



LONG HORIZON INVESTING IN A SHORT-TERM WORLD

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GREAT INFLECTION POINTS: WHAT SHOULD INVESTORS DO?

- **Increasingly *Playing in a Crowded Sandbox*:** Chasing less compelling valuations as Alternative allocations increased, straining investment capacity
 - Global Alternative Asset Allocations increased significantly between 2004 – 2012, now representing up to 25-30% of institutional portfolios in US, Canada, Australia
 - Allocations to private investments provide increased diversification and higher potential return, realizing small-company and illiquidity premiums, but challenges are greater now
 - Yet, erosion of illiquidity premium in unlisted assets requires greater reliance on active management and reducing cost, so reliable sources of excess return more valuable
- **Innovation is accelerating by leveraging technology, but allocation of financing capital for private opportunities remains inefficient**
 - Direct private investing is ripe for those that are: nimble, flexible, disciplined, creative, long-term oriented, well-resourced, and well-connected
 - Asset Owners enjoy distinct advantages in sourcing compelling direct investment opportunities others cannot exploit easily or at much greater cost
 - Future Themes research helps direct our focus on favorable market tailwinds
- **Companies need patient long-term capital to build businesses, commercialize innovative ideas and unusual opportunities**
 - Asset owners are distinctly well positioned to play unique role in the real economy



“CANADIAN MODEL” SUCCESS

- **Success Built on Investment Innovation, Doing Uncomfortable Things**
 - What was new in the 1990s is now conventional, but capacity has lagged demand
 - Private allocations provided excess return with compelling diversification
 - Infrastructure, Timberland, Commodities, and Private Equity was underexploited
 - Benefits of past innovation eroding – overwhelming demand undermined illiquidity premium, so chase has gotten harder, yet still opportunities “between-the-cracks”
- **Economies of Scale Improves Access vs. Capacity Constraints**
 - Large sophisticated asset owners can tap into market inefficiencies others can’t, while Canadian “asset owners” reputation attracts unique private opportunities
 - Focus on reducing total cost from insourcing investment management and direct deal sourcing to reducing external management expense
 - Scale affords institutionally competitive staffing and affords skills needed for overall complexity – Ability to attract, retain, and nurture top talent increases with AUM
 - Unlisted, capacity constrained assets difficult to rebalance, accommodate cash flow
 - Outsourcing through Funds should have been cost effective, but expenses still high, capacity remains limited, and co-investing can be disappointing due to adverse selection, thus realizing size and illiquidity risk premium objectives still allusive



NEW DAWN AWAKENING ASSET OWNERS THE RISE OF LONG-TERM INVESTORS

- **Investment Capital Is Growing Rapidly, Straining Investment Capacity**
 - With scale, many now operating on commercial basis with longer horizons resulting in better alignment for exploiting unlisted inefficiencies, lower direct costs
 - Push into higher private alternative allocations could stall due to reduced illiquidity premium (stretched valuations, deal competition) and high management costs
 - Resistance to build institutionally competitive teams has severe adverse and unintended consequences; No room or patience for non-economic agendas
- **Longer Horizon Expands Opportunities, Increases Potential Return**
 - Yet, Too Many *Playing Not to Loose – Doing No Wrong* is not *Doing Right*
 - Natural long-term investors need courage to defy short-term behavioral bias and not be limited by uneconomic misguided constraints reducing flexibility
 - Short-termism, exaggerated risk aversion, new regulations, artificial constraints, and other behavioral biases are significant hurdles impeding exceeding objectives
 - Greater passion needed for growing great companies, building projects, exploring unconventional opportunities, all with a focus on a longer time horizon
 - Fear of direct/active investing raises cost of capital and lowers return potential; Market inefficiencies inversely correlated with investment quality



CANADIAN PENSION MODEL NEXT LONG HORIZON EVOLUTION

- **Extraordinary Results Not Possible by Ordinary Means**
 - Anticipate new investment opportunities and remain disciplined – If a strategy appears comfortable, time to stretch and explore new horizons
 - Adopt a well-defined, intuitive investment philosophy driving strategy disciplines
 - New approach to sourcing direct investment and co-investment opportunities
 - Promote a better understanding of good vs. bad “Leverage” and “Risk”
 - Embrace active management and direct investing – Don’t dismiss *efficient liquid strategies* and *Global TAA* to lever active return potential without leveraging risk
 - When capacity becomes strained, new *Alpha Engines* must be developed
- **Underexploited Edge for Asset Owners Pursuing Innovative Ideas**
 - Substantial advantage in long horizon investing underutilized because it is difficult
 - Still many opportunities overlooked “between-the-cracks” of traditional investments
 - Opportunities created by financial regulation, inefficiencies, distress, lack of creativity
 - Efficient access to long-term capital needed to accelerate and exploit Innovation, thus better/more efficient and flexible capital financing structures must be developed
 - Explore and understand impact of *Secular and Future Themes* – even if a guide

EASIER TO DO THE COMFORTABLE THING



What is the difference between a bleak and a bright future?

- Rapid innovation has fundamentally lifted our living standards
- Its persistence lies in entrepreneurship and free market incentives
- Potential economic growth of 2-3% is normal – return to risk capital rewarded incentivizing research, development, innovation
- Asset owners are well positioned to play a distinctly unique role providing adaptive long-term capital at critical stages
- Just because its hard doesn't mean we shouldn't try – somebody else's *New Normal* doesn't have to be our destiny



Investment Opportunity

The future may be better than you think – wide range of opportunities to be exploited

- Longer horizon increases opportunities between-the-cracks and potential return
- Need courage to defy short-term behavioral bias and not limit flexibility
- Need to “re-discover” pioneering spirit of active and direct investing