Cuffelinks
Connecting investors with ideas

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## The Harry Markowitz Interview, Part 2: Retail financial advice

This is the second part of my interview with one of the fathers of the wealth management industry, the 1990 Nobel Prize Winner, **Harry Markowitz.** His Modern Portfolio Theory ideas are still taught in universities and business schools. In Part 2, we discussed his retail financial advice business, GuidedChoice. He is co-founder and Chief Architect, including designing the software analytics for the investment solution and heading the Investment Committee. Part 1 of the interview on portfolio selection is here.

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Graham Hand: Can we talk about you do with GuidedChoice? I'm especially interested in how you advise people, how you manage asset allocation and issues such as longevity risk.

Harry Markowitz: What we do is Monte Carlo analysis to get a probability distribution of how well you will do if you invest in a certain way, and save a certain amount of money. You're familiar with Gary Brinson's writings on asset allocation?

GH: Where 90% of your returns come from asset allocation, not manager selection.

HM: Yes. The important thing about Gary Brinson's work, which has persuaded trillions of dollars of funds to do this top down analysis, is where you first decide to be on an efficient frontier at the asset price level. Then you figure out where you should invest, you might consider the managers to use or ETFs. The beauty of that is that people who have no ability to pick stocks can still get good advice.

We do this top down analysis, for all our clients, we do forward-looking estimates of variances and covariances. We don't reestimate values very often because we use long-dated series. A few years back we said we've got to reduce our forward-looking estimates on fixed income because we're

obviously in a low rate environment, but we don't change equity estimates very often. We are doing principal component analysis of the factors, but it's not completely mechanical. When it's finished, we take all the asset classes with estimated expected return on one axis and estimated standard deviation on the other axis.

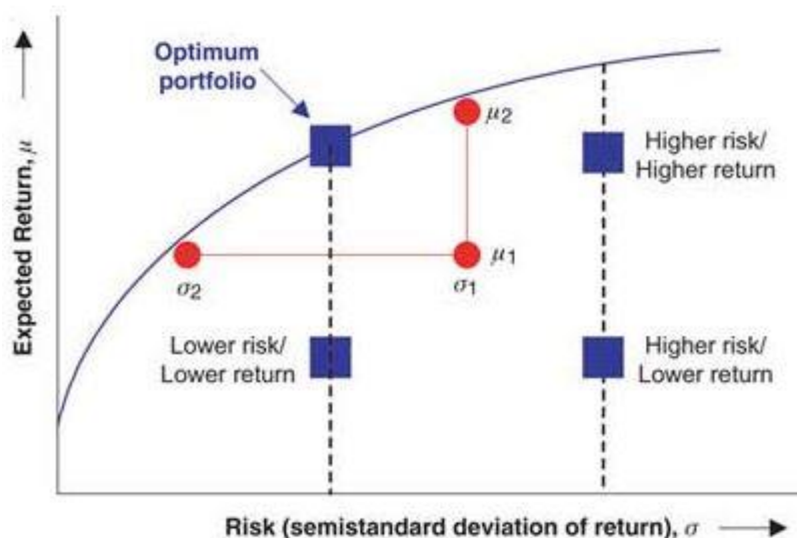
For everybody, we generate an efficient frontier at the asset class level, and we pick off 7 portfolios, number 7 being the riskiest, 1 being the most cautious. Then for specific plans, which have allowed investments, we have a separate optimisation which tries to figure out what are the real investible securities permitted by particular plans in order to match these asset classes. We take into account tracking error, expense ratio, historical alphas. For each participant, we receive a lot of data from their company, and we ask questions like, "When do you plan to retire?"

GH: So there's a type of online questionnaire that the individual fills in? I'm wondering how you work out the client's risk appetite.

HM: Yes, it's interactive online, but we do not ask whether you sky dive. We look at what you already have in your portfolio, assess your current risk level, and we propose to you a portfolio. Then we show you the consequences of changing from your current one to a proposed portfolio. We show you three points on the probability distribution of how much you can spend in current dollars when you retire – in a weak market, an average market and a strong market. You can fiddle with it, you can go up the frontier, or you can save more.

GH: You have these 7 asset class portfolios with different risks, how does someone decide?

HM: You're a client, you've told us when you want to retire, you've said at what rate you are willing to save, told us whether you have a spouse, we can see your existing portfolio. We show you a portfolio which has a similar risk level but maybe a bit more return, and we show you three points off the probability distribution showing the rate you can spend when you retire. You might not want Risk Class 4, so they try 5, and we go back and forth.




Source: GuidedChoice website.

As an aside, you should read a paper I wrote called *The Early History of Portfolio Theory 1600-1960*. I chose 1960 because that was when Bill Sharpe knocked at my door and asked what he should do his dissertation on. And 1600 is when *The Merchant of Venice* was written and Antonio said, "My *ventures are* not *in* one *bottom* trusted*, nor to* one *place; nor is* my *whole estate, upon the fortune of this present* year." Shakespeare knew about diversification.

GH: So portfolio diversification had already happened by 1600. How far have we come since then?

HM: Well, now we know how to measure covariance. We know diversification will eliminate risks if they're uncorrelated, but not if they're correlated.

Another thing I should say is that GuidedChoice now has another product, GuidedSpending, which has to do with how fast you can spend in retirement. We assume your spending rate will depend how well you do in the market, and we ask you for two consumption levels: upper level where you can put away any surplus for a rainy day, and a lower level where you have to see if you can hold out for a while. Depending on how you set your levels, plus all the other factors, we assign a probability distribution on the rate at which you can spend when you retire. For any time pattern of consumption, we assign a utility based on the average consumption you can achieve.

GH: But how do you plan for how long a person is going to live?

HM: Currently, we assume you will drop dead precisely 10 years after your actuarial time, but I have been promised some day we will have a stochastic model.

GH: So you use actuarial life tables. What do you think about the basic default savings plans, such as the 60/40 model or lifecycle funds with more allocated to the defensive asset over time?

HM: The problem with 60/40, it's a little chicken for people early on, it's not right for everybody. 90/10 might be best for a young person. The problem with lifecycle is I'm 85 and I have more in equities than I've ever had, but I have a wealth level that means I am many standard deviations away from not being able to eat.

GH: So you need to consider your income-earning ability and other factors, not just your age.

HM: You need to look at the probability distribution of what they can spend, what they can earn, how long they will be employed. Our models will always be grossly inadequate because there are more things on heaven and earth than we can ever capture in our models. We have to do the best we can but we get a lot closer than 60/40 for everybody.

GH: What do you think of the merits of Tactical Asset Allocation where someone takes a view on the market and changes the asset allocation?

HM: There's my official view and my unofficial view. My official view is that nobody seems to be very good at picking the market. But it does seem plausible that when price earnings ratios are historically high, we should lean towards less to equities. In my own funds in 2007, I sold my ETFs, I didn't get out of equities completely, and I went back in in December 2008 expecting a January effect. Which came in March. On some occasions, it has merit. But if someone reads a weekly newsletter about whether you should be betting up or down this time, going in and out, you'll lose money on average over the long run. There's a wonderful behavioural finance guy, Terrance Odean, who studies the track records of individual investors, and he finds both active and passive investors gross roughly what the market makes, the active do worst due to brokerage.

You know, I'm writing another book, in 4 volumes, first is already at the publishers, McGraw-Hill. The next volume is due March 2015, then 2017, then 2019.

GH: That's a good note to end on. Thanks very much, I really appreciate it.

**Next week: Full interview with Burton Malkiel, author of the best-selling classic *A Random Walk Down Wall Street.***

## How much variability exists in retirement outcomes?


## David Bell


Many of the articles you will find in *Cuffelinks* and other forums make reference to the impact of different risks on retirement outcomes. The risk factors most commonly mentioned are investment returns and mortality risk. There are many other factors including inflation and wage outcomes and our level of discretionary savings. However the big question remains largely unanswered: given all these risks what is the variability in retirement financial outcomes?

This is a difficult question as there is surprisingly little research on this subject. Both Treasury and Rice Warner project retirement outcomes but only produce point estimates. Point estimates are dangerous pieces of information if used in isolation. They are in effect expectations, yet we know little of the variation around the expectation. For individuals this risk creates false confidence in an uncertain outcome and leaves policy makers in a position where they are uncertain whether all possible retirement outcomes produced by the retirement income system are acceptable.

**Simulating the financial outcomes**

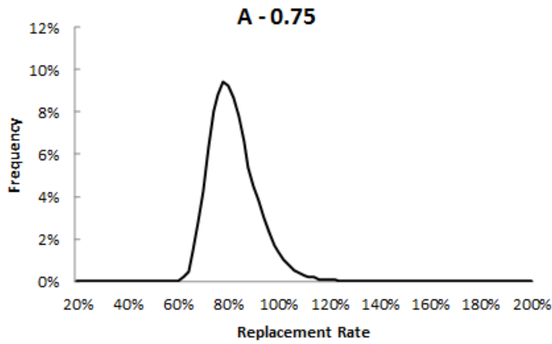
So I investigated this as the core question of my 2011 academic paper titled *"Variability in the Projected Financial Outcomes of Australians."* At the heart of this paper is a large lifecycle model which simulates the financial outcomes of single income households (double income households is extremely complex and a project for another day!). There are two aspects to the model. First, it simulates all the financial aspects of a household through their lifecycle. Second, it introduces variability by allowing some of the factors (for instance, investment returns) to experience random outcomes (around an average). We then simulate outcomes (generally **20,000** for each defined situation) and this provides insight to the variability in possible outcomes.

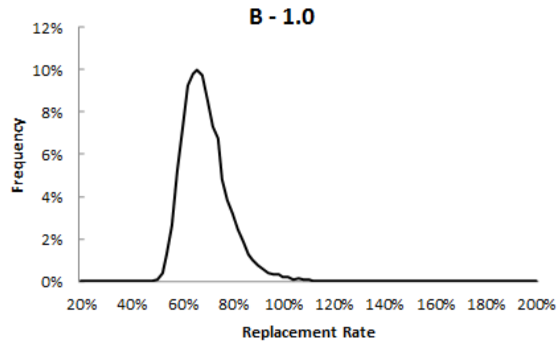
It is important in this type of research that the model faithfully represents the financial actions and exposures of a household. In modelling the working years (the accumulation phase), I assume that we work, earn income, pay taxes, consume, purchase a house, and accumulate savings (in superannuation and other forms). In retirement, we draw down on our accumulated savings, we may receive the age pension (subject to means testing), we may pay tax and we consume to an uncertain age of death. All taxes and other rules associated with income, super and pension are modelled.

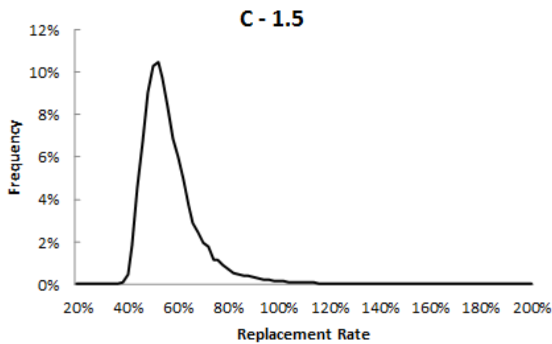
I introduce variability into the model by allowing some factor outcomes to have an element of randomness, around an expectation. These factors are real wages, real investment returns, variability in mortality outcomes, and some variability in savings rates across households.

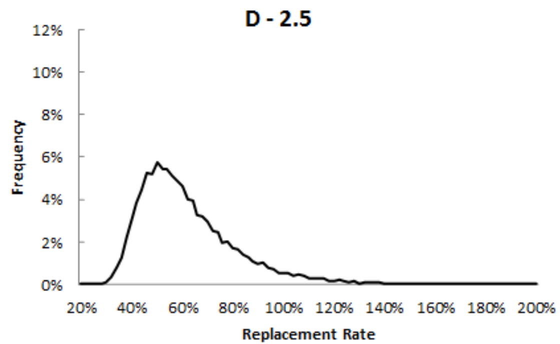
**What were the results?**

The results are measured in terms of replacement rate outcomes, and more specifically the expenditure replacement rate. An expenditure replacement rate compares what we have available in retirement as a percentage of our pre-retirement expenditure levels (think what you have available to spend as a proportion of your previous gross income less taxes and savings). The results are presented for a female (the 'standard' case used by Treasury – male outcomes are quite similar). The modelling considers outcomes based on households experiencing different levels of income (represented as a multiple of AWOTE – Average Weekly Ordinary Time Earnings of approximately $70,000 pa). This is also consistent with how Treasury measures retirement financial outcomes. The distribution of outcomes is presented in the panel diagram below.










In the diagrams above the number at the top (eg. 0.75 in Panel A) represents the income of the household as a multiple of AWOTE. That is, 75% of $70,000, or about $52,000.

What do we see above? First, it appears that variability is quite large across all households, and is skewed to the right, meaning that surprises are generally to the upside, which is good. This can be explained by the safety net effect provided by the age pension.

We can also see that variability increases as household income increases. This is because high income households generally self-fund a greater portion of their own retirement making them more vulnerable to investment market outcomes.

Summary numbers corresponding to the diagrams above are provided in the table below:

| | **Earnings Multiple of AWOTE*** | | | |
|---|---|---|---|---|
| | **0.75x** | **1.0x** | **1.5x** | **2.5x** |
| Expected Replacement Rate (RR) Outcome (%) | 81.1 | 68.4 | 56.0 | 61.0 |
| Median RR Outcome (%) | 79.8 | 66.9 | 53.3 | 56.7 |
| Standard Deviation of RR Outcomes (%) | 9.6 | 9.5 | 11.8 | 19.3 |
| RR Outcome $5^{th}$ Percentile (%) | 68.1 | 56.3 | 43.3 | 38.3 |
| RR Outcome $95^{th}$ Percentile (%) | 98.3 | 85.2 | 77.4 | 97.8 |

**How do we interpret this information?**

In talking to a high income household earning 250% of AWOTE, we could say that we expect you to have a 61% expenditure replacement rate. They might say that sounds acceptable. Then you should say there is large variability around this estimate and that a 5% worse case event (ie a one-in-twenty likelihood of this or a worse outcome) is an expenditure replacement rate of 38.3% of pre-retirement expenditure. Is this palatable? If not then this variability can be partially managed through the investment and savings decisions we make.

However, a lower income household on 75% of AWOTE should expect an 81% expenditure replacement rate, which falls to a reasonable 68% at the 5% worse case level.

While this research is probably the most detailed in terms of calculating variability, it can always be improved. For instance when I presented this work at a conference it was suggested that I should also have considered the risk to employment outcomes (unemployment risk and the chance of promotion). But as it stands this represents useful information.

**Influence of individual risk factors**

You may be curious to know which of the individual risk factors contributed most to variability in outcomes. The answer differs by household type. For all households investment risk was the largest contributor to overall variability in outcomes, but especially so for high income households. Household savings rate was important for high income households (high income (top quartile) households are responsible for nearly all of Australia's household savings (ex-super) and there is a large dispersion of savings amongst households).

Mortality risk has a curious impact across households. For low income households outcomes are improved if you live longer, as relative to inflation the age pension delivers generous indexation which leads to better outcomes the longer you live. However for high income households outcomes are better if you do not live long as you have less chance of exhausting savings and being forced onto an age pension which is well below the level of income you historically experienced.

This research highlights the responsibilities of all in the industry: whether we are policymakers, super funds, wealth managers or financial planners, we are all responsible for contributing to the achievement of retirement outcomes. These outcomes are not just an expectation or a mean: retirement financial outcomes have variability and it is important that this variability is measured, managed for and communicated with those saving for retirement.

It's useful to focus the mind on how living on 38% of pre-retirement income might affect the plans to travel around the world or build a wooden boat, even if it has only a 5% chance.

## The consequences of sustained budget deficits

## Don Stammer

Last December, the Federal Government discarded its oft-repeated promise of delivering a budget surplus this year. In April, it 'fessed up to the deficit being a big one. And instead of a run of surpluses as our economy returns to good health, we're now told we'll 'fail our future' if we don't run budget deficits for a while. The Government is only beginning to tell us how grim the budget outlook really is. The risk is that we'll run a substantial budget deficit over the whole cycle in varying economic conditions.

It’s timely to consider what this abrupt switch in fiscal strategy might mean for the economy and for investors, particularly those planning for, or already in, their retirement years.

**The long-held promise of a budget surplus**

The promise of a budget surplus in the financial year that’s now ending was made back in 2010. The Government wanted to reassure voters that the large budget deficits it would be running during the global financial crisis would soon be wound back and reversed; there’d not be a sustained build up in government debt. Also, the Cabinet had wanted a way of restraining some of their big spending colleagues and backbenchers (older readers might recall the ‘trilogy’ adopted by the Hawke-Keating government to impose fiscal discipline).

On many occasions, the Gillard Government took the commitment to deliver a budget surplus too far, arguing the surplus would be delivered ‘come hell or high water’ and Australia running a budget surplus this year would stand as ‘one of the eight economic wonders of the modern world’.

**The deterioration in the budget numbers**

The deterioration in the budget numbers for the current financial year mainly reflects the fact that the Government and Treasury have now moved to more realistic numbers for tax revenues, replacing the highly optimistic numbers they’d earlier employed both for the current financial year and for the forward estimates.

Also, the Government is committing to, but is only partly funding, significant new spending programs such as the Gonski reforms to schools policies and DisabilityCare (formerly called National Disability Insurance Scheme). There’s no doubting these policies’ appeal and there’s a good deal of bi-partisan support for them. But they will have to be paid for one way or another.

Government revenues from income taxes haven’t collapsed. Instead – and has been apparent for some time - growth in tax revenues has slowed because of modest growth in nominal incomes. However, from the start, projected revenues from two new taxes had been fancifully high.

The Minerals Resource Rental Tax, which the Government rushed through in 2010 after the debacle of the Resources Super Profits Tax, included revenue forecasts based on commodity prices that, though never made public, were extremely ambitious. They must have assumed that prices for coal and iron ore would stay near record highs for three or four years.

Forecasts for receipts from the carbon tax were built on expectations of a carbon price of $29 a tonne in 2015 – and were not downgraded even when Australia first tied its carbon price to the European price, which was always likely to be weak because of the over-supply of permits and sluggish economies there. The amended forecast is a carbon price of $15 in 2015 (still more than three times the current European price).

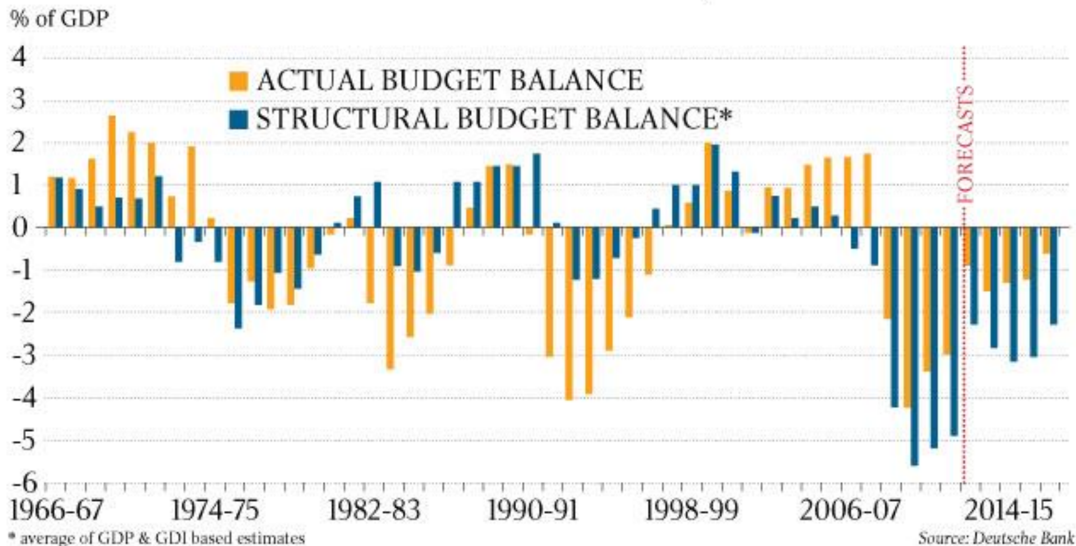
**Why the structural deficit or surplus is important**

Both major parties have long expressed the view – shared, I think, by a majority of voters – that the budget should be balanced over the economic cycle. This enables the budget to be used to moderate the business cycle via both its ‘automatic stabilisers’ and through discretionary changes to revenue and spending, while still avoiding excessive build up of government debt over the medium-term and longer. This anchor for fiscal policy has served Australia well for many years.

For this reason, the budget deficit or surplus has to be looked at in structural (or cyclically-adjusted) terms as well as in cash terms. Deutsche Bank ran the numbers prior to the release of the 2013 budget numbers, and concluded that “the structural deficit (ie abstracting from the impacts of higher commodity prices and the economic cycle) will be around 2¼% of GDP in 2012-

13. Looking forward we estimate the structural deficit will still be around 2¼% come 2016-17 … we see the structural deficit averaging more than was seen under either the Whitlam or Fraser governments."

Of course, most other western countries have structural budgets and levels of government debt on issue significantly higher than ours, although Canada and New Zealand are likely to return to surplus before we do. And the Coalition Government didn't run surpluses as large as the prosperous times before the global financial crisis really dictated they should have. Norway's larger surpluses, fed in that country's sovereign wealth fund, suggest the route we should have followed.




**The worry about persistent deficits**

In the words of the Grattan Institute, persistent budget deficits "incur interest payments, and limit future borrowings … they can unfairly shift costs between generations, and reduce flexibility in a crisis". In my view, the problems facing Europe, where the global financial crisis morphed into a sovereign debt crisis, demonstrate the pain that comes from persistent budget deficits (aggravated of course by the common currency). Deutsche Bank adds, "given the budget will be in deficit … the Federal Government is now contributing to the current account deficit".

A balanced budget over the economic cycle is generally favourable for investors, because it improves prospects that real returns in assets will be more stable, predictable and attractive than they'd otherwise be. Similarly, a balanced budget over the economic cycle generally helps to restrain inflation which, when tolerated, creates pain and uncertainty for investors, particularly for self-funded retirees living from savings.

Deutsche Bank also reminds us that "to the extent that unaffordable policies drive dire projections of the budget position, such policies will not see the light of day in unaltered form" - and, I'd add, they can cause the government to cut deeply into current programmes, even popular and efficient ones. When governments live beyond their means, uncertainties build up and costs are imposed because the bills still have to be paid somehow.

*Don Stammer is an adviser to the Third Link Growth Fund, Altius Asset Management and Philo Capital. The views expressed are his alone.*

# Federal Government budgets and their impact on the stockmarket

## Ashley Owen

While the media coverage surrounding the budget is full of facts, figures and opinions, much of the debate is clouded by political rhetoric and misinformation. Issues like whether deficits are good or bad for the country as a whole and for present and future tax-payers – and indeed what the money is actually spent on (ie productive assets or welfare) - are important questions for another day!

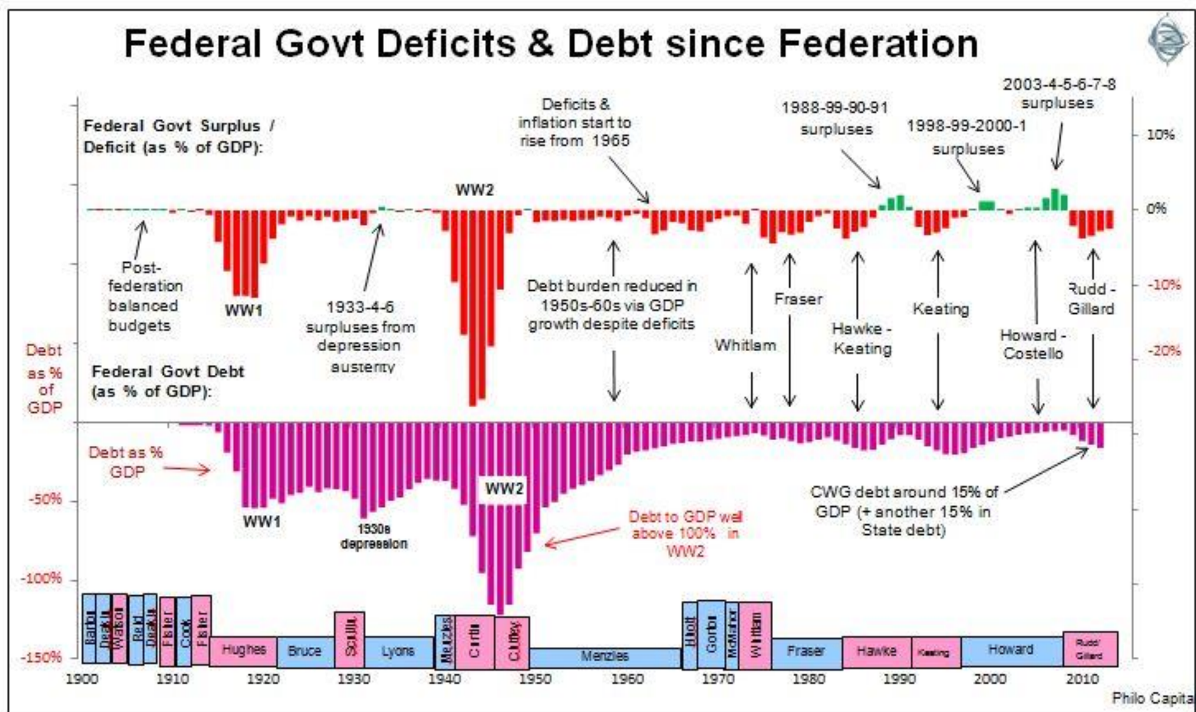
This paper is about facts, not opinion or judgment, and puts the current budget into context and considers what budget deficits mean for investors. In particular:

- how often have governments produced budget surpluses?
- how do Labor and Liberal governments compare when it comes to deficits and debt?
- how serious are the current levels of deficit and debt?
- have government deficits been good or bad for stock markets?

**History of Federal Government surpluses, deficits and debt**

Our first chart shows the history of federal government fiscal balances and debt levels since Federation, and it also shows the various governments in power. Labor governments are shown in pink and 'right leaning' governments in blue.

**Chart 1**: Federal Government Deficits & Debt since federation




The top section shows the annual government balance (surplus or deficit) expressed as a percentage of GDP (June years). We can see that governments have run surpluses (green bars in the top section) in only a very small minority of years.

Chart 2 shows that Labor governments have achieved government surpluses in only 18% of all years they have been in power, while right-leaning governments have done marginally better, with surpluses in 26% of years in power.

**Chart 2:** Surplus/Deficit years

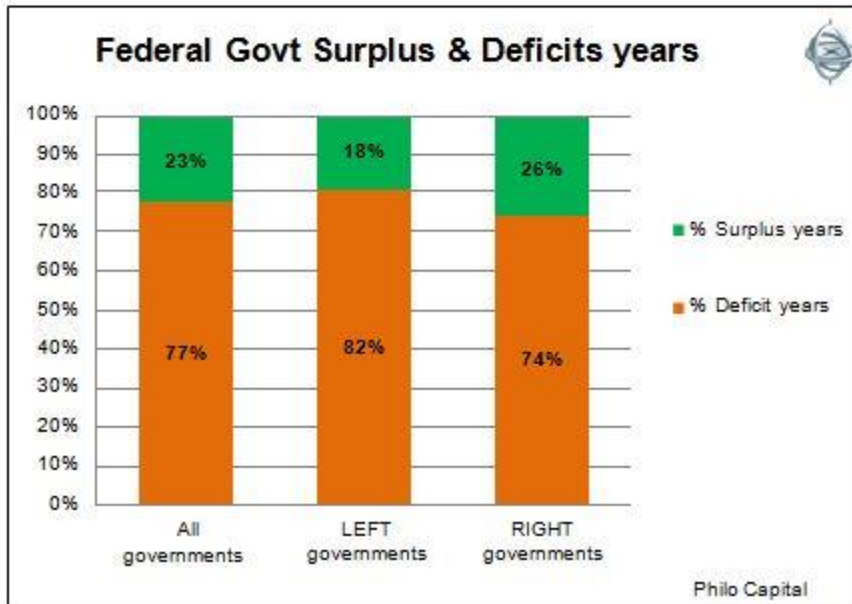
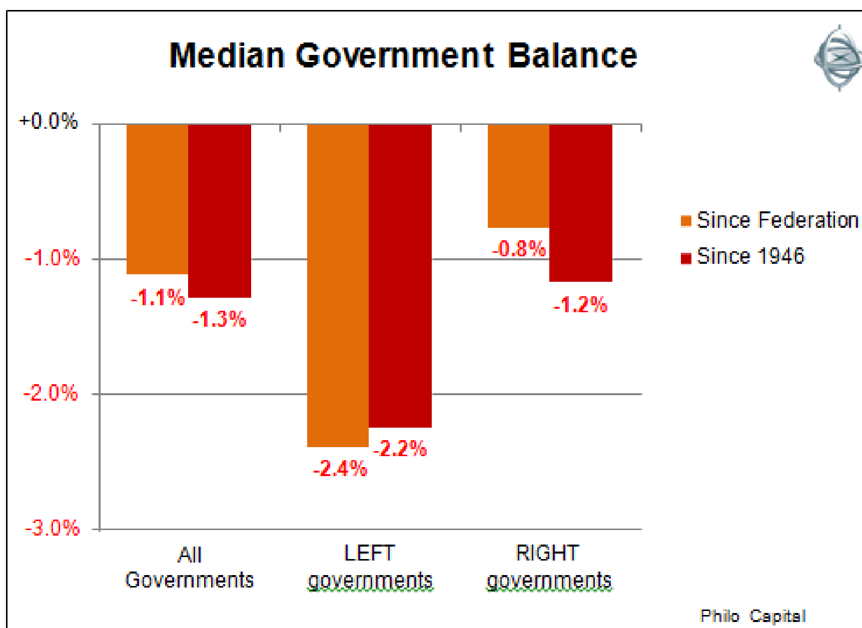



Chart 3 shows that on average Labor budget balances have been worse than right leaning governments (ie Labor have tended to run larger deficits). Even if we just look at the post-war era the differences are still significant, and probably reflect the philosophical differences between the major parties over the role of government in the economy.

**Chart 3:** Median government balance since federation (as percentage of GDP)



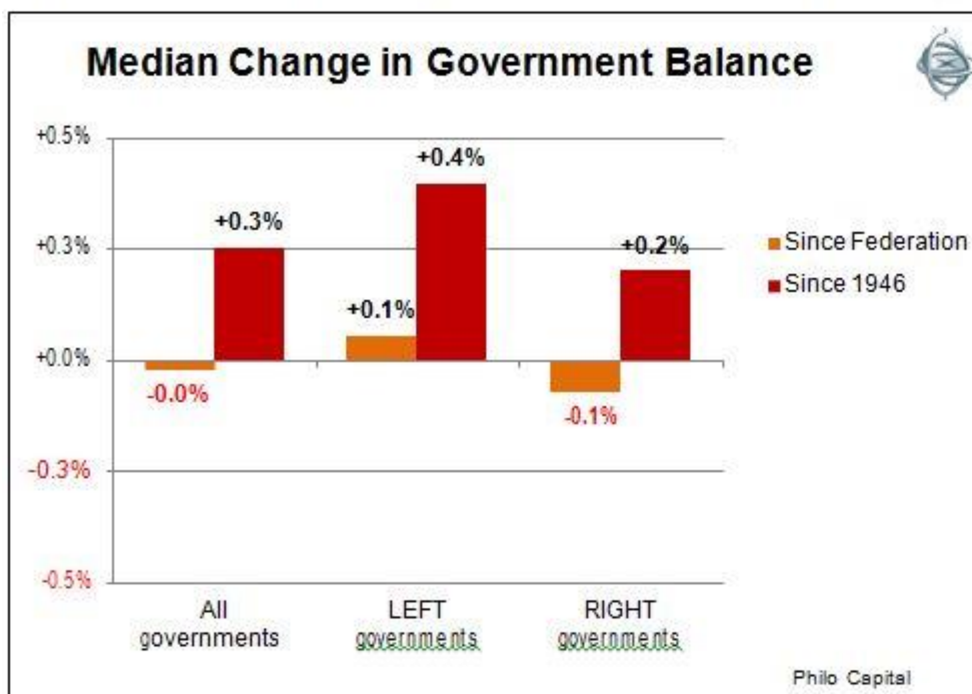
**Changes in government fiscal balance**

More important than the actual level of government fiscal balance from year to year is the change in the balance. This is the case for a couple of reasons. The first is that every government inherits the budget position from the last government and so it has more control over changes in government spending and revenues than it has over the levels of spending and revenues themselves.

The second reason is that it is the change in balance rather than the level that reflects the incumbent government's fiscal stance and its effects on the economy. For example, if a government goes from a deficit of $40 billion in one year to a deficit of 'only' $10 billion in the next year, the $30 billion in lower spending and/or higher taxes in the second year represents a substantial tightening of fiscal policy even though the deficit in the second year appears expansionary if viewed in isolation.

Chart 4 shows that left wing governments have a slightly better record of reducing deficits over the whole period and also in the post-war period, although in most cases it was reducing their own deficits, since Labor governments ran larger deficits overall.

**Chart 4:** Median change in government balance (as percentage of GDP)

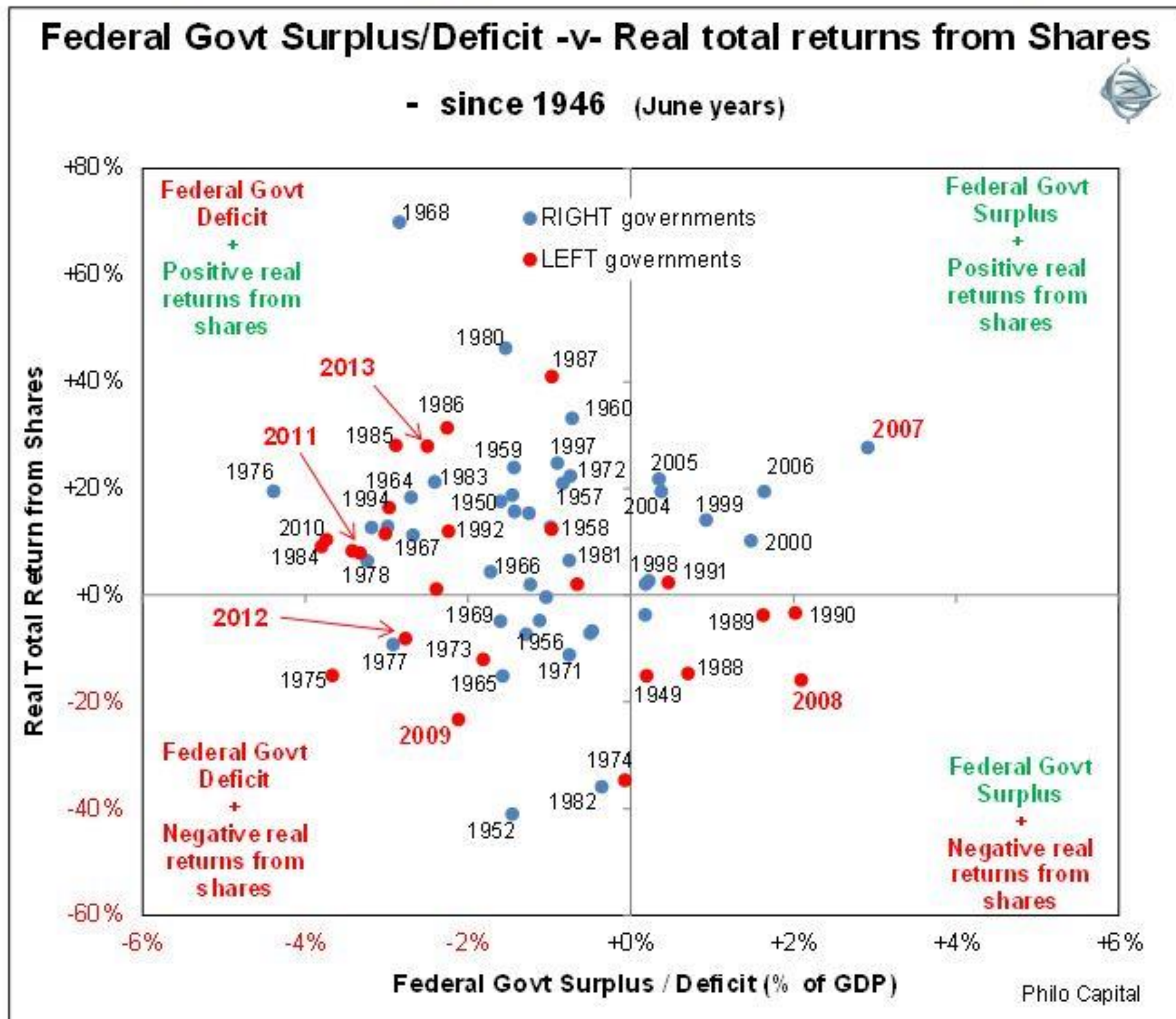



**Deficits and stock market returns**

But what does all of this mean for investors?

Chart 5 shows the annual federal government balance plotted against real total returns from shares (ie including re-invested dividends and after CPI inflation) since 1946. Years are ending in June to line up with the fiscal years. Labor government years are shown in red and right leaning government years are shown in blue.

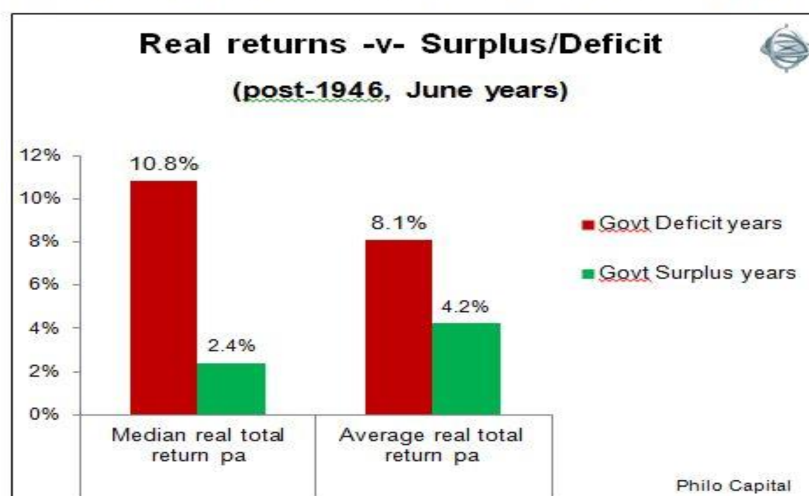
**Chart 5**: Federal government surplus/deficit -v- real total returns from shares - post 1946




There has been a mildly *negative* correlation between the government balance and stock market returns. Most of the high return years from shares were government deficit years (top left section), including 2011 and 2013.

Deficits are generally good for shareholders and surpluses are generally bad for shareholders. In the post-war era the median real total return from shares was 10.8% pa in the deficit years but only 2.4% pa in the surplus years, which is a very significant difference, as shown in Chart 6.

**Chart 6**: Real returns from shares -v- government surplus/deficit




There are two main reasons for this. The first is that deficits come about by governments spending more money (and/or taxing less), and much of the additional cash ends up in company coffers, either directly via contracting to government, or indirectly via household spending. The second is timing. Deficits tend to be high in mid-late recessions (when tax revenues are down and welfare spending is up), and this is when shares generally do best, rebounding out of the middle of recessions. This was the case in 1954, 1972, 1983, 1992 and 2010, (and in the pre-war years: 1922, 1923 and 1932).

There have been very few years when government surpluses accompanied poor returns from shares (bottom right section in Chart 5). The most obvious instance was 2008, when tax revenues from the boom were still rolling in but shares were already falling in the GFC. However the differences are not as significant as the stark differences in returns in deficit years versus surplus years.

**Some conclusions**

This paper adds some factual context to the current highly-charged debate, and we can draw some conclusions:

- government deficit years have generally been good years for stock market returns. 2013-4 will be a deficit year, as was 2012-3
- years of fiscal tightening have been a little better for stockmarket returns than years of fiscal loosening. 2013-4 will probably be a year of fiscal tightening, as was 2012-3
- in the post-war era, Labor has produced four surplus years against the Liberal's eleven
- today's level of government debt is much lower than it was in the two World Wars and in the 1930s depression
- the current interest burden (at less than 1% of GDP and around 3-4% of tax receipts) is no higher now than it was in the 1950s, 1960s and 1970s
- the pre-WW1 period was a golden era of balanced budgets and no Canberra!

*Ashley Owen is Joint Chief Executive Officer of Philo Capital Advisers and a director of Third Link Investment Managers.*

# Leadership lessons from Sir Alex Ferguson

## Graham Hand

Manchester United chose me. I was born near Manchester and I have no recollection of selecting the team I would follow all my life. Nick Hornby says in the best-selling book, *Fever Pitch*,

*"I fell in love with football suddenly, inexplicably, uncritically, giving no thought to the pain or disruption it would bring with it."*

There was plenty of 'pain and disruption' in the early days when United went 26 years without winning the league, including relegation to the old Division 2. Sir Alex Ferguson took over as Manager in 1986, and his lack of league success until 1993 would probably not be tolerated today. He described 1989 as "the darkest period (he had) ever suffered in the game", as United were nearly relegated again. Fans and press were calling for his head.

Yet now, he retires as the greatest sports manager ever, leading United to 13 Premier League titles and two UEFA Champions League wins among 38 trophies. His reign feels like one long, glorious party. What it also shows is incredible resilience in the face of adversity, and a single-minded determination to follow a course and rebuild the club in spite of almost universal criticism. A leadership lesson in believing in yourself.

**Meeting Sir Alex**

On 27 October 2007, I was in the 'VIP' area at the back of one of the stands at Old Trafford, home of Manchester United, talking to a local businessman. The only reason I had access to the area was I had been doing some business with Mark Ferguson, eldest son of Sir Alex and Chief Investment Officer at Generation Investment Management. Mark told me to introduce myself to a lady, Lyn, who had been with Sir Alex for decades and had known Mark since he was a lad running around the training grounds. When I picked up my match ticket from Lyn, she told me to come to the VIP area after the game.

It was not really Very Important, as we were buying our own food and drinks, but it was a good atmosphere as everyone was a United fan and we had won 4-1 a few minutes earlier. The businessman told me Sir Alex rarely came into the room, but the owners of the club, the Glazer brothers, dropped in for a quick chat. I asked one how they separate business from football, and he said they leave all the football decisions to Sir Alex.

Then came one of those moments where you take a risk, and you're glad you did forever. I looked up and through a glass door and down a long corridor, and I caught a glimpse of Sir Alex as he turned into another room. I decided I had one shot at this, so I headed for the room he had just entered. Then I had a massive slice of luck. Lyn was 'guarding' the door, and she immediately recognised me. Without hesitating, she smiled and grabbed me by the hand, pulled me through a small group of people, and almost pushed me to stand right next to Sir Alex.

"Alex, this is Graham, he's a friend of Mark's, come from Australia."

Well, shoot me down with a feather. I've died and gone to heaven. I had not even thought about what I might say. Here I am, shaking his hand and chatting, and he's nothing like the terrifying ogre depicted in the media, the man known as 'The Hairdryer' due to the outrage sometimes inflicted on his players. He had a massive grin on his face, looked very happy, and he called the waiter over to give me a drink. We talked for only a minute or two about football in Australia, when I was intercepted by someone I recognised, an old United player, Paddy Crerand.

The room was actually Sir Alex's personal 'den' at Old Trafford – a small space with no windows, capable of holding only about a dozen people in comfort, with the walls covered in photographs of many of United's great victories.

Then something amazing happened. People started to leave, and I decided I would stay until someone chucked me out. There were only four or five of us left, and Sir Alex came up to me, put his arm around my shoulder, and told me to sit down. The waiter gave me another drink. And there I stayed having drinks with a few Scottish guys talking about the days in Glasgow, conversations full of politically incorrect references and loud laughter, strong accents where I could barely catch the story, and lots of bawdy jokes.

I chatted with Vince, an old friend of Sir Alex who had been with him since the Aberdeen days, and asked if it were true that Alex would have been sacked if United had not won the FA Cup in 1990, his first trophy after four years in charge. He said that Alex had enormous support at the United Board level, and he believes the Manager would have kept his job. So much for that myth.

I was wearing my United shirt, and at one stage, Alex grabbed a felt-tip pen and scrawled his signature across my chest. That shirt now hangs on my wall. He reached for a couple of matchday programmes and gave me more precious autographs. The waiter topped up the red wine. Paddy Crerand told a long joke which I could not fathom but we all laughed like drunken sailors.

It all went by in a flash. I had to concentrate on being in the moment. It was one of those instances where you're almost outside your own body, watching yourself and wondering if it were really happening. Lyn came in and took photographs, Alex putting his arm around me like we were old friends. By the time I walked away, into the cold Manchester evening air as if in a dream, I had been there for over two hours.

**What other leadership lessons can we learn?**

Several things stay with me, and combined with watching Sir Alex for a quarter of a century, they give insights into this great success.

- Loyalty and support. Even when Sir Alex ended a player's career, they left with the greatest respect for him. In his 1999 autobiography, *Managing My Life*, he says, " … loyalty is something I regard as one of the most precious human qualities … the inclination to stick by friends and allies was bred into me and strengthened by my working-class upbringing in Scotland."

- Stay grounded. When I saw Sir Alex at Old Trafford, it was about half an hour after the game had finished. He must have seen the players and fulfilled his media obligations, and come straight up to chat with his mates. These people had been his friends for decades. And he always made decisions for the good of the team, not himself.

- Take control. Watch any United game and there's no doubt who's in charge. Alex Ferguson never tolerated any player becoming bigger than the team, and even when stars like David Beckham and Ruud van Nistelrooy were still at the top of their game, he moved them on when their attitude was not right. Alex never lost control of the dressing room, in the same way a corporate CEO cannot lose control of his executives.

- Regenerate the team. Ferguson rebuilt United many times, often at great expense but also by fostering youth. He knew a diversity of skills was required. The United Youth team of 1992 contained the baby-faced images of David Beckham, Gary Neville, Paul Scholes and Nicky Butt, all future England internationals who were part of the mighty treble-winning team of 1999.

- Board support and stability. Incoming Manager David Moyes has just signed a six year contract, Alex went seven years without a league win. There are many trustees who could learn

from this, that you don't sack a fund manager after one poor year if you've followed a rigorous selection process.

- Relax and switch off. Manchester United games are watched by 500 million people. It is one of the world's leading brands, in every corner of the planet. Everyone wants a piece of Sir Alex. Yet half an hour after the game, he was having a friendly beer with his lifelong mates as if he did not have a care in the world.

- Delegate. No doubt after any game, there are hundreds of things to do. For example, United players often play midweek, including for their countries, and attention to injuries and the recovery process is now highly scientific. But Alex has a team that looks after all that, and he does not need to micromanage everything.

- Resilience and discipline. Even at the age of 71 and after 26 years in charge, Sir Alex was one of the first at the Old Trafford ground at 7.00 each morning. He was very strict with his players. In his autobiography, he says, "A footballer who does not distance himself from the drinking and the late hours is asking for trouble."

- Decisiveness. Sir Alex once said he believes he gets seven out of ten decisions correct, and this is enough to win most games. It allows him to trust his instincts and be decisive without worrying about making mistakes, which is why he always looks in control as circumstances change throughout a game and season.

Somewhere out there is a 26-year-old Manchester United fan who has never known another Manager of his team. Let's hope he is not about to learn the 'pain and disruption' of following a team in the post Alex Ferguson years. There's no doubt the fans of every other Premier League club just heaved a sigh of relief.

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