GRAY ISSUE

How to select the right investment manager

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It is challenging for investors and their advisers to differentiate between investment managers in an ever-changing landscape. When assessing who is best placed to manage your investments it pays off to gather as much information as possible upfront and to ensure that the evidence is relevant to future outcomes, not past returns. Ultimately, selecting the right investment manager is more of a consistency contest than a talent or intellectual evaluation. A good acid test is to ask: will the asset manager likely be doing the same thing in 10 years' time? By answering this, you need to look at the incentives, the business structure, the team stability, experience, breadth and evidence of past investment conviction and temperament. These types of questions avoid the natural inclination of anchoring on past performance when it is the future that matters.

An extension of this thinking is to avoid focusing on funds: rather see a fund as an underlying business, team and process.

So, what evidence is at your disposal and what should you be looking for?

There are generally two types of information. First is the external message: you can source the information that the investment manager presents to the outside world. This is fairly straight forward and is usually available on their website and via newsletters. Second, and more complicated, is to source evidence that evaluates whether or not the manager actually does what it says. There are a few ways you can assess this, for example, you can evaluate their investment holding period and portfolio turnover by assessing the frequency with which their portfolios or top 10 holdings rotate. Are they long-term investors or do they respond to short-term events? You can also see if the top 10 holdings align with those in the index, which may give you further insight into their investment style. In addition, you can look at team changes: stable teams often result in more investment consistency. Websites reflect core people – you can track them and gauge their experience: how long have they been managing this mandate and do they have the requisite experience?

Key criteria

These are a few high level ideas. But complete research involves examining the business and the team and, if done properly, will take time and involve several rounds of information gathering. While it is not recommended to adopt a 'tick-box' approach, there are some key criteria which, if fulfilled, can bring you comfort that an investment manager will most likely deliver on its obligations:

1. A business and shareholder that understands asset management. Look into the intent behind the shareholders. Are they likely to overload their investment team with too many offerings? Will they grow assets beyond what is digestible for active management to thrive? How do they measure themselves? And do they support their portfolio managers during periods of underperformance?
2. One or two individuals who drive the investment process and who love investing (and who are, therefore, often averse to marketing).
3. A team that has significant experience with the specific asset class and has sufficient depth in resources. There is, at times, an odd anomaly with South African asset managers who seem to have far more people allocated to SA investments than global, yet there is materially more work to do in global. Always ask: is the ratio of people to investment ideas appropriate, given the mandate? More often than not, an analyst cannot adequately research more than 15 investment ideas.
4. A low staff turnover environment of senior investment people. Can you trust the track record if the team changes frequently? Also look at the calibre of people who are joining; peer endorsement is a good sign.
5. A clear investment process that is deeply engrained into all corners of the team. It needs to outlive any individual and make intuitive sense.
6. They do what they say they do. It is important to look inside portfolios to see whether past actions are consistent with what is written on the tin. Different people in the same business should be giving the same message.
7. Appropriate incentives: do they align with the client's promise? Are fees appropriate? Are they invested alongside the client? It is usually a red flag when an investment business sees financial rewards as the key determinant of behaviour and culture.

In the end, the selection of an appropriate investment manager is always going to be a judgment. There is no perfect answer. But we think that if you look for consistency (and the drivers of consistency) above all else, you will likely select a manager who delivers on their obligations.

If you lack the time and/or appetite to perform your own due diligence and make your own assessment, you may want to make use of the services of an independent financial adviser. Independent advisers do regular research and can assist you in putting together a portfolio based on your needs and your risk appetite.

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