

Diversification and concentration

In popular presses and textbooks, it is often stated that small investors benefit from diversification. It reduces the risk of investment. However, successful investors generally have concentrated holdings. Whenever possible, Warren Buffett prefers one hundred percent control over fractional holding. Once, Berkshire Hathaway, the investment company controlled by Warren Buffett, owns about 1% P&G shares. In 2014, Buffett swapped these P&G shares with Duracell, a battery company wholly owned by P&G at that time. Warren Buffett bought one hundred percent ownership and privatized many companies that were once publicly traded.

In general, diversification reduces the power of small investors. As a result, power concentrates with the top managers, who reward themselves with hundreds of millions of compensation packages. Company insiders also issue additional stocks or options to dilute the ownership of small investors. In other words, diversification benefits top managers and harms ordinary people, who are forced into stock markets due to mandatory pension deductions and taxes.

Mandatory pension deductions and other taxes rob the opportunity of ordinary people the benefit of concentration. Without pension deductions and other taxes, many people can use the concentrated funds to launch their own businesses, instead of watching top managers of large businesses rip off our funds. Without pension deductions and other taxes, many people can use the concentrated funds to invest in really important venues, such as raising one or two more kids. The societies with heavy pension deductions and other taxes all suffer from low fertility rates.

It is the concentrated effort, not the mindless diversification, that gets us anywhere. Indeed, the very purpose of stock market is to concentrate funds for worthwhile businesses. However, with mandatory pension deductions and other taxes, only small number of companies and their insiders enjoy the benefits of concentrated funds, while the majority of ordinary people pay the costs and suffer the loss of power from diversification. It is no wonder the increase of mandatory pension deductions is accompanied by the increase of inequality.

Ordinary people are aware of the trap of diversification. Even with the incentive of tax exemption, only five percent of the RRSP allowance has been used. However, with the relentless increase of mandatory deductions, our resources are being further diversified and diluted.

The relation between diversification and concentration applies not only to the stock market. For four year's college education, we want to get a single degree. We don't want to randomly diversify into unrelated courses, without getting a degree in the end. However, in educational system, ordinary students suffer from diversified education. Students have to sit through mandatory courses that promote the interests of the powerful people. The students and their parents cannot concentrate on programs that actually benefit themselves.

The ability to concentrate is always an important measure for intelligence and character. Concentration cannot guarantee success. However, mindless diversification can guarantee failure. Only with concentration, we can learn to choose and to master something really important to our life.