

mBaer Necessities

Breaking news from The Office of Alternative Futures.

As if it was not hard enough to forecast the future, researchers have developed the obscure acronyms of TUNA (turbulent-uncertain-novel-ambiguous) and VUCA (volatile-uncertain-complex-ambiguous) to capture the complexity of the problem.

Forecasting essentially reduces the *uncertainty* of the future by using our experience as guidance. The idea is that if today looks similar to yesterday, then we can expect that *today's tomorrow* will look like *yesterday's tomorrow*. This sounds intuitive and simple to apply.

By following this line of thought, we accept a conception of the future as singular and knowable. And we can enjoy the emotional security that our calculations and narratives will show us what to do, with our investments or a company, with the precision of a model of classical mechanics.

This is a healthy decision-making process, and we routinely collect all the information we need to make our forecasts and quantify the odds of their occurrence.

Then Covid hit.

Successful prophets

In reality, all events are so complex that forecasting is always a matter of grappling with "true uncertainty," as Frank Knight called it, which is not susceptible to measurement.

As Knight saw it, an ever-changing and uncertain world brings new opportunities for businesses to make profits. In his words, "at the bottom of the uncertainty problem in economics is the forward-looking nature of the economic process itself".

The essence of economic competition is that entrepreneurs' opinions compete in the markets, and profit stems from some opinions being more accurate than others.

In the investment world, the ability to beat the market, known as *alpha*, is the result of making better forecasts than the market, so only this rare skill should be financially rewarded.

In short, successful entrepreneurs and great investors are good forecasters.

Imagination is profitable

In an uncertain world, the quality of our decisions can be improved, and our forecasting skills can be trained.

One has to step back from the notion of the future as singular and knowable and embrace the possibility of multiple futures.

"We can learn from the future", in Peter Scoblic's words, by building alternative scenarios and planning various courses of action for each of these scenarios. The process works well as it reduces our biases, typically based on experience and commonly accepted assumptions, and renders us more flexible and perceptive to changes in the environment.

In short, uncertainty can inspire superior judgement and a better course of action. This may sound counterintuitive, though, as we are typically discouraged from taking decisions when their outcome is perceived as uncertain.

The hard job is abandoning the notion of a deterministic world, acknowledging the limits of experience and envisioning alternative futures.

What if we are all wrong?

Below is a gust of thoughts on what might go very wrong. Admittedly, our narratives belong to the extremes of critical probability distributions far outside the realm of ordinary experience.

Global debt restructuring

In a joint communique on socials and TV channels in October 2022, Prime Ministers and Heads of Central Banks of major developed economies proclaim default on government debt. A wave of banking crises, recessions, currency and market crashes follows. The restructuring process lasts several years.

Deadly Covid variants emerge

In September, a more virulent and vaccine-resistant mutation of Covid spreads globally. Too late, governments in economies rush into introducing restrictive measures and imposing compulsory vaccination. With medical systems under stress, health emergencies lead to social unrest and eventually to a security crisis. The plague ends in 2027.

Hyperinflation in G10

Uncontrolled budget deficits and accommodative monetary policies in G10 lead to hyperinflation in 2023. Output collapses, financial intermediation sharply reduces and social unrest surges in the run-up to and during the hyperinflation. It takes years to stabilize the economies. China keeps inflation low.

Gulf tensions send Brent to \$200

In May 2022, terrorist attacks successfully target oil facilities in UAE, triggering an inexorable rise in oil and natural gas prices. The oil surplus and inventories are quickly wiped out, and the oil industry cannot increase supply. The prohibitive cost of oil leads to a broader jump in inflation, increased production costs, and reduced output, ultimately resulting in global stagflation.

American civil war

Political divisions, mistrust in the institutions, economic inequality and high inflation, reach their highest level before mid-term elections in 2022 and lead to a deep institutional crisis. Violent protests erupt in the streets and civil war is fought until an authoritarian regime is installed. Democracy in the US is fully restored in 2028.

The value of imagining alternative futures is in the process of questioning assumptions and common mental models and in preparing for uncertain but conceivable futures. Like successful entrepreneurs do.

Francesco Mandalà, PhD
Chief Investment Officer

Investment Office Team



Francesco Mandalà, CIO, joined MBaer Merchant Bank in February 2021. His background is in Economics and Financial Engineering, and his competencies are portfolio management, fixed income modelling, macro strategy, risk management and fund analysis. Previously, Francesco worked at UBS and Julius Baer in various roles. Earlier, he was a Statistician at the European Central Bank (ECB) in Frankfurt and an Analyst at the Committee of European Banking Supervisors (CEBS) in London. He currently collaborates with the Swiss Finance Institute (SFI) and co-leads some Master Classes together with SFI Academics. Francesco holds a Certificate in Financial Engineering & Risk Management (Columbia University), a Certificate in Investment Management with Python and Machine Learning (EDHEC Risk Institute), a PhD in Economics (Pavia University), an MSc in Economics & Econometrics (Southampton University), a BA in Economics (Bocconi University, Marks: 110/110). Francesco is fluent in Italian and English.



Patrick Quensel joined MBaer Merchant Bank in October 2021 as **Investment Advisor**. With more than 10+ years of experience, he has gained broad insights within the financial services industry, focusing on multi-asset portfolio management, risk management, systematic investing, and global macro. Previously, Patrick worked for an investment management boutique as Head Investment Advisory and Senior Portfolio Manager. Among others, he was managing two award-winning investment strategies and was responsible for the cross-asset investment framework.

Patrick holds an MBA from Insead and a Bachelor and Master's in Banking & Finance from the University of Zurich. Patrick is fluent in German and English.



Thomas Büren joined MBaer Merchant Bank in July 2021 as **Investment Specialist**. Before joining MBaer Merchant Bank, Thomas developed corporate finance and financial markets skills and knowledge. He gained experience as a trainee in various countries and financial departments; investment banking (Commerzbank, London), asset management (Salm-Salm & Partners, Frankfurt), deal advisory (KPMG, Paris & Mauritius) and wealth management (BNP Paribas, Paris).

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