

BEST MANAGERS YOU NEVER HEARD OF

UNCONVENTIONAL WISDOM

"For it is the essence of his behavior that he should be eccentric, unconventional and rash in the eyes of average opinion," wrote John Maynard Keynes, in discussing styles of investment management in *The General Theory of Money, Employment and Interest*:

If he is successful, that will only confirm the general belief in his rashness; and if...he is unsuccessful,...he will not receive much mercy. Worldly wisdom teaches that it is better for reputation to fail conventionally than to succeed unconventionally.

PLANSPONSOR's "Best Managers You Never Heard Of," the class of 2009, includes several of the unconventional sort and, contrary to what Lord Keynes might have predicted, they all have a client following. So far, their reputations are intact.

Our goal in this annual feature is to identify a few managers that combine a solid track record with the high expectations of young, entrepreneurial firms. Drawn from the eVestment Alliance database, candidates are screened on the size of asset base, year of founding, and performance against a benchmark (this year's group are all equity managers). We also check their bona fides with our contacts in the consulting world.



BRC Investment Management

Greenwood Village, Colorado, Founded: 2005

Assets under management: \$330 million

Of the three “Best Managers” for 2009, BRC—“Bounded Rationality Concepts”—is the most unconventional. “We look at irrational behavior and aim to monetize a specific inefficiency that we think exists in the market,” says John Riddle, Chief Investment Officer and Managing Principal. “When we go out and talk to consultants or institutions, people don’t say to us ‘We hear this story all the time.’

“When you introduce our strategy to a multi-manager program,” Riddle says, “you get not only our excess return, but also the added benefit of lower correlation and greater diversification, because our track record is very different from those of other active managers.”

The firm went solo in 2005, after the principals left Duff & Phelps Investment Management Co., bringing with them a track record dating to 1996, and \$150 million in client assets. It fields three concentrated portfolios: 30 to 35 stocks each in the large- and mega-market-cap ranges, as well as a new 130/30 strategy based on the firm’s flagship large-cap strategy.

What drive stocks, contends BRC, are the expectations of investors, and it is the day-to-day changes that make picking the right stocks so difficult. Most managers spend most of their time trying to forecast economic variables—say, Intel’s profits next year. “However, having the view that Intel’s earnings are going to grow 15% doesn’t help much, unless you know what everyone else in the market is expecting,” Riddle observes.

“We realized early on that we couldn’t produce economic and earnings forecasting any better than the professionals on Wall Street, and decided to look for a different sandbox to play in—specifically, the variables associated with changing expectations,” Riddle explains.

BRC is not poring over the expectations of investors, but rather looking at the group that informs those expectations: industry analysts. “The underlying job of an analyst, predicting companies’ earnings years in advance, is a near-impossible task,” Riddle says.

Analysts rely on a technique known as mosaic theory, taking little bits of

From Left: Tawnya Zimmerman, Versella Crunkleton, Mark Jaeger, John Riddle (front), Troy Hansen and Alana Montoya

information from many different sources, to build their earnings models. “They’re chartered to be independent thinkers, but there’s also a sense of interdependence in that they don’t want to look too different from their peers. We believe analysts look at each others’ forecasts, and for guidance from the companies,” says Sharon Ward, on the team since 2003 and the firm’s Director of Fundamental Research. “Analysts each have their own ways of coming up with the best view of the future, but it also results in herding behavior that we track.”

“It turns out that predicting the behavior of analysts changing their estimates is more stable and repeatable than trying to predict economic variables and company earnings,” says Riddle.

“If you look at the 1,000 largest U.S. companies,” he notes, “and identify the 100 that are going to have the most-favorable earnings revisions by analysts, you find that those stocks are up about 70% per year in the last 13 years. We have not found any other single factor that drives stock prices more.”

Photography by Don Cudney