



AUTHOR: Dr Keith Suter
Global Thought Leader
Real Insights & Authority



THE BLACK SWAN: THE IMPACT OF THE HIGHLY IMPROBABLE NASSIM NICHOLAS TALEB MELBOURNE: ALLEN LANE, 2007

This book has suddenly become acquired reading matter in the finance sector. The author worked in “derivatives” for a big finance company at the time of the October 1987 crash and he reflects on the way he and his colleagues were taken by surprise by the crash. He also suggests that there could be another financial crisis (which has since hit us). How are we to cope with a low probability/ high impact event?

Before the Europeans arrived in Western Australia, it was assumed that all swans were white. Everywhere they went in Europe all the swans were white and so they thought they could safely assume that all the world’s swans were also white. They generalized from past knowledge. The discovery of black swans in WA (now a state logo) therefore shocked the Europeans.

This is an infuriating book on a very important topic: the role of something occurring outside our regular expectations. It is an important topic but the book is heavy-going. The author has written a very long (over 350 pages), self-indulgent, discursive book on matters which could be treated better in something shorter and sharper. The author, among other things, is trying to settle a number of private scores against writers over the centuries (such as Plato). It is all a bit tedious to try to follow.

But the book’s underlying idea is fascinating. Humans have an ingrained tendency to underestimate outliers, such as the possibility that there is a place in the world yet to be reached by Europeans that may contain black swans. Humans are also reluctant to “unlearn” old ideas.

Former US Secretary of Defence Donald Rumsfeld made notorious the very sensible observation that there are things we know we know, other things that we know we don’t know, and there are also things we don’t know we don’t know (eg that WA has black swans). How can we develop techniques to deal with that final category?

Unfortunately the book does not give us too many specific recommendations for action. The book’s usefulness – if the reader is willing to persevere with it – comes from the fascinating insights and warnings scattered along the way. For example, in a study of risk of within a casino (normally a guaranteed way to make money from foolish gamblers), the casino ran into problems



not from the customers but from events it had not thought about eg it lost US\$100 million when a performer was maimed by a normally docile tiger in the entertainment ring.

Another example comes from the identification of the most important three recent technologies: computer, Internet and the laser. All were unplanned, unpredicted and unappreciated upon their discovery and they remained unappreciated well after their initial use.

You cannot ignore self-delusion. The problem with experts is that they do not know what they don't know. This also goes for the "masters of the universe" on Wall Street.

Keith Suter