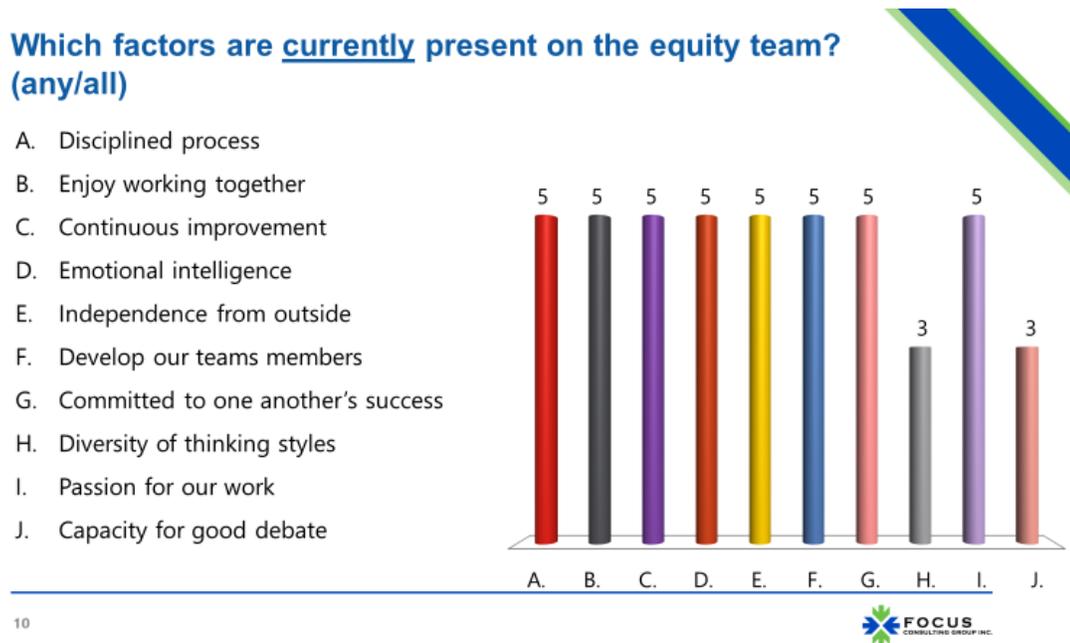


June 26, 2017

LOL: Top Performing Equity Teams in Practice

In another installment of the “Blind Squirrel sagas,”¹ we’re pleased to say that the squirrel team found another acorn. My fellow squirrel Michael Falk and I wrote a white paper last Fall called “Top Performing Equity Teams: The Common Factors.” (available on our website; [click here](#) to read.) In that paper, we presented our findings about the common factors that were identified by ten top equity teams. There were five “hard” factors, like disciplined process, and five “soft” factors, like emotional intelligence (EQ) that contributed to the success of the ten firms.

Recently, an excellent equity boutique firm invited FCG to discuss the paper at their annual offsite. By “excellent” I mean strong alpha production since inception (10/1/2008)² vs. the relevant benchmark. (Like many good alpha shops, this one likes to stay “under the radar” and asked NOT to be named.) The first day of the offsite involved meeting with the five-person investment team. Shortly after we started the session, I put up a voting slide showing the top ten factors that were identified as common to the top firms. I asked the participants to vote on whether or not they thought their firm excelled in these areas. (The vote was a simple “toggle” for yes or no.) The results were as follows:

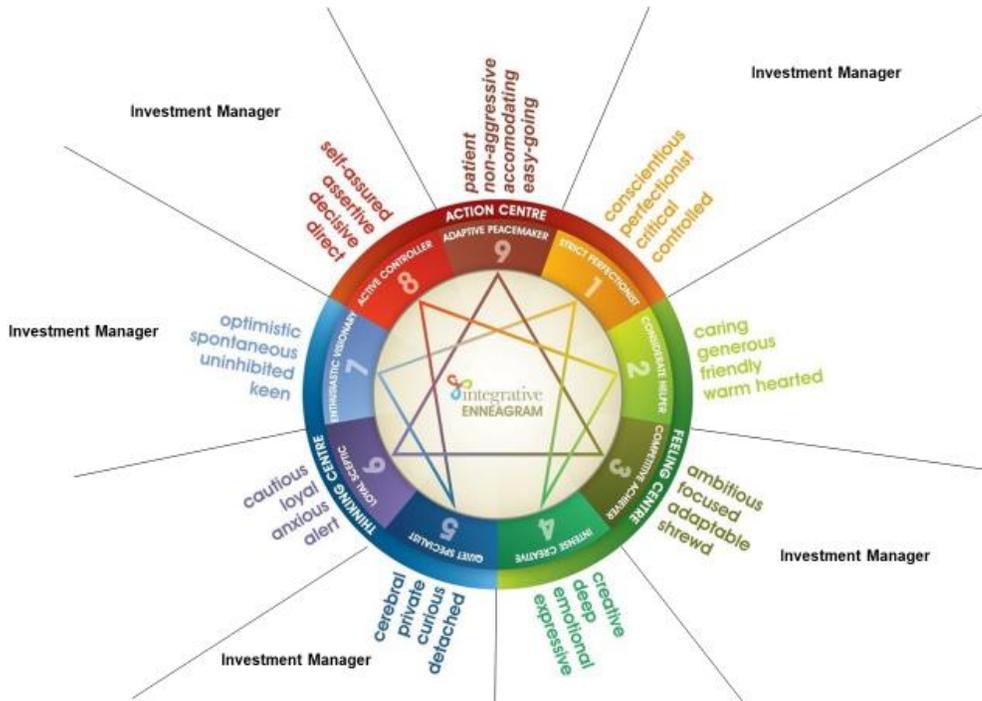


I was surprised by the strength of the results. Eight of the ten factors showed a resounding “yes, we are good at this factor.” In retrospect, it probably shouldn’t have surprised me, as I knew going in that this boutique had a strong track record for alpha. In only two areas did the team acknowledge possible weakness: diversity of thinking styles and capacity for good debate.

¹ Have to confess, I love the ravenous little squirrel in “Ice Age” movies.

² Since inception annually: outperformance of 2.7% net of fees vs. relevant benchmark.

On the first point, I can say that the team actually DOES have a diversity of thinking styles. FCG uses the Enneagram personality assessment to measure this factor, and the results for this team are shown below:



Five investment team members and five different thinking styles. That’s as good as it gets for cognitive diversity. In working with this team, it was evident that they each bring different strengths to the investment research and decision making.

Considering good debate, the team brainstormed the question, “How can we do better?” They came up with these suggestions:

- **Start:** Employ a “devil’s advocate” process to hear counter-points to a given proposal. Use Pre-mortems to test an idea: “if this idea does NOT work out, why did it fall apart?” Hold a follow-up session with the advocate for an idea in which s/he is asked additional questions about the suggested stock.
- **Stop:** Reading the written conclusions of participants BEFORE the actual meeting, so as to avoid anchoring.
- **Continue:** Writing down thoughts in the meeting before hearing what others have to say. (This is useful in two ways: leveling the field for introverts who aren’t as vocal, and reducing conformity bias.) Pushing for increased clarity about assumptions and underlying facts. Continue to be respectful of each other.

In my view, the team demonstrated a high level of candor in openly discussing how their process could be improved. Though not perfect, they are well on their way to good candor and open debate.

In our whitepaper, we discuss what a “dream team” would look like. These are the characteristics we would consider in building one:

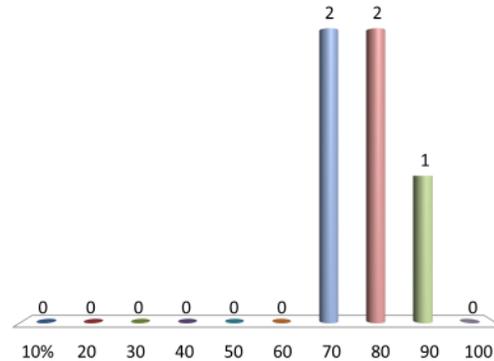
Factor	Dream Team Ideal	Firm’s Score
Size of Team	4-6	5
Enneagram	At least 4 types	5 types
Decision Makers	Multiple PMs	Yes
Gender Diversity	Mix of both genders	3 women, 2 men
Ideal Team Player	Humble, Hungry, EQ	JW’s view: yes
Genius (play to their strengths)	Know and align with it	Yes, see chart below.
Ground rules (curious, candid, accountable, appreciative)	Psychological safety	Yes, very much so. Very safe feel.
Motivation	Intrinsic (Mastery Autonomy, Purpose)	Yes, not driven by Externals: like money.

As you can see from this table, the firm in question nearly perfectly embodies the characteristics of a dream investment team. A few other factors that contribute to their success:

- They are independently owned, so they can control their own destiny.
- Their mission does NOT include growth. They are 100% devoted to strong performance, and have capped their funds.
- The investment professionals get to spend the majority of their time on investment work, as shown in this chart:

How much time spent on genius, i.e. highest, best use of time?

- A. 10%
- B. 20
- C. 30
- D. 40
- E. 50
- F. 60
- G. 70
- H. 80
- I. 90
- J. 100



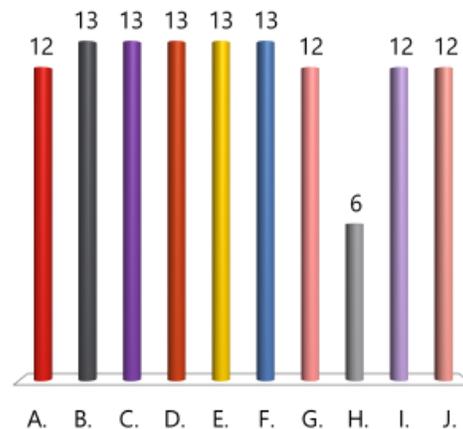
Mean = 7.80

This single chart may be one of the most powerful indicators of performance. Namely, do your talented investment professionals get to immerse themselves in their work? Or, are they distracted with meetings, red tape, and interruptions? It was evident from spending time with this team that they love their work and are free to do it. (Given this reality, I was a little concerned about their view of my taking up their time! Did they want to skip all this and get back to the markets?!)

For the second day of the offsite, the investment team was joined by the operations team, so all 13 members of the firm were present. With everyone together, we explored the culture of the firm. FCG’s research shows that strong culture is essential to success. It was no surprise, then, that this firm showed a strong and cohesive culture. Here is the vote on which values were alive and well in the firm:

Which values are we doing well at? (any/all)

- A. Integrity/Accountability
- B. Clients first
- C. Teamwork
- D. Excellence/continuous improvement
- E. Trust/Respect
- F. Passion/commitment
- G. Work/life balance
- H. Leadership development/mentoring
- I. Curious
- J. Long-term perspective



Keep in mind that these votes are anonymous, so there is little incentive to game the system. The only value that could be nominated for improvement is Leadership development/Mentoring. In FCG's industry work, we see that this is an "up-and-coming" value, largely based on the younger members of the workforce. In my opinion, this firm and other forward-looking ones will embrace this challenge and improve their offerings in this area.

So, there you have it. A firm that is following our white paper formula almost to the letter and, no surprise, enjoying great success. We blind squirrels so enjoy it when we stumble upon another acorn, and this one was a big juicy one! Stay tuned for another installment of the blind squirrel sagas!

Curiously and happily yours,

JW, squirrel #1