PORTFOLIO ADVISER

November 2021 | www.portfolio-adviser.com

View from the top Tassilo Seilern-Aspang, *Seilern Investment Management*

THE FAMILY WAY

Seilern Investment Management CEO Tassilo Seilern-Aspang discusses an honest approach to ESG, playing to your strengths as a business and encouraging a culture of healthy challenge

Julian Marr

Simply put, asset management groups can aspire to one of two goals – try to be all things to all people or focus on one thing and do it well.

Seilern Investment Management – which redefines the idea of 'selective' by boiling down its investment universe shortlist of global stocks to just 70 quality growth businesses, with no more than 25 high-conviction choices making it into each of its four portfolios – sits very much in the latter camp.

"Every asset manager faces different issues – you just have to try and use the skills you have to your advantage," says Tassilo Seilern-Aspang, who joined the firm as an analyst in 2010 and became a fund manager four years later, before being appointed head of research in 2018 and CEO last year. "Large listed players have a difficult time, for example, because you have to keep your investor base happy.

"Your plans need to be very well signalled and you constantly have to go for growth. Arguably, your main asset is your distribution channel so you try and maximise that, which inevitably means you try and compete on cost and size, and you focus on following the flows wherever they go. That changes the type of organisation you can be – and, if you fail, you have to move into M&A as you seek to grow."

For its part, says Seilern-Aspang, Seilern has been doing the same thing since his uncle, Peter – now chairman and CIO – founded the business in 1989. "Inevitably, we are quite good at what we do because we have spent a long time trying to get it right," he continues. "So, if you have, say, three or four years to produce something to compete with us in the quality growth space, you will be hard-pressed to come up with a really good product.

"Yet that is what the big players are constantly trying – and while their product does not have to be that good as it will naturally catch some flows, it does create certain challenges because, over time, investors can become disappointed with the average product quality a lot of very large houses offer.

"Added to that, the timeframes the management of listed businesses get to operate with are too short to make a difference over the long run.

"At Seilern, we have the luxury of being able to think now about things 10 or 20 years ahead. Yet, if you have an investor base that is remunerated on yearly performance putting pressure on management to set targets, and if you have a management team likely incentivised with a stock price and an average tenure of maybe seven years, you really do not have much time between devising a strategy, implementing it and reaping any benefits."

Nor do smaller businesses have it any easier, suggests Seilern-Aspang. "Barriers to entry are rising and rising, and so it is expensive to build up and then keep a good team," he says. "At the same time, the growing regulatory burden is making it harder and more expensive for smaller players to break out and build their own business – to build up the required track record and distribution channels, attract the right people and so on.

"That said, the place you really do not want to be is the middle because then you are caught between not having the size entirely to benefit from economies of scale and being too large to really focus on your product – hence why you are seeing so much consolidation in that part of the market. So, as I say, everybody has their own sets of problems to deal with.

"You have to figure out the strengths you have for where you are and how to

QUICKFIRE Q&A

What is the best piece of advice you have ever been given?
When I was still thinking about what career to embark on, a former portfolio manager recommended I read *Investing: The Last Liberal Art* by Robert G Hagstrom. It totally changed my view of what working in investment could be, and how intellectually rewarding it is.

What single issue should most concern investors at present?
Managing client expectations in a time when future returns are compressing. Generally speaking, asset prices have been rising faster than earnings so, while investors may feel richer, to a certain degree they are borrowing those returns from the future. I fear this may not be understood well enough.

Does anything about your job keep you awake at night?
Making sure there is little to keep me up at night is one of my main drivers. Luckily, at the moment, I sleep well.

What is your 'top tip' for investors to help them run a better business?
Focus on the long term and don't cut corners.

And what most excites you about your job?
Constantly learning, definitely. Investing is a fantastic place to be for curious people.

If you were head of the FCA for a day, what's the first thing you would do?
It's very hard to say – probably resign.

And what advice would you give to someone starting out in investment today?
Take your time to build your knowledge thoroughly. In the short term, you may feel you are progressing too slowly and falling behind but, over time, it will make you a much better investor. To be a good quality growth investor, you need a similar mindset.

View from the top Tassilo Seilern-Aspang, *Seilern Investment Management*

maximise those to tilt the odds in your favour. If, like us, you are relatively well-funded and you think long-term, you do not necessarily have to take every investor who wants a massive discount and you can just patiently build up your business. And, if you are in a position like that, you can be fairly well insulated against your own set of pressures."

Founder's dilemma

One particular issue facing a founder-led business, such as Seilern, is how to pass on the ownership flame without putting noses out of joint. "Part of the challenge for any founder is how to ensure your company outlasts you and works for the long run," says Seilern-Aspang. "The other part is how to ensure everybody is motivated correctly and prioritised appropriately.

"The issue that normally arises with a founder-led business is a natural tension between the founder, those who went on to build up the business and those who are running it now – in the sense of who is really entitled to how much? There can be different permutations of answer for different businesses but what is very unlikely is all three parties will agree on how much each of their contributions is worth.

"That, if you like, is the perceived power relationship between the different parts of the business, but then there is the legal element – who actually has the power to implement things? That will normally lie with the founder, who can either retire and try and hold on through that or look to sell up. And if they sell up, they might get a very good price but, inevitably, the other two parts will feel hard done by and demotivated and probably leave.

"That is why it is very unusual to see asset management companies sold for the right reason – they are normally sold because there is a mismatch, basically, between the legal power of the people selling and the de facto influence they have within the business. And, by the same token, asset management companies are rarely bought for the right reason – because most people who buy them should know this is the case.

"Nevertheless, they buy because they want to increase volumes or to feel like they are doing something – all the while keeping their fingers crossed. So, in that sense, selling is not really an option – and it is not anything that we as a family business ever wanted to do anyway. Instead we set out to break the usual power laws you see within an asset management business and just made every person in this company a shareholder."

THE NAME OVER THE DOOR

Is there an added governance consideration when a founder has their name over the door? In other words, might staff be less inclined to challenge them and, if so, what processes does Seilern have in place to guard against such a possibility? "You need to think about this from many different angles, not just your internal legal and compliance culture and how that is run," Tassilo Seilern-Aspang replies.

"You also have to consider remuneration, alignment of interests – basically that you eat your own cooking – and your non-executive directors and board composition and how you manage all that. And then, to a certain degree, you need to encourage subversion within the team because one of the worst things that can happen to you as a manager is you end up surrounded by sycophants.

"If you end up in an ivory tower where you do not know what is going on and you do not have people tell you that you are being an idiot when you are being an idiot, that is the beginning of the end. Somehow you have to try to encourage within the rest of the organisation a degree of healthy challenging and dissuade people from not wanting to confront you with uncomfortable truths.

"Having said all this, we are a family business and we have been quite open about having no intention of relinquishing control of the business – and we think that is a good thing. Oddly enough, I have just finished writing a newsletter on the merits of investing in companies with dual-class share structures and the conclusion – and why we often do not vote against them ourselves – is the structure itself is not necessarily good or bad.

"The bigger question is how the structure is being implemented and the people behind it. Disproportionately empowering the 'right' type of owners – those looking to manage the company for the long run and in the best interests of stakeholders – is better than having poor managers or people with a very short time horizon. Ultimately, though, transparency is key because you need the end-investors be able to form their own opinions."

Anyone aspiring to create an asset management business for the long run cannot build it on individuals such as star fund managers, argues Seilern-Aspang. "You need to build it on a process and the remuneration structure must clearly reflect that," he continues. "You cannot say you will build on a process but still have the managers of the largest fund take home the largest share of the profits.

"So our fund managers have the same remuneration package, as it were, even though one may manage \$100m (£73.4m) and another \$2bn – and that is accepted because it is accepted the process drives the output; that the decision-making process is collegiate; and their contribution is the same. That makes the business less dependent on individuals and also takes a lot of the pressure off the fund managers.

'ASSET PRICES HAVE BEEN RISING FASTER THAN EARNINGS SO, WHILE INVESTORS MAY FEEL RICHER, TO A CERTAIN DEGREE THEY ARE BORROWING THOSE RETURNS FROM THE FUTURE'

"Then, no matter how many owners retire, since the lion's share of the profits is always spread across the team, you create that stability, which should allow for a smooth transition from one controller to the next. That, of course, is just about the profit pool – on the control side, we are very clearly a family-controlled business with partners and we have a very long view of how we want to manage things.

"So we are very patient, thinking in terms of decades and seeing our role as a neutral mediator between the existing shareholders. We are looking to ensure things are managed fairly and for the long run and that one group of shareholders does not abuse its position and try and to pull the rug to their side and knock the whole system out-of-kilter."

Talk about evolution

Clearly the Seilern team believe they have found a way of doing business that works well and are sticking by it, but how can they be sure any investment philosophy remains fit-for-purpose? Does it evolve? "The philosophy does not evolve but the process will," clarifies Seilern-Aspang. "Indeed, it is constantly evolving because you make mistakes through the years and then you fix them – you have to be constantly averaging up.

"It is a very simple philosophy: look

to identify good businesses that grow – where you have a high chance of calling that right and forecasting it for the long run – and then you hold them and let them drive the earnings for you. Most businesses – though not all – will undervalue longer-term cashflows so, if you buy and hold, you have a relatively high degree of certainty they can grow for the long run and that will drive your future returns.

"That philosophy and the core principles of our process – arriving at the Seilern universe of stocks our managers can invest in – are absolutely immutable. What changes, though, is the environment you are in and then obviously you need to adapt the process to that. New types of businesses arise and we try and find the best ones that fit into our investment philosophy, and construct our portfolios accordingly.

"But adapting to circumstances is not the same as compromising or changing our investment style, it just means the implementation will yield a different crop of investee companies and we must constantly learn about all the new developments. We look to keep everybody on a steep learning curve and put them in an uncomfortable position – in a way they can handle, of course – because that is how you learn the most.

"Our philosophy is set in stone, our process – in terms of what it is trying to achieve – is set in stone, the implementation adapts all the time and the output probably changes the most because it is a result of what the economy can offer us – and that changes. As such our track record – insofar as anyone's track record is worth anything – will not necessarily be much of an indication of how the funds will behave in the future."

Turning to the future of asset management as a whole, Seilern-Aspang worries that while "the general education level for maths is too low and many things are done that are mathematically unsound", the sector is the opposite. "The asset management industry has become increasingly obsessed with statistics and what is measurable," he says. "And within the 'what is measurable', it is not taking into account the quality of data.

"I see it, for example, in the CFA curriculum, in the dominance of modern portfolio theory, in the approach of the regulator and in the real weight quantitative risk management has in the whole risk management process. And the fact this is now received wisdom and the self-perpetuating way the industry is educating new entrants is a problem because, from an accounting point of view, the quality of the data is getting worse."

The reason for this deterioration in data quality, Seilern-Aspang argues, is businesses are becoming increasingly intangibles-based and thus much harder to value. "Both tangibles and intangibles have ways of being capitalised onto the balance sheet and that can definitely create opportunities," he goes on.

"But as the industry goes more and more the way it is, I see a problem arising for companies like us.

"We put all our resources into making a qualitative assessment of businesses and the cashflows they generate but then there is increasing pressure to overlay a quantitative risk management process, which totally subverts everything you have done. Yes, comfort can be drawn from numbers because they are fixed but, if the quality of those numbers is low, you are just fooling yourself that risk is being managed.

"And I think the industry has gone too far down that route – from individual investment analysts all the way up to asset allocators, risk managers and the way the regulator thinks about all this. I am not saying it does not have its uses – just that the way it is being implemented has surpassed the utility that can bring.

"This industry has become overly reliant on statistics and ascribes to them more than they can actually deliver." **PA**

CALL OF DUTY

There is something about Tassilo Seilern-Aspang's sigh when asked about ESG that makes his reply all the more authentic – not always a quality that goes hand-in-hand with the subject. If the guiding philosophy at Seilern Investment Management was formulated at a time when responsible investing was very much in its infancy, how does the company square it with the recent and increasing focus on ESG considerations?

"The ESG question is a huge and challenging one but my main concern is that a lot of the associated issues have become very reductionist," Seilern-Aspang replies. "As such, many situations where you might think reasonable minds could differ have been turned into binary outcomes, with an apparently clear right and wrong, while very complicated questions are put to fund managers as if they were even in a position to answer them.

"Conflicts of interests that inevitably arise with ESG have just been papered over with the statement that what is good for ESG is good for performance – which is not, in my opinion, a self-evident truth. Also, for there to be no conflict of interest, that would need to be true in all instances, which it certainly is not. And, obviously, you are putting together as one thing three vastly different subjects that all have their own specific nuances."

For Seilern-Aspang, the most important question for asset managers here is where their fiduciary duty actually lies. "If you are not an impact investor and you accept situations will arise where a decision that is good for ESG – whatever that means – lies in conflict with driving long-term risk-adjusted returns for your clients, you have to accept one of two possibilities," he reasons.

"You are either going to be acting in the interests of ESG and to the detriment of your clients' long-term interests – so do you have the mandate for that? And if so, if you are not an impact fund, how is that manifested? And if you do not do that, are you willing to accept the consequences that you are acting against ESG? At the moment, almost nobody talks about this.

"Instead, it just feels like a tidal wave of marketing materials and platitudes. I am not questioning people's intentions, I just fear some very complex issues – scientifically and on many other fronts – are being reduced to fewer variables than is required to address the matter and that problems are being posed to people who are not necessarily in a position to solve them."

So where does that leave Seilern? "We have always looked to invest sustainably in the literal sense of the word," says Seilern-Aspang. "We are looking for companies that can sustainably grow their earnings and so, obviously, anything that stands in the way of that is a problem. A lot of ESG considerations will be covered as an output of that, if not as a specific intention.

"We do actually score very well on ESG but we are trying to come at this in an intellectually honest way. And it may be we have to carve out a space that makes it clear there are certain situations where we may vote against best practice on ESG because we consider a conflict of interest arises – that our fiduciary duty lies on the side of returns and that, unfortunately, is the way it has to be as we cannot be all things to all people.

"Of course, every fund manager who is not an impact investor is in the same situation but nobody speaks about this. And we understand – nobody wants to be an anti-ESG torchbearer. We certainly would not want to be. But neither do we want to be the tool of anyone trying to use the money our clients have asked us to take care of and suddenly do something outside the conditions we have set for managing that money. We do not have that right."

Reproduced with permission by Media Licensing Co. (www.medialicensingco.com / + 44 (0) 20 3773 9320). Not to be reproduced without authorisation.