THE PRACTICAL GUIDE TO INVESTMENT MANAGEMENT BUSINESS PLANNING – PART II

"Strategy on the Run - Without Formal Planning"

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Executive Summary

- Many investment management firms are concerned that the time and expense of strategic planning offers very little in return.
- Leaders are unlikely to find information to help their firms from industry data or established industry trends.
- Focus instead on matching the firm's capabilities with current market demand.

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Introduction to Part II

- Does your firm need to sell more effectively?
- Is your firm mainly focused on investing and not business management?
- Does the leadership of the firm already know the best business strategy?
- Are you satisfied with the business, but would like to build up some areas of current weakness?
- Are you trying to keep up with rapid growth?
- Are there too many opportunities?

A positive answer to any one of these questions suggests that a formal strategic planning process would likely not be productive. This guide is intended to help firms who are wary of the costs and skeptical of the benefits, of preparing a formal strategic plan. You know who you are.

Yes, many investment management businesses do prosper without putting a plan on paper. But every leader seeks insights that can supplement their efforts, and ensure the sustainable success of the firm.

Part I of this guide (www.yoursecondopinionllc.com/writings.html) presented a robust approach to creating a formal strategic plan. Many of the suggestions in this Part II guide will also be helpful to firms pursuing ore formal planning efforts.

1. Forget Strategic Planning

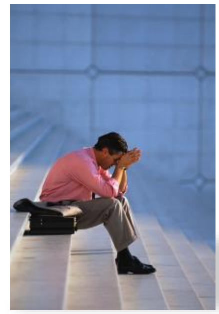
Some people feel that strategic planning is the equivalent of going to the dentist.

How A Visit to the Dentist = Strategic Planning

Dentist Visit	Strategic Planning
We've all had bad experiences	We've all had bad experiences
It takes time	It takes time
It can be painful	It can be painful
Who sees the results?	Who sees the results?

Many investment management firms are skeptical of the benefits of strategic planning for good reasons;

- There may be only a few shareholders who share similar objectives; no need to waste time on planning.
- Planning may raise concerns about placing too much emphasis on the business and not enough time on adhering to professional standards such as autonomy and fiduciary duty.
- Significant shifts in strategic direction could undermine the culture of the firm.
- The firm's passion is often investing, not business management.
- Investment passion may drive product choices, not client demand.
- There may be a concentrated and satisfied client list – why change?
- Profitability may be sufficient to meet the needs of the owners.

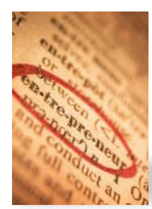


2. Business Pressures and the Exit Option

Many investment management firms feel that they are at a crossroads. Profits may be declining, sales may be lacklustre, and there may be worries about the sustainability of the firm. External forces are ratcheting up the pressure.

- Clients are choosing passive products over active strategies. Even if they select an active approach, they are insisting on fee concessions from active managers.
- Clients and intermediaries are demanding more robust operations and risk management.
- Regulators are ratcheting the stakes higher for compliance efforts with their talk about "tone at the top", and "culture of compliance".

Some firms choose to respond to these pressures by exiting the business of managing client money. Talented portfolio managers have choices, and one choice is to manage private money far from the oversight, inquiries and complaints of clients, regulators or the general public. Portfolio managers who exit client work enjoy earning 100% of the return, rather than a portion of the returns in the form of fees, and they embrace their independence and investment flexibility. The abandonment of client work is a tremendous loss of talent to the industry and clients.



3. Readiness to Step – Up

Fortunately, few firms pursue the exit option. Most firms want to remain conventionally successful by continuing to work with clients. But everyone in the firm has to be engaged in the effort to respond to the challenges of managing client money today. Here are 10 critical questions that can help to assess the current level of internal engagement, and willingness to consider changes to better meet client needs;

1. Are most stakeholders, such as employees, major clients, and owners, satisfied with leaving the firm as it is?
2. Is there an internal consensus about the acceptable balance between meeting professional standards, and seeking growth and profitability of the business?
3. Do most stakeholders agree on the direction of the firm?
4. Are there major elements out of your control (e.g. poor investment performance, reputational issues) that limit the ability of the firm to control its destiny? If your hands are tied, planning should be set aside in favor of rebuilding.
5. Do stakeholders disagree on the facts about the business – for example, what is doing well, and what isn't? Excuses, pet projects and strongly – held but unsupported fantasies may undermine any willingness to move in a new direction.
6. Is there a willingness to acknowledge, and address, the weaknesses of the firm?
7. Are stakeholders willing to think ahead?
8. Are stakeholders willing to reallocate resources if needed to support a chosen direction? This may mean that parts of the firm will have to give up resources.
9. Do your stakeholders have a history of taking action?
10. Are stakeholders willing to balance patience, with urgency?

4. Raise the Stakes

Even if a firm is ready to consider making changes, there must be a strong enough drive to work through changes and achieve success.

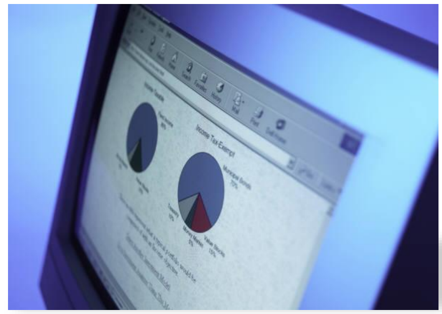
- What are the biggest challenges that your firm faces?
- What must happen to address these challenges?
- What could you be doing better?
- What are the big opportunities?
- What have you tried already to address the challenges; capture the opportunities?
- Why did you choose that approach/approaches?
- Why do you suppose that didn't work (yet)?
- What caused other alternative approaches to be ruled out?
- What lessons came out of the experience?
- How much did it cost – in time, money, emotionally?
- What has been most troubling to you personally?
- How did it make you feel?
- How does an inability to address challenges and capture opportunities affect other stakeholders?
- What is the ideal outcome you'd like to experience?
- Over what time period?
- What other results are you trying to accomplish?
- How will your service, or client be better off?
- Why are you seeking to do this?
- How would the firm be different as a result of this work?
- What would be the return on investment (sales, assets, equity, etc.)?
- How would image/reputation/credibility be improved?
- What harm (stress, dysfunction, turf wars, etc.) would be alleviated?
- How much would you gain on the competition as a result?
- How much further ahead would you be if this effort was successful?
- How would your value proposition be improved?

5. Success Without Planning

There is no reason why enhancing the business has to depend in formal strategic planning. And we can do much more than just improve operational efficiencies.

There are some who separate strategic planning and operational efficiency. It is often expressed in the cliché "Doing the right things versus doing things right". But we can and should seek to do both.

When trying to improve a business, many leaders look for insights from third party data and observe trends to help them to decide which way to go. But focusing on data and trends has severe limitations.



6. Forget Industry Data

In our efforts to improve our business, we often rely on data gathered by third parties to inform our decisions. Gathering data about competitors, clients, products, channels and geographic regions may be useful. But there are reasons to be cautious:

- Be skeptical of benchmarking surveys. It is unlikely that there are firms identical to yours, and this makes it difficult to extrapolate survey results to your organization.
- The data is often unreliable. Every firm gathers different data, and categorizes it differently. They then have to translate what they have readily available into the format of the surveying company. Rarely is there a close fit between company data and the survey questions.
- Even if there are comparable firms, and the data is “accurate”, we do not compete against benchmarks or medians in this business. Being above average in a highly competitive business just doesn't come close to being good enough. Since most clients typically only consider a few firms for an investment mandate, you must rank amongst the best in order to have an opportunity to win clients.
- The surveys are static, and often out of date, and fail to recognize how firms are transforming through time.
- It is tempting to want to immediately address specific issues identified from surveys. The data often strongly supports a particular direction. However, the suggestions tend to be generic, and the advice is available to anyone willing to pay for the research. This dilutes the possibility that you are gaining a significant or sustainable advantage.

7. Forget Trends

Observing reported trends is another favorite approach to strategy. If you listen to management consultants or the media, you might be swayed to believe in trend following. There are three important reasons for most investment management firms to be wary of trend following.

First, only the trends that are most observable and well - established are usually reported. Typically these trends are pursued by the largest firms, and the trends will be of most relevance to them as well. For example, passive ETFs are a hot trend. This is of relevance to a small number of firms, perhaps 5 or 10. Realistically, if you are not amongst the ETF market leaders today, it's going to be an uphill climb to compete directly against trillion dollar asset managers.

Second, trends are usually projected forward in a straight line from today to the future. None of the management consulting firms that project trends in the investment management industry anticipated the Great Recession, nor the subsequent shifts in client needs and desires that have occurred since 2008.

Third, there are few analyses available of the accuracy of the forecasts that have been made in the past. If you are looking for proof of the accuracy of prior forecasts, it doesn't exist.

For the 99.9% of firms that aren't currently positioned in the trending product categories, who live in the real world of discontinuity and change and who prefer proof of forecasting skill, there must be a better way to prepare for the future.

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8. Prepare for the Future

Instead of relying on foggy data and uncertain trends to steer your business, try focusing on the few essential ingredients that determine sustainable success.

An analogy could be no-bake cookies. You don't have to worry about the risk of burning the cookies, and yet these treats taste great. Just mix the ingredients and you're done.

Similarly, the investment management business has some essential ingredients. The risk is small that they'll change very much. I call this focus on ingredients, "The *SIMPLE* Model".

9. The *SIMPLE* Model

Staff

- Anticipate and prepare for key staff turnover.
- *Leading teams is a core leadership skill.* But a portfolio management team may respond very differently to a leader than would other kinds of teams. Leaders may have to adjust their approach. A team with one Einstein and a supporting cast, for example, may require the leader to adjust their management style to be effective.
- *Simply adding more portfolio management and sales talent to a firm is an excellent way to add economic value to the firm.* Sometimes we lose sight of the fundamental role of talented people in our rush to produce and distribute product, and then we are surprised when results don't meet expectations.
- *Poor investment performance is always a people issue.* We need to have organizations that attract, appreciate, support, reward, and celebrate exceptional portfolio management talent.
- Only hire staff who will enhance your best performers.
- Changing a culture usually requires replacing people.

Investment Process & Products

- *Continuously improve investment processes* to stay ahead of the competition, structural market changes, and long-term client needs.
- *Consider adding investment capabilities* with additional new hires.

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- Clients and their advisers are focused on classifying almost all investment return as beta. *Your products need to prove that they will deliver alpha.*
- *Many investment products fall short of client expectations*. Many trendy investment strategies carry unanticipated risks, and are likely to have more modest than expected returns. New product development deserves more rigorous consideration of risks to the reputation of the firm.
- Clients expect you to *control portfolio risk*.

Marketing

- Continuously *search for new distribution channels*.
- Consider *piggybacking on some of the new product ideas of other firms* that have been historically successful with launching new products.
- *Product niches are bigger than you expect*.
- Clients are more alike than different. *Clients share similar needs* everywhere.
- *You too can have a global brand*. Local brands can transcend borders via networking, referrals, intermediaries, local support and media.
- *Solutions (aka bundling) are expensive for clients*. Solutions come and go, but products remain. Solutions will be reverse-engineered by clients and intermediaries. But there will always be a need for top notch product providers.
- *Lousy client service continues to be widespread*. Few firms understand what client service means from a client's perspective. Everyone talks about service but few deliver in ways that are acceptable and appreciated.
- *What attracted your current clients* to your firm? Find prospects who share these characteristics.
- Retain salespeople who continue to exhibit the *attitude and behaviors* required to be successful.

Planning

- Scan the environment, and seek opportunities to *shape, and not just respond to trends* that fit with your firm's unique skills.

- Global liquid wealth is still growing. There will be *continuing global demand for accumulation products*. Not everyone in the world is retiring (at least not all at the same time).
- *Scale businesses only benefit a few firms*. Index funds, ETFs, core fixed income are examples of businesses that will inevitably be driven towards zero marginal economic profit.
- *Do it yourself*. Joint ventures and partnering of front office activities are temporary – odds are very good that the relationship will fall apart. The early benefits usually disappear, and partnering limits the ability of the firm to build their brand.
- In a private company, start building the capabilities today to remain successful after your firm's current owners retire. Ensure that the firm has *transferable economic value* to the next generation, or to another buyer.
- Reallocate *resources to the best future opportunities* that are unique to your firm, don't just cut costs. Consider investing some of your available resources in ideas that are contrary to current industry trends and forecasts.

Legal & Compliance

- Be sensitive to any indication that your clients are not completely certain that you *act in their best interest*.
- *Actively anticipate future regulatory compliance requirements*.

Execution

- As a general rule, most asset management businesses should *keep fixed costs low* in their business model.
- *Technology is too important to be led by the IT department*. Invest in technology to create more economic value for your firm.

10. Accelerate Sales Now

One of the most pressing concerns for many firms is the need to accelerate growth in revenues. Here are ten steps to boost sales of your investment products in the short run.

1. Make it clear to everyone in your firm directly that the current sales slump is unacceptable. Facing reality may be uncomfortable, but making people a little anxious inspires productivity and creativity, according to research.
2. Set a sales goal that has a 50/50 chance of being achieved. This strikes the right balance between a goal being too easy and yet, not too ambitious.
3. Your employees will do what they want to do. What they want to do will be based on avoiding pain and gaining pleasure. Adjust the sources of pain/pleasure to make it easier for them to get on-board with your sales goals.
4. The skeptics in your firm will doubt that your goals can be achieved. Consider ways to turn their mood from pessimism towards optimism.
5. What did you used to do that was successful in driving sales in the past? Many firms have forgotten how they achieved good results in the past.
6. What are prospects/intermediaries telling or yelling at you to do? Have you been ignoring or rationalizing away their requests?
7. What capabilities (investment, marketing) do you have, or can you acquire easily, that will resonate with prospective clients?
8. Allocate most of your firm's resources to funding the best opportunities.
9. What behaviors have to change (even if attitudes don't)? You don't need to change who they are - just what they do.
10. Celebrate small wins to build momentum.

11. Profession and Business Together

One key reason for skepticism about planning is the worry that it will undermine the firm's professional obligations because of an excessive focus on business management. It is possible to reconcile the two, and Warren Buffett is a great example of someone who has successfully combined them.

By any measure, Warren Buffett is one of the best investors of the last century. According to the 2012 Berkshire Hathaway annual report, the book value of the company's shares has increased by nearly 20% per year over the last 48 years. Warren is first and foremost, an investment professional.

He is a storyteller and he tells an investment story about the one that got away. In 2010 on CNBC for example, Warren Buffett said that buying out Berkshire Hathaway, instead of investing directly in insurance businesses, was the biggest investment mistake he has ever made. He estimated that the lost opportunity had cost him about $200 billion over the past 45 years!

This story is a reminder that we are dealing with a passionate investor. An investment business often begins with idiosyncratic talent like this.

Warren's investment skills have continued to evolve over time. In fact, his evolution as an investor is a direct challenge to conventional industry thinking that an investment style is more likely to contribute to better investment performance only if the style remains stable. He once focused on smaller companies, had a rigorous pricing discipline and practiced a more traditional value-oriented approach. But changing market conditions, hard won experience, and the need to invest increasingly large pools of capital have altered his approach.

Investment wins and losses are not the whole story though. Berkshire Hathaway would certainly not have achieved the success it has without Warren's ownership and expertise. But Berkshire Hathaway is also a public company with broader issues than simply being an investment vehicle.

His investment performance has been leveraged effectively into developing a successful business. This has helped to make him one of the most influential people in the world in 2012, according to Time magazine.

Berkshire Hathaway in turn, is one of the most admired companies according to Fortune magazine.

Berkshire Hathaway may be led by strong investment performance, but considerable attention has been paid to creating a sustainable organization. It is possible to create a successful and sustainable business built on the foundation of professional standards.

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Authors Bio

Russell Campbell is the CEO of Your Second Opinion, LLC, a management consulting firm offering expert advice to leaders of investment management firms. He writes a weekly subscription newsletter for leaders, and also works one-on-one and with leadership teams on critical issues.

Russell has led 5 investment groups in his career. Prior to establishing his own firm, Russell was the CEO of The Marco Consulting Group, one of the largest institutional investment consulting firms, with a significant CIO outsourcing business. Previously, he was the EVP of AMCORE Bank, and led the Wealth Management Group which was one of the 60 largest bank wealth managers in the U.S.. Russell was the President and CEO of ABN AMRO Asset Management Holdings, Inc., which managed $75 billion in assets, and was the U.S. investment management affiliate of ABN AMRO Bank. Russell was promoted to this position after having been the CEO of ABN AMRO Asset Management Canada, Inc. He was previously a Vice – President and Partner of Beutel Goodman, Inc., one of Canada's largest investment counseling firms. His first leadership position was as Vice – President, Bank of Nova Scotia, where he led the investment management of the Bank's own pension fund, and a family office portfolio.

Earlier in his career, he worked as a pension investment consultant, in institutional equity sales and managed a portfolio of precious metals.

Russell has an MBA in Investment Finance and Marketing from York University, and he has a BA in Industrial Relations from McGill University. He also attended the Advanced Management Program at INSEAD in France.

He has earned the Chartered Financial Analyst designation, and has attended both the Financial Analyst's Seminar and the Investment Management Workshop. Russell has also acquired the Certified Financial Planner ™ certification. He previously held Series 7 and 24.

Russell has been a director of several for-profit and not for profit boards, and he is a member of numerous non-profit, civic and industry organizations.

He is quoted frequently in the media and has been a speaker at many industry conferences.

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