Marketing To Sophisticated Investors column
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Is Your Bad Investment Philosophy Scaring Off Potential Investors?

Tip 4: Preparing For Post-Pandemic Asset Raising

Welcome to the fourth 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.

Does your marketing collateral reveal you have a sloppy portfolio manager who suffers from a lack of attention to detail?

Sophisticated investors conducting due diligence on new portfolio managers under consideration want more than just the necessary basics: good performance, a sensible strategy and acceptable back-office operations management. They want to feel assured that portfolio managers demonstrate attention to detail, both in running their portfolios and their investment firms. Without that eye for detail a portfolio manager risks carelessness; and that is when mistakes are made, with investors' dollars.

Institutional investors need to allocate a significant sum to a money manager in order for that investment to potentially do enough to 'move the needle' of that portfolio at the family office, endowment, foundation or retirement plan. So, it is no small thing for wanting to avoid portfolio managers who lack attention to detail and might make investment mistakes as a result.

Before an investment committee votes to allocate millions of dollars to new money managers and their strategies, sophisticated investors are vetting what a money manager has put in print, as well as what he or she says at due diligence meetings, to seek out and separate the focused managers from the distracted managers.

Show a lack of attention to detail and you provide the prospective investor with a reason to reject.

Where is a portfolio manager's attention to detail, or demonstration of a lack thereof, first seen by prospective investors? In the flipchart pitchbook.

The very definition of a sloppy portfolio manager

It is incredible how many portfolio managers — otherwise seemingly intelligent, educated people — demonstrate they have no idea what the definition of the word PHILOSOPHY is. The misuse of this word as a flipchart page header — once you read the copy these people put below it — is epic.

Let's talk definitions for a moment. "A particular system of beliefs, values, and principles" is the correct definition of philosophy, when used in writings about an investment firm's portfolio management. If you want to get even more specific to the money management world, you can find it defined this way: "an investment philosophy is a set of beliefs and principles that guide an investor's decision-making process".

Therefore, a money management firm's philosophy is *not* a short statement about its strategy, nor is it detail about its investment process.

Every portfolio manager who uses his or her claimed philosophy statement to deliver wrong content sends up a nice red flag to every skeptical sophisticated investor conducting due diligence on them. And it's not just me that thinks this.

Want to irk your prospective investor?

For the money management firm that thinks institutional investors are somehow going to miss this, you are quite mistaken. I've had such investors share stories with me of rejecting money managers that, in seemingly indirect but blatant ways, demonstrated a lack of attention to detail in the running of their own firms and in their communications with prospective investors.

What does this misuse of the word philosophy appearing as a flipchart pitchbook page header look like?

Here are three actual examples from money management firms where the 'buck stops here' portfolio manager either a) does not know the definition of philosophy, a word taught in elementary school, or b) pays little attention to what he or she allows subordinates to put in print and disseminate to sophisticated, skeptical prospective investors on his or her behalf.

<u>Example 1: Not a philosophy statement</u>

> Investment Philosophy
>
> The strategy is based: (a) on the construction of 3 legged positions in optionable ETFs and some selected large cap stocks. The program buys equities and writes both puts and calls. Most positions are acquired by selling puts at lower strikes rather than placing limit orders. This way investors receive an income even if the prices don't reach the desired buying levels. (b) on the construction of a V scheme profit curve as a function of stock's price and fluctuations. This is achieved by buying stocks with selected betas and dividends and simultaneously take long and short positions in stock's options in proprietary defined strikes.

Example 2: Also not a philosophy statement

Philosophy

- Focus on "off-the-run" and other differentiated opportunities with asymmetric risk profiles.
- Long/short approach to portfolio construction, with no historical use of derivatives and very limited use of indices.

Example 3: Also not a philosophy statement

Investment Philosophy

[Company] employs a diversified investment approach, combining several distinct strategies working across different time frames.

Trading in financial markets is predominantly executed through a value based global macro approach. Consequently, at any given point in time the portfolio will consist of directional short-, medium- and longer-term opportunistic trades, with exposure in such sectors as foreign exchange, commodities, equities, stock indices and interest rate instruments.

Alternative strategies include statistically driven and quantitatively managed trades with little overall directionality.

By deliberately avoiding crowded fields such as "relative value" trades, the majority of the firm's positions will be targeting larger moves thus removing the implicit need for excessive leverage of, for example, pure arbitrage strategies.

Exposure is inherently global and not limited to any one region or country; however, overall the firm's programs are biased towards providing Asian exposure.

Good & Proper

Let's contrast the examples above, which reveal sloppy portfolio managers, with an actual, correct philosophy statement.

> Investment Philosophy
>
> We believe investing in high-quality companies with a culture of dividend payment and dividend growth will result in above-average returns over time, with reduced volatility.

Get the point? It is all about beliefs. You do not have to agree with this portfolio manager's beliefs but you clearly know what they are.

Out-market your competitors with grade school English

You may have competitors that are delivering similar performance and follow a similar investment process to yours, but reveal themselves to lack attention to detail in running their firms.

So here are two lessons:

1. Portfolio managers need to proof-read all copy that is representing them — their data *and* their views — before it leaves the office. It doesn't matter whether the content was written by the portfolio manager or a subordinate, the words still represent and are a reflection back onto the portfolio manager. The buck stops there.
2. Unless you are absolutely positive what a word means, pull out your Webster's and make sure.

Your making it through the due diligence gauntlet of sophisticated investors may depend on what you were taught — and should have absorbed — in elementary school.

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About the author

Bruce Frumerman is CEO of Frumerman & Nemeth Inc., a 33-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. Frumerman & Nemeth's work has helped money management firm clients attract over $7 billion in new assets, yet they are *not* third-party marketers.

Frumerman & 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.

Frumerman & 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 Frumerman & 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.

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