April 11, 2017

LOL: Money, Meaning, and Mindsets: Radical Reform for the Investment Industry

For those of you worried about me, I was not kidnapped or worse. The explanation for my absence is simpler: procrastinating. (It got so bad, I was exercising instead of writing.) In my defense, I had a good excuse: working on our new book. But that was pretty much done in February. Since then, I've just been milking it. Oh yes, and working with clients. There's that.

Finally, partner Liz wrote me for a third time: *are you ever gonna put out another LOL?*

Ok. Back to work.

We originally titled our book, "An Investment Vision: Asset Management as a Noble Calling, something something, bla bla." Immediately we received feedback: "that's boring." After getting defensive, going under the line, and cursing our reviewers, we reluctantly agreed. They were right. (Don't you hate feedback? Especially when it's accurate?)

Anyway, Keith and I revisited the title over beverages on a long flight to Europe and came up with the title you see above. And our reviewers liked it. ("See, Jim, feedback is good…")

There are three big ideas in our new book. (Depending on the day of the week, they change…) Today, I'll summarize them as:

1. Passion without Purpose
2. Tyranny of the ORANGE mindset (explained below)
3. Emergence of new mindsets

<u>Passion without Purpose</u>

We start the book by establishing common ground: everyone wants to be happy. Aristotle called happiness the "goal of goals." (Name-drop Aristotle and everyone must fall in line, right?) So, how can the investment industry help with that mission? How does the industry help the average person attain financial well-being so that they have a better chance of achieving happiness? As obvious as it seems—that the industry must address the needs of ordinary people—many investment professionals seem unaware of this basic point. We use a quote from a client engagement to reinforce this message:

> *"The happiness or otherwise of clients is not really relevant."*

This quote is juxtaposed to another one from the same engagement:

> *"I believe that helping people putting their savings to work and achieving good returns will enable them to live better, happier lives."*

In a nutshell, the difference between these quotes sums up a major problem with the industry. This difference was identified and written about in a paper by Suzanne Duncan and the CFA Institute called *Discovering Phi.* They call the problem "Passion without Purpose." There's no question that most investment professionals are passionate about their work. They love studying companies and markets and playing a high stakes game that unleashes their competitive juices. That's passion. But only 17% of these professionals claim that they are also motivated by purpose. So, their passion for investing is a bit like my passion for crossword puzzles: I love doing them, but it doesn't serve any purpose. I just think it's fun. (And if someone paid me a lot of money to do them, I would have found my career years ago.) But there's no purpose involved in my solving the daily crossword. For many investment professionals, it's similar. They love the challenge and the work, and they do get paid a lot of money. But they don't associate their efforts with a greater cause. They don't see themselves as part of a bigger enterprise—the financial sector—that is contributing to the well-being of people on the planet. How do we know this? Well, Duncan's work supports it with thorough research. But more simply, FCG knows it because we routinely ask investment professionals, "Why do you do this work?" We rarely hear a statement of WHY they do the work. Instead we hear statements of WHAT they do: "We invest to beat our benchmark on a risk-adjusted basis." Ok, fine. But WHY do you do that? When we push them on this WHY question, we often hear, "We have to perform in the top quartile in order to attract AUM and grow." Sometimes the answer is as direct as, "If we don't, we'll lose our jobs."

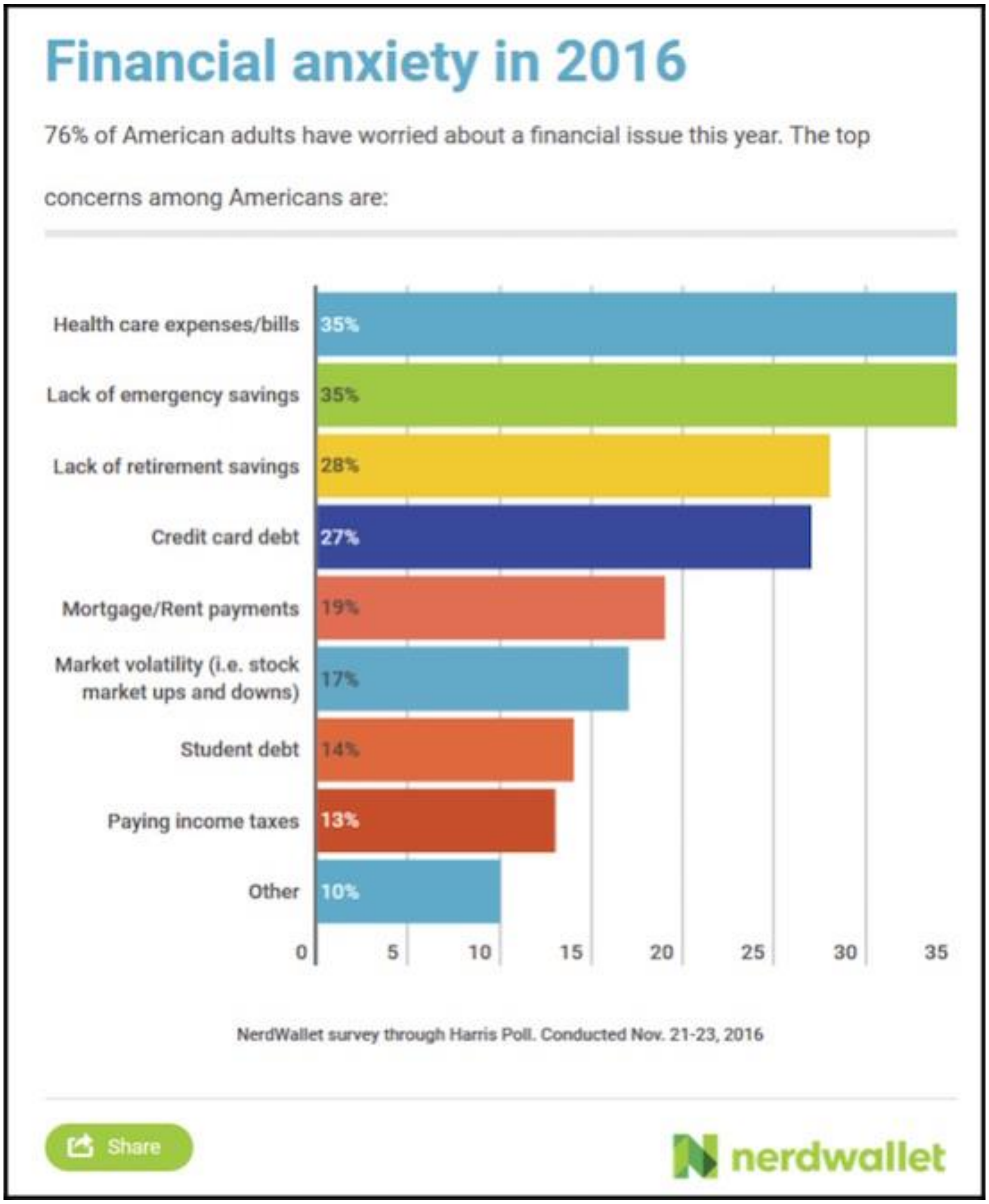
With this last answer, let's segue to one of our models that we use to explain mindsets in the industry: Abraham Maslow's hierarchy of needs. Keeping it simple, Maslow said we have two kinds of needs:

1. Deficiency: survival, security, belonging/relationships, mastery/self-esteem
2. Growth: service, common good, purpose, making a difference

The former are the ones that we all must satisfy to alleviate anxiety. Without these necessities, it's harder to be happy. Once we've satisfied these basic needs, then we more readily look to our growth needs: service, purpose, making a difference, giving back. The deficiency needs stave off anxiety, the growth needs give us joy.

Back to our discussion of purpose, the majority of investment professionals operate from the deficiency needs rather than the growth needs. They are anchored in these fear-based needs—I don't have enough money, power, fame, etc.—rather than aspiring to the growth needs: how can I be of service? How can I make a positive difference? And so they don't connect the dots from the daily work of investing to the larger question of: how does the industry serve the world at large? The perplexing part is that the investment industry does have a legitimate and important role in doing just that: helping the average person achieve happiness through financial security. And this is a BIG need.

A recent survey showed that 76% of American adults worry about financial issues. My guess: it's even higher.



And connecting purpose to motivation--the message in Duncan's white paper--reveals that purpose is indeed a strong motivator for knowledge workers. Maslow, Dan Pink, Frederick Herzberg and others support this same conclusion. Maslow wrote:

> *The self only finds its actualization in giving itself to some higher goal outside oneself, in altruism and spirituality.*

In a healthy adult, who has largely met his/her deficiency needs, it's natural to aspire to the growth needs, i.e. a higher goal outside of oneself. The investment industry displays a kind of stunted growth in its selfish preoccupation with the lower needs. (Read: Ego) So, why is that?

Tyranny of the ORANGE mindset

The mindset of the investment world explains a lot of their "selfish" behavior. FCG hopes that writing about this issue—bringing awareness to it—will help solve it. (Sunlight is a strong disinfectant.) Awareness is an important first step in solving any problem. In our view, the investment world is made up of hard working, smart, and very decent people. Bernie Madoff's are an exception. If the average investment professional better understands the common investment mindset—Grave's called it ORANGE—there's a good chance their behavior will change. At least that's the plan.

So, what is ORANGE? This term comes from Spiral Dynamics, the brain child of Claire Graves.[1] He studied the evolution of cultures and mindsets and discovered that they change over time in a predictable way, based on survival needs. The chart below is from the book and shows these mindsets:

[1] And subsequently supported by a lot of very bright thinkers. NOTE: ORANGE is chosen randomly, with no meaning assigned to the color.

Stages of cultural evolution	Key features	Theme	Key Values	Investment examples	Maslow level
Integrator/ YELLOW	Integral Self: personal freedom to all without harm to others or the physical environment. Limit the excesses of self-interest. Focus on self-expression and systemic approaches.	Live life fully & responsibly, with little fear, and with appreciation for all "previous" mindsets	Purpose Service Ethics Common Good (High SQ, i.e. Spiritual Intelligence)	Just emerging now. The firm of the future	"Growth Needs" Higher purpose Service Greater Good Relatively little fear
Communalist/ clan GREEN	Relational Self: collaborative. Share resources among all. Reach decisions through consensus. Liberate humans from greed and dogma.	Seek peace within, and harmony in community	Trust and respect Collaboration Communication Development (High EQ)	Bridgeway, Boston Common, Polen, & ESG firms	Transformation, moving past prior levels, seeing past "me" to "we"
Rationalist/ ORANGE	Rational Self: search for success and enhance living through strategy and technology. Seek independence and autonomy. Play to win and enjoy competition.	Act in your own self interest by playing the game to win	Success Winning Competing Excellence (High IQ)	Hedge funds, many traditional active managers, like Disciplined Growth Investors	Mastery, autonomy
Guardian/ BLUE	Guardian Self: bring order and stability to all things and control impulsivity through a higher authority. Sacrifice now for later rewards. Laws & discipline builds character	Life has meaning, direction & purpose with pre-determined outcomes	Organized Principled Practical Detailed Loyal	Vanguard, traditional bank trust departments	Connection, belonging, loyalty

Our view is that the investment industry has been largely driven by the ORANGE mindset. FCG does a lot of personality work in the industry, and we can support this claim. But most readers probably agree just looking at the chart that ORANGE fits for many investment organizations. ORANGE has a number of strengths: drive, smarts, continuous improvement. All the typical competitive, type A traits. If you want something done well and fast, give it to ORANGE. They are full-speed-ahead types. The downside of ORANGE is that they are individualistic, success-oriented, and more focused on tasks than people. (Fortunately, one of the authors, Michael Falk, CFA, started his career as a self-declared ORANGE—he's evolved beyond that in my view--so we had an "expert" on our writing team.)

For ORANGE, clients can become a conceptual goal that leads to success rather than real people with real needs. Hence, abstract concepts like benchmarks, efficient markets, and beta are more interesting than helping Mr. and Mrs. Smith. The book provides many statistics to support the claim that clients are NOT happy with their investment experience. (For example, the Edelman Trust Barometer, which places asset managers near the bottom.) Spiral Dynamics helps explain this phenomenon: the fox has been in charge of the hen house, with predictable results.

Emergence of new mindsets

If you are reading this and thinking, "Wait a minute, that's not true about me at all!" Then you are probably more GREEN than ORANGE. GREEN is more people-focused than task-oriented. GREEN is more communal and values relationships. And, evidence suggests that GREEN is a growing factor in the investment landscape. Our book describes this evolution in detail, with both aging baby boomers and millennials playing a large part. The growth in socially responsible investing is a tangible result of GREEN's influence. GREEN is more about social welfare, personalized outcomes, and client service. ORANGE is more about capital allocation, scalability, and alpha. Duncan estimates that 60% of the resources in the asset management business go to the latter. FCG believes that there is a place for ORANGE/active management, but smaller than the current level. Only the really good, value-add (after fees!) active managers should survive. The bulk of the investment industry should be aimed at helping people achieve financial well-being. And as Charley Ellis points out in the forward to our book, financial planning by competent financial advisors is way more helpful to average citizens than incremental alpha. (Charley's new book, *The Index Revolution*, argues that basically all investors should move to index funds.)

Still another mindset emerging out of GREEN is what Graves called the YELLOW mindset. This mindset aligns with Maslow's growth needs, that is, the top of the hierarchy. YELLOW has two significant differences from any prior mindsets:

1. YELLOW has largely met all the deficiency needs, and is mostly driven by the growth needs. In short, YELLOW is what we call "higher self" motivated vs. Ego-driven.
2. YELLOW is the first mindset to see that the other mindsets each have their own legitimacy. YELLOW sees that BLUE, ORANGE, and GREEN each have a valuable function. The other mindsets have the view, "We are superior; they are inferior." A typical Ego view.

We spend a significant amount of space in the book describing YELLOW and how this mindset is best suited for the complexities of the New Era in investing. Fortunately, there are some very good materials emerging about how to develop YELLOW leaders. One is a book called *Spiritual Intelligence* by Cindy Wigglesworth. Another is *A New Psychology of Human Well-Being* by Richard Barrett. And still another is *The Integral Vision* by Ken Wilber. All these books embrace Graves' theory and describe a plan for evolving into YELLOW leadership. The good news is that BLUE, ORANGE and GREEN can all evolve into YELLOW. It involves moving from Ego to Higher Self. Simple, but not easy.

Our book will be out soon. We hope it has a powerful and positive impact on the investment world. (Look for it on Amazon in May) The big idea in the book could be summarized as follows:

The industry should move from doing well to "doing well and doing good."

And our answer is by embracing meaning and new mindsets.

Happy to be back and writing,

JW

P.S. One of the big contributors to our book was Fred Martin, CEO of Disciplined Growth Investors. Fred cares so deeply about this topic that he is hosting a conference devoted exclusively to client/advisor relationships. Speakers include Charley Ellis, Suzanne Duncan. For more go to the website: https://objectivemeasure.org/speakers/2-fred-martin