SPEAKER 1: Hi, everyone. Welcome to the Take 15 podcast. I'm Lauren. And this week we have a really interesting show for you. It's all about entrepreneurship and the asset management space. If you've ever wondered what it might be like to go independent, or whether you've got what it takes, this episode is for you.

But first, a bit of background to set the scene for the conversation. As many of you know, the investment industry is evolving rapidly. There is active consolidation among managers. Banks and insurance companies are divesting ownership stakes and private equity is an active player. These trends have encouraged some portfolio managers to break away and go independent.

So what are the compelling attributes of an independent boutique money management model. What's it like to set up your own shop, and what do you need to be thinking about to make your own money management business successful. To help answer these questions, my colleague Bob Stammers sat down with David Littleton and Alexander Morris. They're the co-founders of FM Acceleration, which helps portfolio managers create boutique firms.

Their conversation covers some of the considerations for going independent, the skills and traits that are needed, and the advantages of being a boutique. So let's get to it. Please enjoy this week's episode with Bob, David, and Alexander.

BOB STAMMERS: David Littleton and Alex Morris, welcome. Thank you so much for joining me today.

DAVID LITTLETON: Thank you, Bob. It's great to be here. Thanks for having us.

BOB STAMMERS: So your firm, FM Acceleration is known for helping investment professionals start boutique asset management firms. And before we kind of get into the nuts and bolts of that, I was really wondering if we could discuss the skill sets that people need to have in order to be successful in going independent, and some of the things they should consider before deciding to do so.

DAVID LITTLETON: Sure. We can dive into that one. First off-- and we probably have hundreds of these conversations every year with different managers, different portfolio managers considering doing something more independent. So we meet a lot of folks. And we do try to figure out what are the common characteristics that would make somebody a good candidate for that.

I'll start. Alex, you can jump in. But first off, you've got to be good at your job, you've got to be a talented. Stock or securities picker, good at asset management, a lot of people are that but they also aren't necessarily ready to be business leaders. So really that combination of fundamentally good at asset management, but looking to actually lead a business.

And in my mind, that means excited about starting and managing and growing a business in addition to being a portfolio manager. Tough things to balance, both, to do to both at the same time, frankly is nearly impossible. And that's really where we come in. But I think in general you need to have a tolerance for risk.

Because you're no longer just an employee. You're not guaranteed anything. You're building a business with us as your partners. So I'd say those are the primary characteristics. I look for more of an entrepreneurial spirit and a desire to do more than create, manage a great product but actually run and grow a business.

ALEXANDER MORRIS: Echoing what Dave said, we've seen that there's no one size fits all model. But the sort of key characteristic is a sense of purpose. You need to want to do this. This isn't the type of job you get to come in at 10:00 and leave at 4:00 and trade just the days you want to trade.

This is one of those businesses that you're going to get dirt on your fingernails with us. And we're here to help you and we've done this before. So we have some experience and knowledge to share. But it is not something to just run away from because you're displeased that you can't get something that you were hoping to get, or think that someone else was treated more fairly than you were.

This is an effort that will require a fair bit of time, energy, skill, and commitment. But once you're willing to make that commitment, the rest of it can relatively nicely fall into place.

BOB STAMMERS: So let's say we have someone that has good business acumen, they have good soft skills, and they want to go independent. What's the steps, what's the natural steps that they would need to go through to start a new boutique firm.

DAVID LITTLETON: Do you want to start with the list?

ALEXANDER MORRIS: Sure. The first thing is, as Dave kind of pointed out, you need to have a thorough and complete understanding of the business that you operate today. Even though you may not fully see everything, it's good to understand the process that you're in, the things that you like and don't like, and the things that you absolutely need to continue to operate your strategy. So that's a combination of the research that you use and what you really use, not what you just like to read, but what's driving actual decision making.

That's how those decisions are being made amongst you and your peers. And if other peers are key decision makers, they should come along with you on that ride, otherwise your track record becomes suspect or may not be portable. Or you may not demonstrate the same alpha over the long run.

And then ultimately, I think you need to have that sense of, here are my clientele, here's my customer base. I know who will come with me. I know what I need to serve to them, and I can continue to do that if I have the following things. And we don't expect everyone to have an exhaustive list of that, that's our jobs. But they do need some sense of that inventory of what's it going to take to do this beyond just the risk appetite to one day walk in and say, I'm going to start a new chapter in my life.

DAVID LITTLETON: And I'd say, you can distill it down to a checklist. Every case is different. But some items are just always going to be there on that list. You've got to create a new legal entity. You've got to register it. You've got to register the brand name and make sure you can get the domain for a website.

You've got to take all the steps required to secure your track record, which includes getting a hold of legal possession and physical possession of the records, the data, behind your track record. You've got to have a plan to prevent an interruption on the track record as you get fired up. You need to, as Alex said, identify all the systems and other things that you're relying upon you may not even know you're relying upon because you sort of take it for granted when you come into your firm to work every day. But we help you figure out what those systems are and make sure we have a plan in place to replicate everything that's essential.

You'll want to do a budgeting exercise. Make sure that the economics are going to work from day one. You've got to register with the SEC or a state agency. As an investment advisor, you got to make sure you've secured the team of support that you require. And then start thinking about communicating with your clients. Because you want as many of them and their assets to follow you into your new venture as possible.

So that's just sort of a quick sampling of all the things you need to consider. If we really open up the books, it'd probably be a list twice as long, but I think you get the idea.

ALEXANDER MORRIS: And I don't want to scare folks off with, oh my god, here's a list of 100 things. These are things that we naturally start to fill out together as we have conversation.

DAVID LITTLETON: Well, it is scary. But that's our job to help them out.

ALEXANDER MORRIS: And we don't expect folks to be able to sit down in an afternoon and know all of this. We come up with, through conversation, we can fill out the rubric. We're pretty good at ferreting out the questions that some things don't quite align and make sense to know how to line them up before you make that leap. And then ultimately, I think the final step aside from communicating to your clients is communicating to where you're currently working with today.

We've learned from talking to hundreds and probably thousands of folks that a disgruntled PM or partner is rarely a secret. And it's never a good thing for the business, for the investors, for the portfolio manager him or herself. And the real art form is, how do you get enough of this in place to feel confident to go in and have that conversation, to negotiate for your track record, to negotiate for your clients, and to make a good partner.

Because this is a really small industry. And it doesn't take long for trouble to find you if you create it on your way out of your former employment.

BOB STAMMERS: Well, you're going into one of my other questions I was going to ask. Because you are known for these lift out, where you are taking a portfolio management team out of a larger asset manager to create a new boutique firm. So what are the characteristics that you're looking for-- you just covered some of them-- but you're looking for to make an investment and to support that new team and firm.

DAVID LITTLETON: So it starts with the human side of it first and foremost. You know, there has there has to be a chemistry between our firm-- Alex and I as the founders but other members of our firm and the portfolio manager or small team that we're considering lifting out. We have to have a consistent vision for the business that we're going to create together. And I said earlier, but there has to be some sort of risk appetite.

One of the red flags that we look for when we speak to somebody who's considering independence and most of that conversation focuses on guarantees or minimum salaries and that sort of thing. That just tells us they could be great at their jobs and good people in general but they're probably not ready to take the slightly risky ride of creating a new firm.

So having that sort of entrepreneurial gene is an important thing that we look for. And high integrity, and obviously a great performance that will continue to attract investors once the PM becomes independent.

ALEXANDER MORRIS: I think the other item, sort of coming from all of that naturally, is understanding what a boutique really is. So many folks try to define boutique by pure AUM size or revenue. And it's really, we think, much more nuanced than that. Boutique is, in our mind, a relentless commitment to your strategy to continuing generating the return and the alpha that you've generated to date.

But also a commitment to service and to client service, above and beyond what you might get from a big box type product. And then separately-- although we do much of the heavy lifting-- it is important and incumbent upon all of our business partners to understand the business that we're doing. We can't improve our product and our partnership if our partners don't know what they need from us and how well we're serving them, and when it's important to have give and take and how to be a good partner, generally speaking.

And that's something that comes with time, we've discovered. But deep down some folks get it right away. And those partnerships tend to start off on right foot and head down the right direction. And others will take some time to get it. What Dave and I spend most of our time trying to do is avoid the folks who don't or won't get that concept.

And that's not to say that we're turning down strategies we think are no good or that's a statement of the person. For this to work, we need to make sure or have a pretty high level of confidence that both we and the team that's being lifted out together can be successful in the first six to 12 months. Because that's the sort of golden time and magic moment for all of this to happen.

Anything that takes three to five years to start is effectively the same as starting over, and that's tough and tricky for a lot of reasons that we can get into. And by the same token, if we can't get this working in the first few months, inevitably there will be client or other attrition that makes it much harder to recover and to find your footing again.

BOB STAMMERS: How difficult is the due diligence process? Because I think that it's different than traditional asset management firm, you've got people with esoteric assets or strategies that may be hard to get your hands around.

ALEXANDER MORRIS: It can be. Most of the folks on the platform today, the five affiliates that we're working with, are fairly traditional if not totally traditional asset classes. And as a byproduct of the teams that we're ready to move as well as market demand. But as we expand the roster, more esoteric items come on.

Dave and I both have experience in the alternative space. So we have some experience in doing that. But to some extent, unlike a traditional research analyst or at a consultancy or at an RIA, it's not our goal to pick the top one percentile fund or manager all the time. We're looking for folks who can hit in the top quartile, top half, regularly. And then build a business that has a product that is saleable, that has reasonable opportunity to be in demand across cycles, and then who can run a business with us and help grow that, which is a combination of that grit, some internal salesmanship to be able to sell the product.

And more importantly-- and perhaps the dirty secret of all of this-- is that performance is great, but if you can't explain the strategy to the folks who are going to use it, you have no chance of garnering assets. And that's what we call narrative alpha. And part of where I think we've invested time and energy is, how do we tell that story about not just the PM and their journey into this boutique, but rather the strategy, how it fits in the portfolio, how it sits in the boutique model with the service component we provide, with the alpha it generates, why it's different than just either passive strategy or than some of the more benchmark hugging active strategies. And really try to differentiate the product.

Because ultimately we're looking for the right people with the right track record, but that needs to be continued. And that's a mentality. That's a personality trait more so than it is any one skill set.

BOB STAMMERS: What I was really interested in finding out, I know you are true believers in the advantages of boutique firms, especially in the post-COVID era. I was wondering, what characteristics make boutiques better or available to create better investment outcome?

DAVID LITTLETON: You know, so everybody's got a slightly different definition of boutique. Although I think we all kind of know them when we see them. In general, a little smaller size, some people would say under $10 billion, some people would say under a billion, but not a behemoth asset manager. Typically owner led-- the principle's making a lot of the decisions. Deep expertise and specialization-- focusing in on a market segment or a few segments.

And just generally more agile and sort of more of a personal touch, focusing on the investors, on the clients, and on generating alpha. Less focus or less distraction to bureaucracy and sort of big business politics. So if you accept that as a sort of general definition of boutiques, then we can get into what makes them, in our view, a lot more likely to be successful and generate good investment performance over the long term.

ALEXANDER MORRIS: I don't know that I would think that COVID changed much of anything at all. If anything, I think it re-asserted what has always made boutiques great. It's that service commitment that's true to label, no matter what the market conditions are. And arguably, markets helped by proving or reminding us that not everything will be a growth stock bull market. And that in those times, you want someone who is actively out the control panel looking at those stocks, those bonds, those options every day, pulling on levers that they're experienced at. As opposed to just sitting back and hoping that a lower cost, more passive product, will work.

Because ultimately in the long run, that may be the case. But our investors-- all of us, even the most seasoned of us as day to day professional money managers-- still watch our portfolios daily. NAVs get printed daily. And emotions come in minute by minute, tick by tick, not year by year.

And you need to be able to be responsive to that, but not cower and try something completely different and risk being whipsawed or missing out on what you're doing. And COVID, I think, gave us the opportunity to show that active management in particular-- and good active management at that-- can and will shine when given the right circumstances, and indeed in the long run when viewed in the lens of looking for the better managers who are actually doing and fulfilling that commitment.

BOB STAMMERS: So, from the vantage point of your business, what do you think are the crucial ideas and thoughts you would like our audience to take away from this interview?

DAVID LITTLETON: Well, I'll start by saying we're big believers in active management done right. So in the active passive debate-- sure, if you're looking for beta market exposure, get it cheaply through passive vehicles. But if you can find the right managers who can deliver real alpha, then active management is well worth the cost.

And boutique managers are, in general, in a better position to generate that type of alpha. We, as a platform, are speaking to, as I said, hundreds of these folks on a regular basis. And it distills down to a very, very small percentage of the conversations that we have really leading to potential business alliance.

And then ultimately, when a manager launches on our platform, we know that they are as likely, quite likely, to be successful in this environment. And in any investor asset allocator or advisor who's speaking to us or one of our representatives out in the field, they can know that, look, not every strategy is correct for every investor. But if the managers on the FM Acceleration platform, they've been vetted. They're backed is rock solid compliance and operations.

And the sort of headline or operational risk has been mitigated as much as possible. And now you're going to be talking to an interesting set of boutique managers with a story to tell. And hopefully there's a fit with the needs of the portfolio.

BOB STAMMERS: OK, great. Well sadly, we'll have to leave it there. Dave and Al, it's been a great pleasure talking with you and getting more information about FM Acceleration, what it takes to go independent, and the advantage that boutique firms may hold in the current market. Thank you very much for joining us.

DAVID LITTLETON: Thank you Bob.

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I am Lauren Foster. Thanks so much for listening, and see you next week.