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David on David: Ten Lessons from the Life & Legacy of Yale CIO David F. Swensen

David M. Darst

Senior Advisor

The brilliantly innovative and profoundly humane David Frederick Swensen (1954-2021) was a legend in the investing world – a pioneer who played a preeminent role in the growth of Yale's endowment from $1.3 billion to $31.2 billion as of June last year. David served as Chief Investment Officer of the Yale University Endowment for nearly four decades.

As an insightful friend, a frequent collaborator in our early days of undergraduate teaching together at Yale College, an author of *Pioneering Portfolio Management* (2000) and *Unconventional Success* (2005) – indeed, David has endowed the financial world with numerous investment principles, ten of which are set forth below.

1. The Critical Importance of Asset Allocation

Asset allocation consists not only of: (i) diversification (meaning having uncorrelated assets, assets that are not all highly correlated with one another); it also includes (ii) rebalancing asset emphases when valuations of quality assets become egregiously expensive or egregiously cheap, and certain asset classes thus come to represent too high or too low a share of the overall portfolio; and (iii) risk management, meaning paying attention to the risks, as well as the return, of investments, therefore taking steps when appropriate to avoid, hedge, or offset such risks.

2. The Fetish of Liquidity

Partly inspired and illuminated by his Ph.D. thesis advisers - Yale Professors James Tobin (1918-2002) and William C. Brainard (b.1935) - David sought to emphasize asset classes that could be expected to generate higher rates of return over the long term, in return for giving up some meaningful degree of short- and intermediate-term liquidity.

The two Davids (myself and Swensen), pre-Covid in early spring 2020

3. Be an Owner Rather than a Creditor

During David's stewardship, the Yale Endowment has tended to avoid low expected return asset classes in the fixed-income and short-term money market realm, in favor of higher expected return asset classes in U.S. and non-U.S. equities and especially, within the alternative investments universe.

4. Consider a Judicious Approach to Diversification

One method favored by David (and there are several, each with their own advantages and drawbacks) involves dividing the portfolio into approximately five or six parts, and investing roughly equal amounts in each.

5. Discipline

Having devoted sufficient time and resources to the formulation of an investment philosophy, investment strategy, and investment tactics (which he pointed out that it is vitally necessary to do), David felt it is important not to deviate from well-thought-out plans in response to the whims and vicissitudes of fluctuating economic circumstances and financial market conditions.

6. In-Depth Probing and Creative Research

Before deciding to invest, and even after having made an investment, David espoused conducting a great deal of quantitative, qualitative, and multi-point investment research to gain and maintain true insight into a proposed investment's dynamics, degree of uncertainty, competitive position, time horizon, upside potential, exit strategy, and possible worst-case outcomes.

7. Decisiveness and Resolution

Constantly seeking to balance flexibility versus conviction, David valued the ability, the willingness, and the resources to take advantage of opportunities created by short-lived price dislocations that were 2-3 standard deviations or more away from normal. A widely-cited example involves David's calling the Yale Investment Committee together to increase the endowment's exposure to U.S. equities immediately following the -20.4% S&P 500 market crash on Monday, October 19, 1987.

8. Critical Importance of Manager Selection

Constantly stressing the widening differential between first-quartile and third-quartile asset manager investment performance in such alternative asset classes as private equity, private credit, venture capital, hedge funds, and real estate, David devoted extraordinary resources to checking, cross-referencing, and re-checking facts, knowledge, and opinions about investment managers even to apparently small details. David also frequently stressed the great difficulty for mainstream investors to develop a reliable and judicious network of discerning references that could put them in a position to evaluate true manager skill.

9. Circumferential and Circumscribed Perspective

David placed great store in understanding the economic, financial, social, political, and geopolitical environment, even as he paid heed to Warren Buffett's famous dictum to "stay within your circle of competence."

10. Keep in Mind the Higher Purpose of your Calling

David was very proud that his efforts were ultimately in service of educating the next generation; all the while as he exemplified humility, he urged and encouraged a deep sense of humanity among the individuals whom he guided and mentored, expressing in a 2007 interview with The New York Times: "People think working for something other than the most money you could get is an odd concept, but it seems a perfectly natural concept to me."

Paraphrasing a Latin phrase read several times on the campus of Yale University: "*Floruit David Swensen, Floreat David Swensen"* - "David Swensen has flourished, May David Swensen ever flourish!"

David M. Darst, CFA, is a Senior Advisor and Chief Strategist to The Family Office Company and Petiole Asset Management, where he served as CEO until April 2020.

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