Marketing To Sophisticated Investors column
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DANGER – When Your Fund Is Only Attracting Performance Chasers

Tip 8: Preparing For Post-Pandemic Asset Raising

Welcome to the eighth 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.

It's a good thing when your investment strategy is delivering good performance and it's a great thing when it is delivering great performance. One of the differences portfolio managers may find when their numbers are putting them in the top quintile of performers for their strategy category is that more prospective investors are likely to come knocking. Topping the peer tables in performance charting databases can have its benefits. However, with that opportunity to develop dialogue with performance-enticed prospective investors, danger lurks.

When I call you up

It was late April, four weeks into Pandemic lockdown. An emerging manager investment boutique coming upon its one-year track record period reached out to me. The portfolio manager told me his strategy has delivered nearly 100% year to date performance. He went on to explain that in February his investment process alerted him to the overseas spread of Covid-19. He figured there were very high odds of it coming to America. He told me of the sectors he then shorted and the stocks he bought. His portfolio benefitted.

The portfolio manager knew it was very good news to have the great returns, but he recognized his returns would not always be this high. He knew he needed help to craft an explanation for how he invested, and he wanted counsel on how to handle sales marketing.

What were the initial observations we shared with him? The good news is that performance chasers may be attracted. The bad news would be if performance chasers became the majority of his investors, or worse, the only investors.

Triad

As my financial communications and sales marketing consulting firm teaches its money management firm clients, there are three types of prospective investors they may attract and win over as new clients. We classify these as friends and family, performance chasers and sophisticated investors.

Friends and family folks are predisposed to have a positive bias toward you and are the kind of people most likely to invest with you without conducting much, or possibly any, due diligence. These are people who have known you, or even your relatives, for quite some time and so are predisposed to whatever you might say. There is also another kind of friends and family type of investor. These are people who are so very impressed with the firm name of your former employer(s), or where you went to school, that they are willing to invest with you simply based on that.

Performance chasers are always on the lookout to see where the grass may be greener. They follow money manager performance tables the way ardent baseball fans track baseball players' RBI records. These folks tend to reallocate to whoever becomes the new top of the heap portfolio manager. These investors tend to come late to the party and leave quickly. Performance chasers can be a danger for a small to midsized investment firm because of the amount of time it can take to replace these investors, who the portfolio manager should have recognized from the start did not represent sticky assets.

Sophisticated investors are most likely to become sticky assets for an investment firm. These are people who follow a money manager vetting process that they established for their family office, endowment, foundation, institutional plan sponsor or wealth management firm. They tend to have investment committees that discuss, debate and vote on which manager should win their next allocation. These are the folks that put in time and effort to decide whether they think it is luck or skill driving a portfolio manager's performance. In fact, among sophisticated investors' due diligence considerations performance ranks third, risk management second and investment process first in importance. So, money managers delivering good or great performance should expect to have their investment process analyzed, poked and prodded in the due diligence efforts of this type of investor.

Lazy days

Money management firm owners face a dilemma when they're in the lucky, temporary position of having top tier performance and performance chasing investors engaging in dialogue with them. The selling cycle may be enticingly shorter than that required to win over a skeptical sophisticated investor. The question is, is the investment firm acting complacently lazy in how it goes about landing the performance chasing investor, since these people are not giving push-back with as probing questions, compared to sophisticated investors, about the portfolio management? Moreover, is the firm putting off pursuing sophisticated investors who, while they can represent stickier assets, require a longer selling cycle to win over, and more up-front time and effort put into developing more explanatory content about how the strategy is being run?

A telling give-away to when a money management firm is being dangerously lazy in its asset raising is when line graphs and monthly tables of performance, and naming top holdings, are the near-complete focus of its communications and sales marketing effort.

Here, portfolio managers — who would never make what they would claim to be the beginner investor's mistake of not building thoughtful diversification into a portfolio — make a very much related communications and sales marketing error that can, and often does, cost them dearly down the road.

I turned around, she was gone

Next thing you know the portfolio manager with the great and not just good performance begins to drop in the peer rankings. This what goes up must come down problem tends not to be a one-month blip, it often continues through a quarter and then a second, and maybe another. To what does the performance chasing investor's attention turn? Right, she is perusing the peer group performance tables to pick which new top quintile performer to reallocate those investment dollars to.

The former top performer now starts a too late investor relations effort to keep the client from bolting. Only now does the portfolio manager attempt to have his firm communicate elaboration about the thinking behind his investment process, hoping the performance chasing investor will change her mind and stay put to await a turnaround. But the performance chasing investor rarely does.

So, that was the start of my financial communications and sales marketing consulting firm's conversation with the portfolio manager. When your numbers go from good to great performance chasing investors may come knocking. With such numbers you have the potential to use them as a door opener in outbound marketing efforts to more skeptical sophisticated investors; people who have the potential to become sticky assets. However, before you go knocking you better have first built out in detail, and in print, how to educate and persuade them to understand and buy into how you invest. When they buy into that you've won sticky assets and reduced the danger of having an investor base dominated by performance chasers.

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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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