Revolution Annual Onsite – 12/1/14 – Michael Mundt, Jim Curely, MH, TR

We conducted the HAMF annual onsite of Revolution in their new Denver, CO office. There were no outstanding issues at the time of the visit. In addition to touring the new office and reviewing key systems/infrastructure, our discussion included a review of team’s current research projects and reconfirming the team members’ roles and responsibilities following the September 2014 resignation of Mark Chapin, who was one of the firm’s three original principals. The build out of the new office space was near completion during the time of our visit and appeared adequate for a firm of their size. The new office’s downtown Denver location should be more convenient for current and prospective clients relative to the previous Broomfield, CO location. Regarding changes within the firm following Chapin’s departure, the Revolution team appears to have implemented a sufficient transition plan by increasing the research and development responsibilities of Rob Olson and Jeff Perini and hiring two new associates to support technical operations and accounting, regulatory, and compliance. Michael Mundt’s role appears to be little changed and he will continue to focus primarily on model research and development as well as supporting investor relations and general business activities. While there were no items identified for immediate follow up during the meeting, additional time should be set aside at the next onsite to meet with Jeff Perini, whose responsibilities have increased in recent years.

FIRM/BUSINESS UPDATES

* Revolution moved to new offices in downtown Denver in November 2014. They have a 5-year sublease on the space and rent expense is the same as their old office (Jim mentioned that three times). The new office was mostly built out at the time of our onsite, TVs were being installed while we were there, but some furniture had yet to be delivered (including the conference table). The office was previously set up with two large offices bookending a few smaller offices by the prior tenants. For Revolution, the two large office are going to be used by several employees and partitions will be installed later to breakup their work areas. Mundt will be using one of the smaller offices by himself.
* As a result of the move and distance of the new location from Mundt’s home, Revolution now has a branch office which is located 5 minutes from Mundt’s home. Mundt said that he only plans to use the branch office when there is inclement weather.
* No systems were changed along move and they experience no issues with systems during the move. The new and old offices were mirrored for a short time before moving everything to the new office. Mundt showed us the server room and noted that he doesn’t think that Revolution could move completely to a cloud based system (as Centurion has) even though he recognizes this as a growing trend in the industry.
* As previously discussed with HAMF, Revolution and Dunn Capital terminated their licensing agreement in 2014. As part of this change, Revolution took over additional operational tasks which Dunn used to take on and the two firms shared the cost of. AUM from Dunn did not change due to the termination of the “strategic partnership”, fees also did not change.
* Mundt noted that the firm is on better footing today even though firm AUM isn’t at an all-time peak because the Alpha program is now a larger percentage of overall AUM. The Alpha program typically charges both management and incentive fees, while the Mosaic program is incentive fee only. Firm AUM is approx. $500mm and the Alpha program’s AUM is approx. $170mm. They raised $70mm in the Alpha program during 2014.
* Revolution continues to use FCI (which is owned by Jim Curley) as outsourced back office. FCI has 7 employees, 6 employees focused on trade execution and Jim. Mundt noted that much of the Alpha program’s trading is automated and most of the work that FCI does for RCM is rolling trades for the Mosaic program. Curley purchased FCI from Dunn in 1998. FCI only works with Dunn and RCM and Curley said that he is not looking for new clients.
* Following Mark Chapin’s departure the roles at RCM have evolved. Chapin had been focused on the development of the Intraday model, a project which had matured and much of his time at the end of his tenure with RCM was spent working on operations. Previously Mundt and Chapin were focused on R&D while Olson focused on operations day-to-day. Mundt will continue to spend most of his time on R&D. Olson and Jeff Perini will now shift more of their time to R&D. Chad Dougherty (new hire in 2014) will take on technical operations responsibilities previously held by Chapin and Olson. Mike Helmstetter (new hire 2014) will support Mundt by taking on accounting, regulatory and compliance tasks. Geoff Dix continues to act as a software engineer working on data feeds, order processing, and automation.

RESEARCH

* Projects focusing on trade cost reduction have been and continue to be their focus. Algorithms from Quantitative Brokers (QB) have been implemented within the Mosiac program, but will not be added to the Alpha program. QB’s service does not show as a line item within a client’s statement, rather it comes as a separate bill. Mosaic’s has a small number of large accounts, and those clients have agreed to the additional bill. The Alpha program has a large number of small accounts making the implementation of QB operationally challenging. RCM is working with UBS and JPM to develop algorithms to reduce cost within the Alpha program. Mundt said that UBS is having some success with ideas that are similar to QB’s style, which Mundt described as being patient when pricing improves and acts as normal if price is moving away. The Alpha program’s trading is approx. split between USB and JPM, and about 1/3 of the UBS trading is using the new QB like algorithm.