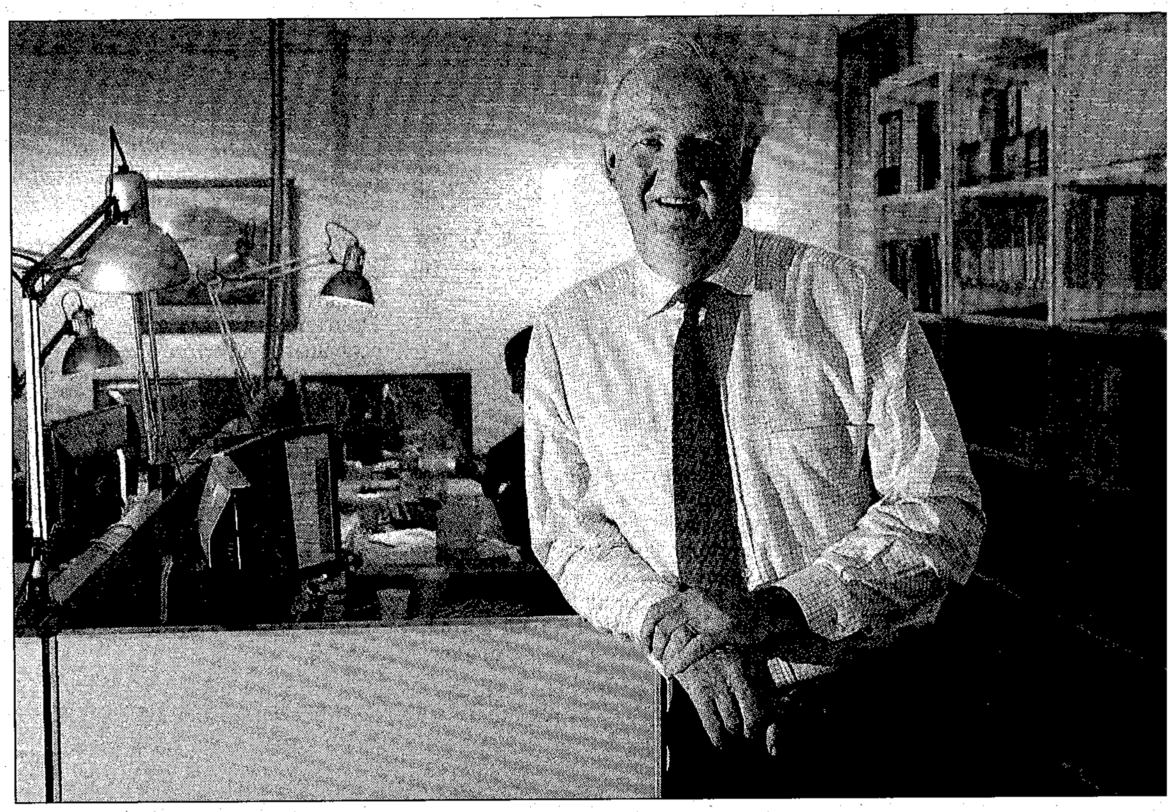
Queen aims to win some hearts

Dunstan
Barrie Dunstan



No holey dollars . . . Steven Vaughan believes boutiques mean money. Photo: JAMES DAVI

Steven Vaughan has spent the past 25 years in the investment world, much of it studying and following boutique fund managers. Now he is preparing to launch an investment vehicle for institutions – Queen Street Partners – which will invest through, and sometimes in, new or emerging boutique equity fund managers.

Queen Street Partners is wholly owned by Macquarie Group's investment arm, Macquarie Investment Management, but it will operate at arm's length, without any sign of the Macquarie holey dollar, with Vaughan and his own investment team in control of investment strategy in Melbourne – and where else but in Queen Street?

Apart from putting together the Emerging Managers Fund, investing in the investment returns from start-up boutique managers, Queen Street Partners will also seek to play a private equity role by taking stakes in selected members of the stable of new managers.

The initial fund will concentrate on Australian equity boutique investment firms; later there is a chance it will also look at any local boutiques investing in global shares. Vaughan says Australia has every right to believe we have capable global managers.

The new fund is expected to be available for investment in the September quarter this year. While new boutiques historically generate higher excess returns in their early stages, he says Queen Street will need special care in constructing portfolios because new managers will have multiple sources of excess return.

Vaughan grew up in funds management, initially with National Mutual (the original home of many current fund managers) and in the Melbourne environment which often seemed more conducive to new boutique operations.

"Melbourne definitely is a boutique town," he says.

He knew many of the earlier, successful boutique managers in Melbourne – like Balanced Equity Managers' Andrew Sisson and Wallara's Peter Wetherall. His manager research, through his own consultancy, specialised in boutiques and included work in conjunction with US group Callan Associates.

He says his associations have helped him understand the business model of boutiques. He says many of the managers who start boutiques are tired of working for institutions. "A true investor likes to be in control of investment decisions," Vaughan says.

"Every good investor just loves [their job]. You talk to these people and, 20 or 30 years on, they still get a buzz coming into the office and trying to pick which stock is going to be the best," he says.

Vaughan contrasts this "buzz" factor with what often became a grind for investment people as the industry was developing and growing in size. This meant more management and business issues, less focus on investment and more on products, distribution and new channels.

"There's a place for that," Vaughan says, "but it takes people away. They get put on committees to look at new opportunities, strategic things and get dragged into corporate activities. I think the institutions have recognised that these are issues and some of them have tried to move to some elements of the boutique structure."

Queen Street's idea of taking equity in boutique managers was originally developed by the giant, $US245 billion CalPERS pension fund in the US. In Australia, a variant of this has been the listed Treasury Group, which has incubated smaller fund managers and offered its shareholders a stake in the earnings of the companies. Vaughan says Queen Street's approach marries the two approaches in a combination to give the institutional investor a stake in the equity as well as the investment returns.

While the movement into boutique managers only became marked from the early 1990s, one of the earliest and most successful was Maple-Brown Abbott, which goes back to 1984 when Robert Maple-Brown struck out from the Rothschild group. Vaughan notes that there were some other boutiques in the 1980s, some of which had trouble surviving the 1987 crash.

Australian equity boutiques with low funds under management have outperformed non-boutiques.

His database of boutiques now covers more than 100 operators and, in the space of the past three years, his working list of managers has jumped from 20 to 60 at present.

In the past eight years, Vaughan says Australian equity boutiques with low funds under management have outperformed non-boutiques by an average of 3 per cent to 4 per cent a year. (He uses a range becau the different types of boutiques – e.g. small cap versus large cap managers – vary in their out-performance).

For all boutiques, however, he says, their average performance fa when they get more funds under management – but they still outperform non-boutiques on average.

Clearly, any outperformance makes managers attractive to the b institutions like superannuation funds seeking that extra investmen return. And part of the reason for success of boutiques is that their business model makes them a profitable business with only $3 billion to $6 billion of funds under management. "You don't have to be a mega manager to develop a good business," he says.

Vaughan says many institutiona investors prefer boutique fund managers because the way they ar organised leads to more stable investment teams. This contrasts with a tradition in the funds indust of a lot of turnover in managemen personnel. "Stability is a good thi for investment returns," he says.