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STRATEGIC INTELLIGENCE FOR ADVISORS

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MULTI-BOUTIQUE MODELS

Investment firms work best when tightly focused and organized around an investment philosophy.

NEWS **When** the Connor, Clark & Lunn Financial Group was formed, toward the tail end of 2002, the driving force was to take a novel approach to asset management in Canada by creating a structure that allowed for unique cultures within each functional area. Co-CEO Warren Stoddart sums it up as an approach that allows people to retain a sense of their own identity, while giving them the ability to express themselves unfettered in areas they are experts in.

The business structure of CC&L Financial Group, which offers the resources of a large organization with the equity-ownership opportunity of an independent shop, is markedly different from the traditional asset management model that views distribution or investment management as cost centres earning a profit from the value created by managers working in those areas, but not necessarily compensating them in line with their contribution.

NOBLE

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JANET KIMBER

WARREN STODDART, CC&L FINANCIAL GROUP CO-CEO

Q: *How is CC&L Financial Group's relationship with your affiliated investment partners structured?*

A: We've established relationships with each of our affiliates whereby ownership is shared between the Financial Group and the investment managers.

The degree of ownership and compensation is directly proportional to the value each manager brings to the business. We find this is the best way to ensure their ongoing commitment.

Q: *What is your compensation model?*

A: Partners in affiliate businesses are compensated primarily through equity ownership. The direct cost of the business is subtracted from revenues, with the balance then divided in proportion to equity ownership. The intention is to ensure a culture conducive to personal satisfaction.

Q: *Can you tell us about the multi-boutique model? It's prevalent in the U.S. but not so in Canada. Why do you think it hasn't caught up here?*

A: The multi-boutique model addresses one of the conundrums of the asset management business: You need to be big and small simultaneously. Both distribution and operational management

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benefit from economies of scale. The bigger you are the better off you are because you can do those functions better and cheaper.

In contrast, investment management is an area where scale can be, and often is, your enemy. Investment firms work best when they're small, tightly focused and organized around a particular investment philosophy, and where all the players buy into that philosophy.

While the multi-boutique structure is a common arrangement in the financial sector in the United States, Europe and Australia, CC&L is the only multi-boutique asset management firm in Canada.

In a traditional model, it becomes more problematic for the business to function effectively as it gets bigger. Either there's pressure to expand into new products that could potentially conflict with the founding investment philosophy, or the business finds it hard to continue to grow. Firms that follow this model are increasingly struggling with distribution and operational management. Compliance is one of the areas usually cited as contributing to increasing costs.

Q: *How are these relationships formed? Do you recognize their talent and ask them to join? Or do they come looking for your support?*

A: Canada really provides only two options for money management. You can be employees within a large institution or you can hang out your own shingle and do everything yourself.

There are tremendous resources available within a large institution but the culture isn't for everybody. Equity ownership in the business—having an opportunity to realize the true value of what you contribute—is often not available. You might get equity options in the entity which you are a part of, but the value of those options is only loosely correlated with what you're doing.

If you hang up your own shingle, you get equity ownership and the distinct culture that comes with it, but the ever-rising regulatory requirements are making it increasingly difficult to be in the business in that way.

We're trying to go right down the middle by offering the resources of a large organization paired with the equity-ownership opportunity of an independent shop. You can only do that through a partnership that provides a functional specialization of responsibility.

Q: *How much of your business is geared toward retail money management?*

A: Retail is directly or indirectly a big part of our business.

About 25% of our $35 billion in assets are managed on behalf of individual investors, with that amount split between intermediary and direct relationships. Intermediated relationships are those where advisors see our name as sub-advisor on mutual funds. Direct assets come from our own high-net-worth distribution. We also have structured products, such as close-ended or flow-through funds.

Q: *What sorts of services do you offer to the high-net-worth clients of an advisor? Are you offering managed solutions that have mandates managed by affiliates?*

A: There are number of ways we could serve an advisor. An advisor might meet with a wholesaler in support of one of our managed asset programs that we run for a bank or the entities they work for.

Independent advisors could have wholesalers from our firm offer them managed, multi-product asset allocation solutions presented under our name or co-branded with their own firm.

The high-net-worth segment is an area of focus for us. We're different here in that we're not organized around a single investment philosophy. Being a multi-boutique investment organization, the solutions we offer high-net-worth advisors are just that—solutions, not products.

We offer portfolios comprised of different asset classes and investment styles, built using the risk and return policies specified by the client, where the mix is shifted over time in response to changing market conditions.

Instead of promoting a single investment philosophy, we understand different asset classes and investment styles perform differently at different points in the cycle. You tell us what your risk and return objectives are and we'll provide a portfolio specifically tailored to meet those needs and actively asset-allocated to always be where we see the returns coming.

Q: *Can your relationship with your affiliates be terminated if they're not delivering the performance you expect for high-net-worth investors?*

A: Our chief investment officer in the high-net-worth business decides which affiliates will be represented in the product portfolios.

Q: *Does every affiliate have complete autonomy over their investment policy?*

A: In the institutional market our clients determine their own investment policy. Our investment manager affiliates determine their investment philosophy. It's important for us that their investment philosophy is well understood, well defined and consistently pursued. That's what they bring to the table—their skill set in that area—and we're determined not to interfere with that.

Q: *Do your affiliates' investment styles ever dovetail into the styles of other affiliates?*

A: Generally, no. With consolidated distribution you can only sell each solution once, so the affiliates provide what are in the market's view differentiated strategies.

Q: *Are you noticing more retail clients wanting their assets*

The CC&L Financial Group was the only firm where we could focus our time on investing and not worry about the other infrastructure. People ask us how a group of three people can manage the stocks of the world, and I tell them it's not three people. It's three people investing with the support of an additional 95 people in Toronto and Vancouver.

When it comes to the index and quantitative screening of stocks, we get help from the quant team at the CC&L Financial Group in Vancouver. The Investment Resources Group are a team of 37 people that only does number crunching."

—Robert Beauregard, President, Global Alpha, a CC&L associate firm

managed like an institution? Are you seeing portfolio construction demands converging?

A: You're hinting at a really important trend in the marketplace. Instead of looking for today's hot product, advisors are increasingly relying on the teams within financial institutions that are responsible for selecting, monitoring, and for changing managers when they are not performing.

We see the retail programs of large financial institutions trying to emulate the manager selection process of the highest-quality institutional investors.

There's an ongoing debate about open architecture versus closed architecture in managed asset programs. The popular notion is that within an open-architecture program you have the ability to go out and find the best managers in the world.

My question is: Are you able to create a system that identifies what managers are going to be the best performers in the world? I know you can pick from the whole universe of managers and it is easy to identify who performed well historically, but show me your track record of picking the people who are going to perform better in the future. I think the jury's back in on that one.

The money isn't all flowing to the open-architecture models because no one has yet demonstrated a consistent ability to pick managers. What we're finding is that clients can be well served by a proprietary platform, but it's critically important that you provide them with access to multiple asset classes.

If you have all the asset classes and strong partnerships with high-quality people, then they're able to focus on investment management, they tend to perform better, and the clients benefit.

Q: *What do you think will be the biggest challenge for Canadian asset managers in the coming years?*

A: It's a rapidly changing business. I don't know of any other industry where names and positions of industry leaders have changed as dramatically over the last 10 years. But looking back, the challenge has been and always will be execution. Can you deliver for the client? If you can do that with some level of consistency, you'll have a successful business. If you can't, you'll fail.

We're focused on giving ourselves the best chance of executing well. Take the best people and let them focus purely on making investment decisions. We believe this approach creates the conditions for success simultaneously for our clients and affiliates.

Q: *Are there lessons you've learned from the recession?*

A: We didn't lay anybody off. One of the main reasons is that partnership arrangements allow for compensation to vary in response to market conditions.

We don't have bonuses agreed upon on an annual basis. We all know what's going to happen if the markets move. They move, it happens, and we're all still here.

We're actually adding to our business, not shrinking. We added new institutional clients during the downturn. In addition, we're seeing growth in our retail and high-net-worth assets, that's not withstanding that the Canadian mutual fund industry was in significant redemptions in the long-term asset categories.

We're also finding managers increasingly attracted to the multi-boutique model that we offer.

The model worked for the most part. We experienced some pain like everyone else, but our structure allowed us to mitigate that pain and to keep growing. By dint of a diversified clientele we also had businesses that were less sensitive to movements in the market.

Q: *Are you going to consider adding more asset classes, particularly in the alternative asset space?*

A: Absolutely. Historically we've been strong in every asset class that started with Canadian. Those aren't going to be adequate to meet all the needs of our clients going forward. We need more exposure on the foreign equity side.

The alternative space, particularly absolute return-oriented areas less correlated to public market activity, such as infrastructure, is increasingly appealing to more people.

Q: *Are you seeing competition in the Canadian marketplace?*

A: There are no other multi-boutique models in the Canadian marketplace and won't be until there are some real shifts in how people think about the investment management business.

People don't change because they want to; they change because they have to. Canada has so far been a forgiving environment, so a lot of folks have not had to change.

For large institutions it's hard to get into the mindset of offering equity ownership to people who work in the organization. And when it comes to independent asset managers, they find it difficult to attribute value to distribution and operational management if their business leaders come from an investment management background. AER

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