FEBRUARY 2018

Organizational Design and Long-Term Investing

by David Iverson and Geoff Warren

This abstract provides an overview of a Brandes Institute white paper on how certain aspects in the design of investment organizations can support the successful pursuit of long-term investing.

Executive Summary

Organizational design relates to the structures and procedures under which an organization operates. It is a critical element for focusing investment decisions toward long-term objectives. We identify and discuss four organizational "success drivers" for long-term investing: investment beliefs, governance, aligned interests and people. These drivers are used to evaluate how various institutional investor types are positioned to be successful long-term investors. We conclude that family offices and endowments and foundations may generally be better positioned than sovereign wealth funds and pension funds.

Overview

A previous Brandes Institute paper considered what it means to be a long-term investor (Warren, 2016). It was argued that long-term investors are best characterized by their *latitude* and their *intent* to pursue long-term goals. Important for latitude is a capacity for patience, supported by discretion to decide when to buy, when to sell, or if to continue holding where necessary. Intent reveals itself in both the objectives pursued, and how investment decisions are made. It was also suggested that long-term investing might be seen as a matter of attitude and perspective—even a mindset. In sum, long-term investors have the capacity to look through the short-term noise and pressures to deliver immediate performance and retain a focus on the long term.

Investment beliefs, governance, aligned interests and people are four "success drivers" for long-term investing.

Given that investing is often undertaken by institutional investors on behalf of their end-investors or "beneficiaries," the following question arises: *What are the characteristics or attributes that are required to enable an investment organization to successfully pursue long-term investment opportunities?*

We identify and discuss four "success drivers" for long-term investing.

Investment beliefs: these should be framed around how long-term investing provides access to attractive opportunities that the organization is well positioned to capture.

Governance: the factors for good governance include board structure, mission clarity and the separation of responsibility for governance and management.

Aligned interests: the key question is whether decision-making aligns with the long-term perspective.

People: among the vital aspects related to people are compensation, temperament, tenure, culture, the ability to take non-consensus positions and leadership.

These drivers might be seen as overlapping and self-reinforcing areas to consider when addressing whether an organization has positioned itself to be a successful long-term investor. They are discussed in the context of multilayered investment organizations, where investment decisions are often handed down along a "chain of delegations." The litmus test of whether the organization is configured properly is that those ultimately responsible for making investment decisions feel they are given the latitude to pursue long-term opportunities and are operating with the full intent of doing so.

We believe investment organizations that can effectively address the four drivers will greatly improve the chances of delivering success over the long term for their beneficiaries. Genuine long-term investors are able to pursue a wider range of investment strategies, including some that are challenging for investors with shorter horizons. Important examples are the ability to take contrarian positions in mispriced markets and providing liquidity when it is in short supply, even though the timing of the payoff may be quite uncertain. Addressing the four drivers should improve the capacity for coherent decision-making, and to remain focused on the destination. It can help avoid being seduced into counterproductive actions such as getting caught up in the euphoria of overheated markets, responding to information that is irrelevant for long-term fundamentals, and trading out at the wrong time in response to pressure to limit the pain of losses.

After having discussed the nature of the four success drivers, we use them to assess four institutional types with a long-term purpose, and how well they are set up to be successful long-term investors. We conclude that family offices and endowments and foundations are likely to be best positioned, followed by sovereign wealth funds, with pensions funds ranked lowest. However, this reflects the broad attributes of each type, and there is likely to be considerable variation within each group. These findings are summarized in the following table.

Four Investor Types and the Success Factors

Success Factors	Family Offices	Endowments and Foundations	Sovereign Wealth Funds	Pension Funds
Investment Beliefs	• •	• • •	• •	• •
Governance	• •	• • •	•	•
Aligned Interests	• • •	• •	• •	•
People	• • •	• • •	•	•

Key: • Low score • • Medium score • • • Higher score

Addressing the four drivers outlined should help an organization deliver over the long run, and make it a more effective investor in general. While the discussion in this paper offers some suggestions for addressing the four success drivers, a third paper is currently in train that will provide some practical ideas that should assist investment organizations to become better long-term investors.

About the Authors

David Iverson is Head of Asset Allocation with the Guardians of New Zealand Superannuation Fund and a member of the Brandes Institute Advisory Board. **Dr. Geoff Warren** is an Associate Professor at the Australian National University, where he is Convenor of the Student Managed Fund and a Director of External Research Engagement. He is also a member of the Brandes Institute Advisory Board.

THE BRANDES INSTITUTE

The Brandes Institute
11988 El Camino Real
Suite 600
P.O. Box 919048
San Diego, CA
92191-9048
858.755.0239
800.237.7119

Get the Latest Research and Ideas: