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# How to select a money manager based on... future performance

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In the financial advisory/planning industry the financial advisors have an enormous amount of investment options to consider for their clients. We can select individual money managers, mutual funds, exchange traded funds and individual stocks and bonds. In my practice, we have screened the available investments to less than 60. These 60 options are a combination of professionally managed mutual funds, index like exchange traded funds, money managers and a few high quality individual stocks. In selecting these options, we look at the following non- financial characteristics:

1) Stewardship Grades: Morningstar investment research has developed Stewardship grades for money managers. The stewardship grades tell us if the money management firm is doing what is the best interest of the end investor-you. In other words, do they care about the investor or do they treat the investor like another dollar in the door. The stewardship grade looks at corporate culture, fund board oversight, manager incentives and compensation, fees paid by the investor and regulatory history. The funds that have the best grades treat their shareholders well. They have a corporate culture based on money management versus marketing and sales, they have independent board oversight versus in-house board members, manager compensation based on long term performance versus short term performance, below average expenses and a clean regulatory history. Should it be any surprise that these types of firms have out-performed their peers? We believe money management firms with high stewardships grades will give our clients the best experience going forward. We obviously can't predict future performance but we have the best chance of consistently achieving above average results with these types of firms.

2) Career Research Analysts: I like to work with money management firms that have a high retention rate within their research analyst's staff. The research analysts are the backbone of the money management firm typically doing all of the hard tedious research work to uncover investment opportunities. If the analysts are hired for a few years and then move on to a competitor, all of their contacts and accumulated knowledge and experience is lost. Many of the firms we use treat and compensate their analysts like portfolio managers. Within some of the firms the analysts are also given a slice of the portfolio to invest in their high conviction ideas regardless of the manager's opinion. This all leads to a competitive advantage for the money manager and the end investor since these analysts have developed long term relationships with the CEO's within their industry.

You may have noticed the above two characteristic have nothing to do with performance or fees. These characteristics give us the best probability of above average future performance. I think it is a given and it certainly is for us that any manager we use would have a good track record - ideally at least 10 years - of above average performance. We also select funds with low expenses or at least below average expenses. The funds/managers with the best long term performance tend to be the funds/managers without the drag of high expenses

One final point, I especially like the stewardship grade in times like these as financial scandals continues to proliferate and "Wall Street" is being accused of excessive compensation schemes. These grades tell the end investor- you and I- that there are still firms out there that really care about managing our hard earned money.

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