funds europe

THE BOUTIQUE STATE OF MIND

The success of Carmignac Gestion in France – a land of large, bank-owned asset managers – is a positive sign for boutique investment managers and shows boutiques do not have to be small, finds Fiona Rintoul.

"A LOT OF people say they are boutiques because it's trendy, but behind it they are not," says Peter Boyle, managing director of Kennox Asset Management.

The attraction of boutiques is performance. "When we talk about active management, only 20% do a good job," says José Luis Jiménez, chief executive of March Gestión de Fondos and chairman of the Group of Boutique Asset Managers (GBAM), an international network of independent specialist asset managers. "The proportion that outperform the index is much higher in boutiques."

If you cannot reasonably claim to be a boutique, you can always say you're a multi-boutique – or have a unique multi-boutique structure, to roll out a phrase we've all heard more than once.

That's the cynical view, and there are plenty of reasons for holding it. But behind the fad, lie genuine success stories – Carmignac Gestion in France, which spawned many lookalikes, being Europe's flagship example. That Carmignac Gestion could thrive in France, land of big, bank-owned fund managers with captive distribution, suggests that something is afoot in the European fund industry.

"In Europe, there is an important trend towards boutiques and specialised asset managers," says Naïm Abou-Jaoudé, chief executive officer of Candriam (formerly Dexia Asset Management). "They form a third of the industry in the US. In Europe, the proportion is still small but the trend is for it to grow."

This is happening, not because fund selectors have woken up and smelt the coffee, but because investors have, says Jean Keller, chief executive of Argos Investment Managers. "Clients are putting pressure on fund selectors. It's very strange that all the research shows newer, smaller funds perform better than large, old funds, but it's hardest to sell small, new funds."

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In fact, there are two parallel trends in Europe at the moment: the top 10 companies have big flows, and boutiques are capturing flows. Data abound that show Europe's top 10 fund managers taking about 40% of flows, but there are also data to support the second trend. Analysis of Lipper data by the research company MackayWilliams indicates that specialist boutiques harnessed 25% of total net sales flows in Europe in 2013, compared with 15% in 2009.

WHAT IS A BOUTIQUE?

This brings us swiftly to one of the main issues with boutiques: what is a boutique? In the absence of an agreed industry definition, Mackay Williams defines a specialist boutique as a group with less than €10 billion of assets under management and less than 20 funds. That would exclude well-known trail blazers such as Carmignac Gestion (€53 billion and 23 funds) and Skagen Funds (€14.9 billion and five funds), to say nothing of Candriam, which, with €73 billion under management, was bought by New York Life in February for incorporation into its multi-boutique structure.

Finding a workable definition of boutiques is certainly a puzzle. However, most people from companies that call themselves boutiques agree that being a boutique is a kind of state of mind.

"A boutique is more about a culture than a specific size," says Keller. "You have to convince clients you're looking at the world in a different way."

MODE OF THINKING: Boutiques are about culture, not size

Beyond that, concepts such as independence, private ownership, specialisation, commitment and alignment of interests are often (though not always) associated » with boutiques. For some companies, private ownership in particular is essential to the boutique idea – the peg on which all other attributes hang – and one such is Kennox, long-term contrarian investors based in Edinburgh.

"We believe this style can only work when management owns everything," says Boyle.

Kennox Asset Managmenet is the quintessential boutique. It has one global equity fund with £260 million (€314 billion) under management, both the fund managers have 100% of their own equity exposure in the fund and Boyle does all the client meetings himself. The fund has been modelled out to £1 billion and will be soft-closed as soon as its size adversely affected the stocks its mangers like to buy. Most support functions are outsourced, and the company has a deliberately small structure.

"We try to make sure we know all our investors," says Boyle. "Investors are looking for a more personal touch – a lot felt let down when things went wrong."

A personal relationship with the managing director for every client will always be the preserve of the very bijou. A larger boutique, such as Skagen Funds, necessarily has a sales team; nonetheless it has a lot in common with Kennox in being privately owned and eating its own cooking.

"The firm continues to be the principal wealth generation vehicle for the founders, and all other members are invested in the funds," says Tim Heffer, Skagen Funds' head of UK wealth management. "That's very important for creating alignment."

Above all perhaps, this kind of alignment allows firms to concentrate on long-term goals. Increasingly, that fits with what investors want, says Dan Mannix, chief executive of RWC, a boutique that has seen its assets under management rise from $4.5 billion (€3.2 billion) to $9.5 billion over the past year.

"In the institutional sector, we see a genuine shift by investors such as pension funds, which want to extract more value from their longevity. Therefore, they are more willing to tolerate short-term volatility."

» THE LARGER AN ORGANISATION IS, THE MORE POLITICAL IT BECOMES. «

Tim Heffer, head of UK wealth management, Skagen Funds

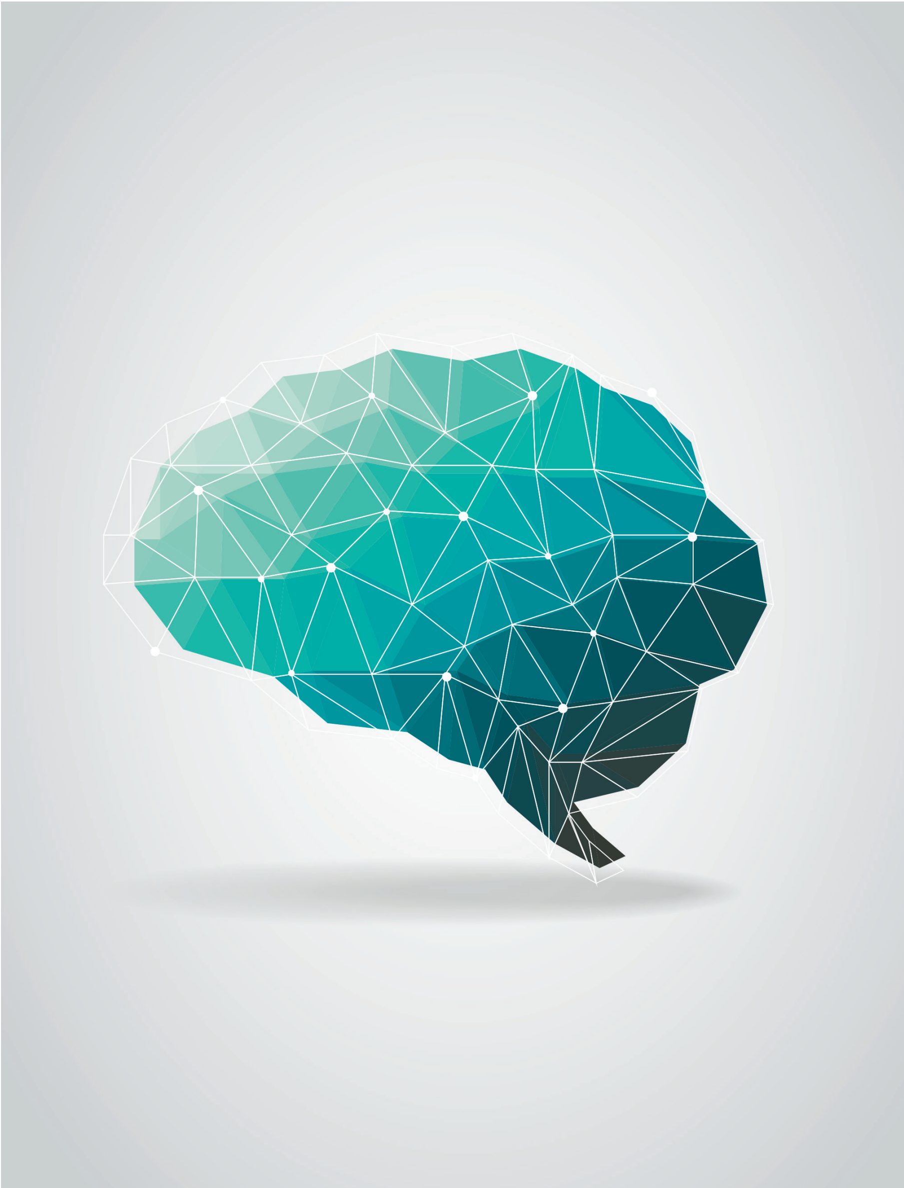
MULTI-BOUTIQUES

There's quite a bit of soil between these pure boutique models and, say, Candriam. However, Abou-Jaoudé believes that a company the size of Candriam can still deliver "active management with a lot of conviction", while doing a better job within a multi-boutique structure of delivering the other things clients increasingly require.

"You have to provide alpha in the whole value chain," says Abou-Jaoudé. "There has been a professionalisation in the market. Clients want to understand how you provide performance. You need capacity to do this."

Some argue that a multi-boutique structure is also a good way to manage another kind of capacity – the sort that destroys performance. "We all know that as assets grow extensively, alpha tends to diminish," says Nick Lyster, European chief executive officer at Principal Global Investors. "A multi-boutique manager can solve this problem by acquiring or growing a complimentary boutique to create more capacity rather than forcing a team to take on more assets than they prudently should."

And there are ways of creating alignment within a multi-boutique. Candriam feels that New York Life's long-term view as an insurance company creates a good cultural fit, while at Principal Global Investors, the portfolio managers have either direct equity or phantom equity in the boutique and a degree of self-determination.



"The boutique structure, or at least the way that Principal Global Investors structures its business, allows the boutique manager to retain a high degree of independence especially in investment matters," says Lyster. "In many cases this includes having their own brand and office location."

Everyone must judge for themselves whether a high degree of independence is enough to kindle the entrepreneurial spark that drives people to launch boutiques in the first place. Certainly, there can be a culture clash between the boutique mentality and the big firm mentality.

"The larger an organisation is the more political it becomes," says Heffer. "People who enjoy a political environment thrive in a big firm."

Tininess can bring its own problems, too. Clients often won't consider firms below a certain size, there can be succession issues in very small firms and specialisation can become a problem if the specialisation in question is out of favour.

"That's why we believe in the multi-boutique model," says Abou-Jaoudé. "It helps you to be diversified in terms of specialisations and clients."

Regulation, which is an increasing burden on all fund mangers, can also be the smaller manager's nemesis. "Small companies don't get enough exemptions," says Mannix.

However, some believe the regulatory pain has peaked. "There is light at the end of the tunnel," says Keller. "People complain about regulation when 90% of it is good."

And for the committed and patient, there are ways round all these problems. An organisation such as GBAM can help by providing a platform for small managers to share their experiences. Beyond that, it's a question of having "a highly differentiated proposition", says Kennox, and being realistic.

"You can't go into it as a romantic dream. It's a long, hard slog, and the ingredients have got to be there or your chances of success are slim. You've got to know your partners and make sure you have the same outlook, because it will be tried and tested."

THE END OF DOMINANCE

There will always be people willing to undergo the test and just as well, since in many ways new companies form the backbone of the fund management industry. Jean Keller points out that BlackRock was founded in 1988, not 1888, and Pimco in 1977.

However, it is a more recent entrant that has really set the tone for the future: Carmignac Gestion.

"There are some wonderful large players in asset management but there are still too many large players that are not committed," says Keller. "If you think about the large continental banks, they don't have the culture. These people are finally being found out. The success of Carmignac spelt the end of large bank dominance in asset management." fe