

Emerging Manager Spotlight

Emerging Managers, Asset Owners Can Benefit From Manager-Of-Manager System

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Manager-of-manager platforms play an important role in the emerging manager ecosystem for both emerging managers and plan sponsors. The managers benefit from institutional insights and capital allocations from manager-of-manager platforms, and participation in these programs can be a significant growth catalyst for future direct mandates. The advantage to the plan sponsors is the ability to make a single investment that provides diversified exposure to emerging managers without significant use of staff resources. They also benefit from the manager selection, convenience and portfolio construction expertise of the manager-of-manager platforms.

Like any maturing ecosystem, there is an opportunity to refine and reimagine emerging manager allocations. Here are five simple ideas that expand the engagement of plan sponsors while complementing the role of manager-of-manager platforms and increasing opportunities for smaller emerging managers to scale their businesses.

Direct Interaction with Plan Sponsors

Emerging managers would benefit from periodic interaction with plan sponsors around investment and business processes, governance and overall firm development. Such interaction could be accomplished by hosting periodic Investor Days to allow unfiltered exposure that gives the plan sponsor a deeper understanding of their current managers and aligns the manager to the expectations and considerations of the plan sponsor.

More Involved Plan Sponsor Commitment

Most plan sponsors have chosen one of two implementation approaches for investing with emerging managers: outsourcing an allocation to one or more manager-of-managers platforms or managing the emerging manager program internally by assigning responsibilities to internal staff, often with limited support. Having been a researcher and capital allocator, I know first-hand of the tendency to allocate to fewer, more established managers in an effort to put more capital to work for the sake of expediency and efficiency. By increasing the staffing of emerging manager efforts, plan sponsors can develop the institutional knowledge and implementation capability to reimagine emerging manager allocations, whether direct or outsourced, and to expand opportunities for smaller entrepreneurial firms.

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Customized Mandates

Customized emerging manager mandates tailored to the plan sponsor's objectives would allow targeting specific criteria, such as a geographic focus, women-owned or small-AUM firms. For example, an initiative that focused on firms with AUM under \$100 million would access a large talent pool and truly represent emerging firms. With a greater sponsor commitment, customized mandates could be scalable and complementary to manager-of-manager platforms. Managers of managers, acting as advisers, could be helpful in structuring and sourcing customized mandates to expand opportunities for smaller, entrepreneurial firms.

Improve the Fairness of Fees

It is well known that emerging manager mandates often come with below-market investment management fees. The fee compression can be particularly significant on manager-of-manager platforms. Emerging managers have little leverage and often accept these lower fees for the sake of AUM growth. In some ways, it is counterintuitive because what emerging managers need in order to scale their business are reasonably sized mandates with fair fees, not smaller allocations at below-market fees, which restrict the financial resources available to address institutional deficiencies.

Definition of Emerging

The definition of “emerging” needs recalibration to include much smaller firms. In some cases, firms with \$5 billion in AUM are still considered emerging managers. In other cases, firms are designated as emerging based on ethnicity or gender alone, regardless of AUM. Moreover, the practice of designating large AUM firms as emerging managers and allowing them to remain in emerging manager programs well after their AUM has exceeded the definition of “emerging” invariably limits opportunities for smaller, entrepreneurial firms. Implementing an AUM ceiling for emerging manager programs is necessary and relatively easy.

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