The Enterprising Investor: Pre-Launch, Set-up and Go-Live

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PART I – PRE-LAUNCH PHASE

Introduction

September 30th was the tenth anniversary of Eschler Partnership. Since many funds don't make it this far, this got me thinking about why the Partnership endured. It certainly wasn't strong returns in the early years (they came later). Nor was it a well-honed investment pitch, infrastructure, working capital or a detailed plan (I had none).

Looking back, the key to reaching this milestone was willingness to adapt and delay gratification, and to do whatever it took to stay in the game. All so that I could keep doing something I enjoy. It was not the romantic trajectory I envisaged at the outset. The life of most entrepreneurs is tough and my experience was no different. Believe me, though, I wouldn't have it any other way. Overseeing the savings of friends and colleagues has been a privilege. I have met so many wonderful business partners. Managing a small business has taught me many life skills.

In the following essay I hope to provide advice to emerging managers through the lens of my experience. Each manager has his/her own unique circumstances but there are commonalities on this journey. I will attempt to provide answers to questions often overlooked in the pre-launch, launch and operational phases. Whether you are inspired or dissuaded to go independent by what I describe (or maybe just entertained), I provide observations in the service of the many start-up managers who by necessity start small. One note: My thoughts are not directed at investors who begin with substantial assets under management on day one. These institutional teams, few in number but more often than not publicized, face an entirely different set of incredible challenges and opportunities beyond the scope of this essay.

How competitive is the emerging manager start-up industry?

Because the investment management industry combines low barriers to entry with the potential for incredible rewards it attracts the best and brightest. So, the best way for aspiring hedge fund managers to maximise this potential is to own their fund management business, right? No. The odds are firmly stacked against most emerging managers. In the aftermath of the global financial crisis the industry has become exceptionally competitive. Between the growth in passive and the institutionalisation of the allocator community, any remaining net flows have gone to gigantic multi-strategy hedge funds. These behemoths have performed better than, and sucked the life from, single strategy hedge funds. Sure, one can still get started in the business relatively easily (and Eschler can help you). But the barriers to scale are *enormous*. Arguably, the competition facing generalist managers with long-only, long-biased or traditional long/short equity strategies is even greater. Even assuming one has access to seed capital, scaling a hedge fund business to manage several 100s of millions of dollars in AUM or more is going to cost several million dollars.

Are you doing this for reasons other than money?

My point is this: The aspiring investor had better be doing this for reasons other than the money in the early years. Because, despite a small number of exceptions, chances are it will take years for a financial payback, especially when factoring in lost earnings from employment.

Why did I start Eschler? I think if you asked people to describe me as an investor, they might say my strength is original thinking. Indeed, I started Eschler to have more control over my time and the implementation of my ideas. That was the mission. It wasn't about building out a business or the money. It was about giving myself space to apply creative thinking on behalf of my clients and maximising the likelihood of a good outcome by creating strong alignment. Growing up I had watched my dad run an independent architecture practice and respected his artistic freedom and total dedication to his clients. My business has become more bottom line focused compared to when I started - one thing we never had growing up was enough money! But had it initially just been about the money, I would not have stayed in the game.

Have you consulted the stakeholders?

Still here? Good! You want to be an entrepreneur and build something. You genuinely love investing. You want more control over your time. You want to own the consequences of your decisions. And while you know what the odds are, you also know that few businesses scale without tying up capital as well as asset management can. There is still a key question to ask yourself. Are the friends and family in your network going to enable you? First and foremost, you will need buy in from your significant other. Of nearly equal importance: Have you cultivated a circle of high-net-worth investors who know you personally from work, study, clubs or affiliations? Have you been fortunate enough to have some mentors who can provide counsel? You might also seek a business partner.

Is your partner onboard?

Does your partner have an income to fall back on? The best overall scenario is where your other half continues to earn a fixed salary. If not, even if you have a deep pool of savings, the lack of stability can cause friction. My wife was not amused about the idea of me relinquishing a stable income to pursue a quixotic reincarnation as an enterprising investor (a much more economically rational view than mine). But ultimately the key issue for her came down to healthcare. We had a child on the way. Could we replicate, at a reasonable cost, the private insurance cover we were giving up? Make sure you understand exactly what the pain point is so you can address it head on. In my case, Eschler's birth pre-dated my first son's by about seven months. I had time to find a solution. Had it been the other way around – who knows! To reward my wife's commitment to the cause, I named the practice after her maiden name, Eschler. Unfortunately, the novelty of this didn't last long. My advice – avoid short-term gimmicks!

Will your network of colleagues, university friends, clients and friends support you?

In the mid Naughties, I was very lucky to land in a seat which allowed me to focus on finding great ideas for clients, not just selling the latest merchandise. I don't think I was very good at sales but clients respected the independent thinking. I took clients on trips across America (and China, India and Japan!) looking for interesting companies to invest in. We sent out a macro newsletter which got the attention of some of the most respected macro investors in the business. So, I went to their office and pitched ideas. It's what got me a job on the buyside in early 2008 with David Kowitz at Indus. Some of the investors in my fund today were reading that newsletter in 2007. All you need is a small handful of ex-colleagues, university friends or fellow club members who trust you. Personally, I decided against soliciting immediate family for starting capital, but each family is different (and some have more means than others!).

Key point: Identify the support of *intimate* acquaintances who will support a minimum level of AUM to get you off the ground.

Have you already gained some experience / have you had a mentor?

I joined Indus Capital in February 2008 to work with David Kowitz, who had been the third-most senior partner at Soros Fund Management in the second half of the 1990s, to work on a go-anywhere long-short strategy with a macro overlay. At that point it really felt like the sky was the limit. As a student of market cycles, I should have known better. The global financial crisis arrived mere months into the job. It was a crash course in how hedge funds manage risk during bear markets. The fund fell 25% in 2008 and we decided to give the money back to the family office backer. But I did focus on short ideas during that time which David found helpful and in early 2010 Indus gave me some money to run which is when I set up Eschler. But they redeemed less than two years later!

I haven't talked about this stint much. It was an intense period: a huge bear market, then my position suddenly at risk, then deploying capital for the first time and, finally, Indus stopping me out. So before launching the Eschler Partnership I had this four-year period working and then managing money for David. It was a great learning experience that I will never regret. My message here is this: get some hands-on experience under your belt working for an experienced investor before going it alone. Try to stay at it longer than I did.

Can you do this alone or should you team up with a partner?

As a bit of a loner working on my own comes easily. I like discussing ideas with peers but put me in an empty office for weeks on end and that's just fine. So, for the longest time, Eschler was going to be a one-man band. By the way, there's a lot to like about being answerable only to yourself, not spending time managing a team and keeping costs ultra-low. One of the great attractions of investing is that such a route to market is even possible. Many of the investors I respect the most have made a virtue out of avoiding the rigmarole that comes with building a team. Having said this, I have seen that small teams tend to get from A to B faster. Divide and conquer is the idea here. Running an investment business comes with a lot of hats to wear. If you are on your own the odds of peak performance in all necessary areas are close to nil. If a partner had been irresponsible enough to join me on day one the business would probably have been the better for it. The message here is: Starting on your own is acceptable – indeed it's the only way for most of us and the preferred way for many of the very best. But in my estimation the odds of achieving critical mass go up if you start with a partner, and that matters when the financial clock is ticking.

What is your time horizon to build an economic business?

"Take an idea and take it seriously" (Charlie Munger)

When you work at a larger organisation you can be forgiven for believing that just maybe institutional scale is achievable in 3-4 years as a start-up with small AUM. After all there are huge allocations changing hands and you may even know some of the gatekeepers. My personal experience says to extend your time horizon. A more appropriate mindset is, *I plan to do this for the rest of my life.* Otherwise you might be disappointed at the pace of growth.

"*Be patient, it takes 10 years to build a career in anything*" (Naval)

Assume your returns will drive growth. Eventually compound interest will overwhelm any perceived issues around AUM. If larger clients decide to join along the way, that's icing on the cake. So, the question becomes, how can I stabilise my finances and avoid a crunch that prematurely takes me out the game?

How can you extend your runway?

When I launched Eschler I put my entire pension into the fund. I'd been paying down the mortgage on our flat so there wasn't a lot of money lying around to finance the management company. So I had to compromise. In late 2011 I had been running a small pool of capital mostly for Indus but found myself down 15% from the launch NAV and, soon after, stopped out. By a stroke of fortune two jobs became available at my former employer, head of research in Hong Kong and business development in Europe. I took the latter role as it allowed me to stay in my office and, critically, allowed me to keep Eschler.

By October 2012 I was in a position to launch Eschler Partnership with all of $2.2 million AUM as a "side hustle" with Indus' blessing (a priceless gesture on their part which I tried hard to respect). I stayed in the new role at Indus for nearly five years, all the while running Eschler Partnership for several clients. The upside was obvious: A great salary, new connections and I didn't even have to move down the hall. The downside was that capital raising for the Partnership was off limits and various constraints made running the Partnership challenging. Not least I was spending 80% of my time on the day job but, at times, 80% of my mental energy on the Partnership! By the time I was made redundant at the end of 2016 it was time to go all-in.

My advice is, don't take the plunge unless you're committed for the long-term. There are many ways to stay in the game financially. Ideally you have a couple years' worth of savings and/or a spouse with a fixed salary and you secure $10-20 million in AUM in the first year or two. But be prepared to compromise. I relinquished being able to solicit investors in exchange for financial security. Eventually my double life caught up with me. In the crucial early years, though, a big salary gave me the staying power I needed.

In a pinch, think about how you can earn money from sources other than the fund. Having a day job like I did is extreme; at most firms this won't fly. What about consulting for a former employer or providing research or advice to a family office? Perhaps your writing or communication skills will support a small subscription- or ad-based side hustle. At Eschler, we assist third-party managers to launch their fund and meet their regulatory obligations in exchange for a regular fee. With luck your profit on management fees after business expenses will pay for your living expenses (never include performance fees in your budgeting). But it's important to recognise that other options to earn money along the way exist if one will only seize them.

Economics – seed capital and fees

It goes without saying that your ability to launch depends on finding clients. I hope I've been clear that your day one investors will most likely be *individuals who know you intimately and thus trust you*. It is far less likely that agents or intermediaries facing career risk and institutional dynamics will invest (though they will be curious and take meetings). Should you

offer economics in your business to a cornerstone day one investor? What about the fee structure? Both topics deserve some investigation.

How available is seed capital for emerging managers?

Sit down with institutional investors who invest in emerging managers and they will describe how they typically negotiate a revenue share in your business in exchange for seed capital of $50-75m+ or more. But wait, I thought you said the best case is raising $10-20 million initially? We are talking about two different market segments. A small number of start-up managers have enough exposure to institutional investors to command these seed deals. They typically were either running a multi-billion dollar long only portfolio at a well-regarded shop or had a P&L of at least $20m at an established hedge fund. If this sounds like you, you will soon be knee deep in prime brokerage conferences, investment consultants, due diligence questionnaires and, not least, people management. If not, you are one of the *vast majority* of less well-known emerging managers with experience, skills and a strong network to which this letter is addressed.

Should you offer economics to a cornerstone investor in exchange for seed AUM?

Facing the reality that raising $10-20 million in AUM will be a challenge in itself for most emerging managers, are there situations where ceding part of the business in exchange for a much smaller ticket makes sense? In my experience, yes. When Eschler needed funds to upgrade our regulatory license recently, we welcomed an equity investment in the management company from a longstanding client in exchange for a top up in the fund as well as working capital. It proved a catalyst. We have returned the client's cost - and then some – in only three years. The great Felix Dennis, in his bestseller *"How To Get Rich"* counsels against ceding ownership. But my experience (and that of fellow managers I know) is that it can strengthen alignment and endurance between manager and client.

What fee structure and alignment makes sense for your strategy?

Having convinced your first clients to invest they will likely accept whichever fee you propose. As an emotional buyer they will trust your judgement. And if you ask a prime broker for advice on fees, they will tell you to charge market rates: "*don't do anything unusual, allocators will find it disorienting*". My advice is: Do not abuse your clients' trust. At the margin, lower management fees and above average performance fees are best. But please use a hurdle (preferably compounding) and make sure you've got most of your savings in the fund. I understand the logic of a manager keeping a large part of his/her savings out of the fund to provide a financial ballast. But what kind of message does that send if you are charging a "*heads I win, tails you lose*" performance fee? As you may have gathered by now, I'm an all-in kind of guy. A manager charging performance fees without massive exposure to his/her fund is a red flag for me.

I launched Eschler Partnership by cloning the Buffett Partnership fee structure, zero management fee and 25% performance fee above a 6% compounding hurdle. Do not do this! I say that tongue in cheek because there are few better ways to align manager and client. Well-regarded value investor Mohnish Pabrai's first 'Commandment of Investment Management' is, after all, "*thou shalt not skim off the top*". But without a management fee you must have other income or you may go broke--because none of us are Warren Buffett and most of us are not Mohnish Pabrai. Eschler Partnership net performance is double-digit

compounded over the past decade but it took me seven (seven!) years to earn a material performance fee. I am proud that my earliest clients who put their long-term trust in me received their return *before* any performance fees – indeed before any fees at all - were paid.

PART II – SET UP PHASE / ROLE OF ESCHLER'S PLATFORM

Getting the structure right - Should I apply for FCA authorisation or join a platform?

A great advantage of the investment industry is that, in theory, a manager can work from anywhere. In practice, regulatory frameworks differ widely between jurisdictions so the location of most managers is governed by a power law. On the one hand, if you're in the U.S., congratulations! There is no better place in the world to get started as an investment manager. On the other, it will be a challenge launching your business in the EEA, including Switzerland, both in terms of time and cost.

Fortunately, the U.K. is acknowledged as a close second to the U.S. (and probably just as economical as the U.S. given recent falls in Sterling) and is unequivocally the preferred location to set up shot in the European geography. The regulatory framework in the UK is well-established, with a thriving fund management industry. True, Brexit was un-welcome and continues to handicap U.K.-based managers from growing in the EU.

What is the role of the platform? Why is it valuable?

If the U.K. makes good on rolling back EU regulations, there may be a silver lining. But in the meantime, UK managers like Eschler continue to be subject to European rules but without the benefit of access to EU markets. What this means is the cost of compliance for emerging managers in the U.K. has risen. At the same time, with the UK regulator on the backfoot, applications for authorisation take longer and have become more demanding. Enter the regulatory hosting platform. Most emerging managers in the UK these days "rent" a regulatory solution from an authorised firm. This allows them to benefit from the economies of scale of the authorised firm and go to market quickly. Unless you are one of the managers with a large seed investment, I strongly encourage you to join a regulatory platform.

By mid-2017, having left full-time employment the previous year, money was running low again. At the same time, my living expenses were skyrocketing with two sons entering school. I averted a crisis by finding some consulting work. But what really got things back on track is when I decided to assist fellow emerging managers launching their businesses. Eschler would partner with under-the-radar managers with proven buy-side experience who could benefit from a set-up offering value for money. It is an irony that Eschler's fortunes improved as we found ways to help our so-called competitors who were poorly served by the industry.

Over the past five years Eschler has helped a dozen emerging managers launch their business and meet their regulatory obligations. We have grown continuously through referrals. As investors first and foremost, we understand our clients' needs. Because we have limited capacity, we can provide an efficient service. We are always happy to speak to aspiring emerging managers so please get in touch.

Interactive Brokers democratizes hedge fund management

When I launched Eschler Partnership a decade ago, I was advised to set up a fund. There was less availability of alternatives at the time. Since then, US discount broker Interactive Brokers (IB) has democratized hedge fund management, lowering barriers to entry with its separately managed account infrastructure. No custody fees, fund-like trading and straight through processing from trade to settlement and reporting in client accounts, make IB hard to beat for the small manager. As a start-up manager, your main ongoing cost, other than paying for a regulatory solution, will be fund operating expenses, typically $70,000+ per annum. IB allows you to eliminate these costs entirely. Sure, it might become challenging over time to run a larger amount of AUM on IB. But who cares if going this route facilitates your launch in the first place? As you grow you will have resources to launch a fund at a time of your choosing.

What type of vehicle should you set up to manage assets?

Whether you choose to run SMAs on IB depends on your starting AUM. To get in business, managers with $1-5 million tend to use IB as a matter of course.

There is another solution for managers with clients in the EEA: The actively managed certificate (AMC). Providers like iMaps Capital provide a private label solution for small managers. The AMC is a stock-exchange listed derivative refencing an insured portfolio with custody at brokers such as IB. The set-up cost is modest (EUR 20,000-25,000) with ongoing costs of ~EUR 20,000 and 20bp of AUM. The unique selling point is that clients can simply call their broker and purchase shares in the listed AMC without any of the know-your-customer rigmarole that comes with investing in a fund.

My advice, is, if you have $5-10 million in day one AUM, set up a Cayman fund. The advantage of Cayman is a) while not the cheapest it is much more economical than UCITS; b) you are going with a jurisdiction where 80% of hedge fund assets globally are domiciled, c) tax neutrality and no tax paid within the fund and d) you can access both offshore (non-US) investors as well as onshore US taxable and tax-exempt investors.

If your starting AUM is $20m+ and your investors are in Europe and the UK, you can look at setting up a UCITS fund. It won't come cheap though (think $200,000+ to set up and a similar amount for ongoing expenses).

One mistake I made when initially running money for Indus in 2010/2011 was accepting capital from one of their funds. When my NAV began to fall in late 2011, limited partners in the Indus fund began to ask questions about why they owned this microscopic stake in Eschler, a private fund. Other structuring issues made the situation worse. My advice is this: Do not accept capital from intermediate funds unless it is from a dedicated seeding fund. With so much outside your control due to greater agency risk, you might get stopped out at the wrong time.

How can Eschler's Cayman platform help you?

By a stroke of luck when I set up Eschler we went with a Cayman segregated portfolio company (SPC). This structure allows for multiple discrete funds to be launched under the same corporate structure. We now manage several segregated portfolios (funds). Fund

launch costs are less than half the cost for standalone Cayman funds. We can set up your fund to accommodate offshore and US taxable investors for ~$30,000 which is paid by the fund on day 1 and amortized into the NAV over five years.

For the first year, we waive SPC operating expenses (e.g., directors, directors' insurance, registered office, Cayman fees etc), a saving of $15,000-$20,000. I estimate your year one operating expenses at about 2/3 of the typical $70,000+. We are happy to work with both third-party and Eschler-regulated managers. Get in touch if you want to save money and set yourself up for success.

What type of custodian should I select?

At Eschler, we have onboarded nearly a dozen custodians from Interactive Brokers to Morgan Stanley and several in between (see my assessment of each in Appendix III). Each works best for a specific manager segment. Do not assume that support levels improve with the prestige of prime broker. If you start with a $75m fund at Morgan Stanley you will be amongst the smallest clients. You may not even receive an invitation to their flagship prime brokerage conference. My fund initially worked with Morgan Stanley but with single-digit millions in AUM at the time, Eschler did not fit their business.

The top tier prime brokers are a major stamp of approval, no doubt, but they don't work for most emerging managers. On the other hand, more entrepreneurial prime brokers may be keen to support launches of $10m and up, backed up by high levels of service. Those we know well that have a London presence include Cantor Fitzgerald and Cowen.

Pay attention to prime broker balance sheet strength (leverage and liquidity) and the location of your assets as well. At the margin my preference would be for a U.S.-based balance sheet with London service presence. The prime broker for my fund, Cantor Fitzgerald, is a good example. Remember, it was the London-based subsidiary of Lehman Brothers that left clients stranded. We have also seen historically that European banks get into trouble more often. Introducing brokers who partner with Pershing (Bank of New York) for custody are an excellent solution as they combine a service culture with the strongest balance sheet possible. Two examples would be BTIG and M.S. Howells & Co. Your challenge with these U.S.-based options as a UK-based manager is the time zone.

If my firm is authorised in the UK, where should you market your strategy?

As I hope I've made clear, soliciting institutional hedge fund buyers as a small manager is highly unlikely to yield quick results. Build relationships with likeminded institutions but accept that allocations will materialize years later, if at all. Where you focus your outreach will depend on your network, where you are based, regulation and where capital is most available for emerging managers. Your first priority will be your personal network and local institutions in your area. As you venture further afield, you will find that institutional money in Europe is more conservative and, due to regulatory restrictions (see below), hard to access anyway.

The fact is, nearly all the risk capital targeting emerging managers (with notable exceptions) originates in the U.S. A UK-based manager is obviously at some disadvantage given the physical (and psychological) distance. As an investment adviser registered with the U.S. SEC, however, Eschler should be at a distinct advantage in engaging with U.S. risk capital. We

have taken the view that the return on investing to ensure we meet U.S. regulatory requirements will be extremely high looking out five years. Despite serving only a handful of U.S. based investors at present, I am extremely optimistic about Eschler's long-term growth in the U.S.

What are the rules around marketing in Europe?

Thanks to over-regulation in Europe and Brexit, marketing a small fund in Europe has become complex. If you launch a fund in the UK the management company and fund will fall under the AIFMD, the fund legislation for alternative funds in Europe. This comes with certain costs and benefits. For example, a manager with AUM over EUR 100m must hold a lot more regulatory capital. On the plus side, accepting high net worth investors as clients in a fund is somewhat easier. The management company will also be subject to MiFID (the legal framework for securities markets in Europe) as will any separately managed accounts (which are not considered funds by the AIFMD). MiFID restricts marketing to « professional clients » meeting strict quantitative criteria on wealth and investing experience. Let's explore how this alphabet soup of rules restricts your ability to market your fund in the UK and Europe.

United Kingdom: In the U.K. an offshore fund is considered an « unregulated collective investment scheme » or UCIS and a "non-mainstream pooled investment" (NMPI). Marketing offshore funds to institutions is straightforward: Notify the FCA that you intend to use the national private placement regime (NPPR). But marketing to retail investors is forbidden. Even if your offshore fund invests in something as safe as treasury bills you can't market it to retail investors. So, amongst individuals your addressable market is limited to sophisticated and high net worth investors meeting specific wealth and experience criteria who area already in your network.

This would be fine, except that UK hedge fund managers must also adhere to the MiFID criteria. Specifically, the MiFID definition of eligible investor, known as a "professional client", is stricter. Investors must meet at least two of three "quantitative criteria": 1) liquid assets of at least EUR 500,000; 2) at least an average of ten trades per quarter over the past four quarters; at least one year of broadly defined financial sector experience. Again, institutional investors are, by definition, fair game. But to satisfy the regulator that no retail investors are being solicited, UK managers must keep records to ensure they are only sending materials to professional clients.

European Economic Area: With the UK now a « third country », UK-based managers cannot use the AIFMD marketing passport. Europe-based investors can invest in an offshore fund run by a UK manager but they must initiate contact (reverse enquiry). Most countries also impose unfavourable tax regimes on offshore vehicles impacting taxable beneficial owners at many European institutions. Managers can rely on national private placement regimes for marketing in individual countries but this requires a notification procedure, following country-specific rules and amendments to a fund prospectus. For all the above reasons and more, raising capital in Europe is cumbersome.

What are some practical solutions for marketing in UK/Europe?

First, it is essential to retain proof of marketing suitability when approaching individuals in the UK and Europe. At Eschler we use a white label fund portal (powered by Edgefolio) that requires prospective investors to confirm their "professional client" (or "accredited investor" /

"qualified purchaser" in the U.S.) status. We would like to roll this out to our manager platform to reduce regulatory risk.

A manager with mostly European (ex-UK) clients might consider iMaps Capital's listed actively managed certificates, a fund-like solution that can be marketed throughout Europe, including to retail investors.

Otherwise, one needs to find a regulated partner in Europe to work with. At Eschler, we are excited to be partnering with a Liechtenstein-based asset management company. Liechtenstein is part of the EEA (European Economic Area) which brings access to the AIFMD marketing passport. Managers on the Eschler platform who opt in will soon have the opportunity to be "employed" by the Liechtenstein entity and issued a business card. Subject to certain rules, managers should be able to market throughout Europe, directing interested parties to contact Eschler, the UK manager. Remember, Eschler can manage assets for European investors but only on a reverse-enquiry basis. Once this relationship is up and running Eschler will be unique amongst UK manager platforms in offering this opportunity to managers.

Another option to address the marketing conundrum in Europe is to set up an onshore UCITS fund. Because retail investors in a UCITS fund are supposedly "protected" by various additional restrictions on what the fund can invest in and how, marketing and advertising throughout Europe is permitted. In practice, all these protections seem to do is limit manager flexibility, increase costs and require obtuse disclosures that, from what I can tell, do not further protect investors at all. I do not recommend the UCITS structure for most alternative strategies, though it works fine for liquid equity strategies, as long as they use little leverage, are diversified and have minimum scale. The fact remains, though, that most investors in Europe can only buy onshore UCITS funds in practice, so the structure deserves careful evaluation for the Europe-based manager.

PART III – GO-LIVE

With what frequency and how should I communicate with my investors?

Each manager/client relationship is different, but more communication and disclosure are probably better than less. Personally, I've resisted this trend and have focused my energies on an annual letter, supplemented by shorter quarterly updates and occasional memos. Only investors with a reasonably long investment horizon are suitable for my strategy; with this tempo I hope to attract such investors. We do send out a monthly factsheet purely for housekeeping purposes. More recently, I have also refrained from discussing current investments in letters. For me, it is easier to sell holdings whose fundamental thesis has changed for the worse if I have not elaborated my idea in the public domain. To be clear, though, I happily provide investors in my fund individually with as much disclosure on holdings as they want. Overall, managers should communicate as they see fit. My approach works for me and my clients but it is not necessarily optimal from the perspective of growing assets. I will say that those managers who can create authentic content, including on social media, will attract more attention from potential investors than those that don't. More awareness correlates with more enquiries. This is where I have decided to focus my energies and I suggest you do the same.

What is genuinely different about your strategy that investors can't get elsewhere?

Each investment strategy is unique and each fund manager brings a distinct style. Since much ink has been spilt on how to invest, I will instead limit my thoughts to three important concepts for an emerging manager.

First, be ready with a thoughtful answer to the above question: Remember, if yours is a trading style, multi-strategy shops or large CTAs are probably doing it better, at scale, with more diversification and less key man risk. If your approach is long-term, hundreds of active investing boutiques already specialize in your strategy at scale and with proven trackrecords.

I tell investors my edge is a stockpicking approach informed by a macro perspective born of experience navigating cycles. I know how to construct a portfolio that can withstand and adapt to bull and bear cycles having seen a huge bull market followed by a huge bust in the formative phase of my career ('96-'02). I further utilize this perspective to focus on cyclical stocks, which are often more volatile and prone to mispricing due to the capital cycle and which tend to scare away value investing competition.

Are you laser-focused on generating high returns?

Second, you must focus on generating high returns. These are the lifeblood of your investment practice without which no amount of financial security can make up for. Now, in speaking to allocators, you may well hear that they desire a targeted level of volatility and would be quite happy with objectively mediocre returns. But if you are starting with friends and family capital you can ignore that institutional narrative. Remember, your competitors have more resources and are wagering huge bets with other peoples' money in a competitive effort to generate outsized returns. Don't get me wrong. There is a lot outside your control in the early years. The NAV per share of my fund was down after three years. But there is no excuse for not taking enough risk early on. Over a decade ago I asked a former client, one of the most famous macro traders in the world, about this topic. His response: "*Whatever people say, high returns are best*." I rest my case.

How much have you really thought about risk management?

Third, don't just pay lip service to risk management. Avoiding large drawdowns can make or break a trackrecord. There is a tension here. You need to take risk to generate high returns but you also need to have a plan to stop yourself from making a bad streak worse (this isn't easy!).

I have chosen a risk budget approach I try to implement at the single position level. It's better than a stop loss because it gives me more flexibility to size up positions but, if over time the position sustains a large loss, it eventually "taps me on the shoulder" forcing an honest re-evaluation. A couple years ago I calculated what my trackrecord would have been had I simply sold each of the worst positions once they had individually detracted 4% of NAV. We are talking about no more than half a dozen positions. The implied improvement in compounded return was absolutely shocking. I don't care whether you are a trader or a long-term investor. Risk management involves selling holdings at a loss more frequently than feels comfortable. Easier said than done.

You can also implement a risk budget at the portfolio level. A former Soros trader with a formidable investing reputation once described his approach to me. As long as the portfolio is up on the year, leave the upside alone and ignore volatility. This is how he doubled his fund one year in the late 1990s. But if the portfolio falls 7-8% below the previous high-water mark, reduce risk because before you know it you will be down 20%. Of course, he was known to use a lot of leverage with a directional strategy. I've adapted this idea for my lower octane approach. When the portfolio is down, it helps me to remember that, at a bare minimum, I should not be increasing gross exposure. More likely, I should be raising some cash. Just writing this is reminding me that my current year-to-date return does not give me the right to increase risk, at least not yet.

Putting some thought into a risk management plan will not stop drawdowns. They will come as sure as the sun rises in the morning. But if your preparatory work heightens your awareness during drawdowns and nudges you in a prudent direction, you won't regret it.

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