How One Small Shop Got Past the Gatekeepers

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By Kevin Burke

It has taken the **AFBA 5-Star Funds** 10 years to get on the big broker-dealer platforms. But after a string of new mandates from national broker-dealer firms, the company is finally poised to gain advisor wallet share.

In recent months, the relatively small fund shop — $350 million in long-term assets — has inked agreements with **UBS**, **Charles Schwab**, **Ameriprise**, **Bear Stearns** and **Wells Fargo** to offer AFBA 5-Star's lineup of seven subadvised funds.

The firm is also seeking relationships with the other major wirehouses. The company expects these mandates to jump-start its flows over the next two years and help the shop realize economies of scale for its fund shareholders.

AFBA's struggle to get wider distribution is a typical challenge for smaller shops that lack the brand recognition needed to get shelf space and the resources to circulate their funds on a massive scale.

"We expect to get some good flows in the fund supermarket channel," says Robert Morrison, president and chief investment officer of the funds and the advisory company **AFBA Investment Management**. Morrison is projecting assets to reach $1 billion by the end of 2008 and $3 billion by the end of 2009.

The new selling agreements are an outgrowth of a reorganization of its fund lineup that involved changing its investment styles, adding share classes, tweaking fees and farming out portfolio management to a greater number of institutional managers.

"Our prior product structure wasn't a good fit for the wirehouses. Some of our products didn't have a lot of reason, so we moved to multiple subadvisors to give us more firepower," Morrison says. The funds now "resonate a bit better with advisors," he adds.

Getting past the gatekeepers as a small, relatively unknown fund can be "a tough row to hoe," says Lisa Cohen, president of sales consulting firm **Momentum Partners** and a former managing director of product management at **Evergreen Investments**. "Unless you have a very unique story to tell, it's really hard to get on those platforms."

And without a large distribution footprint, she says, it's difficult to drive demand at the advisor level and gain brand awareness, something you can get only by being on the various platforms in the first place. "It's a catch-22," she says.

In its search for managers to subadvise, AFBA 5-Star looked for "world-class investment managers" or "undiscovered specialists" in their respective asset classes. Armed with a cross section of reputable subadvisors that includes **Marvin & Palmer Associates**, **Dreman Value Management** and **TrendStar Advisors**, the firm that had once catered exclusively to military personnel is now courting civilians as well.

Smaller managers can boost their chances of getting on the national broker-dealer platforms by following AFBA's lead in providing access to institutional money managers that advisors wouldn't normally have at their disposal, says Owen Concannon, senior analyst at **Financial Research Corp**.

Another way to break through with limited resources is to focus on only one platform and build a relationship with that one firm.

Pairing up with a major distributor is another way to bridge the gap between small shops and their larger rivals. For example, **Valley Forge Capital** entered into a subadvisory relationship with **MFS Investment Management** to run the MFS Sector Rotational Fund.

Dreman, a contrarian value investing shop, is the most notable name on AFBA's list of subadvisors. Dreman manages AFBA 5-Star Mid Cap Value Fund, which recently switched from growth to value and shed its former moniker, AFBA 5-Star Mid Cap Fund.

The fund invests in undervalued companies that exhibit strong fundamentals, above-market dividend yields and historic earnings growth.

In some ways, AFBA 5-Star Funds is similar in nature to **USAA**, which also caters to men and women of the armed forces, and **TIAA-Cref**, which has long run retirement plans for university and hospital employees.

Founded in 1997 as a related enterprise of the nonprofit **Armed Forces Benefits Association**, the for-profit AFBA 5-Star Funds were designed to offer military families their own lineup of mutual funds to add to its existing banking, health insurance and life insurance services.

"Getting on the platform is only one step in the battle," FRC's Concannon says. Most firms have their go-to managers and their backups, and there may not be any room on a broker-dealer's recommended list. "There's a measure of luck to it," he says.

For example, a broker-dealer may feel it was burned by a particular shop and might want to replace it. Another firm can be the beneficiary.

Several factors may have to be in place to make it happen. "It comes down to combining circumstances and performance — that is, building up the track record and being at the right place at the right time," says **Cerulli** analyst Scott Smith.

Getting on platforms, while a rigorous process, has gotten a little easier since the professional buyers have played a more prominent role in selecting managers at most large broker-dealers.

Manager research teams screen based on definable portfolio metrics rather than weighing distribution strength or name recognition. "This has leveled the playing field somewhat," Smith says.

AFBA still has a long way to go before it can play with the big boys, however. From a branding standpoint, it still has very little recognition, and some of that awareness is misunderstood due to its close ties to the military.

Without many wholesalers (three external and two internal) to spread the word, it's going to be an uphill battle — one it is committed to keep fighting.