



Fisher Funds Investor Education Centre

Making investing understandable,
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Investing v. Speculating 30 October 2011

It's Melbourne Cup next week, Australia's most famous Tuesday where much of the nation stops for three minutes or so to listen as the race is called. Some enjoy the dressing up and festivities and many enjoy having a flutter. While I'm as keen as the next girl to don a hat and heels, I've never really enjoyed horse racing, or gambling of any kind actually.

I've often wondered whether that's because I'm an investor and investors are wired differently to gamblers.

To my mind gambling is to risk money on something involving chance, whereas investing is to risk money where the odds can be tilted in your favour.

However it is not as clear cut as that.

I have met enough people who consistently leave casinos and race courses with more money than they arrived with, to know that sometimes gambling odds can be tilted in one's favour. I have also seen investment decisions that were well-researched and well reasoned but yielded results that were no better than flipping a coin.

So is there really a difference between investing and gambling or is it just perception?

Investing is generally regarded as a 'good' thing whereas gambling is seen as a 'bad' thing. Investing is an engine that drives capitalism – it provides capital for companies to grow and economies to thrive. Whereas gambling is not seen to make such a positive contribution, and indeed excessive gambling has some well-documented negative side effects. Having said that, excessive investing can also be negative, particularly when it creates market volatility.

It is often assumed that in investing, the odds are in your favour whereas in gambling the odds are against you because the house always wins. But there are plenty of investments where the odds are against you, particularly if don't know what you've invested in.

Some think of gambling as entertainment whereas investing is business. Apparently the thrill of gambling is as much about the 'action' and the chance of winning big as it is about the money. I'm not sure many investors think this way. Most investors have a goal of creating value rather than just having a good time.

Investing is said to be based on skill and requires the use of research and a system or process, whereas gambling is just based on luck and emotion. However, there are plenty of full-time gamblers who research plenty and develop systems to tilt the odds.



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Legendary investor Benjamin Graham probably sums it up best when he talks about the difference between investment and speculation (which I think is interchangeable for gambling). There is intelligent speculation as there is intelligent investing. But there are many ways in which speculation may be unintelligent.

Of these the foremost are 1) speculating when you think you are investing 2) speculating seriously instead of as a pastime, when you lack proper knowledge and skill for it and 3) risking more money in speculation than you can afford to lose.

Keep this in mind on Tuesday.