

April 2020

Preparing For Asset Raising In The Post-Pandemic, Recessionary World – Tip 1



Welcome to the first of a series of articles offering insights and tips to prepare money management firms for improving their abilities to out-market competitors and attract assets from sophisticated investors in the coming post-pandemic, recessionary world.

ASSET RAISING IN A 'RED LIGHT, GREEN LIGHT' TIME

In these unprecedented times there is, temporarily, no business as usual.

Many institutional investors have put their in-the-works portfolio manager due diligence efforts on hold, and there are too many distractions for them to even consider their pre-pandemic backlog of requests from new managers wanting to pitch for their business.

When it comes to asset raising marketing efforts money management firm owners find themselves in the unaccustomed position of feeling like being back in their childhoods in the game of Red Light, Green Light. You remember the game. A handful of kids stand at a designated starting line. Their goal is to be the first to reach a designated finishing line. One kid is assigned the role of 'stoplight cop'. She turns away from the kids at the starting line, calls out *Green Light* and the kids start to race forward. Next, when she wishes, she calls out *Red Light* and spins around to face the racing kids, who have to freeze in place. Anyone caught still moving is sent back to the starting line.

So, while money managers of all sizes continue to trade their portfolios their new business development sales marketing efforts are temporarily frozen in place as if *Red Light* was called.

What can be a productive use of the time for money management firm owners in planning and preparing for the future call of *Green Light* so that they are ready with improved abilities to out-market competitors once they are able to reconnect with prospective investors, reengage in the selling cycle and undergo what is bound to be stiffer due diligence vetting in the recessionary, post-pandemic market environment?

My 32-year-old financial communications and sales marketing consulting firm has worked supporting money management firm clients through hard times before. The 1987 crash, the yield curve inversion of 1994, the burst of the tech bubble in 2000 and the great recession of 2008 all had their challenges for money managers, particularly when it came to marketing their portfolio management services to sophisticated investors in the aftermath of these major market disruptions. The pandemic of 2020, with its two-fisted hit to health and economic well-being, both on a global scale, may take a longer time to resolve and sophisticated investors already recognize this.

It is my firm's belief that the family offices, endowments, foundations, institutional plan sponsors, investment consultant gatekeepers and some in the independent, fee-only financial planning/investment advisory business are going to become more picky in how they vet portfolio managers. They will require more information — both objective and subjective — for evaluating and passing judgement on each investment strategy being pitched to them. This will require more and better content communications from the money management firms seeking out new mandates from institutional investors.

So, over the coming months in this Harvest Exchange Asset Manager Marketing Hub column I am going to be sharing insights and tips that will help money management firm owners make productive use of their asset raising downtime and prepare for when the time returns for them to educate and persuade people beyond their current client base to understand and buy into how they invest.

Tip 1 - Improve Your Performance Attribution & Portfolio Characteristics Reporting

Restarting the economy in the yet to come receding pandemic and global recessionary environment is not something that portfolio managers or their investors have experienced before. Both the fundamentals and the technicals on most if not all holdings in portfolios have changed, in addition to portfolio performance.

We believe due diligence vetting will increasingly include more strategy implementation and portfolio characteristics questions for the investment management firm competing for a mandate from institutional investors. Money managers should assume they will be getting asked more detailed questions and prepare for this.

Today let's consider what sophisticated investors are likely to ask money managers that relates to performance attribution and portfolio characteristics reporting. Their due diligence vetting will undoubtedly include these questions:

Based on your firm's investment process and strategy implementation:

1. *Where should I expect to see your alpha generation coming from?*
2. *What characteristics should I expect your portfolio positions to have/share?*

Sophisticated investors will be looking for money managers not only to make statements about this, they will also be looking to see data-based documentation in monthly performance reports and in flipchart pitchbook content.

So, your money management firm should reexamine how it can develop and deliver data to better respond to these questions. This goes beyond simply tracking your performance data against a benchmark index or peer group.

Performance Attribution - Case example 1

My firm had a client that ran an emerging market debt strategy. They had good long-term performance but investment committee members at institutional plan sponsors had trouble understanding the complexities of how the strategy was being run. Behind closed doors they were discussing, debating and voting on whose investment returns in the emerging market debt space they felt were due to skill and not just luck.

Our client's investments were made based on its in-house quantitative and qualitative research and analysis. Working with the portfolio manager we determined that five key factors within their investment process impacted their returns: country selection, security selection, whether to buy in local currency or USD, duration hedging and cash hedging.

Since we know portfolio management and speak with portfolio managers as peers, the client portfolio manager and I got into a dialogue about how his firm believed that country selection analytics is the key ingredient to successful, risk managed investing in emerging market debt securities. *OK, I said, If your proprietary country selection analytics is really a key element of your competitive edge and alpha generation how has it looked when you chart performance attribution data to support this claim?* (I have to add as an aside here that Frummerman & Nemeth works with money management firm clients all over the country, and overseas. Much of the work we do is by phone and email.) There was silence on the phone for about 15 seconds. I thought I lost our connection. Then the portfolio manager said *It never occurred to us to run the data to see that!* They then did so and found we could depict yearly performance in a bar chart where each bar divvied up each year's returns attributions by the above mentioned five key factors.

What did the resulting ten-year bar chart depict? You guessed it, application of the country selection analytics contributed the most to its returns. Now there was data beyond just the line chart depicting the strategy outperforming the index. This important performance attribution chart became a centerpiece in communicating the demonstrated veracity of the subjective-based construction of the firm's portfolio management process.

Using this compelling performance attribution data in their sales marketing — along with the restructured long version storyline explanation that my firm crafted for them, improving their written and verbal beyond-the-numbers communications about how the firm assembled and managed its basket of holdings — the client started winning more new business from institutional investors.

Portfolio Characteristics - Case example 2

A family office client running its own managed futures strategy had different challenges. It had been running the strategy just for itself for three years. Other family office investors were beginning to ask about the strategy, inquiring whether they should consider investing in it. The family member/portfolio manager knew net performance put them in the top decile of CTA managers at the time but did not have the data analytics capability to demonstrate and document skill versus luck, and what key elements drove returns.

So, my firm counseled him to hire a specialty firm to conduct a performance attribution and risk management reporting analysis of the portfolio. We recommended a specific independent, employee owned shop that we knew had the needed depth and breadth of experience and expertise to 'look under the hood' with the eye of an interested but skeptical sophisticated investor and see what was what. The resulting report, in which the source of alpha was identified, helped focus the family office portfolio manager's thinking and gave initial direction as to what data and factors were going to be most relevant for bringing the strategy to market to family office investors.

The second challenge related to the fact that the portfolio manager invested in four asset classes: currencies, commodities, interest rates and equities. We determined that it was going to be important to include in the portfolio's monthly performance report a pie chart that showed the most recent month-end percentage weighting by asset class. We were asked to help research which fund admin firms they should consider. The client was an emerging manager. It did not need to pay for the most expensive of fund administrators, who are certainly appropriate for larger money management firms serving the larger institutional investors, but can be overkill for investment firms that are marketing to smaller sized outside investors.

This is the seemingly simple question I posed when speaking with small and mid-sized fund admin firm contacts: *Can you produce a monthly performance tear sheet for the client with the requested 4-slice pie chart on the lower left corner of the cover page?* Some said they could not even generate the data based on the portfolio manager's trade records. Others said that while they could plot it in an Excel file they would then need to pass on the file to the client to redesign the pie chart to follow the family office's investment business's desired graphic look, and then the portfolio manager would have to insert the pie chart himself into a monthly performance sheet he makes in-house.

We finally identified which fund admin firm could produce what we wanted for a reasonable fee, follow our instructions on design and layout and standardize the monthly production of the performance report for the client. And that's who our client hired.

Next Time

In next month's column we will continue with this topic, offering tips to guide your management team for preparing to deliver, in a post-pandemic and global recessionary environment, more and better portfolio data communications in your asset raising efforts with sophisticated investors.

#

© Frummerman & Nemeth Inc. 2020

About the author

Bruce Frummerman is CEO of Frummerman & Nemeth Inc., a 32-year-old financial communications and sales marketing consultancy that helps financial services firms create brand identities for their organizations and develop and implement effective new marketing strategies and programs. Frummerman & Nemeth's work has helped money management firm clients attract over \$7 billion in new assets, yet they are *not* third-party marketers.

Frummerman & Nemeth is internationally recognized for its work in crafting for clients the beyond-the-numbers story of *how they invest* — content that investment committees actually discuss, debate and vote on behind closed doors when considering firms on a short list for potential investment. Importantly, this is required due diligence content that cannot be communicated in pitchbook format.

Frummerman & Nemeth's work also includes providing strategic consulting on product and strategy-specific branding, crafting the required strategy-specific content detail and designing and producing the marketing tools needed to make it through the two-month to two-year institutional selling cycle. Clients also employ Frummerman & Nemeth to help promote the intellectual acumen of management — helping them get speaking opportunities, write and give speeches as panelists or stand-alone speakers at industry conferences, and through media relations marketing services.

Mr. Frummerman can be reached at info@frummerman.com, or by visiting www.frummerman.com.