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This Famous Poker Player Can Help Investors Play a Tough Hand

By Leslie P. Norton and Bonnie Bennett Slater April 24, 2020 7:30 am ET

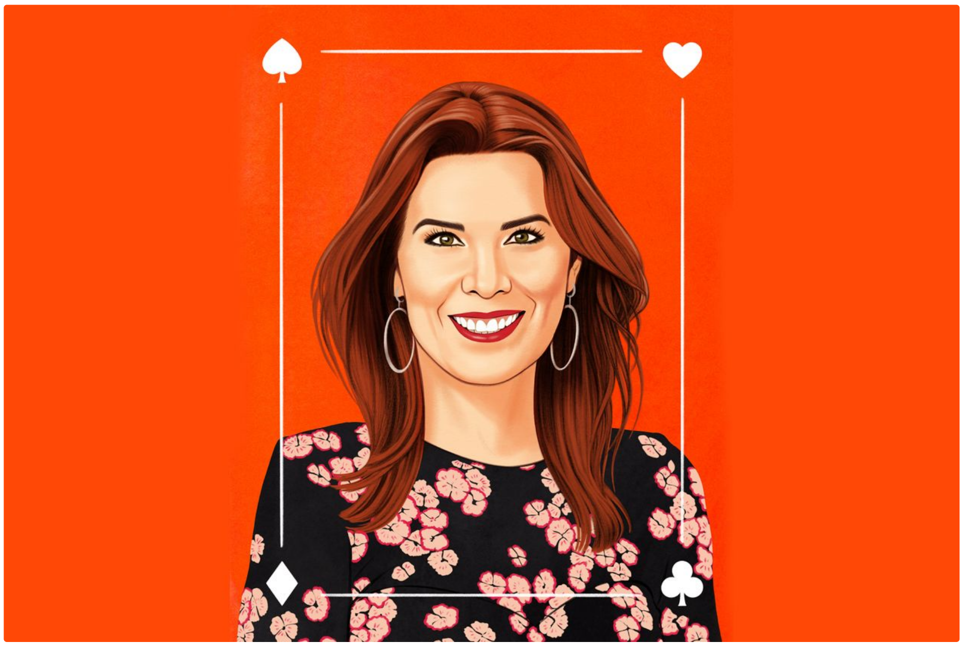

Illustration by Helen Green

After winning more than $4 million in tournament poker, Annie Duke has plenty of experience navigating risk—even the kind of risk that's gripping the world today.

A former winner of the World Series of Poker Tournament of Champions and the NBC National Heads-Up Poker Championship, Duke now speaks widely and advises all kinds of clients who need help in understanding how to make decisions, including people in the financial markets.

Duke talked with us via a socially distanced call recently about removing emotions from decision-making , how global markets are really just one giant poker table, and her biggest bluff. A condensed version of our conversation follows.

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switched to Lady Gaga's *"Poker Face."*

You're an expert at making decisions. What are some useful frameworks for a time of great uncertainty—like right now?

Most decisions we make are under uncertainty—they're heavily influenced by luck, by hidden information. We fool ourselves into thinking that it's not so uncertain. The coronavirus is so clearly uncertain that people are more open-minded today, and because of that you can actually learn. We're always balancing time and certainty.

So more time to decide means more certainty about the decision?

If we had all the time in the world to collect data, create perfect models, and lab-test them, we'd want to do that. But time does have value, and how quickly you act really matters.

There are three ways to think about decision-making. First is when the outcome doesn't matter very much, so the time it takes to make a decision is less of an issue: People taking 15 minutes to order something off the menu fall into that category.

Second, when the outcome matters to you, you need to think about optionality. If I lived in a warm climate and thought about taking a job in a cold climate, I could go live in a cold climate for six months to figure out if I liked it—but the option to take the job would have expired. So I have to make my best guess. How easy is it to unwind your decision? That could help you speed up [making your decision].

What's the third piece?

Thinking about whether time matters. The longer I wait, does the set of outcomes change? This is particularly important in terms of the downside outcomes. Does the magnitude of the downside get worse? The more the answer is yes, then the more you should be willing to do things, including very drastic things, very early.

You saw this with coronavirus. When would you want to lock down, for example? By the time you've gathered enough certainty, it's way too late to be able to contain or mitigate it; the opportunity has passed you by, and the outcomes are going to be really bad. The countries that locked down early, that tested, traced, and contained, had a better curve than the countries that

Interestingly, a bunch of articles were circulating a while ago saying we don't have enough data to make these decisions. Yes—that's exactly right. You should be making decisions with a lot of uncertainty.

How does that apply to simpler decisions?

We tend to delay when we have to do something really hard. Think about decision-making for businesses right now. When are you furloughing employees or laying people off? When are you really going into austerity measures? Most businesses do those much later than they actually should. The reason is that when you want to execute on something really hard, and know it has some downside associated with it, you want to be certain of what the outcome looks like. The problem is, when you obtain that certainty, it's usually too late in the game and you've increased the magnitude of the problem. You've made it much more likely that you're going to go out of business.

The flip side is when it's a fun thing, you tend to decide with too little certainty. So if someone tells me I might get a bonus in December, I'll probably spend it before I get it.

So should people have sold stocks in the first days of the decline, thinking that the magnitude of the downside would get worse?

You want to protect yourself from yourself. The best thing to do, in this particular case, is look at other bad things that have happened to the stock market. Was it a V-shaped recovery? A slower recovery? What would have earned me the most money? Look at the outliers, and hedge part of a portfolio against that.

Until the virus goes away, we don't know. So, in advance, when you're not emotional, figure out what you would need to be true in the world for you to start thinking that a V-shaped recovery, or a recession, or a depression [might happen]. Then, make a list and start watching for these things to happen in the world. Then you can change your probability and your portfolio accordingly, but you've made the decision way in advance.

The one thing we do know is that when there's a lot of volatility, retail investors who try to time the market do much worse than people who just leave their money there. The reason is that people who leave their money are participating in every one of those possible recoveries, whether fast or slow.

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The double-edged sword of poker is you get lots of feedback really, really fast. That should power up your learning ability, but the ups and downs are coming at you really quickly. That creates a lot of emotional decision-making. Think of someone who's day trading, versus someone who just sticks the money in an IRA. Day traders see upticks and downticks in their portfolio, which create emotional responses.

It's really important to get control of that to be successful in poker. You have to do some mental time travel—think ahead as to what the end result is going to be. You can get there by saying, OK, I lost this hand, but do I think in a month this little uptick or downtick will affect my bottom line? The answer is probably not. Second, you try to focus on the quality of the decision, not the outcome.

That gets you out of your emotional mind, because you have to use the rational part of your brain to answer those questions. Let's say someone panic-sold at the market low. Then it bounces back and they're beating themselves up. They could use that as a learning experience and ask, OK, what caused me to panic sell? How could I avoid that in future? You could make a reasonable decision.

How do you choose investments?

When you play poker, you have to be really aware of what your level is. In investing, instead of trading hands, you're trading stocks and bonds. Are you better than the people you're playing against? The less you believe that you can outthink the people in the market, the more that you should be in passive investing. The more that you believe that you can outthink the market, the more that you might want to go active . For people really interested in investing, have a portion to play with that you can afford to lose. And have the rest invested at your level.

> "Recognize in advance the places where you may not make a rational decision."
>
> — Annie Duke

What did you do with your money during the crisis?

Nothing. On purpose. I was 65% equities, 35% bonds going into the crisis. My investment person called and asked, "Do you want to talk about it?" I said no. I'm protecting myself against my own irrationality. I work with people in finance all the time. That could cause me to fool myself into thinking I know a lot more about finance than I actually do. I'm very afraid of the Dunning-Kruger effect [a cognitive bias in which people with low ability at

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So, recognize in advance the places where you may not make a rational decision. People who in 2010 and 2019 just left their money in the market would have done better than all the people who decided they would sell at the high and buy the dip.

Your next book comes out in September. What's it about?

The book sets out to show people how to get a better look at the different ways that the future might unfold. There are tons of thought experiments. It's filled with decision tools. It has wrap-ups, checklists, flow charts.

What was the biggest bluff you've ever made?

It was a cash game, playing something called Pot Limit Omaha. I was playing against this chauvinist. I knew that he had a misconception of me, which was that I didn't bluff because I was a woman. It's the last card of the hand, and he made a $10,000 bet. I had high confidence that he had a diamond flush. But I knew it couldn't be the best diamond flush, because I had the ace of diamonds, but didn't have another diamond to go with it. I went all in. So he sat there, and started counting out his chips, and putting them down into four stacks, and putting them back together in one. This went on for quite a long time. All the time, he's saying aloud, "She never bluffs. She never bluffs." He turned over his hand, and threw it in the middle of the table. I won the pot. The pot was $26,000.

What's the lesson there?

Poker has come in handy in understanding the patterns of people's behavior, and how you can predict what they might do in the future. Just something as simple as overconfidence is important to understand, because it allows you to trade against it.

Thanks, Annie.

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