Market's just wrong", and saying, "Well, actually, maybe they're all right, and I'm wrong." Cause again, it kind of feeds back into the contrarian nature that a lot of value investors like to do. They like to take the other side of the bet, say that, "I'm right. Everybody else is wrong." And when you step back and you think about that, and you think about all the research teams that are at Goldman, that are at Fidelity, that are at all these big, big firms. You're betting against all of those people. Not to say that you're wrong and they're always right. But it's just, I think you have to internalize that bet. And even speaking it out loud makes you realize how absurd you have to be to win those bets repeatedly.

Dan McMurtrie:

Right. So, yeah, exactly. And so what I'm really focused on is being high context as an investor. I want to understand who else has invested in this in the past. Who else invested in now? Why? Who shorted? Et cetera. I want to understand who else is at the poker table, as much as I want to understand the cards. Because I really want to have a really good understanding of what those people's constraints are. And most people, if you're friendly and reasonable and you're collaborative are happy to be like, "Look, I agree with the thesis. I can't own any more for XYZ reasons." Or, we invest in a company called Colony Capital. It's now called Digital Bridge and they were turning it around. And it was a situation where there was an enormous amount of [inaudible 00:29:29] in which a lot of people lost a huge amount of money and the company had changed new management, new business plan, pivoting into digital assets.

Dan McMurtrie:

It was a new business. And two things were true. There one, we called a lot of people we respect who are financials experts. And we said, "Why don't you own this? You cover this space." And one person said, verbatim, "Never fucking mention that name to me again. I lost \$300 million on it. And if I owned a share of it or even mentioned it to my clients, they would fire me." And I'm like, okay, that is a very serious cost, risk or constraint. Right?

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And so he's... what he's saying is, "Look dude, my optimization function is for this to survive as an investment firm and that's just an absolute no-go." And he's also saying to a different extent that he believes he's emotionally compromised. It's not irrational. He's not a depressed Mr. Market, right? He doesn't believe he can be rational in evaluating that particular company, given the emotional intensity of his interaction with the company.

Dan McMurtrie:

And it's actually very intelligent for him to pass on that pitch. And I think as you... We'll talk about process I'm sure later, but you need to really think about your whole process because getting involved in names that are going to put you on tilt is almost never worth it. It doesn't matter how much you can make. If it's going to completely dominate your mind. And you're going to turn into like a one stock account in real life, it's really, really bad and you can't do that. So our whole thing is trying to figure out the cost, constraints, risks, whatever, those things. What are we taking? And then once we really understand those, we can then test hypotheses. And so our hypothesis should be, this removes this constraint. This proves this risk is now only 20% of what people thought it was yesterday.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And that should lead to a proliferation of information. It should change people's interpretation frameworks. It should change the trading dynamics. And it should slowly allow those risks or agency costs or whatever to abate. And that should create more momentum, like patterns in the security. And

I think it's structural to the market and we'll be persistent for some time. On the flip side of this, we also called people who manage large amounts of money doing like normal TMT stuff. And they own every... So colony is pivoting into digital assets. Towers, fiber, cables, stuff like that. Anything that makes the internet work, right? And so we called the guys that cover that, and these guys know, some of these guys have been friends with the management at American tower for, 10 years or, a long time. They know these businesses really, really well. So why don't you own this? You own every.

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Dan McMurtrie:

They know these businesses really, really well, and so why don't you own this? You own every player in the space at some weight. Some of them you have 8%, some may at 1%, but you own them all, but you don't on this one. And they're very blunt about, "Look, the balance sheet is still 80% random healthcare and hospitality assets that we are not really authorized to invest in it. Until it's mostly digital, it's not in our mandate." And so I'm like, "Okay, so you're telling me that as this business pivots over the next couple of quarters into being mostly digital it will enter your mandate." And they're like, "Yeah, once it's a digital business, then that's in our mandate. And then we're going to look at it. We'll probably own it because we own everything. And it's also very, very cheap." So assuming that the CEO and the management team can execute, we will probably have a position in a year.

Dan McMurtrie:

So what I'm getting there, right? Is that due to constraints, costs, et cetera, I know why the specialists are not pricing in the information that they have. Right? It's not that I have information they don't is that they're saying, "Nope, not touching that. Not playing that games." Okay. I understand why the existing people at the table are not playing a hand. And I also know new players will come to the table if the following fundamental things happen the next six to 12 months. So that's usually the setup of how we're bridging fundamental into where we're investing is, do we have certainty that the next few incremental fundamental things are actually going to lead to changes in security market participant behavior? And we also want that at the same time lead to the business getting better. And we want to lead that, we think those two things combined lead to a reassessment of the terminal value, and that's essentially how multiple expansion happens.

Dan McMurtrie:

And so those are the things we're trying to understand. So we have a really big focus on understanding everybody at the table, long, short, etc, as well as understanding the business. And that's kind of the approach, so we do a lot of what we've called inverted shorts where it's bombed out really. And a lot often the shorts had been successful, the shorts were right. We buy a lot of things where we find people who are very short them, who are now it's like, "We're not short anymore." You know, it played out, it's good, but they're not long. And then we figure out, "Okay, is it actually a long thesis that one?" The issue is people are still optimizing to, "I can't own that because a year ago there were really smart funds out, pitching it short, and they made a lot of money."

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And one of the issues going to agency costs is allocators increasingly, rightly or wrongly, I don't know, believe they have at least some ability to understand individual security selection. And they really are

interjecting themselves into the investment process. And so if you go pitch a name and they go pull up their notes and they have somebody who pitched it short the way the allocator interprets it is, "I'm now going to compare Brandon and Dan and whose notes are better." And there's not a really elegant way to always make the point that both are right, that thesis was right last year, this long thesis right this year. And people don't have the mental bandwidth, the allocator doesn't have the mental bandwidth if they're doing 10 calls a day with managers to make those nuanced points. And so they out of risk aversion are going to exert pressure on money managers which creates these circumstances.

Dan McMurtrie:

And so ultimately the structure of the market is creating these socioeconomic constraint systems that is where absolute returns can be found. And that's really the core of what we're doing. And I think as the world becomes more and more digital, it's just going to get worse because everybody... and look I do think that there's a net positive here. I think investor outcomes broadly are better than they were in the past. There's a lot less nonsense fees, yada, yada, yada... But there is a trade-off and I think it's a net good thing that's happening, but the trade-off is we're having weird social constraints imposed in the market. And so that's where the inefficiencies are, they were elsewhere in the past, in the past it was could you get SEC filings and figure out the spin out.

Dan McMurtrie:

And now it's, can you understand the constraint system in the market? And I think that's probably the theme for the next five or 10 years. And I do think that's also part of why there does seem to be a trend of extrovert investors outperforming introvert investors. Now there are massive exceptions to that, but I think it's because you need to really work with infinite information and all of this socialization happening, you need to be very high context. You need to be talking to a lot of people with different opinions. You need to be talking to people of different ages, different geographies, different racial profiles, different genders, different economic positions. The idea that you're going to sit in an office in Manhattan and just do good fundamental work off of Bloomberg. I don't think it's going to be as advantaged as it was in the past, but that doesn't mean people can't do it, there are absolutely people... I mean, I know straight up people who you give them a Yahoo Finance login and they can print money. But from my style, that's not what I do.

Brandon Beylo (host):

I call that the Michael Burry effect. And I'm a huge, huge Michael Burry fan boy it's been well-documented, but I think one of the downsides of that movie was it gave a lot of newly minted fund managers, or want to be fund managers, the false idea that they can just whip up their laptops, go alone in a room for hours, not answer to LPs and basically just tell LPs, "Look, let me do what I do. I don't have to answer to anybody. I'm just going to lock myself in a room." And obviously Michael Burry, he self-diagnosed himself with Asperger's, and so I think a lot of people when they saw that movie and they saw him, they said, "Oh, well, I can do just that." Like, "All that matters is my performance."

Brandon Beylo (host):

And this is something that we're going to get to when it comes to emerging managers and how that hurts. But I think that, and it's the only reason I say that is because extroverted versus introverted managers, I lean on the more introverted side where I could sit in my office for nine hours a day and read transcripts and maybe call one or two friends, and I'm just now starting to get a network of

investors that I can feel comfortable calling and chatting with, one of them is Brad Hathaway, who is a great investor.

Dan McMurtrie:

The man.

Brandon Beylo (host):

Brad Hathaway is the man, and we share a lot of similar ideas and he's someone that I'm starting to finally just pick up the phone and call and say, "Hey, I'm thinking about this idea. And I know that you like these types of ideas." Like, "Why don't you red team this for me." But just interesting to hear your thoughts on this idea on the Michael Burry effect when it comes to managers and how they see themselves as allocators.

Dan McMurtrie:

Yeah, I think that there's another book my friend Elise always mentions, *The Age of the Unthinkable* by Cooper Ramo, and there's a bunch of premises in the book, but the idea is essentially that technology is enabling tools that make highly asymmetric warfare possible. So, two guys in a bedroom can create Google, Hezbollah can mess with Israel with like six guys. I mean, just a bunch of stuff where massive institutional advantage can be circumvented. And the big thing is basically that change is now becoming a constant in the world. And so most games people play, any game that becomes advanced, whether it's Magic the Gathering, or the stock market, or poker, become meta-games, where everybody gets good and then it becomes, why would a smart person lose? And so this is my main focus as an investor is, I will never assume other investors are dumb, other investors are very smart. And I try to assume that I'm the dumbest person in an investment.

Dan McMurtrie:

I'm trying to figure out why a smart person is going to have a blind spot, and if you believe that the world is becoming more interconnected, then it follows that... And I think that technology is allowing communication to be more rapid, so you and I can hop on a Zoom and we can chat in two minutes. It's not a big deal, we can send a Twitter DM, or email, whatever. It's getting faster and faster, so more communications. And so things that used to be problems that might've killed a company or an idea are now getting brainstormed by more people, with more resources, with more perspectives and things are changing faster. People are figuring out ways to solve this problem and circumvent them, hack them, whatever. And so the issue is that if you do not have a network and that's not a core capacity for you, you're going to really struggle because facts can change really fast. And so we have a big focus on underwriting culture and teams at companies, in trying to understand the companies ability to change, or the country's ability to change for looking at the market.

Dan McMurtrie:

And that brings about a completely different lens to look at something because I think we think about businesses as networks of people that have some assets they can use. Those are tools they can deploy rather than assets that happened to be managed by some people. And that's just, I think, different from some of the historical examples of investing. And obviously that's not universally applicable, but that's just useful for where I invest in the long short equity. I tend to be pretty thematic and I tend to do consumer, technology, industrial, healthcare. And those four sectors are also all kind of bleeding together now. And you can see trends and things kind of going from one to the other. And it's very dangerous to assume that an innovation in tech isn't going to show up in healthcare, and isn't

going to shop in consumer because once an innovation happens, it's basically a tool or a weapon that is available to all people on the battlefield.

Dan McMurtrie:

And so, for example, I think that the way Donald Trump and/or like an AOC have used social media is a precedent more than a historical fact. And so they just showed, both of them in different ways, and many other people just showed an ability to hack society essentially, and all of mass media and social media in a way that is profound from their phones. And that is absolutely incredible, and so that's not a table stake technique. And so one of the things is the underlying thing you're looking at is changing, and basically you're going to need people to collaborate with, to tell you, "Hey, I think this is changing." Or, "Hey, it's not changing." Or, whatever.

Dan McMurtrie:

Too, you're also going to need other people to spot trends for you. Because a lot of times these new strategies or tactics, like using social media, or streaming, or collaborating online, or what have you, are going to happen in communities, is that you aren't a part of because there's just a time constraint, or it's not interesting to you. And so you might not be personally interested in something like Only Fans, which is in the news today, but Only Fans might be an indicator of a broader trend in the consumer economy, and how the user interface is going to work and how micro transactions might work. And there's a lot of precedent that pornography tends to lead technical trends. I mean, it's like a joke, right? It's like Betamax versus VHS... DVD versus HD, or Blu-Ray versus HD-DVD. And a little that's over-hyped, but you need to have as many perspectives as possible.

Dan McMurtrie:

The other thing that's really tricky about this, and this is something we have in the outline of things we want to talk about is what we're calling the Maslowian evolution of markets. So there's this trope, right? Where every parents or grandparents look at the younger generation, they always look to the younger generation and say basically the younger generation is soft. And that's absolutely true. I mean, my generation is ridiculously soft compared to the World War II generation. I mean, it's crazy. We didn't have to go through any of the stuff that they did, and so there's always a joke of, "I had to walk uphill both ways in the snow to school." And stuff like that, but invert that and it becomes clear that the reason everybody's getting softer is the world is becoming a better place. There is not as much of a need for manual labor. There's not as much of a need for soldiers, thank God. There is not as much of a need for all of these really brutal, hard things.

Dan McMurtrie:

And so as a result of that incremental value is coming from things that are higher on the Maslow hierarchy of needs. We are not as concerned with crop yields, but now we're concerned with crypto kitties. Now, if you're somebody who came up in an era where food was uncertain, can you imagine how ridiculous it sounds that your kid is working on a cryptocurrency cat pic that makes monies on internet and doesn't actually do anything in the real world? It sounds and it feels ridiculous. But if you believe that the world has gotten better, I think it objectively has, with many trade-offs, and that it's continuing to get better, then actually you should expect incremental value to come from ever more trivial things.

Dan McMurtrie:

I mean, what's the difference between the last few iPhones? It's that you can get instant, high quality video to your phone, that you can download songs faster so that you don't have to spend the five

minutes or 10 minutes downloading songs on to your iPod from your phone, you don't have to carry two devices. We're talking about, these are products that are 10, 100, \$200 billion products that what they really do is they save people five minutes, or they don't have to think about this one thing. And the products that are incrementally selling more and more and more are just dumb. Like, and I guess it's just the reality, right? So now the issue is it's so easy to look at all of those and say, "That's stupid. That's a fad." "That's..." whatever, but actually that is the nature of progress. The nature of progress is ever more trivial nonsense.

Dan McMurtrie:

So that's something that as you age, there's this great quote, I think it's Douglas Adams who did Hitchhiker's guide to the galaxy was like, "Anything that's created up until you're 15 is..." I'm going to butcher the quote, "Anything if it's created after you're 15 is cool, or is exciting, everything up till you're 30 is something you can do work with, anything created after you're 30 is unnatural and against the ways of God." Or, something like that. And I think there's really something to that. Where it's very hard, especially now, as things are speeding up to know what is signal and what is noise because the things that are signal are getting dumber, that's really the main take, is that all of a sudden... I mean, who 20 years ago would really have thought that Instagram would be one of the dominant social media platforms. It actually does the least, of probably most of the social media platforms, it's basically photos of random stuff, and it's hyper dominant, and it's just because people like it.

Dan McMurtrie:

So if you can't... So there's the great, I'm a huge Ted Lasso fan on Apple.

Brandon Beylo (host):

Oh, I love Ted Lasso. I just watched the latest episode last night, actually. Love that show.

Dan McMurtrie:

It's fantastic. And we had an intern come in and I told the intern, he said, "Anything I should do before I come in." And I said, "Watch Ted Lasso." And he came in the first day and I said, "Did you watch Ted Lasso?" He said, "No, I thought that was a joke." I said, "No, that's not a joke..."

Brandon Beylo (host):

"You're fired."

Dan McMurtrie:

"Go watch Ted Lasso." "Get out." Fired the kid, no.

Brandon Beylo (host):

"Get out."

Dan McMurtrie:

But I think there's that line that I think it's Walt Whitman, that he quotes, "Be curious, not judgmental." That is more important than it's ever been. And I think the thing you need to understand is that most things that are happening now, there's so many new things that are happening now that most of them are not going to be for you. Like, I don't get 90% of the things in crypto. I don't understand half the consumer businesses. I understand the Xbox, right? I understand Star Wars and Disney, and I can do

six hours of podcast content on Star Wars, but I don't get half this stuff, but that doesn't mean... I can't judge it because it's not representative of everybody else, and I need to talk to people like who are really into whatever that is.

Dan McMurtrie:

And so we call it tasting the Kool-Aid, where when we see something that seems insane to us, we have to go into the lion's den and go talk to the people who are really into that thing and figure out, what is this from their perspective? And sometimes you walk away like, "No, that's madness." Like, I went to like the Ethereum conference in November of 2017, right before that Thanksgiving where everybody was like, "I bought a Bitcoin." And then crypto crashed. And the take away from that conference was, "This is absolute madness, run." But often it's not, often you find that it's just different from what you're interested in.

Dan McMurtrie:

And one of the big things I think you could see this on Netflix. Anybody can appreciate this, as the amount of content and ideas and all this stuff is expanding exponentially. People are a little more open to and open about weird niche-y stuff they like. So all of a sudden it's not that unpopular to like anime, and there's a big anime section on all of the streaming services, and you're finding nichier niche-y categories. Like my girlfriend and every other woman I know is obsessed with serial killer content. Like, it's My Favorite Murderer, or all this other things that I'm really worried they're going to run out of serial killers, and we're going to have to start killing women just to have enough content.

Brandon Beylo (host):

Making new ones.

Dan McMurtrie:

Right. I mean, I think we're going to run out. But so there are these micro-communities developing in all of these things and they're becoming really big businesses. And a great example of this was the CEO of Cody, the fragrance conglomerate was one of the first I saw, I think she spoke about, instead of having a big movie star promote their fragrance, they went and they found 50 or something, TikTok influencers that had very specific audiences that bordered the large spending audiences they wanted. So instead of looking for 18 to 35 year old affluent women in New York, which is really expensive to advertise to, they would find a really obscure set of 50 small target audiences that bordered that so that those people would see it, but they're very cheap to acquire.

Dan McMurtrie:

And by going to these micro communities, they're able to laser target at people. And that actually led to them having the biggest fragrance launch they've ever had, during COVID when nobody needed fragrance because everybody's inside. And so that's a great example of a meta game coming into existence using micro-communities on a new platform and then using as a strategy and a tactic to sell a product that doesn't even need to be bought at that point in time. And so that's something that like-

Brandon Beylo (host):

Revolve also did a good job of that too, where most of their advertising and marketing was partnering with really, really good looking Instagram models, and that was it. It wasn't huge advertising campaigns. It was, "Hey, you shop, use our clothes." Like, "Why don't you just post our clothes here to your 500,000 followers." Way easier to do that on all ends.

Dan McMurtrie:

Absolutely, and so what you're looking for is situations where these meta-games are developing, that's an example of the meta-game forming and then starting. But you're not going to spot meta-games that are developing, unless you're talking to people in different communities all over the place, right? Because you're just not going to see them, like I have enough things that I need to pay attention to that I want to pay attention to, and I have my family and girlfriend and I have a whole life I have to have to manage. And I can't act actually appreciate everything in the world, right? So the only way to possibly do it is to have people that are plugged into these networks, maintain those relationships, and you can use these digital tools like Twitter to augment your ability to do this.

Dan McMurtrie:

So there's this concept that shows up a lot in social science called the Dunbar number, and it's basically, I think it's like 250 people, and it's the estimate of how many people you can really have a friendship with. And it's basically like how many hours in the day, how often do you talk to somebody, et cetera, et cetera... Now that number changes significantly with the advent of the group chat, right? The second you can have 15 people in one group chat, talking about a topic, all of a sudden you might be able to actually maintain a reasonable conversation with a thousand people, a reasonable relationship with a thousand people.

Dan McMurtrie:

And also if you're in public, like I'm on Twitter all the time, people feel... I was at a bar last night there was an event my friend through and five people came up and they greeted me as a friend and I got to know them and it was cool. And it was because they were very familiar with me because I'm just using Twitter to be seen around town essentially, in a way you would be old school in the town square, or a social club, or the gym, or whatever. But you can do it at so much bigger scale, so all of a sudden we're escaping the Dunbar number as a human limitation. So that's another example of constraints being removed, so a constant theme, the thing you were looking for are constraints being removed, meta-games developing, and I think you need to be building a network of networks of really smart people who you collaborate with. And one of the things that is underappreciated is that given how many interesting opportunities there are, how many smart people, all of that, is that you really don't need to be selfish.

Dan McMurtrie:

And it's probably counterproductive to be selfish now because most of the favors that you can do for somebody in their life are introductions or simple feedback. And so if you can spend 30 minutes a day sending a couple of thank you notes, sending a couple of introductions, doing little favors for people that compounds so rapidly over 3, 5, 10 years. It's absolutely crazy in this digital era, and if you're the person who is making awesome things happen by introducing two smart people that should collaborate on a team, you're going to be fine. You know, I don't know what that looks like, it depends what you're doing, what you want to do, all of that. But really the people that are worried about, "How do I get paid on this." Or, "What's in it for me?" Or, WHAT is this person going to do for me?" Or, "That person, I didn't like what they said this other time." They're just obsolete. It's a very, close minded, ignorant way to go through life. And I feel sorry for people who think that way.

Dan McMurtrie:

And there was an era where in order for you to win somebody else had to lose, but the world is becoming a lot less zero sum. And in America right now, it's very easy to be pessimistic because of

how crazy the news is. But we're having hundreds and hundreds of millions of people come out of poverty globally every year. There are so many incredible people who are arriving on the national and international stage that are just doing fascinating things. It's one of the most exciting times ever to invest, I think you have to come out of COVID profoundly optimistic for what humanity can accomplish. And yes, understanding that there are both trade-offs and there are significant challenges to be met, but I've never been as positive as I am right now on everything. And I think that the core skill everyone needs to develop is this ability to think about building a network, not as networking to get stuff from people, but as building an ecosystem of people where you're adding value and you're creating new value by connecting those people.

Dan McMurtrie:

Because if you understand that everything else will fall into place. And actually that network will give you, that ecosystem is going to give you signals on where to go. You're going to see the deals people want to do, you're going to see all these other things. Stuff is going to pop out of it in an emergent way that you can't really predict, but it makes serendipity almost automatic. And that is the most powerful skill set anyone can have right now, and it is the key to being successful over the next 10, or 20, or 50 years.

Dan McMurtrie:

And I think that some people have a negative aversion to networking because they view it as manipulative or extractive or otherwise a kind of taker-y thing. But I think what you need to reframe that as understanding that the reason people value networking, the reason that networking is important. It is not about nepotism, people always default to nepotism or lack of meritocracy, "Oh, they only did that deal because they're friends." No, no... the actual reason is that anything that matters in human history that you can find was accomplished by a team, not by an individual, it's always a team. We did not build the atom bomb by a single guy. Turing could not have cracked the Enigma Machine, or whatever it was called, by himself. There was a whole team of people, right?

Dan McMurtrie:

And the reason that networking is important is you are doing a bunch of little low stress, low impact runs of people testing out, can they collaborate with you? Can you be a good team? And then when there's an opportunity that lines up where whatever the content is and the capital or whatever, they're going to form teams based on their assessment of the ability to have a team, more than any other factor. And people don't understand that. And a lot of people I see who are kind of anti basically social engineering, they only this very scarcity mindset, dark version of building a network. And they don't understand that it's really about building teams so that you can actually accomplish great things and solve problems. Because if you can't, it doesn't matter how much resources you can marshal, if you can't marshal people and you can't marshal buy-in, you cannot accomplish anything, and it doesn't matter if you want to.

Dan McMurtrie:

I was talking to a friend of mine the other night. He really wants to do something significant with his life in nonprofits. And I gave him this exact advice, I said, "The number one thing that's going to determine whether you make an impact, or you're bitter and you don't is your ability to build an ecosystem of people." So that's the number one thing. That's why extroverts are doing very, very well in the market, and introverts are struggling with obvious exceptions. And it's more important than anything else in the digital realm, and it relates back to that Maslow hierarchy of needs concept, that's

making signal to noise harder. And I think it's just the absolute number one thing that everybody should be focusing on, regardless of what field you're in.

Dan McMurtrie:

Whether you're an analyst [inaudible 00:59:44], random person, non-profit, for-profit, it doesn't matter. And if you're a student, you should be doing this even more because the earlier you start it compounds.

Brandon Beylo (host):

Right.

Dan McMurtrie:

People think about compounding their monetary capital, but they don't think about compounding their human capital. And you can compound your human capital, anybody can compound their human capital at a triple digit rate. And that is the absolute number one thing. And in this era with these tools, when you can shoot somebody at DM and get on a Zoom, I mean, there's nothing holding you back. And yeah, some people are going to say, "Fuck off, I don't want to talk to you." Right? That's fine. But I think one of things you realize if you ever try to sell something, most people have never sold anything.

Dan McMurtrie:

But if you ever tried to sell something, you ever try to raise money, you realize that if you are friendly and have good intentions... And I think it's important to only try to sell somebody something, if it actually solves a problem they have. Like, I never want to go convince somebody to buy something that they don't like. If somebody is not a suitable client, I'm not going to talk to them about what I do, unless they care. I don't believe in conversions to the faith. It's like, if you already liked the... You know, "Are you interested in Catholicism? I'll tell you about Catholicism." Otherwise we're good.

Dan McMurtrie:

But from that perspective if you're approaching people reasonably politely with good intentions, collaboratively, all of that, and they respond negatively to that, then they were never going to be a good partner of yours or a friend of yours anyway. And you have to get over it, you got to realize that, "Okay, that's just part of the distribution." A lot of people just it wasn't meant to be, it never was going to be. And I think people don't take swings as they should on building relationships because they're worried about that because some part of them thinks that if they put more effort in, or waited, or planned it better that then they would make it work. But that actually is not the case.

Dan McMurtrie:

And instead, actually, if you build a big enough network to where you get social proof through other people basically vouching for you and saying, "Hey, Brandon is a good guy. I know him really well, he's really smart." You know, whatever it is, that person might come back and say, "Oh, hey I talked to my friend, he mentioned you, I saw you sent me an email. I didn't respond. I apologize. I'd love to get on a call." That's the only way you're going to convert somebody back is basically if somebody they already like says, "Why don't you like this person?" And also the other advantage is given that there's so much chatter out there, people can't attack you really because people pretty frequently people talk trash about me on Twitter, I see it, I usually mute or block people. But I'd say 80% of the time when somebody says something negative about me, and it's always completely uninformed nonsense, or they're just making wild claims, or just calling me an asshole, or fag or something.

Brandon Beylo (host):

So what is it usually? Like, what are the run of the mill Dan McMurtrie shit-talking?

Dan McMurtrie:

I think there's a lot of people who are just like, "He's not that smart." Like, "He runs a small fund." A lot of people like to... some people have said my haircut looks like shit, or just random nonsense. It's all like high school, whatever. There was one guy who's like, "He's a fraud." And I was like, "What does that mean?" Because I've been audited like six times, I'm embedded by very serious people, and that's a really big claim.

Brandon Beylo (host):

A very big statement.

Dan McMurtrie:

Yeah. And I'm like, "I mean, if you have anything to say behind that I'm glad to hear it, but I don't think so." And that's really isolated, I mean, it's just these are kind of people that are very a bitter and are doing the exact wrong things with the internet. But what I found is that because I spend a very considerable amount of my time just getting to know people, meeting people, talking to people, and most of the conversations don't yield any direct benefit to me or anyone else, it's just interesting. There's all these bank shot things that happen. And now what I find is whenever anybody... it basically forms this like energy shield around you, where if somebody tries to say something about you, somebody maybe you don't even know, pops in and is like, "That's bullshit, he's not fat, he's in the gym every day. I just saw him at Equinox." Or, something. You know, just making up a...

PART 2 OF 6 ENDS [01:04:04]

Dan McMurtrie:

He's in the gym every day, I just saw him at Equinox or something, just making up a situation. People will start defending you because of your social credibility and then it becomes very difficult for people to come at you because they can't even map what your network is. In the past people basically were a lot clicker in the past, right? I mean people forget, it was only 25, 30 years ago that the banks were still segregated by basically Jewish and non-Jewish. I mean, that was not that long ago. This was a clicky business, and that's not that it's not clicking now but now you can have... You could do it in the past but now you have a real ability to have friends all over the place.

Dan McMurtrie:

I know a lot of hedge fund guys and a lot of friends in the art world, film world, venture world, farming, random and all of a sudden it's like really dangerous to just malevolently try to bash that person because you don't know who's going to pop out of the woodwork and be like, "Yo, that guy is the man. What is wrong with you? How dare you?" I think basically Twitter is policing itself better over time because of that because the online relationships are translating to offline relationships, and vice versa also the offline relationships are going online.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And just like everything else in life, it's the same people over and over again. Occasionally people go away, but usually people don't go away. The people that make it in markets I think three or five years, five years is probably the mark, if you make it as an entrepreneur for more than three years or you make it in markets within five years you're probably a lifer. And so it's the same people over and over again. And then you start realizing enemies are really expensive. And you're actually like, despite what movies might tell you when you're a kid there's never a pay-off from having a beef with somebody, right?

Dan McMurtrie:

Life is a video game and what you're trying to do is add people to your party, right? It's Final Fantasy and you'd much rather have Sephiroth on your side of the game than on the other side, and that's really like the whole game. I think there's this massive social game building out around digital media and how the digital media is becoming augmented onto real life 24/7. And I think we might sound like we're really far off markets, but it's not because this is how information is moving around in markets. If you ping somebody and you say, "Who knows about Blank." The world's real small.

Dan McMurtrie:

When you start calling around serious people about who really knows Match Group, there's like 10 people who everybody thinks is the ex. Now they might not actually be the ex but it doesn't matter because everybody thinks they are, right? And some of the things you can do to add value is if you meet somebody who's really well known on Match and you know a 23-year-old kid that's super passionate that actually knows more, you can introduce those two and that might be a great mentorship relationship or something like that. There's just a lot of things you do.

Dan McMurtrie:

But you have to keep this mindset of always trying to figure out how do you add value to everybody you're interacting with if you can? And everybody has constraints in time and all these other things, so you just got to do what you can. And if you're on the other side and you're reaching out, if you reach out and somebody doesn't respond the reality is they probably get three or 400 emails a day and they just missed it. You got to develop a little bit of a thick skin and you got to try to be helpful. And if you keep doing that your human capital will compound way faster than your monetary capital. And I think once you get to five, seven years of doing that it's way more valuable than any investment results you could have. And it's going to inform your investment results over the next five or 10 years.

Brandon Beylo (host):

Mm-hmm (affirmative). I'm going to go back to something you said a while ago before we went off on that awesome tangent about networking. Which actually made me think before I ask the question, a great networking strategy is the perfect anti-bullying defense mechanism. Where if you're getting bullied and you've got this awesome network it's like rolling up when you're in grade school, rolling up with a squad behind you. Where someone mentioned something and then six kids come out of the bushes and you're like, "Well, where did they come from?" And they're all ready to back you up. It's just this fun mental picture.

Brandon Beylo (host):

But one of the core, I guess, theses that you've described and I think both of us agree on is it seems like all of the major friction in society from problem-solving has been resolved. And the reason I

mentioned that is now all these incremental improvements are seemingly more contrite and more, I guess for lack of a better word they're just stupid and they don't seem like they're worth much. And you mentioned earlier the idea of walking uphill both ways to go to school I think it's funny now where I think the equivalent of that is people tweeting how they have been four days without sleeping on their Eight Sleep mattress and now their recovery is back to 80%.

Brandon Beylo (host):

That is today's equivalent of walking uphill both ways. My big issue is, and this is something that plays into my big metathesis on markets which we'll get into later, my big issue is how does one invest and allocate bets on businesses and technologies that at the margin seem to solve such small problems? In other words, how do you convince yourself that these little incremental improvements are big businesses? And I guess a way to frame that is Peloton for example is just an iPad with a bike.

Brandon Beylo (host):

You can break it down to that level. And from their earliest days they were turned down because a lot of people were like, "This is stupid. This is just a Nautilus with an iPad. Where's the incremental improvement and yet Peloton is this massive successful fitness community that's way more than just the hardware?" So there's so many bodies in this graveyard of incremental improvement. How do you in your process separate the wheat from the chaff? Where it's like, "All right, this thing may seem stupid at first but you can actually build a business around it."

Dan McMurtrie:

Yeah. Peloton is really tricky too, because Peloton is not the first company to try this. So that's the other issue is that a lot of these, if you get a lot of reps especially if you do short selling and you have a little bit of a pessimistic [inaudible 01:10:54] like I do, people bring you stuff and you're like, "Dude, I've seen this 12 times and I'm 12 for 12 on shorting it or something like that." So it's tough. So I think at a high level begin with one, you're not going to catch them all, this is not Pokémon. And you need to be very okay with missing certain pitches.

Dan McMurtrie:

Because what we're ultimately concerned with is your ultimately concern as investors is your whole investment process and how that syncs together and how that syncs with your life and how that syncs with your partners and all of that, right? So it's not about getting all of these. I'll tell you my solution then I have thoughts on different ways to do it. My solution is there are names like roadblocks or a stripe or something where they're just trading at astronomical valuations, because there's a very high degree of faith that this is the winner.

Dan McMurtrie:

And there's a lot of reflexivity involved in that with people giving them that really low cost of equity to go do things. And with some exceptions I'm not able to do that in a way that I feel I have a structural edge, and so I don't generally do that. And so that's stuff where there's clearly a tipping point has occurred and I think it's already apparent that there's something there and the question is basically the magnitude of it. On the flip side, there's things where there's a new idea and it's a little bit speculative and we're not really sure if this incremental thing is a big deal.

Dan McMurtrie:

There's something in the middle, and in the middle a lot of people want to argue about stocks that are at 30 times sales or three times EBITDA. I'm a lot more interested in businesses that are trading at

exactly the market multiple, because that's actually the bucket that makes the least sense to me. Because I don't really believe in the idea of an average business, because if it's actually completely average then it's completely undifferentiated and it won't stay there. So things that don't screen abnormally at all to me are really interesting more than things that clearly are exceptional [inaudible 01:13:21].

Dan McMurtrie:

And I love businesses, as I mentioned earlier with Celsius, I love businesses that have an existing business that have a new growth effort inside them. Where they have a strong business it's maybe a little bit outdated, whatever, but if they basically have a cashflow co, that's what we call it, then we have an internal growth engine. And what we're really looking for is something where that incremental thing that seems silly, one either removes a significant constraint inside or outside of the business particularly in B2B businesses or changes consumer behavior significantly in B2C businesses.

Dan McMurtrie:

And one of the things is that the initial data must look like a fad, right? Definitionally it has to look like a fad. So fad is a reason to put something on your screen not a reason to invest. What you're really looking for is the sustainability of that. And so if you go look at growth curves, if something doesn't burn out within a certain period of time basically if you extend time out. If something doesn't burn out at some point it's not a fad, right? So what we're trying to do is figure out can we create a hypothesis we can test about if this was a fad when would it die? And why would it die?

Brandon Beylo (host):

Interesting. Like the half-life of a fad basically.

Dan McMurtrie:

Correct. So is it a one-Christmas toy or is it a 10-Christmas toy? And also when we look inside the business is the special thing at this company that product? Or is it a company that can produce products like that? So this goes back to culture. Culture we think is the most important thing that allows you to handle dynamic environments and we think it's comprised of three things, values. And obviously it's your stated values, here's what we're about, here's what we do, here's the ethos and obviously that can be bullshit and backfire.

Dan McMurtrie:

The second is rituals, the actual things you do at the business every day to make that stuff real. And then mantras, what you say and how you say it. Because if you repeat something enough and if you behave in a certain way, enough, if you pretend to be something long enough you will become it. If you want to be an athlete, you know the best way to be an athlete is? You go to the gym and you practice pretending to be an athlete. And if you do that every day and if you do it at your meals, you're going to be as much of an athlete as you can ever be after a couple of years, right?

Dan McMurtrie:

John Danaher's name is big and may coach like he says, you can transform your life completely in five years if you just do that. Because if you do it for a year you're going to change it, but in five years you'd really gain some mastery. So we're trying to understand a few things there, is this a company that has a culture that produces things like this? Is it something that's changing the network inside and outside the company? Is it changing the customer behavior? How sticky is it? Things like that. And so one, we want to see initial traction, two we want to see community form around it.

Dan McMurtrie:

So I'm looking at a fad, we break fads down into four, or fads that may become something bigger, we break it down into four steps. And this generally relates to internet content related things, but there's similar things in other places. Step one is content. So the material of the product, whatever it is. It's getting out there, people are seeing it, and there's the question of is it good/do people like it? Step two is reference. Does this become what my friend Dennis Hong at ShawSpring calls a cognitive reference? Do people say Google or search, right? Like nobody says, "I'm going to go do a video bike." They say, "I'm going to Peloton." Right?

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

So it does become a reference point. Because then people start to have a really base level association with the product. And once people have a base level association with the product, then you get to the third level which is advocacy. And one of the really powerful things is consumers without even thinking about it start recommending the product, start selling the product for you. And so what you really want to look at it as that the handoff from the company selling the product to the user selling the product. And if you get something where the users are selling the product and they're all advocating for it.

Dan McMurtrie:

So you've seen this with Eight Sleep and you're seeing this with a bunch of stuff. Packing McCormick is killing it on the blogs and all this stuff. And I'll tell you that I'm raised Irish Catholic so there's a deep cynicism streak in me, and I believe everybody should be confessing all the time and weaponing yourself. I've really struggled as I've seen these promoter snake oil salesmen looking strategies, to me, strategies become market standard. So multi-billion dollar companies do stuff that I think is latent skinner box manipulation. There's a great South Park episode on mobile gaming that I think everybody should watch and deciding to stop.

Dan McMurtrie:

And so as you go from there once people start advocating, then there's another question of what do people do with the product once they start getting it? Do they start building stuff on top of it? Do they start integrating it into other processes? Because what is stickiness really? Stickiness is something's important to other things, right? So stickiness is we can't replace that accounting software because we have to do taxes every three months and it's a pain in the ass. And we can't be down for a month, and if the switch time is over three months there's no window during which we can switch. That stickiness.

Dan McMurtrie:

Stickiness is I need this device to make dinner for my family every night, stickiness is if my wife doesn't watch this before bed she's cranky and not going to be happy, if my husband doesn't do this he's not happy and our house has to remain in order, that stickiness. John Hempton at Bronte Capital always says that he wants to know who has the gun in the situation, which I think is a really funny way to put it. So if all those things happen and the company is listening to how users are integrating the product or whatever it is into their lives, whether it be B2C or B2B or whatever.

Dan McMurtrie:

Then there's step four which is community. And community is where you don't have to necessarily think of what the next business or product is because the users tell you. And the users go, "Hey Tobi, you know it'd be cool if Shopify did blank, blank, blank, blank, blank." And then Tobi in a brilliant move would do something like call that actual individual person and say, "Hey, I got your note. Be sure to open Shopify tomorrow morning at 8:00 AM." That person then writes a Twitter thread and is like, "Oh my gosh. The CEO of Shopify built my request. Dah, dah, dah."

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And one, that person is thrilled as they pay you an incremental \$300 a month.

Brandon Beylo (host):

That's a customer for life.

Dan McMurtrie:

Right. And then they're going to advocate for you nonstop and dah, dah, dah. And then you have that reputation. And then imagine trying to poach that customer. You're never going to get that customer away from them because the trust they've built is so strong because that community creates... Any business ever the CEO could call and personally sell you, and that probably means a lot to you. And that human old school touch business still works, but you can do it digitally at scale. Again, it's what we were just talking about with social engineering and building a network. You're using the digital tools to do old school human-to-human handshake or company type business, but at scale and passively and 24/7, 365 always on and that is the cutting edge of a business competition right now. It is so ridiculously hard to compete with it.

Dan McMurtrie:

So that's kind of the process we're looking at. That's a framework, so we're going to go look at an individual business, dig in, and then we're going to try to find things that we're seeing these patterns and we can get data on users or whatever the relevant thing is. And then what we're trying to do is when you get deep enough on something, you can then zoom back out and you can create a rough but accurate hypothesis test of if this is a fad it won't make it past X. So for example if you think like, what are those little funny head toys that make the video game toy company.

Dan McMurtrie:

Anyway. So if you're worried about something being a fad and Christmas being a one-time event, maybe you don't want to own it into Christmas, maybe that's not the time to... So let's say you're a long-term investor and I'm looking now on things for three to five years, If I buy it pre-Christmas this thing is going to happen in the next couple of months, is going to determine my return for the next year or two. And the other thing is you got to look into things like the culture or the stock cop and things like that. Because it can be really damaging to a company if the stock gets obliterated in the first six months of being public, you might lose a lot of talents, something like that. So it actually can have a negative reflexive effect.

Brandon Beylo (host):

Mm-hmm (affirmative).

Dan McMurtrie:

So there are things like that where I might believe for whatever reason that there's a great tenure thesis for five years, whatever. But if the next incremental test is putting a binary risk in front of me and that long-term thesis, I'd rather just wait. I don't really need to take that bet. Because again, I don't really like these tales of the distribution. I think there's plenty of stuff in the middle that you get a great business that you want to own anyway that also has a call option that doesn't have those types of binary risks, where you're going to be able to add as risk is taken off the table.

Dan McMurtrie:

So when we're going through that step 1, 2, 3, 4 we're going through content advocacy or content reference advocacy community. As that's happening the question is, am I paying for that option? If I'm not paying for that option and I see it advance from step one to step two, I can increase my position. Versus those other bets where if it doesn't advance from step one to step two, I'm down 60% over night. I'm not interested in the second type of bet. And yeah, there's going to be things in the second half of bet that'll make a lot of money, but that's not what I'm here to do. I'm here to make money in a way that I can understand, that my team can understand.

Dan McMurtrie:

And the other thing is, again, going back to at the beginning trade structuring, position sizing it's so hard when you have a discrete binary event in the middle there. And one it's hard in terms of when do you put the position on? How much do you size it? All the other things. But also it's really acidic effects to your team, because I don't want my team sitting around obsessing over what do sales look like after Christmas for a toy. That's just not a useful use of everybody's time. And when you have a big uncertainty bomb sitting out there, it's going to just suck time from the team.

Dan McMurtrie:

Because everybody's going to try and get more data, more data, more data and we're going to try to have a few presented. And you could have the best data in the world and you know what? The street could say, "We don't buy it, sell it off." Or you get a data proving something's false and the street could say, "We believe and it's going up." And we've all seen this with reopening trades moving up and down where some of these valuations as things were moving up or were batshit the whole time. And so we're just trying to avoid getting ourselves involved in those situations where there's a high probability that the market essentially gaslights you.

Dan McMurtrie:

Because we want to maintain a position of indifference and be an athletic balls of your feet position where we can adapt. So we're going to look at a lot more things that we're going to invest in. And we're really just trying to find of the 50 names we might look at where we'd asked this question of how do I tell if this is incremental? There's probably going to be three that are really investible for us. Because it's not just about the risk return of the security, it's about is it investible for us for our process, right?

Dan McMurtrie:

Because at the end of the day, no individual investment is worth compromising the process, compromising the stability of the team, compromising the psychology of the team, it doesn't matter. There is no investment in my portfolio that I wouldn't sell right now if I knew it was going to improve my team's process going forward, I'd kill any thesis in my portfolio. I don't care if I think it's a 10X. It's just not worth it because that's the engine of my returns not the companies.

Brandon Beylo (host):

Right. So-

Dan McMurtrie:

Which is a little heretical.

Brandon Beylo (host):

Can you give us an example of a fad stock where you guys incorrectly guessed the durability of that fad? And then if so, what were some lessons that you've learned?

Dan McMurtrie:

Yeah. I mean, my weakness has always been over conservatism. Off the top of my head, I can't really think of something where I thought it was long-lasting and it turned out to be a fad because I just pass too often. Again, I'm optimizing. I used to have a really big belief in conviction bets, and then I was succumbed to what I described earlier as that C plus problem. And now I'm really all about easy bets, because I need to manage, 15 longs, 25ish or something like that plus new ideas, lots of other things. So I am not ashamed at all in staying I'm all about the idea that requires minimum stress, time, et cetera.

Dan McMurtrie:

And so I have a bunch of things that are particular to me that I care about. For example, there have been companies, an example would be Snapchat, that I viewed as obviously a fad and what was so wrong about. And part of that I think it was age base. I was never a user, I didn't get it, and then when I did ask some people like my younger siblings they ditched it for a while and then they went back on it and it just I didn't buy it and I didn't get it. But what I try to do is I'm trying to get away from my Irish Catholic upbringing and not beat myself up too much about it.

Dan McMurtrie:

So my advice on how to determine earlier is, I want to read about these companies to learn about them and see if there are patterns or things I can... I want to try to learn as much as I can, but I think there's a tendency to want to spend more time to get an answer now. And what we're ultimately asking here is the question of is will this be enduring? So a good signal if something's going to be enduring is, does it endure?

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And so I think the answer is often to just do a few hours of reading and some calls and things like that, keep some notes and put it on a screen and check into it every now and then, and wait until you can see it. It's like you're playing baseball at night and people are obsessed with how do I hit pitches I

can't see? I think you should just probably wait until the morning and try to hit the pitches you can see. And that's-

Brandon Beylo (host):

I like that.

Dan McMurtrie:

... Really what circle of competence is about, right? So for me there's a lot of things I look at and go, "That's really interesting." And I make a note of it and I try to get better at making sure I go back to the things I made a note of. That there's some slippage there and that's something internally that I'm always trying to optimize for. It'll never be perfectly optimal. I'll never have prediction, but I'm really trying to make sure that I'm swinging at the pitches that I can see that are fad pitches to me. Because again, on the long side I really only need two to four good ideas a year to put up a monster year. So when I view it from that perspective, and I don't need to own whatever the hedge fund name of the year is, there's always a Sea Limited that's killing it. And I probably should have owned Sea Limited, but-

Brandon Beylo (host):

The amount of times that I've said that I would own Sea Limited if it ever... There's been times where it's retrace to its 20-day or really basically its 20-day moving average. And every time I've told myself like, "I'll just buy a little or when it gets to the 20." And it does and I don't, and it goes higher.

Dan McMurtrie:

... Yeah. I think right now there's a big competition. You can see it on Twitter, everybody's basically competing to who can be the most bullish on the most popular stocks? Who can be the biggest Facebook advocate? The biggest Sea advocate? Or whatever? They have a Substack that does a breakdown on this, that, or whatever. And that's just like it's not that that's bad, and I actually think it's really cool to see [inaudible 01:31:55] how people are doing. I've been really impressed with some of the people and things that have been done, but that's not what I'm here to do. I'm here to produce absolute returns for my investors, ideally every year and compound over time.

Dan McMurtrie:

And so I think that when you look through the fullness of time I think there's a Klarman, Klarman has a bunch of trash talky lines about other managers where he says, "If you're the top [inaudible 01:32:21] manager one year you're statistically going to be bottom [inaudible 01:32:23] the next year. And if you compound at this rate for X years but then you have one down whatever year, your compound rate gets wrecked." Things like that. And I'm very sympathetic to those arguments. But I'm really just here to swing at the pitches I can see clearly, swing at an appropriate level. As sure that I can never blow up my fund is my money is in it and my partner's are in it and I just don't think I have the right.

Dan McMurtrie:

I don't think I have the right regardless of the risk reward to ever where it could blow up. And there are funds that are of different mandates where they're trying to really slug it. And they have blob risk and the LPs are okay with that, that's not what my product is. That's not what I sell, I'm trying to sell a compounding machine. So given that again, I think it's very important to always zoom out and go, "What are we here to do?" We're not here to be right on that stock, we're not here to have the best research, we're not here to see things before other people, after other people. Don't care about any of

that, we're here for absolute returns, we're here for compounding money, we're here for defending our investor's capital.

Dan McMurtrie:

And we need to defend capital and we need outperform, those are the two things. And when you try to put up strong absolute returns. So there's one learning process that needs to happen of expanding your circle of competence as a Buffett acolyte would say. And there's a second learning process of evaluating things that are in that circle of competence. And I am finding it very useful to look at private companies and I think there's some set strategies you can use. Like one, I think paper trading accounts are vastly under utilized. And some various smart funds that I know have basically set up what they're calling an R&D portfolio, or I think Lone Pine, Mandel, or somebody had an analyst override portfolio where 5% of the book the analysts got to choose on.

Dan McMurtrie:

But I think having a little bit of gamification inside your firm or your collaborative group can be good to force that. I think it's useful to have an allocation of your capital that is basically experiment capital to keep you a little more serious about it. It's too easy to always punt on the new stuff exchange and improvement in your operations. So we are of the belief that if we're not twice as good every year as we were the prior year, we're dead. And so, I think my biggest edge is that I'm about to turn 30 and I've been doing this full-time for seven years and prior to that. And I've touched damn near every hot stove in the kitchen. I haven't blown up, I haven't had major impairments of capital but I made a lot of little mistakes on it. And I understand the nuances of those and I have a gut feeling, rather than having an intellectual understanding which I do, but I have a gut feel for a lot of things. And I know myself better than I think I did, or I don't want to say better than other people, but I think I know myself really well. And I think that's what informs my ability to invest.

Dan McMurtrie:

And so there are some things we do, like we have a system here of basically poker chips. And if somebody I'm working with who is doing work can't... Has an idea and they really believe in it but they can't formulate a really compelling pitch or they think that I have a bias that will prevent me from pulling the trigger, which I might, they can just put a poker chip on my desk...

PART 3 OF 6 ENDS [01:36:04]

Dan McMurtrie:

They can just put a poker chip on my desk and I'll put a small position on, just so we have it in the book. And so it gives people an ability to circumvent potential social pressures when they really want to punch it on something. Now, it's not a big position. It's nowhere near my positions, but it's a really useful signal that people you're working with, they don't want to start a thing with you. They're not willing to rock the boat at the firm, which is priority two, after capital. But they want to make something happen, right? We think a lot about how do we create little games and incentives and constraints, things like that, inside the people work with, inside of the firm, in order to encourage constant learning and things like that. And so the answer is basically just to follow stories and to follow companies and see what happens because it is very rare that most of these things are the same story over and over again.

Dan McMurtrie:

We are trying to look for commonalities of winners and losers, but again, I am valuation sensitive. The valuation part does take a lot of names out of consideration for me. My view on valuation is essentially cash flow duration. I'm trying to think of, "Okay, over the next five years ... " Because I just think the idea that you can predict 10 plus years is ridiculous.

Brandon Beylo (host):

Agreed.

Dan McMurtrie:

I'm really trying to think about how much free cash flow is this company going to generate in the next five years, what are they doing with it, how does that influence the terminal value? And so the questions are really confidence in the terminal value, et cetera, et cetera, et cetera. And so there are certain growth businesses, like Tinder and Match, Match Group, where the way they were building their business was making the terminal value, in my opinion, very certain. As the terminal value becomes certain, then what's the TAM becomes a non-stupid question, the way I think about it. And so if I'm certain this business will exist in 10 or 15 years or 20 or whatever, then I actually have to think about how big is the market? How much of a VIG can they charge in that market? What do the economics look like at scale? Et cetera.

Dan McMurtrie:

And so what I'm really trying to figure out is what do I need to know in order to have certainty that the terminal values money good? And then from there, everything gets way easier. Most of the more deep value type stuff I'm doing is something where I think I can prove kind of on an expectations investing framework that the market thinks the terminal value is zero or even negative and I think it's non-zero and I know what's going to make that clear in the market.

Dan McMurtrie:

So the dream scenario for me is, I find that situation, something's cheap, market is pricing terminal value zero. So, free cashflow yield's super high because people think that the coupons are not going to repay principle essentially. I think that something's going to happen in the near future that's going to prove the terminal value is not only positive, but actually the new business, whatever it's going to be, is going to be a compounder and a better quality business than the old business.

Brandon Beylo (host):

Right.

Dan McMurtrie:

That's really rare. You need a bunch of things that happen contextually in order for that scenario to pop up. That was Colony Capital transforming into Digital Bridge where it was like, we're getting this deep value, discount to liquidation value type entry, into something where, if we're correct, we're going to own a compounder that we might want to own for a long time.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And in that case, we have other things. We talk about culture, we pay a lot of attention to incentives. And the distinction we make is, there are aligned management teams where if the total share return over X years is this. It's fly, Right? That's one thing, but there's also in the summing, like NonGaap on Twitter talks about, there's also management teams that are making very explicit bets on outcomes. And so if I'm seeing that deep value type set up into a compounder, where things are getting really simple and lining up, and I understand all that social context around the thesis, and then I see the CEO make a nine figure bet on it. Well, let's go. Let's fucking go-

Brandon Beylo (host):

Let's back up the truck.

Dan McMurtrie:

Yeah. Yeah. It's like "Boys, bring it in here."

Dan McMurtrie:

Again, that's kind of the conjunction of where we really push it is, we have all the fundamental stuff. We have a ton of behavioral stuff. We've got price-based stuff. Basically, we have a good thesis from the perspective of two or three different investing fields. And we think they're all going to line up. And if you can do that also at a size where if the other framework is kind of mandate inclusion. And so we are very focused on what we call mandate arbitrage. The best time is short a stock is where it's about to get kicked out of people's tradable universe. Because it doesn't matter what they think of it, they're just selling it or vice versa.

Dan McMurtrie:

Best time to do long is when people want to buy it. And so if you can find something where there's like a six inch pot on fundamentals, where all of a sudden it's going to get included in this index and this index. One, a ton of people are going to buy the stock in advance of that because they know that they can sell the index. Two, the index is going to buy. Three, a bunch of other managers are going to have to have some position to the index or the benchmark or whatever it is. But then the question is, is this a business they can actually use that now lowered costs of capital? And is the management team aware of that. And it's like Marc Ganzi at Colony, very aware of cost of capital. Very, very savvy guy. And was super ready to just game the out of that, right?

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And that's just the reality of the market. And so part of that is once we understand what we think the game is, right? Where the company is, are the cards we're playing. The other thing you need to do is you need to figure out, does the management see the game the same way you do? I think where a lot of investors who get into trouble, and you can see this every day on Twitter, is there is a lot of uncertainty about whether the management team actually gets it or sees the board the same way that the investor does.

Dan McMurtrie:

And I, very simply will never invest a dollar into a company where I'm not 100 percent certain that I see this business the same way as the CEO. So a really good behavioral indicator, if I'm talking to a

management team, and I'm of the opinion that I need to tell the management team anything about their business, I'm fucking out, right? I shouldn't be teaching an executive about his industry. I shouldn't be telling him how to market. I shouldn't be telling him how to recruit new talent. That's insane. He should be telling me. He should be like, "You stupid, stupid hedge fund, man. You know nothing about my business." Right?

Brandon Beylo (host):

Yep.

Dan McMurtrie:

So, if I'm talking to somebody and I don't get it, or I think they're wrong, it means one of two things. It means either management's dumb or has some other issue, or maybe has messed up incentives. Or more likely it means I don't understand the business well enough. Right?

Brandon Beylo (host):

Right.

Dan McMurtrie:

So, actually a good example of this is Naked Wines, which is a company that we invested in and has subsequently become a massive finance Twitter name, which keeps happening to me and is quite frustrating just because people like to claim that I ape ideas off of Twitter. And A, most of our portfolio, not names you've ever heard about Twitter and B, if I could beat the market by just apeing Twitter names, I would begin and end my pitch with just that sentence. Like, "I'm so good. I just open Twitter, and I just ripped those names and I beat the market." That would be-

Brandon Beylo (host):

The thing is, you can almost take the opposite approach to that and say, well, Mohnish Pabrai says there's nothing wrong with shamelessly cloning. You know?

Dan McMurtrie:

You've got to send me that.

Brandon Beylo (host):

So, what's the damage. As long as you didn't clone Alibaba, then that's okay.

Dan McMurtrie:

Yeah. I mean, I lived in China for a while and I can still speak pretty rusty Mandarin. I can get dumplings and beer and get around in a cab, so I think I'm good. But I was not going to be on that one.

Dan McMurtrie:

But the reverse indicator is essentially to our Naked Wines. When I started looking at the company, I had a serious disagreement with how they acquired customers. And so we started looking at how they were doing their digital advertising, how they were routing those, who they were paying, et cetera. And I basically said, this is not the way cutting edge companies do this. You have your social media presence, just bullshit. It just didn't appear to me that they knew what they were doing on

digital advertising, right? And the CEO, Nick is a data scientist who came to the company and what they'd been doing was using mailer ads and a lot of these things that I consider to be obsolete.

Dan McMurtrie:

And so I kind of sparred with him on a couple of calls about, kind of like, "Dude, what the fuck?" I mean, more respectfully than that, but I was just like, "I don't really get it." And I was like, "Do you need introductions to programmers? Do you need introductions to really good digital ad people?" And I do know people who are really good at that stuff, so, I mean, I wasn't trying to be like that arrogant. But over a couple of months, as I really started to study the business, I realized I was wrong, and Nick was right. Nick realized that the actual customer cohort, and we, get this, we went and met with the private competitors too Naked. And we realized that those guys had all built out really impressive Instagram funnels and all of that. But what had happened is they just basically incinerated an insane amount of money trying to acquire 23 year old white chicks to buy Sauvignon Blanc and Rose who turned out immediately. And so they're paying 30, \$50 a customer and they were making 20, \$30. And the numbers just didn't make any sense.

Dan McMurtrie:

And what you really want, is you want a mom in Ohio who wants a new, interesting wine after she drops her kids off at soccer. She's had a long day and she likes learning about the new, different wines. She likes the diversity of selection. She's really interested in the community and all that other stuff. And, you know what? She reads mailer ads and nobody else was going into mailer ads. And so basically, the outcome of the bet, it's kind of like a sports betting line. The market had priced in my opinion, and the market also wasn't aware of the cohort that he was going after, because it's not a vocal cohort. The wine snobs are very small percentage of the wine market, but they talk so loud and so much, and they're so smothering to other people.

Brandon Beylo (host):

So it's like the silent majority bet, almost. Even, just to go back to Trump. It was kind of the whole campaign. It was like, "Oh, we've got this silent majority. Nobody wants to speak up." It was that, played out on Naked Wines.

Dan McMurtrie:

Right. exactly. And so what Naked actually did was used these supposedly obsolete cheap techniques. Using the lowest quality ads, the mailers and things like that, to acquire essentially the silent majority of the wine market. And that gave them scale. And then with that scale, they could then go after the other markets, because then they had vertical integration and they had really good incremental unit economics that allowed them to really pull the ladder up after themselves versus their competitors. And so that's the really instructive process where you begin with essentially a hypothesis that you disagree with management. As you get to know the company better, you realize that they have figured out something that other people won't know until they try something 100 times and fail.

Dan McMurtrie:

My friend always refers to the scene in Iron Man one, when the two Iron Man suits are fighting in the sky and Tony Stark's says, "How'd you solve the icing problem?" And the other guy goes, "What?" Because he's never flown that high and the suit freezes. So there's problems you only find once you've actually done something for an extended period of time. And so if you find yourself learning from management team, as you're setting a business, that's a really powerful indicator. And so in that

case, the first time I looked at it I didn't invest because I disagreed. I said, "Okay, this might be a short." And then I did more work. And I realized, no, I'm wrong. He's right. And I met in my view and then invested and the company's done very well since then.

Dan McMurtrie:

And there's a lot more to it. But because I understood the nuance of how they think about the market. So that gives me a bunch of signals on culture. This is a company that's able to look through, very popular ideas to actually find a smart idea and do stuff that's not sexy that actually makes money. And that's a really rare culture, particularly, candidly in wine, where there's a lot of prestige games played. So that, and other work we did, told me that we had a company that had an actually very differentiated culture and perspective relative to the rest of the industry. And we thought they had a business model that was essentially anti-fragile relative to other players and was advantaged in a number of other ways.

Dan McMurtrie:

And so we looked at that, we looked at the valuation, looked at the people that were selling the stock, buying the stock, and we thought it was a tremendous setup. But, we're kind of using ourselves as contra there and manning our view. But the big takeaway there is, when you're studying a business, one of the indicators, things you should maybe keep looking at is, are you learning while you're studying in the business? Cause a lot of the companies you end up looking at, if you have a value bent are just kind of frustrating. Because you just studied these companies, and basically one of two things is happening at all times. Either management's doing something stupid or something stupid is happening in the world, that's hurting the company. And so the company-

Brandon Beylo (host):

It's just a slow, melting ice cube, given structural things happening in the world, whether it's technology. And they're basically just boring too. Most of them are boring.

Dan McMurtrie:

Yeah. I'm just like, "Right." I guess, I don't want to invest in a company where a commodity price records in this quarter and the next quarter management does something dumb with cash and then dah, dah, dah, dah. And then the way it ends up happening is management agrees to take \$30 million for themselves and sell the company to Blackstone at three times EBITDA. And then Blackstone fixes it and IPs it at a 12 times EBITDA and then it re shortens it back to four. And it's back to four times EBITDA where it was at the beginning.

Brandon Beylo (host):

And the value investors circle back in.

Dan McMurtrie:

Right. And then we resurrect the 700 page on our brochure on Fairfax thread on it. But enough about the Horsehead holdings. And that was a particular trash fire investment. We are trying to think through all that stuff in terms of, what can we learn about businesses and business processes that we can also apply to ourselves? And so really, the thing that I really loved about studying Naked Wines was their clarity on their goals. What are they really here to do? They're not here to have the fanciest wines. That's not the point. They're not here to be the most popular. They're not here to have the most Instagram followers. They're here to make the most money selling wine. And they're doing

really, really well at that. But the only reason they're doing well at that is everybody else is actually optimizing to those other things.

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And, that's been a fascinating process of getting into that company and I have an enormous amount of respect for the team there and just the journey they've gone through. And I'm very excited about the future of that company, full disclosure. We are long still.

Brandon Beylo (host):

On our first conversation, we went off on a tangent because mainly it's due to my personal passion about it. Over time as I've grown, I guess, as an investor, I only try to focus on companies, and I only try to study companies that get me excited. And the beauty of that definition is that it's subjective to whatever excites you. But I think where you and I share similarities is, does this business get us excited because what they're working on, or the industry that they're in or the game that they're trying to play is multi iterative. And there's not just one application to what you're learning. And I think that, that's something that new investors that are listening to this podcast or people that are struggling to try to find their identity might find some solace in where, just follow what interests you.

Brandon Beylo (host):

And if you get excited about studying this business, or if you're excited reading an S-1 and you find yourself going down the rabbit hole, then that's probably a good indication that you found at least the inner circle of your circle of competence. Because I think you need that passion to really develop that circle of competence. Where you're not just studying some railroad, because you read a few books about railroads or you're studying banks because you read a few Warren Buffett letters or something like that.

Dan McMurtrie:

Absolutely. I mean, I think, there's a great Druckenmiller line about how there are people in the markets who love this, and when you're tired, they're having fun. And, when I grew up, I did a lot of boxing, kickboxing, MMA wrestling, back when it was called Shootfighting, before it was MMA. And there were people like that in cage fighting. Where you'd be exhausted, you'd be on your 10th round of sparring. And these guys would have this smile on their face. And you're like, "Man, this is what you were supposed to be doing." And, I had a lot of fun doing it, just like there was a special type of shtick that you didn't really want to compete with. People who start laughing when you can pop their elbow out and stuff. And you're like, "Nope. Nope. Don't want any part of that. That is so scary."

Brandon Beylo (host):

That's a little bit psychotic.

Dan McMurtrie:

Right. Yeah. There was this guy who was a SEAL or something. And I remember his shoulder got popped out and he popped it back in and said, "All right, let's keep going." And I was like, "Oh my God. Dude."

Dan McMurtrie:

So, I think that there's a double edged sword element to the passion question on investing. So one, I think getting to know yourself as incredibly important. I'm really big believer in that line. I'm blanking on who said it. Was it, Koechner. No, it wasn't Koechner. But, everybody gets what they want out of the markets.

Brandon Beylo (host):

Oh, Ed Seykota.

Dan McMurtrie:

Ed Seykota. But yeah, I really believe that. I think a lot of people go in, wanting to speak truth to power, and they accomplish that fabulously and they don't get money cause they're not there for money. And there's a lot of different approaches. It's what are you really here for?

Dan McMurtrie:

And so one of the things you have to be very careful of in that angle is are you using the markets to express your fears or your biases, right? I think a lot of the early value investors, their families went through the great depression. And so they really liked hard assets because the United States legal system really favors hard asset ownership in a lot of different ways, real estate tax treatment, et cetera. And so there was a huge focus on physical assets, liquidation value, private market value, because you were back fitting to basically the legal system. That was kind of your actual grounding rock. Not really DCF, really legal recourse. Which I find a bit odd. And also, these are your environments where insider is everywhere, or insiders are trading their own stocks. Blah, blah, blah.

Dan McMurtrie:

It's a different realm and the gangster shit going down and Ben Graham's era is crazy. If you ever go look at what was happening at that point. So, it's just very different contexts. And so I do know investors now, that you can feel that their fear of overpaying. One of these I've said, elsewhere, in the past, is you can be so afraid of overpaying that in seeking to avoid that risk, you take enormous amounts of other types of risks. And there are risks besides valuation, right?

Brandon Beylo (host):

Like omission risks.

Dan McMurtrie:

Right. Well emission risks, but also, you could be buying a business that's obsolete or something like that. Or you could be taking regulatory risks. You could be taking agency risk, or all these other things. Often very cheap assets are cheap because management does not have your best interests at heart.

Brandon Beylo (host):

Correct.

Dan McMurtrie:

And it could look great on paper, but it's not going to end well for you. And if you go talk to people who are old hands in certain industries, they're going to be things that to a young man, maybe look

attractive, and they're going to tap you on the shoulder and be like, "Hey, kid, it's not going to work out the way you think it does." So you got to be careful with that. On the other hand, when you're young and when you're learning, and when you're just passionate, it's a great way to have fire, to keep learning and keep getting better. And I think you have to have it if you want it, and if you don't have it, I don't think you should be investing in individual stocks.

Dan McMurtrie:

You go on, you're learning a ton. I do think you need to make sure you separate that from trading because, you don't want your trading just to be based on what excites you, unless you have a really well worked out kind of technical based trading system. There are people who essentially buy things because they excite them because they think it's going to excite others. And they have stops in their positions. And I know people who make money that way. Everybody on Twitter talks trash about short term traders, but every one of the most profitable traders, I know over the last five years, rarely hold things over a week. And I think it's become so invoked to be a long-term trader that nobody's noticing that the prop shops are killing it.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

But, nobody wants to talk about that because, it's religion now that short-term trading is falling, which maybe it is, maybe it isn't.

Dan McMurtrie:

So I think passion just super important in whatever you're doing. At the end of the day it's all about your process and the things that you need to. What are your constraints? Understanding the constraints of others, and the constraints of yourself. I'm a believer that if you're really passionate about one to three industries, you know the industry really well, there's going to be an opportunity once every year or two to make a big bet on something that's super obvious to you. It's not obvious to the market. And you can put up outrageous returns doing that. Now it's not something I advocate everybody do, but it is something that I think is true. And I also think that there's certain advantages to. There's a great [Soros] line where he's, trash-talking Byron Wien, a little bit where he's like "Byron, you go into work every day, and so you can always think there's something to do. But I only go into the office when there's something to do. And when I go into the office, I do something. Like big boy trade."

Dan McMurtrie:

And I do think there's something to that of people who are not full-time investors sometimes actually having a slight advantage only because, when they're going to make an investment, it's something that is really sizeable and really, really significant. And I do think you can zoom in too far and you can just end up over tinkering. But I think most people suffer from what we call the zero or 100 problem. Where when you're talking about something like trading frequency or passion about investing or any of these things, usually people who at zero on the 100 scale. If they never trade, right? Why not? You know this company's had to miss earnings and the stock will get cut in half. Why don't you just hedge it or sell it and buy it back after?

Dan McMurtrie:

And they're like, "Well, if I do that, then... If I give a mouse a cookie, then I'll start trading all the time." And it's like, "Dude, it's in your genetics not to trade. You're at zero. If you put the pedal down, you might go to 20, you're never going to 100." This isn't heroin. I'm not sitting there being like, "Hey man, just try a little bit of crack." Right? I'm just saying, right? And so a lot of the times when we talk about thinking about timing, thinking about macro fundamentals, thinking about the other things. Thinking about valuation versus never sell. People are very worried that if they incorporate anything outside of their particular dogma, that they're going to blow up their whole process.

Dan McMurtrie:

And that's a really tricky question, right? Because one, I think it's obviously absurd. But at the same time, if somebody has got something that works for them and it's optimized their whole process and what they're trying to achieve in their life, it is risky to change anything versus just stick with something that does work. And so I think you've really got to figure out what works for you, what you enjoy doing, how you enjoy living your life and figure out how do you make all those things match? Because I know a lot of people that have spun out of big shops and lost their own funds, whatever. Who've tried to be professional investors. We can maybe segue into the emerging manager topic. I've watched 70, 80, 90% of them fail. Maybe two, I know have failed from stock picking. It's never the stock picking. I've yet to really see a situation where I actually think the guy just picked shitty stocks.

Dan McMurtrie:

It's always something like, they were trying to do fundraising, and that led to them not being able to really do adequate research for a few weeks. And they were also up late going to dinners and things like that, playing that game. And they were really burnt out and tired. And then something happened in their family. Somebody got sick or something like that. And then they got taken off for another two or three weeks. They haven't really slept in eight weeks. They stopped working out. Their diet kind of goes to shit cause it's all take out, cause it's near the office, right? They're not drinking enough water. They haven't taken a day off, away from screens in six months.

Dan McMurtrie:

And you see these people who are geniuses become neurotic, borderline unfunctional people. And then, something happens and they can't react to it. And they double down and they shouldn't, they make basic mistakes. It's like somebody going into a prize fight when they haven't slept for six weeks, they can't hold their hands up to box. It's not Mike Tyson versus Mohammad Ali. They are non-functional, and they implode. Most managers implode rather than explode. The blow ups are really spectacular, but it's usually an implosion. And this is something that is never discussed on Emerging Manager Twitter. It's never discussed by allocators, cause allocators never see these, that's the thing. They don't understand because they have a filter or they're trying to find the best people when they pass out.

Dan McMurtrie:

And so they literally never observe that part of the distribution.

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And it's a huge part of the distribution. And so the biggest advice I have when somebody asks me about being an Emerging Manager is, the only thing I'm not concerned with is your investment program. Because if you don't have that figured out, we shouldn't even be having this conversation.

Brandon Beylo (host):

Yeah, It's a non-starter.

Dan McMurtrie:

Right. It's like, "How is your process going to handle erratic LPs to start basically sabotaging you? How is your process going to handle something happening in your family? Somebody beginning cancer, somebody getting sick. How are you going to handle, if blah blah blah." All these externalities come in, because what you don't realize, especially if, it's generally a young man who's never lost. Straight A's, went to a good school. Dah dah dah dah. Does a great job, never taken an L. Let me tell you, the second you get in markets, God, your win rate is 60ish percent.

Brandon Beylo (host):

Yeah. If you're really good.

Dan McMurtrie:

Right? And all of a sudden you're going to realize-

Brandon Beylo (host):

If you're really good.

Dan McMurtrie:

If you're really good, right? And you're going to start taking Ls a lot. And you're also going to realize that if you don't do something, it doesn't happen. There's no safety net. If that paperwork doesn't get filed, it's not filed. You have to handle all this other stuff. And bad things always happen in clusters. And so you're going to realize is that your system needs to be robust to hundreds of different types of shocks that you're not aware of.

Dan McMurtrie:

So when people talk about their investment program, in terms of how to just optimize returns, this, this, this that's adorable to me. You need to explain to me why you are fully robust as a system to life. How are you going to manage your personal life? How are you going to manage your family, your relationship? How are you going to manage your service providers? Because your service providers are going to try to screw you on every little thing they can, just to be very clear. And that not really my level. I'm not trying to rob you. But they're going to make you do this spreadsheet when they're really supposed to do this spreadsheet. Just little, little thefts of five to 30 minutes of your time are going to accrue everywhere.

Dan McMurtrie:

At the same time. How are you going to continue to build your network when all these pressures are applying? Do you have any way of managing all of this? Have you ever managed other people? How are you going to manage other people? What are you going to say to these people when you're down? What are you going to say to people when you're up? Right? All these things get really complicated and really, really brutal. And the core thing is if something can go wrong, it will go wrong.

And the kicker is multiple things will go wrong at the same time. And it is an inevitability of the first few years of your fund, some crazy shit's going to go down some part of your life. You don't know, but it's going to happen. It has happened to everybody I know has ever started a fund.

Dan McMurtrie:

So, if you can figure out how to be robust to that stuff, you have a shot. But that's the bar, right? And now given that perspective, what's your goal? Protect capital, grow capital, maintain the team. You need to think through your whole process, research, monitoring, trading, risk management portfolio, construction, investor relations, marketing, operations, tax, compliance. All of those things need to be robust to all of those shocks.

Dan McMurtrie:

And, from that perspective, it's a much more complicated game than people really realize. And also, keep in mind, it's competitive. So you're always having to upgrade all your shit all the time. So it never stops. So, and this goes back to where you're just going to have passion. If you're not passionate, it's going to eat you. It's going to rip your intestines out and hang you with them. It is ridiculous because it literally never stops. You wake up every day, there's 15 fires to put out. You can put out five today. You have to rank the fires, put out five and hope that the remaining 10 don't burn the place down by tomorrow. Most of them are minor. I mean, it's just "Hey, this person wants this document." Dah dah dah dah.

Dan McMurtrie:

But that's what being an entrepreneur is. Ranking fires, putting them out and you do it. And you wake up, you go to sleep every day. And your social relationships are going to struggle. All these other things. There are major trade-offs that are going to have to happen. But if you're passionate about it, you can push through that and you have to really keep getting better, keep figuring out how to improve, keep figuring out how to make all of those things flush together. And if you can get it all to come together, it's a beautiful thing. And it's one of the most rewarding feelings in the world, when you've built this machine where you get to do something that you love with partners who are fantastic and supportive and open and just, they're partners and they're friends and-

PART 4 OF 6 ENDS [02:08:04]

Dan McMurtrie:

... open and just the partners and their friends, and with teammates that push you and challenge you and support you when you're having a down day. A great test is basically if you're having an off day and people, without even needing to say anything, do people step it up if you're having an off day? Because there will be off days.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

If you can sync all of these things together where your CEO knows that you're tired today and he needs to step up a little bit more in this call or something like that, once you put all these things together, it's an absolutely incredible feeling, but it's brutally hard to do it. It has nothing to do with resting, and so I just think that entrepreneurship right now is lionized, but it's not appreciated how brutally hard it is. And there's a reason that VCs all seemed like cheerleaders.

Dan McMurtrie:

I understand the perspective of basically looking at them and seeing a shale, but if you actually spend time with founders, and I've been doing more of this, you just realize that most of being a venture capitalist is being a therapist, if you're really working with the founders, because it's so psychologically taxing for the founders, even when they're doing well, that it's made me a lot more compassionate and empathetic over time towards founders building my own business because as an Irish guy, I have an instinctual habit of just trash-talking because, genetically, I'm supposed to be at a bar with a Guinness talking nonsense about somebody I don't know. It's just what I do. I don't know why. Nothing behind it. We just sit there. And then nobody gets ripped up more viciously than my friends, but I've really dialed that back in my personality because I've just seen how hard it is behind the scenes, and I've seen how much some of these people go through.

Dan McMurtrie:

And on Twitter, there is a very vicious culture of people attacking each other, and you just don't know what's going on. I mean, you have no idea the struggles other people are dealing with or may deal with, and it just makes you basically want to be a nicer person because you're like, "Damn, man. I didn't know his dad just died, or dah, dah, dah," or just crazy stuff all the time. So I think the process of being an emerging manager for me has made me a lot more empathetic, a lot more balanced and humble, I would say, because I just realized how hard it is, how hard it is for everyone else that's doing it, how much about this nobody understands, and it just makes you realize you should just be helpful to everybody you can be helpful for because you don't know what's going on with them. You don't know what's going to go on with you, and you want to be a part of a ...

Dan McMurtrie:

One of the other things is it's very lonely, I would say, at points when you're a founder, and you want to have a tribe of people around you that support you, that are your friends. This idea that you're going to go out and you're going to be a lone wolf and you're going to conquer the world, that's not really how it works. Even if it's your company, you need partners and friends. You need a team. You can never actually succeed alone in anything. Even if you're a one-man manager, you still need to build a team of people you collaborate with, of your family, of your partner, as well as the other things.

Dan McMurtrie:

And so it all comes back to that social strategy I was talking about before, about managing your own psychology, about knowing yourself, all of that type of stuff, and those are the things that if somebody has a really profound level of confidence in that, they have a shot. But it's a serious trial by fire, and most people implode rather than explode.

Brandon Beylo (host):

Hmm. What are some things that you would have done differently, looking at Tyro, knowing what you know now? Maybe just one or two big changes that you wish you would have made in your process before, knowing the struggles, knowing the fires that you have to put out, knowing all this, Murphy's law, what can go wrong will go wrong, and it goes wrong in bunches. If you can name maybe one or two big things you wish you would've done differently.

Dan McMurtrie:

Yeah. I think maybe three things. So one on the investment side, my tolerance for fire drill risk is about zero now. In the past, I think at the beginning, honestly, there was a part of me and my

business partner, we wanted to prove how smart we were. So we really complicated hurray, special situation, predict any binary BED, blah, blah, blah. "We're going to wake up one day and we're going to be geniuses and have all this P&L," right? And I have no interest in any of that now because the reality is I know that the day that something terrible happens will be the day that my problematic company that's speculative, that's a deep value play, will also report a massive write-down, the stock will be off 40%. And that will be the day my LPs are really mad because, "What the hell? You just blew 600 basis points on this thing or something," and all that stuff is going to happen [inaudible 02:13:27].

Dan McMurtrie:

Again, going back to the research process, we're trying to think about how do I see linked together? I want to invest in companies that ... I never want to find something out and be worried about whether or not the company is aware of it, is proactively dealing with it, is taking the right steps, right? Because that's the stuff that will eat your mental capital and stress you out. I want to invest in teams where if there's a headline, I have absolute certainty that the company is aware of that, has already taken the absolute best actions, already took preventative actions, et cetera.

Brandon Beylo (host):

Right.

Dan McMurtrie:

If I don't think these guys are world-class firefighters or even proactive, I want them to be the one who knocks, to put it in Breaking Bad terms, right? I pay a lot of attention to the specific wording that manager teams use, and I'm looking for passive worldviews, and if they're the type of person who thinks the world happens to them, I'm out. I'm out. I want management teams who do things to the world, teams who go impose their will on the playing field. I mean, people love to hate on the New England Patriots, but here's the reality. The entire NFL system is designed to prevent dynasties, and they are still a damn dynasty. I want the New England Patriots, and I want them at a market or some market multiple, and it's not that much more complicated than that. It doesn't need to be. The second is I think that you need to think very closely about what tasks are you really good at, and where are you actually adding incremental value in terms of your role in the business?

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And you need to think about your businesses as an algorithm. There's a series of steps being taken, and they're going to all come together in different ways, and they can be computerized, human, whatever. One of the things might be like, "Dan reads the 10Q." That's fine. That's a step. Okay. But if you're not actually differentially good at that thing, you shouldn't be doing it, if you're an entrepreneur. Somebody else should be doing it. You should be doing the thing that you're really adding value to, and you should look to reinvest your cashflow in everything that you're not an A-plus player in.

Dan McMurtrie:

There's a related term, which is, I forget, I know it was constellation software or something like that, but there's this conversation of A players hire B players hire C players, and that's killing organizations. And that's a really big issue, but there's a different thing, which is A player should hire A+ players. You should also be looking to hire people who are everybody you invest in and everybody you hire and

everybody you partner with should be better than you at something. If you're in a room and you're not challenged by other people in some sphere, that's not somebody that you should hire. It's not somebody you should partner with. You want somebody that is bringing something to the table, and it doesn't need to be big, but it needs to be something. So I think that's another thing, is just really thinking through that thoughtfully, moving things off.

Dan McMurtrie:

I really struggled nearly of wanting to do everything myself or be involved in everything, and then the amount got too big and I couldn't do it. We brought in a full-time CFO, and he manages basically everything that's not investing related, and now we've moved other processes over. And so just making sure that those things are ... investor onboarding is automated, and making sure that information requests, tax documents, if anything like that needs to happen, that needs to be automated. That should take up zero bits of my RAM because I'm not exemplary good at it, and it's not accretive to the firm for me to do that, right? So just thinking through things like that.

Dan McMurtrie:

And I think when you're talking about team members, don't try to round out people. If you have an analyst who's really fucking good at growth stocks, don't make them go look at a mining company. It's not helping anybody. He's never going to be good at mining or whatever it is. Just let him do growth stocks, and if growth stocks are chilling out, then be like, "Cool. Go work on a long-term project because I'm not interested in the sector," and that's fine. But really try to just make sure each slot in your roster is filled with the A+ part of that person because I think very few people are A+ overall. Most people are A+ in a very specific area, and just let's make sure that those are the parts of the person that are sticking throughout our process.

Dan McMurtrie:

And then the third thing, I think I do it pretty well now. I'm still trying to get better, but again, just the social stuff is the number one thing, over the course of your career, is your network. Period. End of story. And do everything I described throughout many of my ramblings on this podcast. Build your network, make more friends, be a team player, be helpful, add value, be collaborative. That's what determines your 50-year career success. And nobody wants to admit that when you actually start talking about doing real stuff that matters, your networking and your interpersonal abilities becomes the meritocracy. You want to be CEO of a company, you want to be chairman of a board, you want to be head of a university?

Dan McMurtrie:

Think about a university, right? You're going to have to deal with massive ego professors that head departments that you can't fire. Think about the interpersonal skills you need to manage that political situation, plus a bunch of rich donors that have very strong opinions, who will constantly be conspiring behind your back. If you don't have a lead interpersonal skills and people that will ... and maybe even you don't have the interpersonal skills yourself, but if you don't have them yourself, you need advocates. You need people that are going to say, "Hey, this is what we're trying to do. He can't communicate it well, blah, blah, blah." It's only a matter.

Dan McMurtrie:

So that those are the three things is interpersonal skills, really amplifying network, and being helpful. That's really the number one. That should be one. Optimizing every role in the firm to what people are actually good at and trying to automate or add ... and make incremental investments, so reducing

non-super optimal workflows and eliminate fire drill risk because it's not accretive to the overall investment process. People are super focused on this one investment, but you really have to pull yourself away from caring about any one investment. It's a mental trap. It'll kill you. You need to focus on the overall process because 10 good invest ...

Dan McMurtrie:

I mean, I realize right now everybody's focused on it. You've got all the outliers, and never sell. I'm like, "Yes, there's something to that, but here's the reality. Ten good investments outweigh one. Sorry. That's just the way this works." And if you're reliant on one investment, your firm will die. Your path risk is too high. You cannot be relying on any one investment if you're trying to build a business. If you're already immensely wealthy and you're looking to become super immensely wealthy, then you are in a position to make concentrated bets and ride or die with that. But that's not what we're talking about.

Brandon Beylo (host):

That's something that's discussed last recording, which honestly, I thought it was one of the best brands that took place that day. But before I get to that, you mentioned how you've got an analyst, and let's say he's really good at growth stocks and you try to have him cover a mining stock, or let's just say a commodity linked company, and he fails. I think that's very important for individual investors, too. Maybe people, even one-man shops, and just going off of personal experience, I'm still in the process of finding my, I call it my inner circle, within my circle of competence, which is the marriage between where I think I can understand a business and combined with what I get excited about learning, and I call that my inner circle or circle of competence.

Brandon Beylo (host):

And so over time that has shifted, and obviously it's gotten smaller in terms of the thematic, but now it's more technology, consumer facing, like what we discussed earlier, earlier stage consumer facing, it's got some sort of technology play, a marketplace play, a lot of the early stage growth, typical growth, VC type bets. And that's taken me a long time to get to, but the frustrating part is I spent a lot of time focusing on value ideas that were in industries outside of that inner circle, which I consider wasted time, and I know that that's a bit controversial because there's one camp, and I think Geoff Gannon of Focused Compounding said it where if you read a 10K, it's not time wasted because you learn something new, and granted, I think that's true.

Brandon Beylo (host):

At the same time, the more I've studied and the more I've failed as an investor, I think there is such a thing as wasted time, where if I spend a week learning about a graphite company, like a low-cost graphite manufacturer, and that knowledge goes away when the investment goes away, that's wasted time. And it's taken me years to figure that out, but I just think it's important that you mentioned that because if you find something that you're interested in and you're seeing results, and it's not even price action results. It might just be your comprehension of the business, getting feedback from other people, and now you're starting to become the industry expert, like you were with online dating, where you wrote that big thesis, and I would consider that part of your inner circle of competence. And so you should feed off of that and take those types of cues to optimize your time.

Dan McMurtrie:

Yeah, and so I think that we have a formal framework for how we think about that because the question is "What 10Ks do you read?" Right?

Brandon Beylo (host):

Exactly.

Dan McMurtrie:

So I have a very, I think, simple solution to this. When you read a 10K, you're spending time, which I'd argue is more valuable than money because you can't get any more of it, right? So you're spending money and you're producing an intellectual property asset. It might be in your head, it might be on your Evernote, whatever. You're producing an intellectual property asset. So, actually, we can think about this like any other asset, which is "How do we ensure the value of it?" And one easy way to do it is, "Is it a long-lived asset?" So we're thinking about things in terms of, "If I understand this business, is this something I can invest in, long and short, over the next 10, 20, 30 years?" That's a really important question. If it's something that maybe not, maybe I should not invest money in it because it's a speculative investment of my time, or my money if I choose to spend money on research. So that's one thing.

Dan McMurtrie:

The second thing is, does this investment give me optionality into many related businesses where there's also a high probability of monetization over the next 10, 20, 30 years. So there's other clusters of ideas. Do I understand a theme or something like that where I know I'm not getting one shot on goal. I'm getting 50 shots on goal, if I understand this, right? Because when I go do it, when I research ... Our whole shtick is we do a lot of high-context value chain work. We talk to all the suppliers, all the customers, partners, the VC guys investing in the disruptors, the private equity guys, everybody we can. And we're trying to understand all of that, not just where to position the table, but also I want to understand their fundamental understandings, and I want to talk to the old guard in the industry and everybody like that.

Dan McMurtrie:

So I'm going to build that network of people in the industry. As I do that, okay, so now I have a network asset and I have an intellectual knowledge asset, and so how long is that going to last and how many shots at my goal am I getting with that? Right? So all of a sudden, if I go, "Wait, this is going to last 30 years. I'm going to get 50 shots on goal," and then, "Wait a minute, I'm going to know 50 of the most interesting, dynamic people who are involved in a lot of other things."

Dan McMurtrie:

So also, will this network allow me to more rapidly diligence other things in the future? Could these people be partners in Tyro or anything else? Is this somewhere I want to be a part of the community? And so those are, those are the assets that you're building, is you're building core IP on the thing itself. You're building optionality into other things that are related, and you're building a network asset. So I think about those three things as those are the assets that I'm building.

Brandon Beylo (host):

That's so good.

Dan McMurtrie:

And if it doesn't make sense from that perspective, it's an instant pass. And so I probably pass on 70% of the ideas, maybe more, that get sent to me in that I literally don't read them. I read two sentences and I go, "Nope," because I just have a knee-jerk on, "Eh, nope, I'm out."

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And even within sectors that you might not expect, like biotech, for instance, I have a very good filter in biotech for what I am and am not interested in. If it's a small market esoteric thing with a bunch of clinical risk, I'm out. And it's not that somebody else can't make money on it. That's fine. Not what I do. It's not accretive to my process. If it's anything to do with liver or kidney, which I've invested in pretty successfully over the last 10 years, I won an award for it when I was in college for ... I wrote a 200 page paper about Gilead and their Pharmasset acquisition.

Brandon Beylo (host):

Two hundred pages?

Dan McMurtrie:

It was this ridiculously massive document about how Sovaldi was going to be the biggest drug launch of all time, and it was because hepatitis C was basically the last mega drug category in the United States outside of heart disease or Alzheimer's, and we have no idea what we're doing with either of those. So basically, the size of the hepatitis C market was massively underestimated because it wasn't tested for, and so we had no idea how many people had it, and once the drug launched, it was just an insane success. So I made a very large amount of money on that and did really well with that. But to this day, I still reuse the network and the research I did. We have an investment on today that I use research I did in 2011 for. It's the same people, it's the same doctors, it's the same everything, all over again. It's the same mental models.

Brandon Beylo (host):

Get it back together.

Dan McMurtrie:

Right. Exactly. And so we literally have one thing we call the greatest hits portfolio, and it's basically our conviction bets over the last 10 years, and there are prices we have at all times where if nothing changes and the price goes to there, we're ready to go. And we can get up to speed on those names in 48 hours, from a cold start, because we just know a ton of them, and most of them, we don't own them because they've gone to valuations we don't think make sense. But we always have a greatest hits portfolio of those things. We always have a database of everything that we've ever looked at. We pay a lot of attention to our contacts and that network we're building out. We're trying to build some customized software for mapping together all that stuff so we can try to add more value into that network.

Dan McMurtrie:

But yeah, that's the way I think about it. You're building IP, you're building optionality, you're building a network asset, and that's really what any analyst or individual investor should be doing because that's the stuff that actually is going to determine your investment success or investment ability over the

next 20, 30, 40 years. Not how much Zoom or C or whatever it is you own, but how can you play the next game? And as you might've picked up through this entire conversation, I am not in the decision minimization camp. There are a lot of people who believe that the point of investigating is to make fewer decisions because the more decisions you make, you have higher probability of making an error.

Dan McMurtrie:

I am more of the opinion that you're just going to make errors, and you're trying to build a system that is efficient to errors to results, and I'm more in the Bezos school of we had better be making errors, because if we're not making errors, we're not trying enough stuff. So yeah. I mean, I want to be building those three things for [inaudible 02:30:13], and that's my top of ... So we have a Kanban board Trello type system that we have a prospect list where basically anybody can propose, "Hey, I think we should go do a deep dive on blank." We discuss basically whether, and you can put a little blurb on why you think it's worth looking into, but if it doesn't meet criteria of those three things, if it's not strategically useful to the firm, it's a pass. And I might-

Brandon Beylo (host):

One question. You said you could shoot down ideas within a couple sentences based on, "Is it strategically advantaged to what you guys are trying to go for?" What are some examples of sentences or models or businesses where you can just easily shoot it down? Because that's a tall challenge, right? To read a couple sentences and throw it away, that's a tremendous skill. I think that's way more important than identifying a great idea, is knowing which ones to throw away immediately. What are some examples in writing where let's say someone sends you a SumZero article, or your buddy sends you a write-up, and you read the first three sentences and you're like, "Nope, this isn't for me." What does that look like on a granular level?

Dan McMurtrie:

A lot of them make really implausible ... The example in healthcare is always they have a drug for Alzheimer's. Pass. "We have the first device that can do diabetes treatment at home." Pass. Anybody who's going to a claim to me that if you're going to make a really audacious claim to me, like, "We're going to go after a trillion dollar market and crack it," there are ways people present those. If people are serious, they don't just put it as the tagline.

Brandon Beylo (host):

That's a great point.

Dan McMurtrie:

And the sell side guys will send you outlandish claims daily. Basically, the sell side guys, I think they code things in a certain way to tell you what's up because I talk to the sell side. I mean, a lot of people act like that's a waste of time, and it's not, but they can't trash stuff that they're supposed to send you, but they're going to be like, "Here's what it is," and you're going to be able to tell really quickly if it's nonsense.

Dan McMurtrie:

Again, going back to, let's zoom out here. When I'm looking at ideas that are sent to me or wherever, and I always want to listen to ideas, but I need to make decisions based on evidence that I have. I can't punish myself emotionally or otherwise for not seeing something I couldn't see, and I can work on expanding my site, but I can't punish myself for not seeing something that I can't see. It just

doesn't make any damn sense. So if somebody presents an idea to me poorly, I pass on the idea because it was presented poorly.

Dan McMurtrie:

So we did the first finance Twitter stock pitch competition, and I'd say a third of the ideas there actually seemed like pretty interesting ideas, but they were presented terribly. And essentially, all I got out of it was I could maybe go do a deep dive on this and maybe find something. But the analyst who's attempting to pitch me has not told me why I give a shit. Right? There were a couple also that made a claim where if they could give me one incremental piece of information ...

Dan McMurtrie:

So let me give an example of something I would go after. There were several pitches in the finest Twitter pitch competition that Compound and Acram and Bill Brewster and Elliot Turner and I did. There were several pitches where they made a pretty big claim about the business. "This is going to be a big payments player. This thing is going to roll with itself. This is launching a digital thing," blah, blah, whatever. "Something's changing the business. It's going to be valued, blah, blah. It could be a big thing." But there was a key thing that needed to be vetted out. They haven't talked to a customer. They haven't explained to me why this is sticky. They haven't shown me scale. They haven't done anything to prove the potential there.

Dan McMurtrie:

Now, if it's being proposed internally, if there's one question we need to answer to know if this is actionable and we don't have anything else going on that day, if it's three hours, okay, go do it, especially if it's an intern, go figure that shit out. Great. That's fine. But the best pitches are something where it's like, "Okay, we at Tyro believes that, for example, technology is being used more broadly to program people rather than the other way around, whether it's eyeball tracking, dopamine manipulation, you can look at Tinder, Facebook, whatever, TikTok, Twitter, all these things, but they're all addictive products. They're all manipulating subconscious parts of the mind, and people are using them for reasons they don't understand.

Dan McMurtrie:

And so we're very interested in companies who are evolution gaming. We're very interested in companies that are into that and understand what's going on because they're playing a really advanced game. And once they get going, they're addictive. So they're just really hard to rip out and they tend to be fixed costs, high-operating leverage models. So we have a list of paradigms that we like, right? So as we go through businesses, we write down names for the patterns we like. So one is cashflow co plus internal growth business. There's a yielding cashflow business that people don't love. It's a value business, but there is an internal growth business, like American Eagle with [inaudible 02:36:03] or something like that, where we go, "Oh, that's really interesting because in two years, this is going to be half the business. It's growing at 50%. The core business is growing five, and all of a sudden-

Brandon Beylo (host):

Yeah. [crosstalk 02:36:12] after this podcast, I've got something I'm going to send you.

Dan McMurtrie:

So that's one we like, right? So we can tag that out. So we can basically go, "Okay, we were at an event. Somebody was talking about their business. It sounds like it's this, this, this. The CEO used to

work for this other CEO that we really like. The board members are part of this other thing we like. The talent there, these people ... So basically, it's a network we want it to be a part of. The valuation doesn't seem crazy," blah, blah, blah, whatever other indications. We know half the large shareholders. There's a bunch of things like that where you can basically make it ... You need to make an argument to me about what is the asset we're going to create, the IP, the optionality, the network? And you need to explain to me the cost, right?

Dan McMurtrie:

And so I DQ things because the cost is too high or the assets too uncertain, or some combination thereof, right? So if you explain to me that I need to go into a completely new sphere, somebody sent me a pitch for some ear-related medical device. I don't know anybody in anything to do with the ear. I don't know anything about that.

Brandon Beylo (host):

Don't know any cochlear [crosstalk 02:37:22].

Dan McMurtrie:

No. Right? So I'm not going to go get up to speed on the ear business for a 200 million dollar microcap thing in Canada that's been burning money for seven years and it's never produced a product in 25 years of existing. No, that's a pass. And so a lot of it, and it also matters how are we sourcing ideas? Because a lot of times the ideas are adding up there because they're popping up while we're diligencing another idea. So we're looking at a company that we like, and while we're speaking to management, we're saying, "That's really interesting. Are you aware of any other companies doing something like that?" And they'll go, "Oh yeah, these guys over here, my buddy was on the board there. They're really into this. They're really good. I respect them a lot, dah, dah, dah, dah," and I go, "Oh, no shit?"

Dan McMurtrie:

And then that might be some reason we go talk to them, or we might go talk to a customer, and they're like, "We're looking at eBay or something," and then somebody is like, "Oh, we're using Payoneer's backend," or something like that, and that's really interesting. And a lot of it is just building an industry map and then going and circling those things out, because we're already dealing with the industry and we're adding an adjacent name, we're basically already going to do the work. We're just going to add a little bit more company particular analysis, and that's what makes sense.

Dan McMurtrie:

I can't really describe for you exactly what makes me ... It's like pornography. I know it when I see it, but I can't really give you a good definition of the instant passes. It needs to immediately appeal to me as reasonable ... I'm not trying to necessarily get super amped up. I'm just trying to have things that I think are reasonable, and there's also mental models around companies that I reject because I think they have too much of a wild goose chase potential.

Brandon Beylo (host):

What do you mean by that?

Dan McMurtrie:

There are certain like high-growth consumer product companies, healthcare, medical device ... Medical devices, in particular, has very high wild goose chase potential because you can get 10 of the best doctors in the country to tell you that a product is the best thing since sliced bread and they use it every day, and that product could still flop. And that dynamic has taken out more smart people than I can say. I mean, oh my gosh, it's crazy. And on the same side, their consumer product-

PART 5 OF 6 ENDS [02:40:04]

Dan McMurtrie:

There are consumer product companies that have a lot of momentum, and there's an issue because when something's going absolutely crazy, it's very hard for the person that's been on the victory train the whole time to see when it's slowing down. The question is, if you have a momentum product, a product that's selling more every month, is there really that much more work to do other than just looking at the monthly sales? Obviously, you're going to go look into the background of the company, you're going to read the fines, you're talking to management, you're going to do all the normal stuff-

Brandon Beylo (host):

From a KPI perspective.

Dan McMurtrie:

Yeah, no. Right, from a [P&L 02:40:47] perspective, do numbers go up? Yes, no. That's it. That's the only thing that's actually going to matter. And you can do a regression or whatever else you want, but it almost always is just, numbers go up, yes, no, that's it. That's period. And so I am sometimes not a fan of, sometimes people really like a product, it's doing well, they want to invest in the company, so they're pitching it to you. And really, they're just hyped up about it. And I'm like, "I'm not really interested in having you go do a lot of work on that for me." And they're like, "Why?" And I'm like, "Because I think I can just Google trends it and I'm going to catch it better than you are." And that's offensive to some people, but it's true, I've just seen it too many times. Right, yeah. So I'm-

Brandon Beylo (host):

Well, that's also the inverted shorts thing. Where people make these really convoluted short bets, and really the only metric that matters is, are people buying more Celsius drinks? Do they have trouble filling the shelves? And if that stays true, that's a lot of headwind you have to go up against as a short. And it's just so simple on the other side of the bed.

Dan McMurtrie:

Yeah. So maybe back to [Cee Limited 02:41:55], for example, rewinding to the end of 2019. If somebody pitches me Cee and they're like, "[inaudible 02:42:04] growing," it's like, "Okay, that's interesting. What's there?" Now, the interesting pitch there is, and they have these other businesses that cross leverage. And if those work, there work bing, bing, bing, bing, bing. And we just need to figure out do they exist? And if so, it's the cheapest thing on the planet, because then you're telling me is the definable is... Because it's not necessarily a binary of first pass and then deep dive. If we're going to deep dive, we're going to spend weeks or months really getting to know everything about it. We're going to authorize like, "Okay, go spend a day." And so ideally what I want to know is, can I authorize one day of man hours to get to a point where I can tell, is this worth spending more time on? And what is my cost benefit there, and all of that.

Dan McMurtrie:

And so there's a lot of things where I just know there's no way, I'm going to have to go spend two weeks to just get to a point where I know if I should do deep work, that's out. And the other thing is, when you're running your own fund, I think it's something most people wouldn't want to admit, but there's a lot of seasonality to fund management. So for example, there's this labor day, it's September to Thanksgiving, you can raise some money. That's one fundraising window. And then there's a right after January to April fundraising, maybe a little longer. But right around the holidays and the summer are out. Everybody's in the Hamptons or whatever, you can't raise any money. And also most of these funds, offshore funds have different fiscal years than onshore funds. So you have windows of your year where all of your fundraising meetings are going to happen, and also all of the big conferences the banks have are going to happen, also investor days happen. So there're windows of time where two or three days of your week are just taken by any of that stuff.

Dan McMurtrie:

And then there's earning seasons, and there's all these other things. And when you stack all of that stuff up, there are times of the year where you don't necessarily have time to go do a three week goose chase on something. You can assign it to an analyst [inaudible 02:44:29], but it doesn't make more sense. You've got to make some judgment calls on where your human capital is going to be. And I think people are so obsessed with the stock prices. Like, "Okay, you have a core position that's up 50%, congratulations." It's about to report earnings, this could be the top quarter for the next six quarters. Okay? And even if you're a long-term investor, you're really down for that 18 month drawdown? I don't know. So do you want to have your analyst go look into this new emerging business model that's not clearly at a reasonable evaluation [inaudible 02:45:04], or do you want to have them go really check into the core position where you have a massive risk allocation?

Dan McMurtrie:

I think you probably want to do the latter. Now on the other hand, during the summer, or maybe on Christmas and things like that. And you might have blocks of weeks where the team is relatively unencumbered with fundraising, with tax, with bank stuff, with whatever it else it is. And you have a couple of windows a year where people can really go sit in a room alone for nine hours for five days, read everything ever, and then come back. So you need to think about time of year and all this stuff. And then meta-game, here we go again, you also know this is true for other funds. So I'm sure, as I'm saying this, I can hear the shit talk on Twitter of, "That's not true, it's just cause runs a small fund." And I'm like, "Okay, bullshit. I know all of your analysts." So you also know that this is how it works for other funds. So you know when they have time to do actual research, when they are likely to express new conviction bets.

Dan McMurtrie:

So for example, I'm sure it's not the case that a lot of hedge fund managers take a lot of the summer off and go to the Hamptons. I'm sure they're working full time. But there's a weird habit of people putting on brand new high conviction bets right around labor day, magically coincidentally right when people get back from holiday. I don't know why, it just tends to happen. It tends to happen two weeks into January, people start putting on their new big boy bets. So there's also some things there around, so then you have a question of, "Well, do I want to have my team do the work two to six weeks earlier in case there's something here? Because then we're going to be ahead of everybody else."

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

So it's just all a bunch of gaming on it. For me, I have so much more idea flow than I can possibly process that I am just optimizing to things where I'm like, "This is very clearly related to the things where we have really good information access, really good network access, things we already know. Because if I go with the ideas that I can run down in a day on a first pass basis, I can do five a day, my analysts can do a five a day. Okay, now we're processing 10 new ideas a week, and that just scales a lot better. So you just got to think about stuff like that. There's no correct answer for it.

Dan McMurtrie:

What I advise students and people who are interested to do themselves is, if you're a part-time investor or you're a student or something, the number one thing you can do is build a core competency in an industry. And I think you should basically just stock down, first the big mega cap blue chips, then go to the mid caps. You need to understand basically where is 70 ish percent of the spending in the industry. Once you can understand that and the incentives and also the history. It's very important that you understand in the last, at least 30 years of an industry before you invest, because a lot of the things in the United States that are weird, especially in regulation, are because somebody in 1975 said so. You got to understand that. And so just to go build that one core area.

Dan McMurtrie:

And then once you've done that, then go look at the small caps. One of the reasons that I pass on a lot of random Twitter ideas or things like that from the stock pitch competition or whatever, is you can tell it's hobbyist investor who just stumbled on this name on Seeking Alpha or somewhere else, or another blog, is regurgitating somebody else's idea, he doesn't have industrial contexts, so he doesn't understand how this business fits in the larger context of the industry. And so the pitches that I key into are stuff where I can tell the person writing, or the things that I like is when I can contextualize the information very quickly. Where I go, "That's true. That's true. That's true. This asset is [inaudible 02:49:11] structurally." So right now we're buying new position. I can't say, because we're still buying.

Dan McMurtrie:

And I'm buying it because I've done a whole bunch of work on this particular sub industry and I think the market is making a mistake due to a bunch of headline issues where they're not understanding that the core asset is probably going to get bought. And if it doesn't get bought, it's going to cashflow compound. And I'm happy if it doesn't get bought, I'd buy it as a compounder anyway, but I think it's going to get acquired within the next year, because I just can't see how it doesn't, given the industry dynamics and the competitive positioning of larger players who have more than enough money to buy it. The bill it versus buy it is just crazy attractive. And so when I hear an idea like that I'm like, "Okay, I know everything about the industry, I know what the big players are doing, I know what people need to do with their capital, I know what assets these guys need to have. I know what the consumer wants, I know where consumer trends are going."

Dan McMurtrie:

And then maybe I'm listening to companies talk, I'm reading transcripts. And let's say I saw a theme in one industry, and all of a sudden I see a new industry, a new company pick up a very effective tactical weapon I saw somewhere else. I'm like, "Oh, that was a really sneaky, vicious moves that I saw this industrial company do, and now I'm seeing this healthcare distributor doing it. That's really interesting." So we'll also do things like, if I see really clever things happening, we'll go try to do some text mining where basically we'll do really complicated word searches within transcripts and stuff to try

to find stuff like that too. But I need you to be able to contextualize the information as quickly as possible, because if I have to build context, that takes a lot of time. And it just compounds over time.

Brandon Beylo (host):

That's important what you said about building context and understanding that context at first, because I think it was Bill Gurley, who is one of my favorite investors of all time. And I'm totally going to butcher this quote, but I think the gist of it was, "An ideal investment is something that applies some sort of technology to make human processes and very carnal human actions easier for others." And I think what I'm trying to say is, betting on human things that are Lindy, the quote unquote "Lindy effect", and just betting on that thesis and then companies that are making it easier for people to do those types of things. And the reason being, it's what you touched on earlier, where you get into this wild goose chase of whether you're trying to keep up with the latest technology or you're just trying to catch a hot fad. That is way harder to get right than it is to bet on something that you don't think is going to change. Whether that's a human nature problem.

Dan McMurtrie:

Yes.

Brandon Beylo (host):

And this goes back to the hierarchy of needs where it's like, "Look, we know that these needs are going to exist for probably the next thousand years. So what companies are helping humans solve these needs? And then which ones are doing it in the most frictionless way?" And I think that's the-

Dan McMurtrie:

We have a tag for that, the tag or what we call that as a neurological inevitability.

Brandon Beylo (host):

Okay. So you know what I'm trying to say?

Dan McMurtrie:

Yes. It's something that it's a subconscious... Not to get a little weird here, but I'm a big believer that consciousness is an emergent thing from how our brains are functioning. And majority of what's going on in our brains and bodies is subconscious. And I think that the brain doesn't really understand... I'm a really big fan of this book called The User Illusion, which is about the nature of consciousness and how flawed it is. And when you read it, there's a lot of big holy shit moments because you realize, "Oh my God, this might be..." I don't know if you watch Rick and Morty, but, "This might be a little bit of a Roy."

Brandon Beylo (host):

I don't. I've been told I should. But I've also been smart enough to understand it.

Dan McMurtrie:

No one is. But there's a video game they play, it's a VR where basically you live an entire life as some guy named Roy and then you come out of it and you just lived a whole life. And you're like, "Is this real?" And I think there's a bunch of weird stuff in there. Anyway. I think there's a bunch of very base needs that the brain is optimizing for and creating really elaborate illusions to trick us into thinking that

we're entirely driven by higher level thinking. And I think that, again, going back to why portfolio managers fail, I think it's because they think those things aren't real.

Dan McMurtrie:

And so they don't realize how much their equilibrium is off, their homeostasis is off, because they're not eating healthily, they're not getting sunlight, they're not getting water, they're not getting sleep. They don't have a meaningful relationship at an age where their body is kind of like, "What the fuck? Why do we not have babies?" And that's all stuff that is weird to talk about. I don't mean any of this in a negative way towards anyone, I just think that your brain wants to eat and wants to sleep and wants to have babies, there are just things that it just wants to do. And regardless of whatever you want to do, your genetics are like, "We're here to keep being genetics. We're trying to keep gene line going, that's what's going on here."

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And one of the big things that's present in that book and there's another book called The Intelligence Trap that I really love. And one of the things that The Intelligence Trap talks about a lot is how much of the brain is actually just optimizing for minimizing stress. And so one of the things they talk about is there's this thing called the second language effect. And essentially when people are asked to reason problems in a second language, they use demonstrably better logic and evidence than in their first language. And the reason is, when you need to make definitive statements, it's stressful. You're going to put an exact number on it, you're going to make a stand. And so your brain will slot in wishy-washy words, like, "A lot of people like this," instead of getting a number and saying, "72% of people, according to this study." because then you have to say, "Well, what's the legitimacy of the study?" And all these other things.

Brandon Beylo (host):

Correct.

Dan McMurtrie:

So you just say, "A lot of people." This actually relates to something like Jeff Bezos has how to write guide for Amazon, there's a writing guide for inside Amazon. And one of the things is you can't use wishy-washy words for this exact reason. But when people speak in a second language, the entire process of speaking is stressful because your brain is not used to it, even if you're fluent.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And so there's no real difference between saying 72% and saying a lot in a second language. And so you end up with much better reasoning and people in their second [inaudible 02:56:19]. There's a bunch of cognitive blind spots, things like that.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And so I really like businesses which are interacting with essentially subconscious processes of the brain, because I think there's a lot of products that are basically a subconscious pitch that people make up a narrative for in there. And so when I see a company who's doing that versus another company that's like, "We think our product's cheap relative to comps." I'm like, "Dude, this is not a rational thing." And again, it goes back to the Maslow stuff I was talking about, how serious products are, not serious products are.

Brandon Beylo (host):

Yep.

Dan McMurtrie:

How addictive social media is, online dating, all these other things. Online dating is fascinating because your brain essentially [inaudible 02:57:21] oversimplifying and I'm not talking about everybody, but generally speaking, if you're a straight male, if a woman is interested, you're good. That's the big challenge for men historically is, does she think you're not hideous? There's a lot of complicating factors, but that's it. And so to the male brain, a female swiping right on you is an enormous event. It's like, "Holy shit, we did it. Pop some champagne. We're fucking good."

Brandon Beylo (host):

We're not ugly.

Dan McMurtrie:

Right. We're not that ugly. Yeah. We know we are, we're disgusting. I think my girlfriend said something the other day, she was like, "I know what it's like when men live by themselves, everything covered in pee." And I was like, "I don't think it's that bad, but that was funny." But when you're using Tinder, what people don't realize is that your brain isn't actually necessarily optimizing for sexuality or any of these other things, your brain is really optimizing for interest. Because interest meant you had a very high chance of everything else working out for you.

Dan McMurtrie:

And so that's why the apps are so addictive, is because when somebody says they're interested in you, your brain is like, "Yes, we won." And you're getting basically most of the response there. And actually going on a date is stressful. First dates are stressful. And so if you think about it like a sharp ratio, like your return to risk neurologically, swiping is such a better return because you just sit there and flick your thumb around. And then you get this massive dopamine spike of affirmation. But to actually go on a date, that's scary. It might not go well-

Brandon Beylo (host):

I don't really think dates are that scary though. I've always been in the camp that first dates really aren't that scary if you know how to structure them, like any sort of bet. As long as you structure it and position size correctly, you're fine.

Dan McMurtrie:

Yeah. But on the flip side in the aggregate, I think the average Tinder user a couple of years ago was spending something like 47 minutes a day on it just swiping. The swiping thing gets really addictive. Twitter gets really addictive, Facebook gets really addictive.

Brandon Beylo (host):

I've found my fiance on Tinder, full disclosure.

Dan McMurtrie:

There you go. Yeah, it's great. And the other thing is, the brain is also super off because the brain evolved for a scarcity environment, it doesn't know how to be satisfied, it always wants more because it always fears there not being more. And so one of the things so fascinating about studying e-commerce is any time, for example, the delivery times get shorter, we go from a week to two days to one day, it all of a sudden becomes ridiculously unacceptable for something to take any longer than that. I bought something off eBay recently just to see if it even still existed. And I bought it and it was like, "It'll be here in four business days." And I bought it on a Saturday, I think. And so I'm like, "What? It's going to take five or six days to get here? Are you kidding me? It's the stone age?"

Brandon Beylo (host):

I literally just bought that book that you recommended and it's going to be here tomorrow.

Dan McMurtrie:

Right. And it's the comparison is the thief of joy line people say. And so going back to business, that's such a vicious thing to compete with. If the other person is developing very strong subconscious instincts about how things should and shouldn't be, and I like this and I don't like that, and that's acceptable and that's not acceptable, and one player in the market is determining what those are going to be.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And they're the casino, not the gambler. And then somebody else is like, "We think we have a good value proposition for our customers." I'm like, "Dude, you're in deep shit right now. You have a big problem." You got to understand, there are companies now, market standard is they track your eyeballs on your damn phone. And they have people in machines and they're scanning people's brains while they watch their eyeballs, while they're using an app, to track the exact neurological response to UI/UX changes. It is crazy what's happening now. And this is just to make it a little less stressful for you to order your Starbucks while you're on the subway through the app.

Brandon Beylo (host):

It goes back to Peter Thiel's argument where if you look out over the last, I don't know how far he goes back, but one of Peter Thiel's main arguments is, where has the technological innovations gone? We went from building rockets, blasting off into space, to creating cool, faster web browsers and different calendar apps.

Dan McMurtrie:

It's all just very hedonic. Yeah, it's all very hedonic stuff. I don't mean to sound negative, but we're building ourselves really nice rat cages. We want instant gratification on everything. And when you look at where we've actually advanced in the last 10 years, it has all been about how to take the lower Maslow elements and make them almost predictive. And you actually have predictive elements, you have things like subscribe and save on Amazon. Where, what they're literally trying to say is, "These are the products you buy every month. They're just going to show up now and you're going to get a discount for it. So you're going to get to feel good about saving money and this is going to happen."

Dan McMurtrie:

And businesses are trying to hack that. You've got subscription coffee now, you've got beds that automatically alter the temperature when you go to sleep, when you sleep, when you wake up. You've got smart TVs, you've got unlimited entertainment. The video game companies just announced, they have these game pass things now and you get every Xbox game and PlayStation game ever made available to stream any time. Instead of one game for 50 bucks, you get all of them. I think the PlayStation thing is \$60 a year and you get pretty much every PlayStation game ever made.

Brandon Beylo (host):

That's unbelievable.

Dan McMurtrie:

Right? So the number of ways we have to manipulate our dopamine and to feel something all the time, it's crazy. And meanwhile, the world is getting infinitely better in terms of lower tier Maslow stuff. Infant mortality is dropping, poverty is dropping, obesity is now globally a bigger issue than starvation, which is crazy to think about.

Brandon Beylo (host):

Yep.

Dan McMurtrie:

And our brains are not at all right for it. Infinite information, infinite noise, infinite instant connectivity, it's wild. And so now, like I think that your information diet is probably as important as your food diet. Because one of the other things, I don't know if I said this last time we talked, but I'm a big nerd about complexity and systems theory and things like that. And one of the things is systems can behave, if there's a bunch of people in the system who all have a slight incentive, the system can in aggregate act essentially or produce a result, an emergent result that accomplishes the outcome of those incentives without anybody actually knowing it. And so I call that emergent collusion. And there's a bunch of weird things that come out of that.

Dan McMurtrie:

And I think there's just a lot of bizarre dynamics that happen. And one of them that I'm increasingly suspicious is happening, and if I had a lot of spare time and a lot of compute power I'd try to prove it, is one of the effects of... So I invest in some emerging markets. And one of the issues that emerging markets have had is that the people in power are really old. They're in their seventies, they're in their eighties. And the gap there between the young and old is even wider than in the United States where there's already an issue. And technology is moving faster and faster. And I think there's very legitimate arguments to be made that there's just a serious problem with having 75 or 80 year olds regulating technology. It just doesn't make any damn sense.

Dan McMurtrie:

On the other hand, I don't know that I necessarily want 25 year olds doing it either, but one of the effects that's happening that I'm really fascinated in is I think one of the effects of social media and digital media and cable news is if you're not used to truly unlimited information, the negative things on those networks will trap your mind and you will just get more of it and more of it and more of it, and you'll subscribe and you can't look away because your brain is seeing very real threats. There's an unlimited supply of very real threats. And your brain thinks they're lower Maslow threats. When somebody goes on TV and says, "Obama's going to take your guns," or whatever the hell, or, "Trump is going to come kick your children out of the country," people's amygdalas are lighting up, people are having fight or flight responses.

Dan McMurtrie:

And it's addictive because your brain is like, "By paying attention to this, I might be able to prevent it," or something like that. And this is driving people, particularly older people, but not exclusively older people, fucking crazy. Clinically. You're having a pretty noticeable spikes in mental health issues in older people. And a lot of people I know, especially through quarantine last year, basically when we get beers are like, "Dude, my dad's losing his mind." It was politics at the beginning, and now the opinions are just nuts. And it's not funny anymore. Alex Jones in real life is not political, it's a mental health concern. And I think it's basically forcing people into these extreme places because they're getting into these information vacuums.

Dan McMurtrie:

But going back to why I think it's like a emergent pollution, I think it's basically forcing people to lose their shit so that they basically exit the tribe. Because those people get really upset, politics or whatever it is, and they basically remove themselves from decision-making positions. Because they don't understand the world as it's going on, they don't like it, they think everything is a scam or a scheme or whatever, and they're basically baling. And the weird thing is if they weren't doing that, they'd be really holding back institutions, progress, et cetera. And so it seems to be one of the effects of social media is the second your mind is unable to be flexible and open and curious, it basically will smoke you out of the tribe by gaslighting you.

Brandon Beylo (host):

Yeah.

Dan McMurtrie:

And I think it's a really interesting phenomenon. Basically anybody I've noticed, and some of my mentors who are in the late forties, early fifties, are noticing in their friends that are older, that when those people can't ingest new ideas and adapt, they're really quickly changing psychologically and then disconnecting from most of the world and just exiting the herd. If you're unable to keep learning, it's just kicking you out. And it's a really weird dynamic, but I'm really interested in it.

Brandon Beylo (host):

Yeah, no. Gosh, that's something for another whole three hour podcasts we could do, is just emerging complexities and post consciousness. And I really wish I could merge the two podcasts that we did into one mega six hour episode, but unfortunately-

Dan McMurtrie:

[crosstalk 03:09:57] blowing my nose.

Brandon Beylo (host):

I'm going to keep that audio file. And it's just you and me, those were the only people that are going to enjoy it.

Dan McMurtrie:

Oh yeah.

Brandon Beylo (host):

It'll be the Wu Tang clan album and Dan McMurtrie's unreleased podcast. So Dan, I've got some closing questions that I ask everybody. And just due to time constraints, I've got to get to dinner in a little bit, so if we could make these quick hits. One question that I haven't asked anybody before, and I'm stealing it from Peter Thiel, what is one thing that you believe that almost everyone else around you doesn't?

Dan McMurtrie:

I'm going to go with something that I was talking about earlier. And I think that almost all of the decisions people make are made subconsciously. And then I think conscious reasoning is bait, is fabricated after the fact.

Brandon Beylo (host):

Got it. Second question. Where can people go to find out more about you? I know you're all over Twitter, you don't really introduce at this point.

Dan McMurtrie:

Yeah. Twitter, we have our website, pyropartners.com. If you want to read our dating paper, if you Google Tyro dating paper, it pops up a bunch of places. Anchorlists.bc if you want to see what we're up to in Bangladesh. Yeah. And Twitter is obviously, anybody can talk to me on Twitter.

Brandon Beylo (host):

And then final question. If you could have dinner with one person from the past or the present, who would it be and why?

Dan McMurtrie:

I'm going to go with Robin Williams. I'm a huge comedy nerd, I've done some standup comedy, and he is the one guy that I'm very sad that I won't get to meet.

Brandon Beylo (host):

Got it. Dan, this has been fantastic. Thank you.

Dan McMurtrie:

Thank you so much, Brandon. I really appreciate it.