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Marketing To Sophisticated Investors column
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April 2022

Inaccurate Portfolio Managers' Communications That Damage Asset Raising

Tip 25: Preparing For Post-Pandemic Asset Raising

Welcome to the twenty-fifth 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 world.

Previously in this column (https://is.gd/4HjC6c) I introduced an asset raising obstacle often self-inflicted by portfolio managers in their communications marketing that I call one of the Sins Of Omission.

That column was about where portfolio managers are Talking In Shorthand, leaving prospective investors unable to correctly infer and extrapolate off of comments a portfolio manager makes. So, potential clients may miss or misconstrue what the manager was actually thinking or meaning, and not invest as a result.

Today I'm pointing out a different Sin Of Omission. This one can be double damaging, both to a money management firm's asset raising efforts and its brand identity.

With this Sin Of Omission, portfolio managers are making a specific type of inaccurate statement to prospective investors during their due diligence vetting. I have found that when this imprecise and therefore not factually correct communications is made by a portfolio manager it is always unintentional. Nonetheless, it can set off a string of unintended consequences, from having prospects stop short their due diligence evaluations to having an incorrect image about strategy implementation be projected to be a money management firm's brand identity.

This Second Sin Of Omission

The Sin Of Omission we are looking at today occurs when, in describing her or his investment process, portfolio managers truncate the explanation about the methodology that they created and follow in running their strategy. Such an action often short changes a money management firm of what should be the full perceived value of how it runs its portfolio because it makes it more difficult for a sophisticated investor to conduct due diligence and places asset raising obstacles in the money management firm's path that didn't have to be there.

Sophisticated Investors Judge You By *How*

When sophisticated investors are putting due diligence time and effort into examining and evaluating your investment strategy and the portfolio manager who built and runs it, they are looking at much more than just the data — objective-based information such as performance numbers and the like. They are not just judging based on what your numbers are, they are also evaluating how your portfolio manager got them.

In judging you by *How* they are looking to understand and buy into the subjective-based information that adds up to what constitutes your added value, your differentiator, your competitive advantage.

These prospective investors want to gather accurate descriptions about two specific subjective considerations. The first is *How* the portfolio manager views the marketplace, its opportunities and risks. The second is *How* the portfolio manager assembles and manages the strategy's basket of holdings. These elements of communications by and from portfolio managers comprise the intellectual acumen of management at the investment firm. These are, in turn, the key elements that make up a money management firm's brand identity: *How* it does what it does.

It is the second of these two *Hows* — communication about investment process — where too many portfolio managers unintentionally harm their asset raising potential.

Too close to tell

In working with portfolio managers who are running strategies of their own creation — by which I mean they are the ones who selected and put in place the investment methodology steps being followed for assembling and managing the portfolio holdings — I frequently find a very curious thing. They have trouble recalling and recounting to another person all of the steps they actually take and the order in which they take them.

So, instead, they tell — both verbally and in print — what is an abbreviated, incomplete and therefore inaccurate explanation about how they think and the investment process they follow. This creates a number of problems for the money management firm.

Experienced investors who take what portfolio managers say to them verbatim, with their incomplete and therefore inaccurate explanation about investment process, may find it too easy to pick holes in the strategy implementation (as described to them) or the portfolio manager's thinking. This constitutes grounds for getting kicked out of further due diligence vetting by a sophisticated investor.

A far and wide communications marketing challenge

Attempting to asset raise using a truncated explanation about a portfolio manager's investment methodology is far from a rare occurrence. It is found with both domestic and overseas-based money management firms and among a wide range of strategies, from seemingly plain vanilla value equity investing to real estate, from private lending to quant-based strategies, from investing based on deep and detailed fundamental analysis to crafting AI programming-based methodologies to make position sizing and trading decisions.

For over three decades my financial communications and sales marketing consulting firm has found itself brought in to work with money management firms where portfolio managers recognized the need to improve explanations about how they think and run their strategies. Some managers may realize they have been seeing a disconnect between what they think, know and do and what prospective investors conducting due diligence on them perceive the managers think, know and do. But that doesn't mean that most managers have the perspective to recognize when the shortcoming is due to explaining an investment process in a manner that is incomplete, and therefore both inaccurate and less powerful than what a money management firm has to convey to prospective sophisticated investors.

To make this more tangible, here are three case examples.

The equity manager

An equity investing portfolio manager who had worked for a large firm had a 15-year track record running a largely diversified portfolio. He resigned and launched his own fund where he intended to run a concentrated portfolio instead. To accommodate this, he made changes to what had been his previous investment process. When his newly appointed fund administrator reviewed the written explanation the portfolio manager intended to use in marketing, the manager was told the marketing document over-emphasized what he'd done before and under-delivered in explaining enough about what he intended to do now. He was referred to my financial communications and sales marketing consulting firm.

When I got the call, the portfolio manager said to me that he was sure that, working together, we could improve how he explained his strategy, which, he claimed, was a well thought out four-step investment process. He expected that some thoughtful language tweaking would surely help improve what he was communicating, but that was it.

Carrying out a process my firm developed back in the early 1990s to get to the bottom of what portfolio managers actually think and how they implement that thinking in running their strategies, we got out of his head much more than what he had been explaining when making his initial comments about knowing his process. In fact, we uncovered, he was running a 10-step investment process, and the six previously missing, uncommunicated steps all included risk management related decision making.

Responding to us after we had reported back with a detailed, in print explanation of his strategy implementation, stating what he was actually thinking and doing, he said Yes, he did in fact do all of the things we had written out, and that was the order in which he did those things.

He then said something that was both very revealing and gets to the core of why money managers unintentionally leave out such important information in their asset raising marketing: "*It never occurred to me those were steps!*"

The PE fund of funds manager

Before coming out with their third fund, the firm requested for its sales team a rethink and restructuring for how the portfolio manager's investment process for the offering was explained. One of the fascinating things my firm uncovered using our process was that with the very first step of their screening of outside small to midsize PE funds to consider, their strict criteria ended up eliminating all but one percent of that universe; and in the end they allocated to no more than 20% of that one percent. We built out detail on this, and other previously missing investment process steps and explanations, into their new marketing communications.

When presented with the new, more accurate marketing collateral the head of sales, with surprise in his voice, posed a question to the portfolio manager. Do you mean to tell us, he asked, that for the last few years when we've been marketing the previous fund of funds that you've been using such a dramatic first round of screening where only one percent of outside managers might be good enough for our consideration? This is a significant difference in risk management considerations versus our competition, he said. Why in the world didn't you ever tell us this before, the head of sales asked? "*It never occurred to me that it was that important!*" was the portfolio manager's reply.

Here, the portfolio manager felt that it was so obvious (to him, it turned out, but no one else) that what he used as his initial screen to identify what constituted his investable universe had to be how everyone would be thinking about his area of specialization. So, he never before communicated that this important risk management protocol step was in fact the very first step he took in running his investment process.

The quant manager

The portfolio manager and his team crafted a systematic process to invest in a particular asset class. In creation of their methodology, they built their own AI modeling and tied it in to some more traditional technical analytics steps. So, their software was taking in a data feed, making multiple simultaneous calculations at various stages and generating statistically calculated trading actions.

As with all computer programming for a money management firm's custom built software program to run a systematic, quantitative strategy, the programming had to set certain tasks, actions and calculations to occur in a very specific order. Yet, despite the fact that the portfolio manager had built and programmed this, there had been a disconnect in how the firm had been communicating about this to prospective investors.

Working with this portfolio manager my firm uncovered a different truncating problem. While building and running this investment process required following certain chains of calculations in a certain way within the software, the manager and his team could not visualize — removed from the pages of coding — all of the steps the investment process was carrying out. Undertaking a fresh flowcharting of the process with the portfolio manager, and finding what additional questions we knew sophisticated investors would challenge them with, we were able to come up with a clearer way to explain and contextualize the range of analytics and statistical calculations the investment firm was taking. Additionally, there was now a new, non-truncated investment process diagram that was able to be shared and talked through with prospects conducting due diligence.

Commonality of all this unintentional truncating

What we've found is that often the investment process steps that came easily to a portfolio manager in developing his or her process are the ones that they later tend to skip over in their minds when having to communicate about how they invest. The steps that may have taken them longer to come up with or refine are the ones that tend to be more clearly in their minds and communicated as stages in their methodology.

This truncating the investment process storyline is a communications Sin Of Omission that few money management firms have recognized they might have been committing.

Reexamine your firm's communications to sophisticated investors to make sure you have not been unintentionally delivering an inaccurate description of how you invest. Marketing with an accurate, more complete explanation of how your portfolio manager runs the investment process will help you pass muster through more due diligence vettings, attract more sticky assets and build a brand identity based on *how* you invest — the key, subjective value-add your firm has to sell.

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About the author

Bruce Frumerman is CEO of Frumerman & Nemeth Inc., a 34-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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