

Understanding the Role of Luck in Our Lives

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The video for “Gangnam Style,” a song by the South Korean rapper PSY, surpassed one billion views on YouTube just months after its release. The tune has a catchy beat and PSY breaks out some imitable dance moves, but it’s not clear why this particular song went viral. One pundit attributed the song’s success to its humor and shock value, which makes people want to tell others about it. But that only leaves us wondering why all artists wouldn’t include those elements in their bids to create a hit.

There’s another, more accurate explanation for the success of “Gangnam Style”: luck. Sure, really bad songs rarely top the charts, and not all of the most popular songs are the best ones. The fact is, if you rewound the tape of the universe and played it again, a different set of songs would take off. Although quality songs have a better chance of success, you can’t anticipate which ones will be hits. And for the products that succeed, the spoils are immense. These are winner-take-most, or winner-take-all, markets.

This phenomenon also applies to art, books and movies. The Mona Lisa, Harry Potter and Star Wars? Luck, luck and more luck. These products are all very good but enjoyed success wildly out of proportion with any objective measure of quality. Scientists who study how hits happen tell us that the social processes that catapult products to the top are inherently unpredictable and create massive inequality.

Most people have a difficult time accepting that super-successful products are not special. The reason is that your mind is expert at creating stories to explain results after the fact. Indeed, there’s a module in the left hemisphere of your brain that’s so good at post-hoc answers that neuroscientists call it “the interpreter.” The interpreter doesn’t care about the process that led to the result, it just seeks to close the loop between cause and effect. You see an effect, come up with a plausible cause and all’s good. Here’s the key: the interpreter is really bad at knowing how much of the result is caused by skill and how much is from luck. But in order to make good decisions, you have to know the difference.

Imagine a continuum where on one end only luck determines results - think lotteries and roulette wheels — and on the other end skill dominates — say, a chess match or a running race. Most of life’s most interesting activities are in the middle of these extremes, and knowing where an activity lies can provide you with insight into how to predict what will happen next.

Skill or Luck? Three Questions to Ask

There are some analytical approaches to placing activities on the continuum, but answering three questions provides a good start. The first question: Can you readily assign a cause to the effect you see?” If pointing to the cause is easy, you’re on the skill side. If it’s challenging, you’re on the luck side. Anticipating what happens next is easier when skill dominates because luck is not there to break the cause-and-effect loop.

The next question: What is the rate of reversion to the mean? Reversion to the mean occurs when an outcome that is extreme is followed by one that is closer to the average. Take six people at random and ask them to run a race of the same distance at two different times. Chances are good that the same person will win — skill dominates. But if you buy last year’s hot mutual fund, this year’s results are more likely to be closer to the average than another sizzling gain.

The final question: Can anyone predict well? In some fields, prediction is very accurate. Man can do the necessary calculations to land a rover on Mars and luck has little to do with it. But in other fields, prediction is notoriously difficult, including almost anything having to do with social or economic outcomes. While there is no shortage of commentators on television telling us where the stock market is headed, experience tells us that their crystal balls are just as cloudy as everyone else’s.

Coping With Luck

Here are some tactics that you can use to cope with a world that combines skill and luck. To start, get into the habit of considering what you would expect to happen by luck. Take a professional baseball player who hits for a

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.300 average during a whole season. He'll have stretches when he's hot, posting a scorching batting average and stretches when he can't seem to buy a hit. How different is the player's record than a model of a simple spinner that lands on "hit" 30 percent of the time and "out" the other 70 percent? The answer is the spinner model does a credible job of representing a real player's ups and downs. So, recognizing the role of luck can prevent you from overreacting to short-term highs and lows.

Another tactic is to determine when you need to focus on process. When you're near the all-skill side of the continuum, results very accurately reflect skill. Practice the piano properly and diligently, and the music you produce will sound better. But near the luck side, results are not always indicative of skill because of randomness. You can play your hand at the blackjack table just as basic strategy dictates and still lose. The lesson is to focus on process, not outcome, when a good dose of luck is involved. A good process provides the highest probability of a quality outcome over time.

Finally, you can use the process of reversion to the mean to your advantage. When dealing with an activity that has a lot of luck, recognize that extreme outcomes — either good or bad — are likely to be followed by outcomes closer to the average. So, avoid betting on recent success and betting against recent disappointment. Whether you're placing bets on a hot player in your rotisserie baseball league or a hot fund in your investment portfolio, recognize that good luck is unlikely to persist.