Thinking Ahead Institute

An agenda for change

Transformational change for investment organisations

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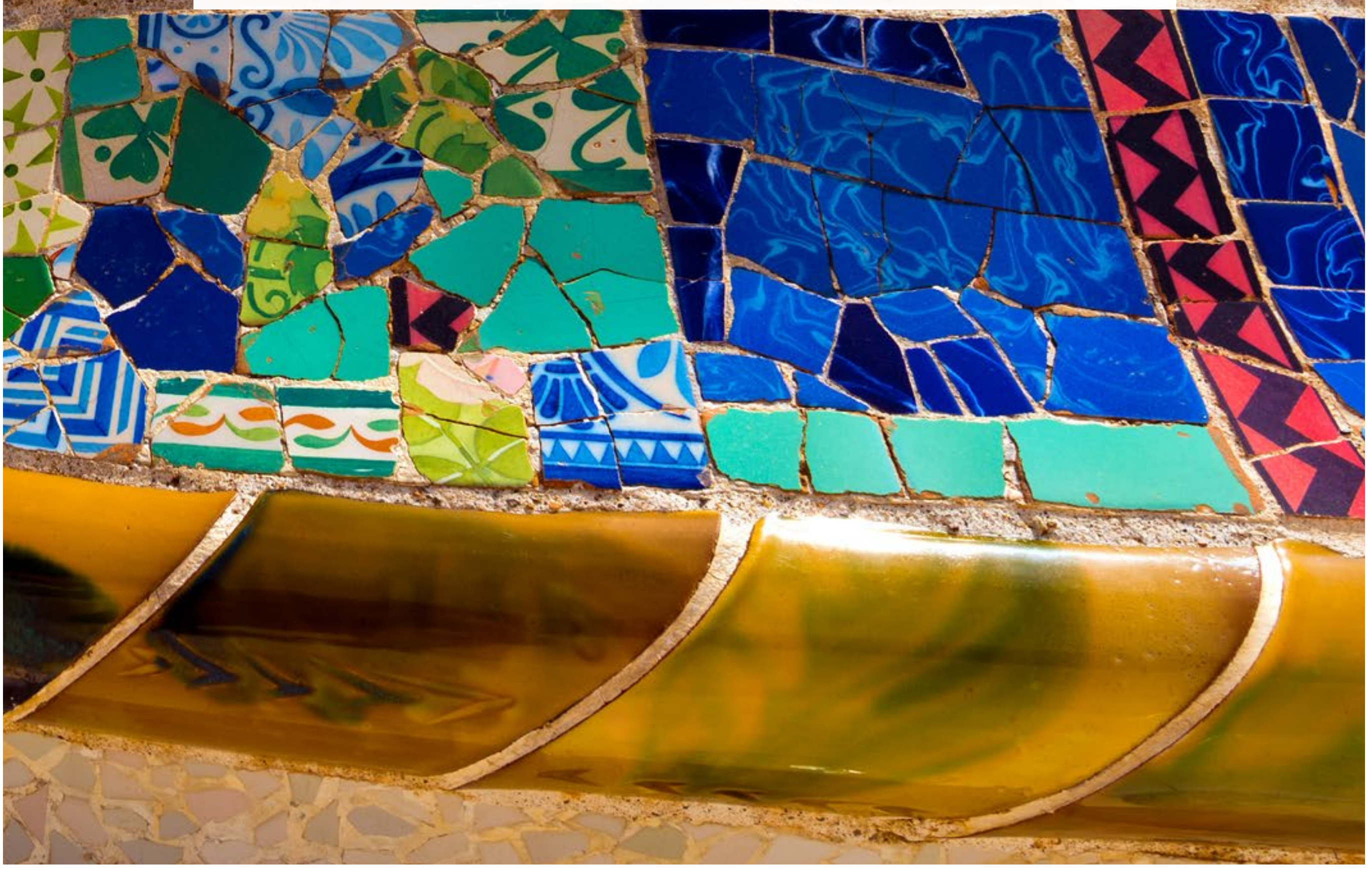

Executive summary

This research paper is authored by Roger Urwin, Paul Deane-Williams and Marisa Hall following research and discussion by the Thinking Ahead Institute's (TAI) Investment Organisation of Tomorrow (IOOT) working group.

We are grateful to the members of the group for their input and guidance as we continue to advocate for change in the investment industry to improve the value proposition for the end saver, wider society and the planet. The authors alone are responsible for any errors of omission or commission in this paper.

The members of the two IOOT working groups, chaired by Roger Urwin of TAI, were as follows:

West group (Europe / Americas)

- **Robert Brown** (Univest)
- **John Chilman** (Railpen)
- **James Davis** (OPTrust)
- **Emilio Garcia** (Santander AM)
- **Marisa Hall** (TAI)
- **Tom Lee** (NYSTRS)
- **Ruth McDonald** (TAI)
- **Eoin Murray** (Federated Hermes)
- **Frank Naylor** (BTPS)
- **Luba Nikulina** (WTW)
- **Russell Picot** (HSBC & USS)
- **Mike Sales** (Nuveen)
- **Jaap van Dam** (PGGM)

East group (Australasia)

- **Sue Brake** (Future Fund)
- **Stewart Brentnall** (TCorp)
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- **Tim Mitchell** (WTW)
- **David Neal** (IFM Investors)
- **Sarah Owen** (New Zealand Super)
- **Sonya Sawtell-Rickson** (HESTA)

The two working groups (the 'Group') met (virtually) seven times between March and September 2021 and set out to accomplish the following:

- Help its working group participants move forward in their investment industry thinking
- Develop a set of principles and accompanying narrative through a peer co-creation process
- Transfer knowledge to colleagues, other TAI members and the wider industry
- Use convening, co-operation and cadence principles and build a participative group culture.

The Group adopted a starting thesis:

- There is a paradigm *shift* about to happen in the industry, brought about by a widening of organisational purpose within it. The working group calibrated this *shift*, by considering and developing an understanding of the rapidly changing context
- This shift will require organisations to adopt a much more agile, substantive and socialised *change model* than has been prior practice. The working group should co-create what that *change model* should look like
- To do this requires a commitment to think through issues respecting all material *systemic factors* influencing investment industry outcomes. The thinking pursued by the working group should make deeper and better connections between these systemic factors.

> *"There is a paradigm shift about to happen in the industry, brought about by a widening of organisational purpose within it."*

Principal conclusions

The Group's principal conclusions were these:

- **Purpose and vision** – Multi-stakeholders increasingly frame asset owner direction of travel. Societal context has changed, stronger stakeholders have emerged, investor goals have multiplied and shifted. Solidarity and collective action are increasingly favoured with systems and strategic leadership being critically required
- **Investment conventions** – Risk intelligence and real-world impact need to reach new levels. Investment practice is shifting, with value creation seen differently, particularly on sustainability in ESG, active ownership. Total portfolio thinking, 3D investing and universal ownership together define a stronger investment framework
- **Infrastructure** – Asset owners' infrastructure critical to deliver change but the soft stuff is the hard stuff. Investment infrastructure critical for success – thinking and practice, reporting and data, resourcing and collaborations. We need Superteams that capture diversity, culture and governance excellence; and the stronger value chain that will come from stronger mindset and relationships
- **Holistic picture** – To effect change on the scale suggested, the leadership needed is holistic and strategic. Successful change is premised on articulating a strong and compelling vision plus building a leadership coalition of board and executive stakeholders plus applying a disciplined change process that works on multiple strands.

Research sources

The paper builds on six years of TAI research, largely captured in the following research papers, and also other research works cited:

- Smart leadership. Sound followership – *a peer group study of asset owners*
- The Asset Owner of Tomorrow | *Business model changes for the Great Acceleration*
- The Asset Manager of Tomorrow | *Critical requirements for asset manager success*
- It's about time | *Total portfolio thinking and practice*
- With great power comes great responsibility | *Duty of ownership, engagement and stewardship*
- The Asset Owner 100 | *The most influential capital on the planet*
- A year needs a score but a decade needs a purpose | *What makes purpose fit-for-purpose*
- Strong Investment Theory and Practice | *Alternative investment principles to current practice.*

Other research:

- The dawn of systems leadership | Peter Senge et al | SSIR 2015
- Milton Friedman's hazardous feedback loop | Duncan Austin | RI 2020
- Should a pension fund try to change the world? | HBR 2019.

This paper

The paper is organised around five main sections, which are the principal areas covered by the working group: The system-wide framing; the business model; the people model; the investment model; and the change model.

Each section starts with a narrative that explains the working group's overall thinking, and then provides practical application in the *principles*. This construct does involve some intentional overlaps and duplications, by design. We also include polling of group members related to the issues in each section. The paper concludes with an assessment of the challenges ahead and an appendix listing of eight high-level *principles* to address the above substantive issues and provide guidance to assist Asset Owners (AOs) and Asset Managers (AMs) in the form of transferable intellectual capital.

"We need Superteams that capture diversity, culture and governance excellence; and the stronger value chain that will come from stronger mindset and relationships."

Section 1: Introduction

Being an investment leader in the 2020s and shaping tomorrow's investment organisations can seem mind-bogglingly complex. And life in the next five to ten years is not expected to get any simpler given the changes in technology, demography, globalisation, environment and social norms that are all speeding up.

Investment leaders will need to reposition their business models, operating models and investment models, which requires considerable shifts in mindset and practice. This is particularly relevant for AO leaders, given these organisations are too important to fail in their mission.

With this in mind, the Group scoped its work around five areas:

- The **system-wide factors** affecting the organisational effectiveness of AOs (particularly) and AMs
- The external forces of change affecting these organisations – economic, environmental, social – that are altering their **business model**
- The internal and external factors affecting them through their **people model**
- The alternative pathways they can choose in their respective **investment models**
- The shape and scale of the **change model** that is best suited to meet these changing organisational goals.

In covering this ground, the Group were motivated by the accelerating levels of change being experienced in the investment industry and its **shifting context**. There was a shared belief that investment organisations need to adapt at a speed and scale to match the increasing uncertainty and complexity around them. The external disruptions of net-zero transitions, sustainability pressures, a 'new normal' investment macro and changing societal zeitgeist were considerable and presented a high bar for this adaptation. And most critical of all, investment organisations are changing as a result of revisiting their purpose and adopting a multi-stakeholder identity[1].

One helpful definition of purpose is: *"An aspirational reason for being which inspires and provides a call to action for an organisation and its partners and stakeholders and provides benefit to local and global society."*. We also cite Colin Mayer's work, for the British Academy: *"To create profitable solutions for the problems of people and planet, while not profiting from creating problems for either."* This has particular significance to the sustainability and externality issues of the investment industry.

Extending this thinking, the purpose of the investment industry should be to contribute to societal well-being, expressed by its opportunity *of providing risk-adjusted returns to savers and investors and directing capital flows*. In addition, it should be defined by its capacity to contribute (resources and legal and regulatory framework) and its moral incentive to contribute (values and principles).

Shifting context

The Group believes that this fast-changing context for investment organisations has made change as much an imperative as an opportunity. Organisational effectiveness in the investment industry has centred on the need for internal capabilities and enablers that are of sufficient strength to create sustainable long-term value in line with the organisation's mission and intrinsic identity (subjects we return to in chapter 3). The area of organisational effectiveness is covered in more detail in the TAI paper: [With great power comes great responsibility.]

[1] Harvard Business Review | 2015

These capabilities and enablers can be summarised in three major areas: business model, people model and investment model. Here the word *model* indicates a high-level look at how aspects of the organisation functions and aims to fulfill its purpose and strategic objectives. The business model, investment model, and people model are all critical capabilities and are the central areas that need to be covered for successful outcomes, while adapting to changes in circumstances.

The goals of the Group were to contribute towards successful change in organisational effectiveness and resilience. The central premise of the Group was a belief in the merits of change, indeed 90% (18 out of 20 members) thought that large-scale change was very important or somewhat important. But the prevailing view is that change represents one of the biggest challenges they have in their organisations, with 55% believing that their organisations are not very comfortable or not at all comfortable with large-scale change.

The Group adopted a practical version of what defines large-scale change – also referred to as *transformational change* – as follows:

A complete change in an organisation designed to bring big improvement[2] *that commonly involves innovative, substantive, time-intensive, and multi-strand project management features.*

Transformational change has been most applied to technology projects, associated in particular with the digital opportunities of straight-through processes, platforms and inter-face technology. We note that examples of applications to other areas of the business model have been less common. We explore transformational change in chapters 6 and 7, having covered the high-level specific changes in the previous chapters. The over-riding principle is that a systems-wide framing is needed for all these issues and we elaborate on that in the next chapter.

The key to overall success is leadership being able to see these areas holistically, with particular regard for the influences of interaction, collaboration, and incentives.

"The goals of the Group were to contribute towards successful change in organisational effectiveness and resilience. The central premise of the Group was a belief in the merits of change..."

[2] Cambridge dictionary definition

Section 2: System-wide framing

Principle 1 Be holistic and systems-savvy when approaching change

There are many system-wide factors affecting the organisational effectiveness at AM and AO organisations. These factors, which can be very disruptive, require investment leaders to become more T-shaped. Most will be deep experts in their field – this constitutes the vertical bar of the 'T'. But many will not be as expert with the horizontal bar of the 'T' which only comes with having situational fluency around wider issues and is achieved through being *in-touch* with a wider network and other disciplines.

More *in-touch* here means for example a greater understanding of stress and fight or flight responses in brain science; the balancing of dominant and serving leadership in management science; the critical quality of safe space in psychology; and how to apply the delicate art of being human. But critically, being T-shaped requires a thorough appreciation of systems-theory. In the current context, this includes how our organisations function as organisms within an ecosystem; how pandemic systems affect our lives and health; how the mistreatment of our environmental systems may brutalise our planet; and also, if we get it right how the financial system can lay the foundations for wealth and well-being to be more fairly distributed.

So a key challenge for investment leaders is to build sustainable organisations that harness people and technology to create value in a wholly integrated sustainable investment system.

Systems thinking and systems leadership

This leads into the subject of *systems leadership* – a new type of leadership that seems helpful to enable the collective action so critical for future success. This is collaborative leadership that finds joint solutions to common problems framed by a joined-up understanding of the interconnected systems of which we are a part. It is built on respect for the multiple strands to the challenges and the multiple people that have a stake in the problems, and on a realism that there are multiple facets to any problem requiring thought-through and holistic solutions. A *systems leader* works with the belief that their success, and their organisation's success, depends on co-creating wellbeing within a very large system.

Table 1 – **Systems-thinking principles**

The investment system is:		The investment system's characteristics
▪ Defined by its purposes and associated (and often unintended) consequences ▪ Utilised by its participants: businesses, providers, savers and consumers ▪ Expressed through its functioning in markets and technologies and regulation ▪ Influenced by its social, economic and ecological environment.	**Reflected in** →	▪ Everything connects but nothing adds up ▪ Data is messy ▪ Combinations are critical ▪ Behaviours matter ▪ Associations not causations ▪ Path dependence arising from evolution, discontinuities and emergent properties.

Conclusions and principle for change

- Societal context has changed, stakeholders have shifted in the investors' mindsets and so have investor goals as a result
- Solidarity and collective action are increasingly favoured. Investment organisations that previously might have thought about going it alone now think more about collaborating with like-minded investors
- Context is shifting in the industry. This fast-changing environment for investment organisations makes change as much an imperative as an opportunity.

Supporting polling data

The following polling data provides an insight into the Group's views on key systems-thinking areas. The sample sizes are generally drawn from the 20 members of the Group.

AOs identified their main strengths in positive purpose and effective culture, while AMs have stronger technology and more talented teams.

AOs' main weakness is in shorter time horizons being reflected in goals and influencing decisions. AMs' weaknesses flagged up as more spread out with limited ability to manage organisational change coming on top.

Investment organisations are striving for more innovation and diversity, a longer-term focus and greater alignment across important teams (Table 2).

"Context is shifting in the industry. This fast-changing environment for investment organisations makes change as much an imperative as an opportunity."

Figure 1 – **Which of these areas are strengths of larger AO and AM organisations**

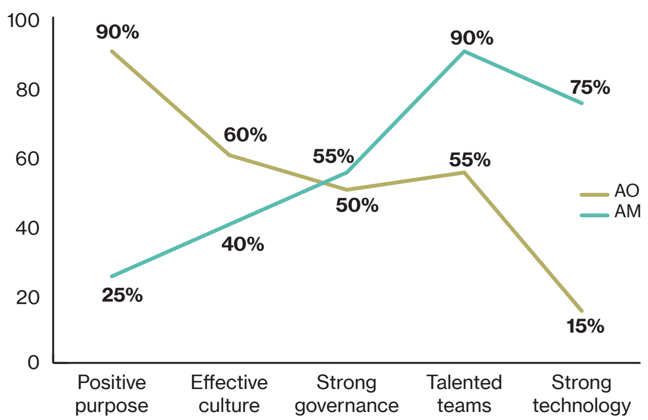


Figure 2 – **Which of these areas are weaknesses of larger AO and AM organisations**

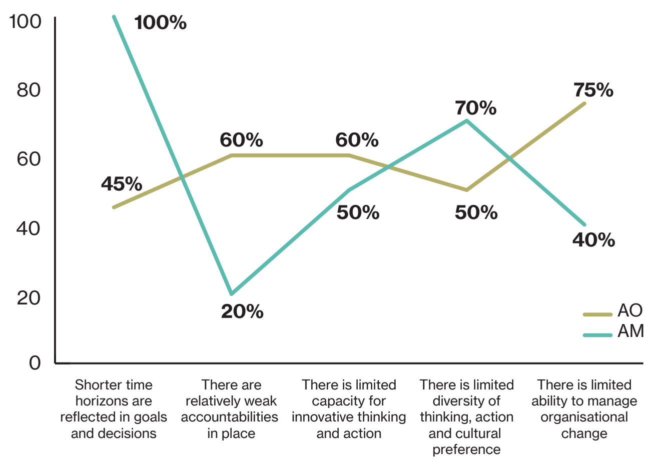


Table 2 – **Cultural edges and cultural challenges**

Which of these cultural edges would you wish your organisation to have more of?		Which of these cultural challenges would you wish your organisation to have less of?	
Innovation	95%	Board vs internal team (AO) or cross-team alignment (AM)	75%
Diversity & inclusion	70%	Short-term vs long-term focus	70%
Resilience & staying power	50%	Inter-generational (AO) or stakeholder alignment (AM)	55%
Purpose	45%	Green vs non-green ambition	55%
Transparency	35%	Board vs sponsor (AO) or client vs owner alignment (AM)	30%

Section 3: The business model

Principle 2: The purpose of investment organisations is shifting in the direction of a multi-stakeholder orientation in which wider stakeholder interests are factored into activities and decisions.

Principle 3: The priorities and boundaries to the business of the investment organisation need to be clearly set and communicated through identifying stakeholders with accompanying goals and accountabilities.

Value creation

The *business model* describes how organisations create value and implies a combination of mission and vision, stakeholders and boundaries, goals and strategy. Of course, this is a broad subject, and we will separately develop the *people model* and *investment model* parts in further chapters. But what is a key aspect of the *business model* concerns the focus of the value creation in terms of the key stakeholders that benefit from it. And here the investment organisation is faced with some important issues on the breadth of the multi-stakeholder commitment and, particularly, how deep is the net-zero emissions commitment, where undertaken. Importantly, these aspects have been changing in recent times and will no doubt continue to move in future, so remaining vigilant around **shifting contexts** will be important.

The Group had considerable respect for the 'multi-stakeholder model'[3] that has come to widespread usage among major corporations. In many respects this was seen as correcting an old imbalance whereby the industry had previously created too many negative externalities for society. And that it has ethical reasons for its value-creation activities to be more balanced in future and to curtail certain inequalities arising. This general issue has had a more explicit test around climate change where investment organisations have made net-zero commitments to 'do the right thing' with respect to people and planet.

Business generally is increasingly expected to 'do the right thing'. Those expectations are expressed in areas to act on including climate change, racism and automation / re-training[4]. These are issues that previously seemed like areas where investment organisations deliberately avoided attention. Here though there are distinctions to be drawn between for-profit AMs (where multi-stakeholder interests can be legally supported at the corporate level) and profit-for-members AOs (where member interests have significant priority through fiduciary duty[5]). This is an issue we return to in chapter 5, the investment model, where we also explore the 3D investment framework.

The Group agreed that organisations need to explore more regularly and searchingly why they exist. And answers to such questions need to form a compelling backbone to organisational identity which then shapes and reshapes the strategy. It's a case of getting the *why* straight before the *how* and the *what*.

Why does this version of *why* we exist differ from previous versions? The growing convictions about sustainability reflect the widening responsibility carried by AOs. One aspect of this is respecting the full scope of the ecosystem and its boundaries. The investment organisations of tomorrow need to be more thoughtful on how the whole system works, how they interact with it, and how it interacts with them.

How will future versions differ from current ones? This is a bit harder to be clear about. But there was the sense that the sustainability aspects and climate in particular would be bigger influences in future. This bears on a particularly critical element of existing purpose which is inter-generational equity. Here the Group felt reasonably at ease with placing greater emphasis on long-term sustainable value creation. Out of this comes the need to build greater stakeholder management in a world requiring increasing accountability.

[3] In the multi-stakeholder model, the company's purpose is to create value for multiple stakeholders which the Business Roundtable (September 2019) described as 'companies should serve not only their shareholders, but also deliver value to their customers, invest in employees, deal fairly with suppliers and support the communities in which they operate'.

[4] Source: Edelman Spring 2021 Trust Survey

[5] Fiduciary duty has been extensively covered in the Duty of Ownership working group publication 'With great power comes great responsibility'.

The Group, in their polling, were overwhelmingly clear that their organisational purpose was crucial, with 80% (16 out of 20 members) viewing their own organisation's purpose as having considerable resonance. But their sense was that the industry had not yet come to see it the same way, with 50% believing that purpose is not generally resonating, but will do so in future. One factor considered to be accelerating this shift is the development of net-zero commitments in the industry with 90% of the Group seeing this as *game changing*.

The complex nature of net-zero arrangements is reflected in multiple issues that the Group thought needed resolution. A crucial example is in the new climate-change goals which introduce inter-connected accountabilities to different stakeholders.

Defining each organisation's stakeholders requires considerable thought. For an AO, the broad basis for this thought process is to identify certain inner stakeholders, principally the members whose savings and retirement benefits are being managed. But also, the board and management which are the fiduciary and the sponsoring organisation. Then to recognise the government and regulator stakeholders, the relevant NGOs, the provider and supply-chain organisations and other partners. In addition, it means recognising a wider group of stakeholders in certain communities and more broadly to society at large. Stakeholder management implies respect for multiple parties, but responsibilities must be graduated somehow. There must be realistic limits. Clear thinking and documentation of these priorities and boundaries is called for.

We can best see stakeholders as those constituents that have mutual interests in the ecosystem. Those stakeholders that are directly served in return for their business (e.g. members); those more indirectly served (e.g. communities and society); those that influence success (e.g. providers); those that have other direct influence (e.g. regulators). The systems-view recontextualises these relationships by understanding that the organisation's success depends on creating wellbeing within the larger systems of which it is a part.

Many would argue that purpose is a constant feature at all enterprises, but the Group took a contrary view. They see the ***context shifting*** in the change in societal forces, and indeed in regulation too, that requires reorientation from time to time. And the significance of the climate crisis has made such a reorientation essential.

One other aspect for consideration is member outcomes and experiences. These experiences are substantially about ultimate financial outcomes, but the intermediate experiences come into this – the attainment of financial and non-financial utility and comfort. As an example, we have the world of defined contribution pension plans where reflecting member wishes in responsible and sustainable investing has grown to be a significant issue[6]. This implies that the industry is now increasingly on a more humanistic mission, which organisations are grappling to mirror in their business models.

Supporting polling data

The following polling data provides an insight into the Group's views on key business model and organisational purpose areas.

The polling data shows that the Group's majority views their organisational purpose as crucial and it resonates considerably with them. However, the industry overall has not reached the same understanding yet and is still on the way towards resonating with the idea.

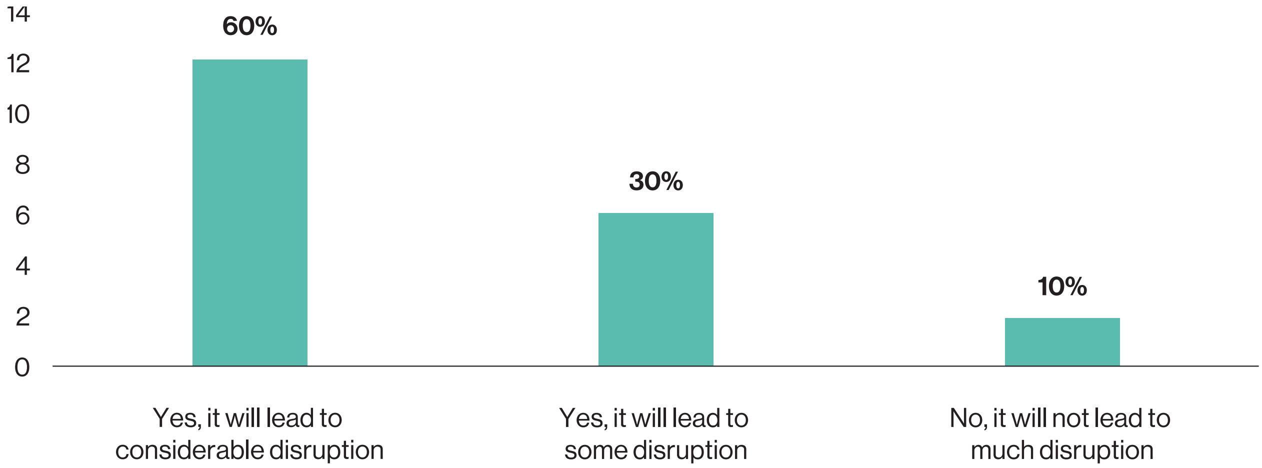
Table 3 – **Organisational purpose**

How does our organisational purpose resonate with me?		How much does organisational purpose resonate in our industry?	
It resonates considerably	**80%**	It is resonating considerably	5%
It resonates	10%	It is resonating and increasingly so	40%
It does not yet resonate, but is likely to do so in the future	10%	**It is not resonating much, but is likely to do so more in the future**	**50%**
It does not yet resonate	0%	It is resonating hardly at all and I do not expect more in the future	5%

[6] The Freshfields review of impact in investing expressed the issues as follows: *Investing for sustainable impact essentially addresses the same issue as current attention to corporate purpose, but from the point of view of investors: what is the purpose of economic activity and how does it relate to the wellbeing of people and planet?* Questions of investment purpose and corporate purpose both concern what is valuable, not just financially but also in terms of outcomes for the social and natural environments on which people depend. Investment for sustainability impact approaches these questions from the perspective of investors, corporate purpose from that of the companies in which they invest.In answering them it is helpful to recognise that they converge on similar ground. **Growing evidence suggests that this more purposeful investing is what many individual investors want from those who manage their assets.**

"Net-zero commitments are seen as a game changer in accelerating the change within the industry and 90% of the Group think these commitments will lead to some disruption."

Figure 3 – **Do you see net zero as an industry disruption and game-changer?**



These issues concern me with respect to adopting net-zero ambition	
There are considerable challenges in measuring and reporting on carbon transition (scope 3 emissions, offsets, etc)	80%
Investment policies that aim to maximise risk-adjusted returns and align to net zero may not coincide	75%
There are dependencies in net zero trajectories on public policy	70%
There are considerable reputational risks from the public scrutiny and accountability of net zero journeys	60%
There are considerable challenges in identifying and executing appropriate investment policies	55%
There are considerable challenges in governance of net zero pledges including binding the next generation leaders	55%
There are no issues that cannot be managed	5%

Section 4: The people model

Principle 4: Investment organisations have a significant opportunity to apply Superteam principles to how teams are organised and function.

Work structure and culture

The people model and how it operates concerns: work structure and its evolution (often referred to as 'future of work'); and organisational culture and team practices, where we use the concept of *Superteams* to describe best practice. As investment organisations are human-capital enterprises, the people model is a fundamental building block of how value is created.

The Covid pandemic is **shifting the organisational context** by generating sharp accelerations to existing work trends – hybrid working, talent shortages (including the 'great resignation') and purpose in work[7] are all resonant examples. The 'future of work' also encompasses the reimagining of new skills, forms of learning, work environments and worker wellbeing. Emerging work structure points include these:

- Work is being transformed both incrementally and in more discrete steps, with the shift to remote work and the emergence of the hybrid model being a distinct feature
- Organisations are taking wellbeing beyond the previous considerations of work / life balance by designing wellbeing into work
- The growth in attention to Diversity, Equity & Inclusion (DE&I) has been striking
- Organisations are shifting in some cases to work programmes that integrate the dynamic nature of work and the potential of workers to reinvent themselves and be empowered
- Skilling, upskilling and reskilling are all being worked on by employers and employees
- Both employees and employers are making changes in their ways of thinking, acting and being.

The Group's polling results neatly summarise the challenges involved in this area. The commitment to a hybrid-working model was very strongly supported. Only one organisation out of 17 thought the return to work would not involve a major transition to a new configuration mixing physical and virtual work and more flexible work arrangements. Almost half of the Group thought that 45% to 70% of their organisation's work could be done from home and all members believed that at least 30% of work could be done that way.

Overall the Group is expecting work structure changes to be more than just an opportunity for improvements in productivity and performance. They regard them as essential imperatives to staying competitive with leadership, co-ordination and empowerment playing shared roles in successful roll-outs. They rated the importance of Learning & Development (L&D) highly and viewed their organisations' engagement activities in this area as moderate. Engagement requires leadership to develop L&D resources using supporting technology, and employees committing time and self-starting initiative to their learning. In a minority of investment organisations, we see a streamlined and significant L&D platform. In a tightening market for investment organisation skills, the employee value proposition (EVP) around L&D seems large and growing, representing a particular opportunity for differentiation.

[7] Hybrid is shorthand for how remote and office work models are blended along with other flexibilities in work practices. The *great resignation* covers much higher attrition of current staff – in the US official data suggested a peak of 25% of the workforce leaving their current job in 2021 with almost 3% departing in a record set in that August.

The organisations represented in the Group indicated even stronger levels of engagement in organisational culture, as disclosed through top-down leadership initiatives and organisation-wide traction. This tallies with the wider industry experience where organisations have increasingly seen culture as highly influential to improved organisational outcomes and have tried to shape it to be more effective for the following reasons.

First, culture in investment organisations has critical connections to the advancement of the ESG and sustainability area. And it provides critical support to purposeful organisations.

Second, many members commented on how culture had been particularly critical through the Covid crisis. Here the two groups experienced different outcomes with culture being strengthened somewhat in the West (Europe / Americas) group but becoming weaker in the East (Australasia) group. This may have arisen because the Covid crisis produced more significant stress in Europe and the Americas where death tolls and welfare impacts were higher. Organisations in Europe and North America were able to use their culture to generate more supportive practice and this had a positive reinforcing effect. By contrast organisations in the Australasian group found the Covid issues simply disruptive and saw culture as weakening from the enforced remote-working arrangements.

Third, cultures in all cases had adapted to higher levels of welfare concern, with mental health the biggest single area of attention, and overwork and burnout figuring as a subject of significant focus in addition. Overall, organisations have shown much increased awareness of their workforce's personal context with issues like childcare and eldercare much more noticed and they are increasingly seeing the workforce through a humanistic lens.

The focus on the workforce has been exercised in many cases through formal initiatives and change processes. The majority of organisations in the group have current commitments to develop hybrid work arrangements, strengthen DE&I practices and outcomes and use culture more deliberately to advance the organisations' goals.

Several individuals in the Group have committed leadership attention to specific cultural initiatives, ranging from a focus in employee-engagement surveys to becoming part of the TAI Power of Culture programme in which organisations measure, review and – as a result – adapt their cultural attributes and edges.

Superteams

In synthesis, investment organisations are fundamentally a *team of teams* which have their specific value-creation goals and interlocking functional responsibilities. People in organisations are members of multiple teams and also multiple groups.

Teams are highly interdependent – they plan work, frame and solve problems, review progress and make decisions. Team members need one another to get work done. Contrast this with work groups that are characterised by lesser interdependence and greater organisational hierarchy.

We observe that teams have value creation as an intrinsic motivation and are the primary unit of value creation in investment organisations. Their value-creation potential is predicated by various factors, notably their talent, behaviours, culture, diversity and execution effectiveness. Their way of working has developed through various experiences and iteration. But it is reasonable to suggest that their practices are not honed and their engagement is not exactly trained for. Comparisons with sports teams suggest that investment teams do less preparation for their tasks and apply more ad-hoc practice ('winging it' is the phrase we have heard used).

With the growing complexity and disruption endemic to the industry we argue that teams could employ a variety of stronger disciplines:

- Culture has unique potential in a team setting to be a better and broader influence through social capital and trust. And culture can be set by deliberate design and managed
- DE&I is a constructive team force, balancing the edge gained from cognitive diversity[8] with other diversity facets
- Teams can benefit from coaching (e.g. bias training) and frameworks (e.g. shared beliefs) to build the collective intelligence[9] of the team
- Teams can rebalance priorities and trade-offs to de-emphasise near-term marginal gains and emphasise long-term absolute gains
- Teams can benefit from particular styles of leadership, notably serving leadership, systems leadership and distributed leadership
- Teams can benefit from organisational design that is flatter, less hierarchical and more like a network of leaders and doers than being structured with a single point of command and control.

In TAI research, 'Superteams'[10] are teams that combine a diverse array of talent that through effective culture and governance achieve exceptional outcomes. The research conducted suggests diversity, cognitive diversity and collective intelligence are the key Superteam attributes, and we define each as follows:

Diversity: strong values of fairness driving the organisation to promote goals around creating a diverse workforce, equity in its workforce practices, inclusion in workforce culture

Cognitive Diversity: adding talent together via diverse competencies, perspectives and experiences

Collective Intelligence: combined effectiveness through how team members interact and collaborate in which these features play a part:

- **Inclusion.** Create culture of belonging, identity of purpose and equality of voice through engagement
- **Trust**. Commitment to trust as a critical value and culture; focus on building trust and ways to benefit from trust
- **Frameworks**. Beliefs and principles as fundamental scaffolding (or frameworks) for critical thinking and to support decisions
- **Rigour**. Effective decisions from accurate judgement, accountability, and growth and socialisation mindset
- **Innovation**. Culture that rewards creativity and agility and is comfortable with risk-taking and long time horizons.

In survey work, members of the Group used the TAI survey tool to make assessments of their own organisation's Superteam attributes. In summary, we saw a range of team scores for Superteam attributes, but the overall conclusion was that this line of research is important and would be of value both case-by-case and also in general.

The Group were concerned about how *top teams* – ie ExCos and boards – were dealing with an ever-lengthening list of complex issues. There was considerable support from more than 70% of the Group that *top teams* need to: improve their effectiveness in issue resolution in diverse complex settings; target and manage change better; and develop better leadership on purpose and vision. The opportunity to tie Superteams practice to *top teams* in particular was agreed in the Group.

[8] Think of cognitive diversity as differences in types of experiences, competencies, perspectives, information processing and ways of thinking that create a richer, more nuanced understanding of problems and faster, better problem solving.

[9] Think of collective intelligence as the experience and expertise across a team and the collaboration and flow within a team. We can think of this as mostly about talent, culture and governance.

[10] See TAI Culture – the organisational superpower

Supporting polling data

The following polling data provides an insight into the Group's views on expected work structure changes and Superteams principles.

The polling data shows that the Group's majority views their organisation's optimal state as a hybrid work model, which introduces new work flexibilities and requires a major adjustment.

Hybrid work model and diversity, equity & inclusion are the initiatives that most Group members are currently working on.

Table 5 below is the summary of the Group's members survey results using the TAI survey tool to make assessments of their organisation's Superteam attributes. It identified a range of team scores and resulted in the conclusion that this line of research is important.

Table 4– **Polling data**

What is your belief about your organisation's optimal state?	West Group	East Group
Return to workplace orientation, new work flexibilities a minor adjustment	0%	11%
Hybrid model, new work flexibilities a major adjustment	**75%**	**56%**
Hybrid model, major transition to WFA model	25%	33%

Which of these areas are you currently working on change initiatives or about to do so?	West Group	East Group
Hybrid work model	**27%**	**29%**
Diversity, Equity & Inclusion	**22%**	**25%**
Cultural initiatives	22%	21%
Wellness programs	16%	13%
Learning & Development reimagined	11%	8%
Other	3%	4%

Table 5 – **Superteams special polling – All Working Group responses – one per organisation**

	Number of organisations						
Superteam attributes	AAA	AA	A	BBB	BB	B	<CCC
1. Cognitive diversity	0	8	3	3	1	1	1
2. Culture – inclusion	2	5	0	1	4	3	2
3. Culture – trust	1	3	1	4	3	2	3
4. Governance – framework	1	4	5	2	2	2	1
5. Governance – rigour	0	3	3	6	2	1	2
	Number of organisations						
Composite	AAA	AA	A	BBB	BB	B	<CCC
Collective intelligence	1	1	3	6	3	1	2
	Number of organisations						
Composite	Short	Balanced	Long				
Focal length	12	2	3				

Section 5: The investment model

Principle 5 : 3D investing frameworks can and should be created that balance the risk, return and impacts of strategies.

Principle 6 : Total portfolio approaches support the integrated thinking that is needed for the achievement of sustainability within fiduciary constraints.

Stronger investment theory and practice using systems-thinking

Investment management has evolved its practices somewhat since the adoption of modern portfolio theory in the 1960s[11]. However, we suggest these investment conventions are being increasingly challenged and investment theory and practice may be ready to undergo certain changes in response to external forces and **shifting context**.

What lies behind this shift? First, not all existing theory is practiced as there are significant limits to mainstream investment theory and how it is used in mainstream investment practice. This starts with over-rigid theory that adopts an unrealistic ambition to build unified theory when complexity is innate to the system.

Second, the theory fails to acknowledge subjectivity and ambiguity when building investment theses, and fails to incorporate the specific place of institutions whose behaviours in the system are significant. So, we have insufficient allowance for the investment industry's *inconvenient truths* with complex cultural and governance interactions affecting real-world behaviours. As a result of these limitations in the mainstream of the industry, decision-making has relied on accepted and established practice more than theory. But the drawback of being guided by practice is that this is essentially a backward-looking, or at least historic, viewpoint and can lack rigour and consistency.

Third, existing theory and practice has no answers when it comes to the new dynamics concerning the dual objectives of investment portfolios: maximising risk-adjusted returns and net-zero commitments or alignment to climate outcomes.

We present a set of alternative principles[12] to current practice which we might term a systems investment framework that has certain differences of emphasis from previous versions. These are the stronger practice organising principles:

- **Stronger governance** through synchronisation of mission, values and beliefs, risk framework and long-term orientation
- **Stronger investment frameworks** for value creation, risk, time diversification, long-horizon investing, sustainability and portfolio construction
- **Stronger portfolio construction** in which factors and buckets are classifications that rank ahead of asset classes in a portfolio quality competition for capital aligned to total fund goals
- **Stronger accountabilities** in which numerical discipline in performance attribution is blended with qualitative analysis to produce overall views on merit and contributions to pay. There needs to be a clear point of accountability ensuring the quality, robustness and holistic nature of this process. This is more art than science of course.

[11] The key features of MPT were originated by the seminal work of Markowitz who first published on Mean Variance optimisation, in 1952 which gave rise to the distinction between diversifiable idiosyncratic risk (alpha) and systematic risk (beta) . Like many theories there was gap before the ideas were taken up but the rudiments were in place in the 1970s. MPT is a convenient term for several associated theories which were recognised when Markowitz along with Merton Miller and Bill Sharpe shared the Nobel prize for economics in 1990.

[12] These principles are originally included in the TAI paper: Stronger investment theory and practice. The longer version of the stronger investment framework principles is included in Appendix 2.

Table 6 – **Stronger investment framework features**

Features
Value creation involves advancing the mission through the lenses of multiple stakeholders by deploying a governance budget applied to a risk budget
Risk is unique to each investor and reflects multiple lenses across stakeholders and time horizons and path dependencies
Long horizon investment involves applying flexibilities in the organisation's characteristics to long horizon premia that are earned not just taken
Sustainability is approached from three directions: long-term investing efficiency; values and a sense of responsibility; and from integrating sustainability impact to financial outcomes
Portfolio construction and management decisions follow from portfolio quality considerations via diversification of risk budgets, resilience, implementation, sustainability and impact elements.

3D investment framework and universal ownership theory

The stronger theory includes the paradigm shift in impact strategies which we term three-dimensional approaches ('3D' for short) where the management and goals of real-world impact are put alongside risk and return. Investors have choices from one of two 3D approaches:

- **ESG core strategies** that exploit ESG issues through integrated ESG portfolio construction and active ownership; here the impact is *lite* in that it arises from collateral influences and is generally second order
- **ESG universal investor strategies** that aim for real-world impacts and better long-term financial outcomes through additional strategies in systematic engagement and more significant ESG allocation strategies on top of ESG core strategies; here the sustainability impact is termed *full* in that it is being directly targeted and accounted for.

Figure 4 – **3D framework – a straw model**

			Lite	Full-on
1	3D goals	The portfolio and strategy seeks to integrate risk, return and impact (= positive and measurable social and environmental impact)	✓	✓
2	Total portfolio thinking	Strategy is focused on producing long-term absolute returns contributing to the total portfolio risk and return consistent with goals	✓	✓
3	Strategic partnership	Adding IP to the AO outside the mandate; providing strategic input – investment strategy ideas, and reverse enquiry new mandate ideas	✓	✓
4	Core sustainability strategies	Integrated ESG and active ownership adding insight and engagement to support value creation, short-term and long-term	✓	✓
5	Impact strategies	Targeting and achieving real-world impact using UI strategies – portfolio and stewardship positions – including climate management		✓
6	System-level engagement	Addressing the systematic risk elements in their portfolios – climate change, financial stability, social stability		✓
7	Scorecard monitoring	Combination of hard and soft measures TCFD reporting	✓	✓
8	Other mandate details	External managers governance and culture Also termination, could involve closed-ended structures	✓	✓

Currently, most strategies fall into the lite area as they will focus on allocations to companies that have in the past performed well using ESG metrics. This is an approach focused on secondary market exposures which can produce only modest investor impact. By contrast, the full 3D strategy gives emphasis to achieving much more significant and intentional impacts, tapping substantially more into active ownership actions to manage sustainability change.

The full 3D strategy seems to imply some significant changes in the AO value chain. In this switch of emphasis towards building better beta there is a natural rise in strategic engagement (to produce the corporate change needed), strategic partnership (to support the innovation and idea generation needed) and engaging with coalition organisations (to mobilise more focus and action). This is likely tied in with changes in measurements which becomes more fragmented with balanced scorecards to keep score better, produce better accountability and align rewards.

In current practice for most mandates, these generally emphasise alpha measurement on relative risk and return over a three-year horizon. There is a time-horizon and goals mismatch here which may be difficult to address. Ideally, mandates should be focused most on absolute risk and returns and performance horizons of five to ten years and beyond and a well-designed scorecard should reflect this priority.

We refer particularly in this research to the AO challenge but include many issues of key relevance to AMs. First, AMs must design their portfolio construction by understanding the client mandate and interpreting the key differences between Strategic Asset Allocation (SAA) and Total Portfolio Approach (TPA) arrangements. Secondly, while most mandates are specialised and limit the asset classes to be used, in some cases AMs manage multi-asset mandates in which either SAA or TPA arrangements can be applied. The multi-asset mandates where TPA may have merit include diversified growth funds, absolute return funds, target date funds in defined contribution mandates and Outsourced CIO (OCIO) mandates.

3D mandates will specify their targets for impact. In some cases, the impact will be the climate outcome that is sought, but in other cases may be goals that reflect other sustainability impacts. The globally agreed taxonomy for legitimate impact targets is the UN-sponsored listing of 17 sustainable development goals (SDGs).

There is perhaps more scope for the *lite* impact version of the 3D mandate to be integrated into both the financial and impact objectives. This less challenging model may result in it being more widely adopted than the *full* version, but of course the impact achieved will then be limited in scale and visibility. Many AOs currently prefer this approach to the more complicated *full* strategies.

We have a particular example of the *full* 3D mandate in the so-called 'race to zero' UN-sponsored initiative. Net-zero aligned mandates subject to fiduciary constraints must meet two goals – the normal goal of maximising risk-adjusted return and also the goal of aligning to climate outcomes in a strategy that is consistent with the transition to the zero-carbon economy. This transition is generally projected to the date 2050, and therefore represents a very long-duration journey, although with earlier milestones and a particular goal around 2030.

The 3D framework can embrace both active and passive mandates where passive mandates may take active positions in engagement and use benchmarks that have strategic tilts / exclusions versus market-cap. Passive here can be a misleading description for the rules-based strategies that are represented by various indexes both in mainstream ESG mandates and in Paris-aligned strategies. These strategies are active in both their allocations versus market-cap indexes; and their ownership activities and active management is central to a healthy investment ecosystem both with regards to price formation and forms of effective engagement (including activism).

The Group, while seeing the merits of the 3D investment framework, saw the need for quite significant changes if their organisations were to make this transition. 85% of relevant individuals in the Group saw the gap to be bridged as moderately large or very large, confirming that there is plenty of work to be done on this model.

Universal ownership theory

Universal investors (UIs or universal owners) are generally defined as very large investors that own a slice of the world economy and world portfolio and with it a slice of all corporate externalities. Their mindset is to aim to achieve real-world impacts on the environmental / societal system and to obtain better outcomes for beneficiaries by taking a joined-up approach to managing longer-term risks, particularly externalities. The Group developed some comfort with the following taxonomy for universal investors in four parts:

1 **A small number of investors are full UIs** – they are very large, long-term and leadership-minded AOs and, as a consequence, are deliberate in their commitment for impact ('intentionality') through their ability to produce positive system effects ('additionality') – we suggest the minimum assets under management for such an AO might need to be US$200bn, and we believe there are about ten AOs in this group with total assets of about US$6trn.

2 **A slightly larger group of AOs by number selectively employ UI strategies** – these are large and impact-minded but not quite so large or as committed as the full UIs and so they can only be effective in some impacts and in some mandates, particularly in collaboration with larger asset pools. There are about 100 AOs in this group and we suggest their asset size is not the main issue, it is influencing capital sourced from financial capital and political capital; this group also totals about US$6trn.

3 **A larger group of AMs by number selectively employ UI strategies by delegation** – these are impact-minded and can be effective in impacts through their larger asset pools. The AMs in this group are motivated by mission, values and beliefs considerations but require the AO mandates for full conviction.

4 **All other investors, the vast majority, are non-UIs** – they may be deliberate in recognising and reporting on impacts, but without intentionality to act to impact the system. They are free riders that benefit from UI actions.

We suggest that success with the universal investor model and the 3D arrangements will depend on successfully working with long time horizons and a more complex measurement framework. The measurement challenges arise from the difficulties in reporting highlighted in the double materiality discussion[13]. Investors have to come to terms with measures having validity issues, which no amount of hard work can overcome. This suggests that investors have technical, governance and cultural challenges to produce data management excellence.

Funds and mandates must specify these impact goals and then manage the process of meeting them. We suggest that the accomplishment of two goals (risk-adjusted return and impacts) is akin to working on two objective functions and calls for joint and separate organising principles. We mean by this that each goal needs some separate attention, but attention must also be paid to considering them together. While some investment organisations might wish to manage one process that manages an optimisation across risk, return and sustainability, it is doubtful that this is practicable given the distinctly different nature of financial risk and impact.

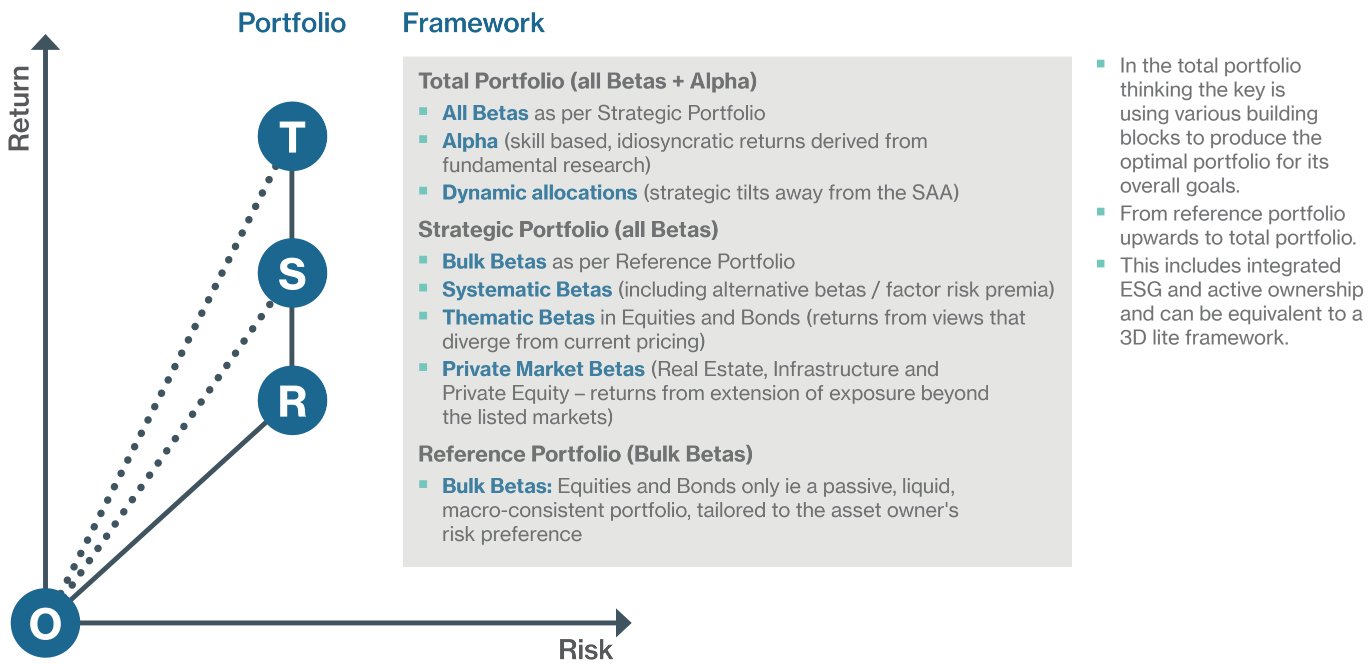
"We suggest that success with the universal investor model and the 3D arrangements will depend on successfully working with long time horizons and a more complex measurement framework."

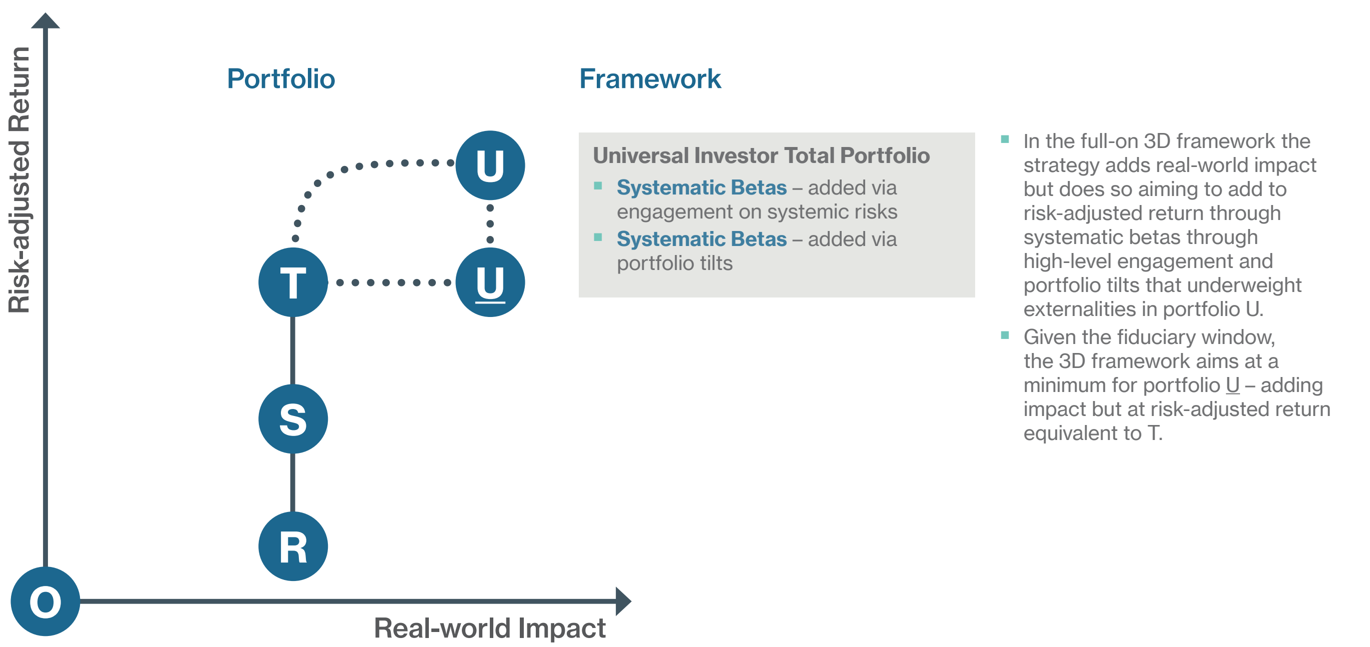
[13] Double materiality is both the materiality of ESG-related impacts on the company but also impacts of a company on environmental and social or any other dimension of sustainability.

A relatively simple joint organising framework is shown below in Figure 5. Here the two parts of the goals are mapped. First, the risk and return optimisation is covered. Second, there is a risk-adjusted return and impact optimisation. The fiduciary duty test is a critical consideration. The key test is whether the impact activities in the second part of the chart will reduce the risk-adjusted return. This is where the universal investor opportunity can be additive to risk-adjusted return via in particular better beta using systemic engagement to derive the long-term benefits of reducing systemic risk.

The Group, while seeing the merits of the universal ownership approach, saw the need for quite significant changes if their organisations were to make this transition. Two thirds of relevant individuals in the Group saw the gap to be bridged as moderately large or very large, and no individuals saw no gap at all, confirming there is plenty of work to be done on this model too.

Figure 5 – **Total portfolio framework and 3D frameworks**





Total portfolio approach

AOs have tended to adopt relatively static approaches to asset allocation and portfolio construction, based around a SAA or ‘policy portfolio’. While there are various reasons for this practice, we argue that investment efficiency is not one.

The investment drawbacks of SAA are principally due to there being a looser connection between the resulting portfolio and the fund’s goals and how these change over time, combined with a slower and more constrained decision-making process.

In the working groups, there was strong support for a switch of thinking to better connect the total portfolio with the fund goals. Such thinking leads to an alternative approach to portfolio construction, in which the central theme is to construct the portfolio of assets such that there is a continuous and dynamic focus on achieving explicit objectives. Such thinking has been embedded in alternative methodologies which are referred to collectively as total portfolio approaches.

The acceptance of SAA approaches in the industry has been relatively strong. But the movement to a 3D investment framework is certainly misaligned with the use of SAA whereas the total portfolio methodology is aligned. There are governance challenges in transitioning to this approach, but the net benefits make it important that these challenges are tackled.

One of the key tools in this transition is moving to a scorecard approach to assessing process and portfolio quality. The parameters of these scorecards are discussed in detail in specific research on total portfolio methodology[14].

“The acceptance of SAA approaches in the industry has been relatively strong. But the movement to a 3D investment framework is certainly misaligned with the use of SAA whereas the total portfolio methodology is aligned.”

[14] It’s about time | TAI | 2021

Supporting polling data

A significant number of the Group members identified the gap between an ideal state on 3D investment framework and Universal Ownership strategies and their actual state as moderately large with the gap on total portfolio approach (TPA) and ideal investment model as a smaller gap.

The survey results indicate that required change capability in terms of the skill-set and mind-set is only partially in place in 80% of the Group's organisations. With a minority of 13% having this substantially in place.

"Total portfolio thinking was identified as the investment model change that is likely to deliver the most benefit to the investment industry with 3D investment framework closely following."

Table 7 – **Polling data**

	There is no gap	Small gap	Moderately large gap	Very large gap	N/A
The gap between our ideal state on TPA and our actual state is..?*	7	**40**	13	20	20
The gap between our ideal state on the 3D investment framework and our actual state is...?*	0	13	**47**	20	20
The gap between our ideal state on universal owner strategies and our actual state is..?*	0	27	**33**	20	20
The gap between our ideal investment model and our actual investment model is..?*	0	**33**	27	13	27

* This question is for AOs and AMs that have fiduciary multi-asset roles, they do not fit AMs with specialist mandates, hence the N/A for not applicable

Table 8 – **Survey results**

The degree of consensus and alignment in my organisation of these model issues and gaps is...?		The degree of change-capability (skill-set / mind-set) we have to make these investment changes in my organisation is...	
None at all	0%	Fully in place	0%
Small	40%	Substantially in place	40%
Moderately large	**53%**	**Partially in place**	**80%**
Very large	7%	Not at all in place	7%

Of these investment model changes, which does the investment industry stand to benefit from substantially?	
Total portfolio thinking / methodology	**87%**
3D investment frameworks	73%
Use of systems-thinking	67%
Universal owner theory	80%
Other (please specify in the box below)	0%

Section 6: The change model

Principle 7: The three areas of change – business, people and investment – need to be undertaken and delivered together with significant change required across all three.

Principle 8: Various enablers are needed to successfully achieve change: a strong organisational culture and the right skills and technologies together with a compelling vision, an aligned coalition and rigorous process.

Key change areas

The key organisational vision discussed as a collective straw model for AOs was the following:

1 The central mission [of the AO organisation] is sustainable long-term value creation for members and other key stakeholders

2 The vision is successfully managing risks and returns in the short-and long-term to achieve fulfilment and integration of stakeholder interests through internal alignment of board and management

3 Ancillary to this vision is applying integrated sustainability thinking and active ownership practices into all elements of the investment arrangements.

This exact model was extremely closely tied to the working group's vision (81% were well aligned or better with this). The context for the group was a stakeholder model which saw the investment industry have a principal focus on creating value for their end savers but also doing its fair share for wider society, defined by its capacity to contribute (mostly about resources and influences) and the moral incentive to contribute (mostly values and principles).

Given the core areas of change developed in chapters 2 to 5, how might we combine these into a 'change model'? And what are the enablers that need to be in place for the changes to be successful when the **context is constantly shifting?**

This involves considering some additional fundamental questions. What is the quantum of movement involved. What is the effort and time commitment required? Is there a natural sequence of change actions? What are the factors for any attempts to change to be successful?

To answer these questions, the working group conducted a unique study of their own businesses. The 20 members used case studies of their own organisations to design and shape the agenda for change they think they need to implement. To facilitate some cross-comparisons and aggregation of data they summarised their answers using the change areas and enablers below, in the form of a dashboard.

Table 9 – **Change areas and enablers**

	Change areas		Enablers
Business model	1. Multi-stakeholder ambition	**Culture**	A. Effective culture
	2. Net-zero ambition		B. Purpose-driven
People model	3. Talent / DE&I / superteams	**Skills**	C. Systems-thinking
	4. L&D commitment		D. Aligned thinking / governance
Investment model	5. Total portfolio thinking	**Technologies**	E. Change-capability
	6. 3D investing framework		F. Effective technology
	7. Universal ownership		G. Collaboration commitment

As an overall comment, the change plans prepared by members were both highly aspirational (with ambitions to move significantly and across multiple dimensions) and highly holistic (with recognition of the need to address all areas and accomplish multiple enablers to achieve key goals). The common feature of moving up one notch, on a scale of one to five, can seem simply 'incremental' but when applied to multiple dimensions it would be transformational. The amount of resourcing required and energy consumed was captured in the timings where significant commitments where envisaged into a second year and even beyond.

In discussion it appeared that the Group was in some cases somewhat optimistic about their present status particularly when it comes to new dimensions like net zero, TPA and 3D investing and complex enablers like systems thinking, joined-up governance and technology.

The Group agreed that transformational change needs a coalition of leaders to come together with respect to a strong vision. While it was seen as a difficult task to create the compelling vision, it was not thought that building the coalition would be the hardest task.

It was accepted that the organisations needed to be joined up in all parts of the enterprise to carry off a successful change programme. This entailed close coordination with the multi-stakeholders using a worldview and version of the 'truth' that was right for everyone. Therefore, the big emphasis on systems thinking and systems leadership resonated across many members because these carried precisely the requirements for this collective commitment to be present.

A few specific points stood out on individual change areas:

- There was a surprisingly positive view of the importance of universal ownership while recognising this would involve considerable influencing work to gain traction
- There was a notably positive view of needing Superteam capabilities which is premised on the size of the organisational challenges involved
- There was a disinclination to be focused on a select few areas in the plans, all members saw the inter-connectedness and so emphasised the need to work on the multiple challenges together. The principle of 'good enough' was not being applied
- The investment value chain was given significant focus, particularly the combination of strategic corporate engagement, strategic partnerships and engaging with coalition organisations all brought together in balanced score cards (to produce better accountability and align rewards)
- The net-zero target scores averaged over four out of five. These are significant new commitments for all given that net-zero positioning has been developed so far in just the last 12 months.

Enablers

A few specific points stood out on the enablers:

- The commitment to enablers was essentially the same scale as for the change areas themselves and by their nature they need working on right up front
- The full set of enablers covered effective culture, purpose-driven, systems-thinking, aligned thinking and governance, change-capability, effective technology and collaboration commitment
- The link between culture and sustainability was emphasised in the plans. Organisations that have a strong purpose-driven culture have had natural advantages in succeeding with sustainability and stewardship. It may be that the world's current vulnerable state will also work in the opposite direction and make sustainability a force for stronger culture
- The cultural factors also connect strongly with inclusion and diversity; the innovation to make change happen and stick; purpose; and collaboration: cultural values needed to capture the combinatorial benefits of co-operation and inter-dependence, both within organisations and across organisations in 'co-opetition' situations
- The area that seemed under-discussed was technology disclosing a lack of comfort with what progress and success look like.

The other enablers relate to the how of transformational change where the Group agreed on this set:

1. **Higher purpose**. *Change is far more likely to gain traction if there is a compelling vision that inspires confidence and awe*
2. **The soft stuff is the hard stuff**. *Building leadership coalitions is really important, and new coalitions need to be created through the programme, as faces will change*
3. **Project / programme management is a highly specific skill**. *Disciplined project work in change programmes is essential*
4. **Let go of the past**. *The status-quo bias, while extremely difficult to move, does need to yield to both unlearning and learning*
5. **Innovation as a strategic capability**. *Innovation is a central plank to any successful value creation in the change area*
6. **Systems leadership**. *The importance of leadership to change cannot be underestimated, but it is a particular type of leader that can inspire a sense of being part of something much bigger than themselves and something that is extremely meaningful.*

Supporting polling data

The following polling data provides an insight into the Group's views on the change model.

The Group sees resourcing and process as the biggest obstacles to successful organisational change.

Aligned organisation and value chain and net-zero emissions, pathway were identified as the most resonant elements in the Group's vision 2023. 3D investment model and managing and influencing risks were also highlighted as important.

Table 10 – **Polling data**

In respect of your agenda for change at your organisation: where do you see the biggest obstacle to successful change?	
Resourcing and process	**50%**
Vision and its socialising	20%
Culture and legacy issues	20%
Leadership coalition	10%
Other	0%

Which of the elements of a future vision are most resonant?	
Aligned organisation and value chain	**82%**
Net zero emissions pathway	**82%**
3D investment model	64%
Managing and influencing risks	64%
Bigger societal role	55%
Co-creator of new wealth	27%
SDGs using universal ownership	27%

Section 7: Conclusions

The issues we are facing are multi-faceted, complex and contested. The Group's coverage of these issues was broad and deep, brought clarity and we appreciate their insights.

The key conclusions were these:

- **Purpose and vision** – Multi-stakeholders increasingly frame asset owner direction of travel. Societal context has changed, stronger stakeholders have emerged, investor goals have multiplied and shifted. Solidarity and collective action are increasingly favoured with systems and strategic leadership being critically required
- **Investment conventions** – Risk intelligence and real-world impact need to reach new levels. Investment practice is shifting, with value creation seen differently, particularly on sustainability in ESG, active ownership. Total portfolio thinking, 3D investing and universal ownership together define a stronger investment framework
- **Infrastructure** – Asset owners' infrastructure critical to deliver change but the soft stuff is the hard stuff. Investment infrastructure critical for success – thinking and practice, reporting and data, resourcing and collaborations. We need Superteams that capture diversity, culture and governance excellence; and the stronger value chain that will come from stronger mindset and relationships
- **Holistic picture** – To effect change on the scale suggested, the leadership needed is holistic and strategic. Successful change is premised on articulating a strong and compelling vision plus building a leadership coalition of board and executive stakeholders plus applying a disciplined change process that works on multiple strands.

"The whole context of the industry is most certainly shifting and the current configuration of the investment ecosystem does not seem to work given the changes taking place."

The whole context of the industry is most certainly shifting and the current configuration of the investment ecosystem does not seem to work given the changes taking place. A significant shift to consider wider stakeholders, modernise thinking and incorporate sustainability issues is critical to stay relevant and resilient.

Making certain changes offers the chance of creating a bigger and better industry where there is alignment to stakeholder goals and protections from systemic risks, notably climate change. Investment organisations need to adapt at a speed and scale to match the increasing uncertainty and complexity around them. With change on the outside happening at an accelerating pace, it becomes critical for investment organisations to adapt in all major areas – business, people and investment models – in order to fulfil their full potential.

How will the change model progress? We have three high-level points with which to conclude.

First, we suggest AOs and AMs can and should play a bigger societal role through systems leadership aligned to inner stakeholder wishes and wider stakeholder needs. Second, the AOs and AMs need to be collaborative organisations that value teamwork and inclusiveness and are effective and influential in the value chain through various engagements / partnerships. Third, the advancement of the investment model involves a paradigm shift[15]. Essentially the narrow *alpha* and *beta* paradigm needs to move to a *sustainable value creation* paradigm which is reflected most through 3D investing.

This takes us from risk and return only to real-world impact, whereby the well-integrated 3D investment model is aligned to net-zero emissions and Paris in both portfolio and operations. In addition, there is a close link to working on universal ownership principles and impacts on the SDGs as well as the successful management of all risks with particular coverage of, and influence over, systemic risk.

[15] Paradigm shifts involve a fundamental shift in how people think and get things done that replaces a prior version.

We note a congruence in the need for AOs and AMs to change in similar ways for there to be overall success. The key reason for this is that AOs have heavy dependencies on AMs to achieve their goals and the degree of philosophical agreement and cultural alignment will act to create more effective arrangements. Investment organisations cannot manage their way to this desirable future using forms of incremental change. Instead, transformational change is needed, with approaches that are more substantive, co-ordinated, agile and time-intensive. We look forward to studying this in IOOT22. Where IOOT21 was about *laying the foundations* for change, IOOT22 will focus on the *execution of change* and will produce a *roadmap for change*.

In conclusion

Through the skill and diligence of the Group we have created a vision following the key steps of developing a narrative and a set of principles. We believe the narrative is transferable to others in the industry and supports socialising the Group's thinking in other contexts. Similarly, the principles can be transferred as open source materials to support the application of the thinking in other contexts. In so doing, the Group has accomplished its specific goals of providing transferable intellectual capital to benefit the industry and its end savers.

In this paper on 'an agenda for change' we define broadly what changes are needed at a foundational level. We suggest further work is now required to consider the execution issues to successfully complete the agenda for change, the subject of our next target for research in this field.

Appendix 1: Principles

Eight high-level guiding principles for transformational change

System-wide framing	**Principle 1 : Investment organisations should be holistic and systems-savvy in approaching change.** ▪ This involves integrating perspectives from the big picture (covering the social and ecological environment) and the detail of the investment industry (covering the organisations and their people, their incentives and other influencing factors) ▪ This advocates for employing systems-savvy leadership that finds collaborative solutions to complex problems framed by a joined-up view of the systems of which they are a part ▪ Systems thinking is an essential method of combating unintended consequences when taking actions and interventions by recognising the ripples in the financial ecosystem.
Business model	**Principle 2 : The purpose of investment organisations is shifting in the direction of a multi-stakeholder orientation in which wider stakeholder interests are factored into activities and decisions.** ▪ A combination of systemic forces – social, cultural, institutional and regulatory – are creating this direction of travel ▪ The organisation must be responsive to changes in these forces and be prepared to adapt its purpose over time. **Principle 3 : The priorities and boundaries to the business of the investment organisation need to be clearly set and communicated through identifying stakeholders with accompanying goals and accountabilities.** ▪ With a wider range of stakeholders involved, the management of stakeholders becomes a bigger priority ▪ While more stakeholders may press their concerns onto AOs, retaining a realistic focus on your purpose and influence is important; so exercising realistic boundaries to your mission is important.
People model	**Principle 4 : Investment organisations have a significant opportunity to apply Superteam principles to how teams are organized and function.** ▪ Exploiting the influences of culture, diversity and execution skills to create exceptional conditions for better outcomes ▪ Evolving teams into more devolved and networked groups that carry more distributed power with tighter goals and better-defined accountabilities ▪ Investment organisations have a significant opportunity and imperative to reimagine and reconfigure work given changing context by demonstrating greater leadership, co-ordination and empowerment.

Investment model	**Principle 5: 3D investing frameworks can and should be created that balance the risk, return and impacts of strategies.** ▪ The key objective in the 3D framework is to integrate risk and return with impact, giving separate attention to both elements while satisfying a strict fiduciary principle to add impact with no concession to the risk-adjusted return ▪ This framework will always include core sustainability and impact strategies and scorecard reporting. In its fullest form, it will be likely to include total portfolio thinking, strategic partnerships and universal investor strategies ▪ Building better beta, via significant active ownership and public policy engagement, is critical to 3D frameworks. **Principle 6: Total portfolio approaches support the integrated thinking that is needed for the achievement of sustainability within fiduciary constraints.** ▪ The application of total portfolio thinking to the 3D framework is essentially allowing for all the above features in a competition for capital that is sensitive to shorter and longer time horizons and fitting the needs of 3D mandates ▪ The use of a scorecard for 3D mandates helps support the strategy determination and the reporting and accountability. This involves portfolio quality being assessed as a combination of (1) risk / return efficiency; (2) other key factors like resilience, liquidity, costs, governance;(3) the addition of sustainability and impact metrics integrated into the scorecard.
Change model	**Principle 7: The three areas of change – business, people and investment – need to be undertaken and delivered together with significant change required across all three.** ▪ There is inter-dependence in this list, no one area is going to be as successful if any other area is not included ▪ The investment model is particularly strongly oriented towards an unlearning as well as a learning process ▪ The resources needed to carry out successful change will be substantial, but the rewards are commensurately sized. **Principle 8: Various enablers are needed to successfully achieve change: a strong organisational culture and the right skills and technologies together with a compelling vision, an aligned coalition and rigorous process.** ▪ The link between a certain organisational culture and sustainability commitment and effective practice is strong ▪ The influence of culture on change is considerable and for transformational change will be dominant.

Appendix 2: Stronger investment theory and practice

Stronger investment frameworks

Key areas	Stronger investment practice features
▪ **Value creation** is derived from the origination and implementation of beliefs in a portfolio allocation and ownership setting	▪ Value is created through disciplined implementation which is aligned to strong beliefs in both investment content pinpointing market efficiency and inefficiency and investment context derived from self-knowledge and knowledge of others
▪ **Risk** has multiple facets in which impairment to the mission stands out; risk is the fundamental building block to return both across portfolio and across time	▪ Risk is unique to each investor based on organisational, technical and behavioural factors with dimensions around time horizon and stakeholder goals ▪ Risk management across portfolios requires portfolio diversification ('portfolio quality'), risk management across time requires time diversification ('risk management plan quality') ▪ The risk management plan sets out a trajectory for risk budget size using time diversification and reflecting path dependency in risk capital and risk buffers
▪ **Long-horizon** investors possess flexibilities that short-horizon investors lack that can be exploited with mindset and implementation	▪ Long-horizon investors need to be disciplined in mind-set and dynamic in action to exploit good judgement with respect to prospective risk / return views ▪ Long horizon investment involves premia to be earned not endowments to be given
▪ **Sustainable investing** embeds the principles of long-term investing that is efficient, inter-generationally inclusive to stakeholders, and considers real-world impacts	▪ Approach sustainability from two directions: for long-term investing efficiency and for values and sense of responsibility ▪ Universal owner strategies aim to achieve real-world impacts on the environmental / societal system (sustainability impact) and drive better financial outcomes
▪ **Portfolio construction** is guided by capital and risk allocation through multi-faceted portfolio classification and a competition for capital and risk	▪ Risk buckets include asset classes, but other buckets matter – bulk beta, illiquid beta, smart beta, alpha, etc ▪ Allocation reflects portfolio quality ahead of optimisation via intended total risk / effective diversification, resilience, implementation and sustainability elements

Source: Strong Investment Theory and Practice | TAI 2016

The key differences between mainstream investment theory – essentially Modern Portfolio Theory (MPT) – and what we term system-thinking in investment theory are summarised below.

Key differences between mainstream investment theory

	MPT investment framework	Systems / 3D investment framework
Goals	▪ To produce maximum expected return given risk (volatility)	▪ To build portfolios and implement engagement that optimally meet given goals and trade-offs
	▪ Single objective and numeraire	▪ Multiple objectives and numeraires
	▪ All stakeholders see goals the same producing one efficient frontier	▪ Stakeholders may see goals differently requiring efficient frontier trade-offs in efficiency, resilience, sustainability, implementation
Assumptions	▪ Investors have rational expectations	▪ Investors have biases
	▪ Markets are efficient markets	▪ Markets are largely efficient
	▪ Risks are systematic and idiosyncratic	▪ Risks include wider elements, particularly systemic
	▪ Shareholders have primacy	▪ Stakeholders have priorities
	▪ Externalities are second order factors	▪ Externalities are first order factors
	▪ There is stability in assumption setting	▪ Assumption setting is inherently problematic
Strategies	▪ Policy, security selection contributing towards alpha and beta	▪ As opposite plus engagement contributing towards integrated value added
Arguments favour MPT	▪ Strong academic literature and endorsement	▪ Has much more limited academic support
	▪ Has straightforward quantitative framing	▪ Has complex quantitative framing
	▪ Has wider collateral support – lawyers, regulators, etc	▪ Has very uneven collateral support
Arguments favour 3D	▪ See risk unrealistically through volatility	▪ Sees risk realistically through multiple lenses
	▪ Deals with ESG and impact as extension issues	▪ Deals with ESG and impact as integrated issues
	▪ Omits consideration of externalities	▪ Addresses issues of externalities
	▪ Systemic risk exogenous – outside the framework	▪ Systemic risk endogenous – within the framework

Source: TAI 2021

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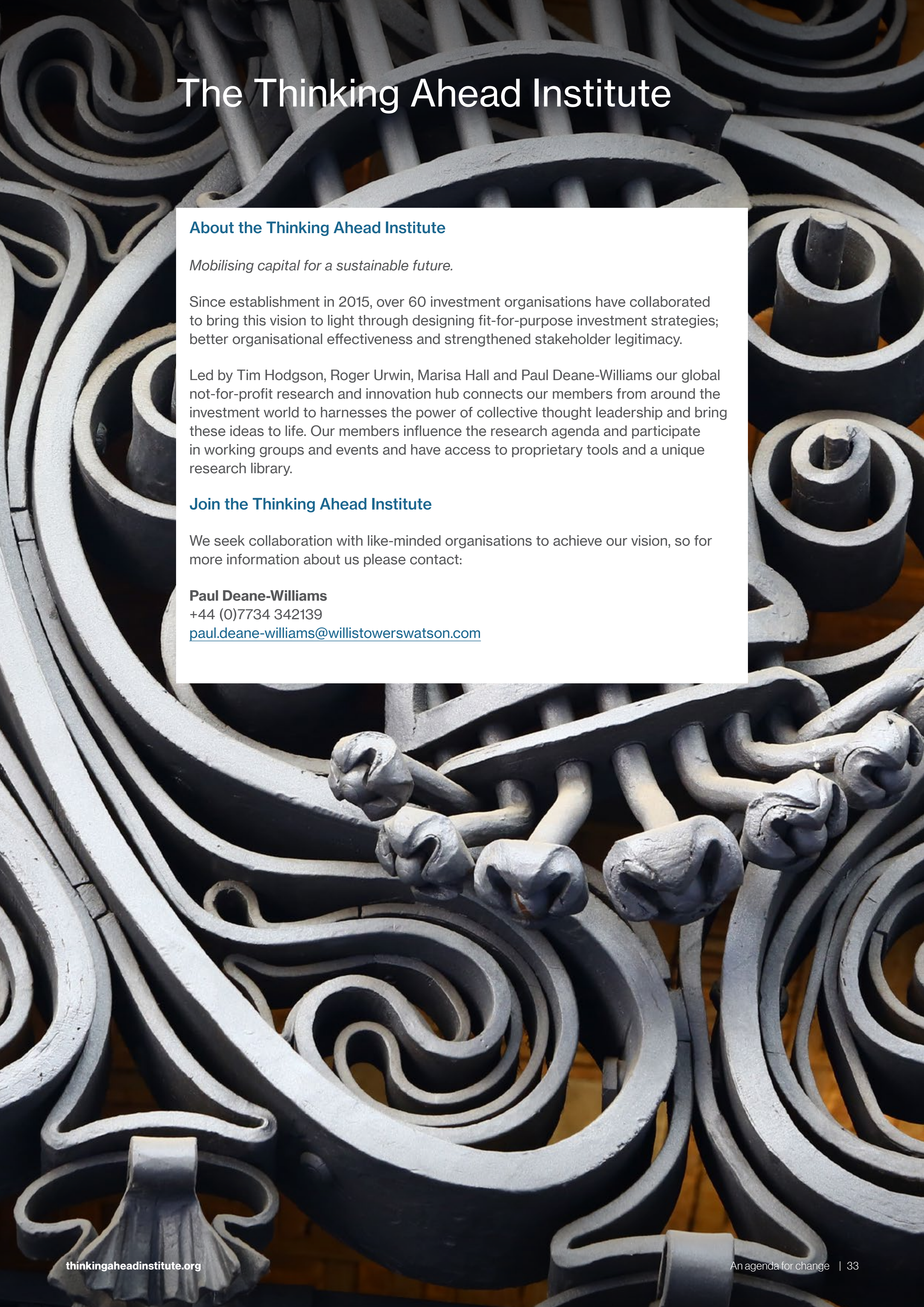

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