
Fooled by Randomness Summary PDF Cheatsheet —

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? 1. Remain Uncertain: Having less confidence in current theories and models

Most traders and economists put too much confidence in abstract models. This blinds them to the risks of large and rare events that the models do not predict, like the many ‘unexpected’ crashes throughout history.

? 2. Be Inconsistent: Remaining independent of our past beliefs

Humans have a natural tendency to become attached to our past positions, which often causes failure in business. Instead, we must avoid certainty in our beliefs, only seeing them as more or less probable.

? 3. Don't Value Track Records: Past success may not mean anything

Even several-year-long “track records” of success may be the result of randomness more often than we assume because of: 1. Survivorship bias (paying attention only to the winners), 2. chaos theory (a small bit of luck compounding), and 3. short-term evolutionary fitness (strategies that work for the current market cycle).

? 4. Prioritize Certainty: Estimating the risk in a path to success

When looking at examples of success, we should consider the alternative histories that could have happened. For example, a doctor's success is relatively more certain than a lottery winner's, so it should be worth more.

? 5. Limit Your Maximum Costs: Insuring against unlikely worst case scenarios

In many situations, what matters more than the odds of a positive/negative outcome are the asymmetrical gains/losses. This means you could have a small chance of losing money, but if you do then you lose it all. Clear, predetermined stop loss points can often help avoid this disaster in trading.

? 6. Ignore Short-Term Noise: Focusing on ideas that have stood the test of time

Humans carry many cognitive biases that cause us to make systematic flaws in our decisions. We are more influenced by specific concrete events rather than abstract probabilities. Perhaps the best move is plugging our ears to short-term noise that feeds our biases like the news media.

?? 7. Control Your Behavior: Facing life's randomness with dignity

In the face of life's randomness, ancient Stoic philosophy tells us that we can only control our actions. Beyond that, we must trust there is a deeper reason for misfortune that comes from a higher power.

This is just a sample!

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