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Stars in their eyes – do the big names add value to funds?

The likes of Anthony Bolton, Neil Woodford and Warren Buffett have become household names on the back of startling past fund performance. But *David Oakley* asks if their glory days are in the past

Is there really such a phenomenon as a star fund manager, the financial equivalent of a creative or inspirational footballer who drives a team to new heights to produce sublime or outstanding performance?

This question has grown in relevance in recent years as active long-only fund managers struggled to beat increasingly efficient markets and justify their fees. Technology and more readily available data have helped investors price in good and bad news themselves, while passive managers have cut their fees to the bone.

Warren Buffett at Berkshire Hathaway, Bill Gross at Pimco, Invesco Perpetual's Neil Woodford and Anthony Bolton of Fidelity have all been given the star label at various times in their careers. But all have struggled at times to produce world-beating returns over the past few years.

Mr Bolton, who retired this week after more than 30 years at Fidelity, is an example of a fund manager who produced outstanding returns of more than double his benchmark with investments in cheap, small companies at the height of his career in the UK. But he suffered when he tried the same formula in China, although his performance picked up last year and he left Fidelity with the China Special Situations trust well ahead of its benchmark.

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Mr Buffett has only performed in line with the market in the past 10 years, while Mr Woodford and Mr Gross have both suffered recent setbacks as their styles have not fitted the changing times.

Cult of the manager

The very idea that there is such an animal as a star manager, an exceptional person with the X-factor to produce top returns, is relatively new. Mr Buffett was one of the first to gain this special status back in the 1960s. The "star manager" concept then became popular with salespeople as a way to sell funds and products in boom years, just as Real Madrid uses *galacticos* such as Cristiano Ronaldo or Gareth Bale to help sell club merchandise.

But for some, there is no such thing as a star fund manager, particularly in the wake of the extreme volatility after the crash of Lehman Brothers in 2008. Even the top investors are reluctant to label themselves as stars.

Mr Bolton says: "I think performing well is more about working as a team and investing in something that you understand. It is not about one star person.

"You can beat the market if you invest for the long term. But it is much more competitive today than it was 30 years ago. Technology means everyone has the same information, so you need to offer something different."

Another investor attributed star status by some is Hugh Young, global head of equities at Aberdeen Asset Management. He has produced consistently high returns in Asian equities from his Singapore base over the past 25 years.

"I would love to lay claim to be a great star fund manager, but it is more complicated than that," he says. "It is about the culture of the investment group, process and conviction rather than one person, and one bad year can pull down performance. The only thing a fund manager can guarantee is that they will have a bad year."

Financial advisers such as Patrick Connolly at Chase de Vere say successful active funds typically have a talented manager in charge, but producing consistently high or market-beating returns is down to a combination of factors.

These include the process involved in the build-up to a decision to buy or sell, and having the discipline to stick to that process. The culture of the firm is key, as it provides the environment and backdrop that enables individuals to flourish.

Rigorous analysis and a long-term investment strategy, which must be adaptable to changes in the market, are also important. This often means the need for a strong back-up staff, sales team and research force.

Finally, a decisive chief executive with a clear strategy should not be underestimated as one of the requirements for delivering top-notch returns.

Digging into performance

Analysing the performance and styles of six managers widely regarded to have the X-factor, or star quality, provides some revealing insights.

The six – Mr Bolton, Mr Buffett, Richard Buxton, who left Schroders for Old Mutual last year, Mr Gross, Mr Young and Mr Woodford, who departs Invesco to launch his own fund management group this month – have strong long-term records.

On the acid test of performance over 10 years (a time span deemed long enough to judge skill, as opposed to luck) Mr Buffett and Mr Young have only performed in line with the markets, while the others have comfortably outperformed, according to Morningstar data. But over 20 or more years, all six have easily beaten their benchmarks.

The top performer was Mr Bolton, who delivered a 14.6 per cent annualised 10-year return between January 1998 and December 2007 for the Fidelity Special Situations Fund compared with his FTSE All Share benchmark, which delivered 6.2 per cent.

He stepped down and then launched another special situations fund in China in April 2010. After a rocky start, the Chinese fund has delivered a cumulative return of 5.25 per cent compared with its MSCI China benchmark of -3.05 per cent, says Morningstar.

Mr Buxton is the next best performer, delivering an annualised 10-year return of 11.1 per cent between 2003 and 2013 for Schroders, compared with the FTSE All Share's 8.69 per cent. He has also delivered 16.56 per cent since joining Old Mutual in June, compared with the benchmark's 11.8 per cent.

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Style matters

Mr Bolton and Mr Buxton, like their contemporaries, stress the importance of investing in companies that they understand. For this reason, the five equity investors have tended to shun technology companies with high valuations based on future performance.

They also typically hold on to companies for a long time. Mr Buffett says that the ideal length of time to hold on to a company is forever, a view Mr Woodford has backed at Invesco, holding BAE Systems off and on since he started managing money there in 1988. Stock preferences are usually solid blue-chips that produce everyday goods, such as Coca-Cola and Walmart in the case of Mr Buffett, or British American Tobacco and Reckitt Benckiser in the case of Mr Woodford.

Mr Woodford and Mr Young are both considered safe or defensive investors, stressing that a company must have a solid balance sheet, generous dividend payments and strong growth prospects.

Mr Buxton and Mr Bolton are more aggressive. Both place a lot of store on value as a guide to selection. They come from what Mr Buffett termed the "Graham-Doddsville" school of investing, which maintains it is essential to work out the intrinsic value of a stock before you buy it. This might explain their better performances, as value investors tend to outperform investors who place more emphasis on growth.

Although not outright contrarians, who choose out-of-favour companies that are typically close to bankruptcy but with the potential for turning round, both Mr Buxton and Mr Bolton have often gone against the grain and taken bigger risks than their rivals.

Mr Bolton has also done well as an investor in smaller companies, which have historically outperformed mid-caps and large-caps. This bottom-up value approach contrasts with the greater weight Mr Woodford puts on the macro environment. Some blame this for his underperformance in recent years as the economic landscape has changed in a world of quantitative easing and aggressive central bank intervention.

Mr Gross, the odd one out of the six as a bond investor, has also arguably suffered in the so-called new normal environment. This week, it was revealed his Total Return bond fund was beaten by 94 per cent of other fund managers.

Some say Mr Gross is a classical investor, who has pinned his reputation on his ability to make the right calls based on his macro view. A notable error was to sell Gilts four years ago, saying the market was "sitting on a bed of nitroglycerine" because of high public debt levels. Yields subsequently fell to record lows, as prices rose further. However, he has still outperformed over the longer term.

Size matters

For Mr Woodford, though, some critics are more concerned about the size of his funds, which underperformed as they grew larger. Invesco's High Income and Income funds, in effect the same fund, had £23bn under management at the end of last year. Both have underperformed the market in the past five years, a far cry from a close to 80 per cent outperformance at the end of 2004, when they were roughly a sixth of the size.

Terry Smith, the multimillionaire businessman who launched his own asset manager, Fundsmith, in November 2010, says funds should not grow too big. More importantly, he says a fund should be concentrated with a maximum of 25 stocks, otherwise it is difficult to keep abreast of all your companies.

The Invesco High Income Fund has 120 stocks. Many other funds have more than 100 stocks too, as managers like to diversify their portfolios.

Mr Smith dismisses the diversification argument, repeating the view held by Mr Buffett, who says managers only need "diworsification" if they do not know what they are doing. Fundsmith has delivered cumulative returns of 64 per cent since its launch, compared with the 22.9 per cent by its benchmark the MSCI World Index.

Others warn against using past performance as a guide to future returns.

Tom Becket, chief investment officer at PSigma Investment Management, says: "There is no link to a manager's ability to outperform in the future based on looking in the rear view mirror. Past performance can be totally misleading." Mr Becket says

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a manager should be judged on philosophy, such as whether they are a growth or value investor, process, whether they are disciplined enough to stick with their plan and strategy, and positioning, which involves adapting to the markets, either on the macro front or in terms of how different companies and sectors might perform as their industry changes or develops.

Assessing whether a manager meets these criteria is not easy, prompting some highly successful active managers to advocated a passive approach. Mr Buffett recently revealed that his will advises his wife to invest her legacy in a tracker fund.

Mr Smith agrees. "My advice to most people is to go passive. They are cheaper and offer better returns over the long run. There are certain managers who are stars, who do make a difference and do beat the market, but they are very, very rare indeed – and they are difficult to find. Forget the stars and go with the market."

David Oakley is the FT's Investment Correspondent

» Jonathan Eley and guests discuss the performance of fund management's 'galacticos' on the FT Money Show podcast. Download it at **FT.com/moneyshow**

Stars of the future

Who are the current stars of fund management, the investors you would want in your Fantasy Fund Management team? Looking at the tables for cumulative returns over the past five years, there is an array of talent on display.

The equivalent of the star striker would be Ed Legget. He has delivered 353 per cent for the Standard Life UK Equity Unconstrained Fund in the UK All Companies sector. This is unsurpassed in any other sector in the UK market.

Mark Slater's MFM Slater Growth Fund, in second place in the UK All Companies sector, with 319 per cent is also eye-catching, putting him in a fantasy team, alongside Mr Legget.

Samantha McLemore, who manages the Legg Mason Capital Management Opportunity Fund, has produced cumulative returns of 249 per cent to top the North American sector, while Adrian Bignell, who runs the Invesco Perpetual European Opportunities Fund, has delivered 237.4 per cent to finish first in Europe (excluding UK). The team that runs the Aberdeen Global Asian Smaller Companies Fund tops the Asian table with cumulative returns of 167 per cent.

Topping strategic bonds is Eric Holt, manager of the Royal London Sterling Extra Yield Bond Fund, who delivered cumulative returns of 158 per cent.

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Aces in the pack

Stars in the making?

UK All Companies sector

	Fund	Manager	5 year performance (%)
1	Standard Life UK Equity Unconstrained	Ed Legget	**+353.1**
2	MFM Slater Growth	Mark Slater	**+319.3**
3	Cavendish Opportunities	Paul Mumford	**+285.8**
4	River & Mercantile UK Equity Long Term Recovery	Hugh Sergeant	**+260.6**
5	SVM UK Opportunities	Neil Veitch	**+237.4**
Sector average			**+124.2**

North America

	Fund	Manager	5 year performance (%)
1	Legg Mason Capital Management Opportunity	Samantha McLemore	**+248.8**
2	Legg Mason ClearBridge US Aggressive Growth	Evan Bauman	**+191.8**
3	GAM Star Gamco US Equity	Mario Gabelli	**+166.7**
4	Janus US Research	Jim Goff	**+163.3**
5	GAM Star Capital Appreciation US Equity	Wellington Management	**+148.8**
Sector average			**+109.6**

Europe (ex UK)

	Fund	Manager	5 year performance (%)
1	Invesco Perpetual European Opportunities	Adrian Bignell	**+237.4**
2	FF&P European All Cap Equity	Not disclosed	**+185.0**
3	BlackRock European Dynamic	Alister Hibbert	**+181.4**
4	Scottish Widows European Focus	Alexander Darwell	**+146.8**
5	J Chahine Digital Stars Europe	Julien Bernier	**+144.1**
Sector average			**+92.8**

Asia Pacific (ex Japan)

	Fund	Manager	5 year performance (%)
1	Aberdeen Global Asian Smaller Companies	Asian Equities Team	**+166.5**
2	Baring ASEAN Frontiers	Soo Hai Lim	**+142.8**
3	Newton Asian Income	Jason Pidcock	**+142.3**
4	First State Asia Pacific Sustainability	David Gait	**+135.3**
5	Schroder Asian Alpha Plus	Matthew Dobbs	**+131.6**
Sector average			**+82.1**

Strategic Bond

	Fund	Manager	5 year performance (%)
1	Royal London Sterling Extra Yield Bond	Eric Holt	**+158.2**
2	AXA Framlington Managed Income	George Luckraft	**+138.8**
3	Old Mutual Monthly Income Bond	Christine Johnson	**+132.9**
4	Baillie Gifford Corporate Bond	Stephen Rodger	**+126.0**
5	Invesco Perpetual Monthly Income Plus	Paul Causer / Paul Read	**+121.6**
Sector average			**+69.8**

Source: Morningstar

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