

Annual Review of Boutique and Employee Owned Australian Equity Managers 2001

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Melbourne

Dr Steven Vaughan & Associates has recently completed its annual review of emerging Australian equity managers. This research followed an earlier in-depth investigation of these firms, sometimes referred to as boutique managers, which concluded that these firms would be a significant force in the funds management industry in the years ahead.

Commenting on the Review, Dr. Vaughan said "the purpose of this review was to examine how these firms have developed, determine whether they have been winning business from superannuation funds, and prepare advice for clients.

"We focused our in-depth research on 16 managers who fitted the employee owned business model although we are aware of some 30 other small firms, some of whom will inevitably enter our deep research list. "

"These firms are partially or fully owned by the investment professionals managing the money. Some have external capital provided by silent partners and some other firms are part of larger organisations."

"Our first study concluded that employee ownership defined a particular subset of equity managers which superannuation fund trustees would typically group together. These managers are not household names and appointing them to manage fund moneys often requires more deliberation."

"The latest research goes one step further. It has highlighted that size of funds under management, even at levels hitherto considered low, is also having an impact on portfolio style and investment performance. Hence, funds under management becomes a critical aspect of the manager selection decision" Dr. Vaughan said. "We believe it is essential to understand the impact of funds under management on the managers capability. Some institutional investment managers, though not having employee ownership as part of the business model may well offer superior active management potential than the traditional large firm."

The earlier research paper classified emerging managers as Lifestyle, Entrepreneurial or Institutional depending on the features of the firm. Some want to grow aggressively; others plan to stay small, with less than \$1 billion funds under management.

The notable feature of this group managers is their success in growing funds under management over the recent period. Despite a relatively short incubation period for many of the 16 surveyed managers, they have grown total funds under management from A\$4 billion to over A\$9 billion since December 1999, an increase of over 95%. Funds under management have trebled over the past three years (see attached graph).

"We have examined the investment performance for each manager for the period of inception of the new entity and the average performance of the surveyed managers compares very favourably with that of mainstream managers covered by major performance surveys." Dr. Vaughan said.

"The overall success rate on monthly excess returns exceeds 62.5%, which represents a high rate by industry standards. Whilst some of the managers have yet to build a long term track records, these signs are very positive. The incidence of positive rolling annual returns is also relatively high and these managers have on average avoided large negative returns."

"Overall, this research confirms our view that the group of managers will attract more attention. This group will spawn the new stars of the Australian funds management

industry and superannuation funds that are seriously seeking active management for their equity portfolios will find attractive opportunities here" Dr. Vaughan said.

