The 6Ps

A Quick Reference Guide for Understanding & Marketing Managed Money

Summary

Understanding managed money is easy when you apply a consistent, repeatable discipline to the process. Here are some basic questions that will help you cut through the marketing babble to the heart of what a manager actually does. They will also help you frame your story so you can share appropriate information with your client.

Top financial advisors like to feel completely comfortable with a money manager before recommending them to a client. Here's a brief list of questions that will help you make that decision. Not all questions apply to every type of portfolio nor will they be of interest to different advisors. Most are way too technical or detailed for the client...but you should know them. They form the base of knowledge you need to succeed if you intend to use managed money.

The trick with this analysis is that there are very few right or wrong answers. For example, what's better...an individual or team approach to managing money? A strong case could be made for either method. To interpret these answers intelligently you need a deeper understanding of money management that goes beyond the basics to the psychology of the process itself.

Why *psychology*? Well, unless you're dealing with a pure "black box" model, you have human beings running this money. Portfolio managers may be some of the brightest people in our society, but they are subject to forces, pressures, conflicts and motivations that would probably freak out the average person!

For example, most portfolio managers like to portray a stoic, un-emotional exterior. They want people to believe that their decisions are based on discipline and logic. And while that's true to a great extent...the human element is a massive part of the total picture. Having worked around portfolio managers for over two decades now, I can tell you that what goes on behind closed doors is not the same story most financial advisors get to see.

Regardless of that, these questions will get you off to a great start. If you need more help, please e-mail me at frank@frankmaselli.com.

1. PEOPLE

- Who manages the portfolio?
  - An individual or team approach?
  - If it is a team, who leads?
- What experience do the PMs have with this or other types of assets?
  - How many years do they have as portfolio managers or analysts in the discipline or in general.
- What's the overall management and analytical team structure working on this portfolio?
  - Average experience of the managers and analysts
  - Are they CFA's?
  - How many companies and industries does each analyst cover?
  - How are they compensated...relative to the market or peer groups?
  - Are they free to travel?
  - What industries does the team miss?
  - How much money do they manage and how is the total broken down by asset class?
  - Do the same people work on different asset classes or are they dedicated to specific disciplines?

2. PHILOSOPHY

- What is the overall investment philosophy of the management company and of these particular portfolio managers?
- Why have they chosen this asset class or this approach to investing?

- Have they been consistent and successful in this process?
- If they have made major philosophical shifts, what caused them to do so?
  I like manager flexibility to a degree, but I am uncomfortable with a lack of conviction when their approach temporarily goes out of favor.

3. PROCESS

- Describe in detail the buy and sell disciplines.
  - Give specific examples of recent buy and sell decisions with detailed rationale
- How do they research securities?
  - Describe their application of fundamental vs. technical analysis
  - Describe the use of quantitative security screening
- How are ideas uncovered and presented for purchase?
  - Describe the interactive process that leads to decisions within the team
  - How do they accumulate or liquidate positions? Why?
  - Do they scale in and out or do they buy or sell full positions?
  - What determines this?
- How do they structure the portfolio? Why?
  - Sector weightings vs. benchmark
- How do they define, assess & manage risk in the portfolio?
  - Do they hedge or augment with derivatives?
  - Why or why not?
- How do they manage the taxes in the portfolio?
- How do they expect the portfolio to perform in various market environments?
  - Bull, bear, neutral, rising rates, falling rates
- Give an example of a problem selection (i.e., a security that is not performing up to their expectation)
  - What originally caused them to buy it?
  - When and how did they notice any problems?
  - What did they do (or are they doing) with it?
- How proactive are they at communicating their actions to the clients?

4. PERFORMANCE

- What's the absolute performance for all standard time periods? (YTD, 1, 3, 5, 10, since inception)
  - What benchmark is used to judge relative performance?
  - Why are they using this benchmark?
  - What is the relative performance to peer group & benchmark?
- If the portfolio is new, how has the manager done in the same asset class?
- How has the portfolio/manager performed during different market cycles or bad years for their discipline?
- What is the Alpha, Beta, R2, Standard Deviation, Information Ratio, etc?
  You may need to understand this type of portfolio analytics, but this information is often confusing to clients, so my advice is to share it sparingly.
- Describe the normal portfolio turnover?
  Some managers hold core positions for years and flip a segment of the portfolio frequently. This can make the raw turnover number unrevealing...so dig deeper.
- How do these statistics compare to other managers in their discipline?

5. PRICE

- What are the management fees for the portfolio?
- How do these fees compare relative to the peer group?
- Have the fees dropped as the portfolio has grown?
- Is the manager making an effort to reduce trading costs and other expenses?

6. PORTFOLIO

- How does this portfolio fit into various asset allocation models?
- What effect should this individual portfolio have on the client's total investment strategy?
  Enhance growth through exposure to a specific asset class or style?
  Reduce volatility?
  Strengthen it in a particular type of market?
- What other asset classes compliment or conflict with this portfolio?
- How should other things in the clients overall portfolio be altered to blend better with this individual segment?

Well...that's about it! Our industry spends a tremendous amount of time and resources on analyzing the various characteristics of portfolios and money managers. You can literally get lost in the data and the research. I urge you to remember that we are in a people business. Mastering the numbers is great, but learning how to work with clients is far more important. So this is about as technical as I ever plan to get. I hope it helps!

I wish you all the best! ***Frank***