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Lodestar Investment Counsel is located on South Wacker Drive in downtown Chicago.

Conservative investment strategy pays off for Lodestar

by **DAVID NOELL**

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For the past 20 years, Lodestar Investment Counsel LLC, a small Chicago investment advisory firm, has grown by catering to clients who prefer a low-risk investment strategy.

The firm held more than \$750 million in assets under management in 2007, and then hit a bump in the recession, like all investors.

Even so, Lodestar became more confident because of the recession, according to President Bob Dearborn. Why would an investment advisory firm brag about losses? It comes down to investment strategy and clientele.

According to Mark Ganchiff, a vice president at Lodestar, in 2008 Lodestar's conservative portfolio significantly outperformed the Standard & Poor's 500 Stock Index, which plummeted nearly 40 percent, and then, although lagging the S&P's sharp recovery in 2009, beat the S&P's two-year performance of a 23 percent decline.

Sallie Wilson, a Lodestar client for around 10 years, is extremely happy at Lodestar. "My experience with Lodestar has been fantastic. I have absolutely no complaints," she said, giving Lodestar an A+ in down markets and a B+ in up markets.

Wilson appreciated Lodestar's performance during the recession. "We held on. We were certainly down, but not down the way some people were."

Most of Lodestar's clients are individuals and families. "That's really our niche, is serving that market as opposed to the institutional business," Dearborn said.

These individuals, mostly professionals and owners of closely-held businesses, can't replenish their funds in the same way institutions can replenish a pension fund. Therefore, Lodestar focuses on easing the pain of down markets for its clients.

"Typically they don't have a symmetrical risk-reward bell curve," Dearborn said. "They want to do well in the up markets, but they certainly want to do a lot better in the down markets and preserve their money."

Lodestar has a uniform investment strategy that reflects this sentiment. The firm attempts to avoid risk and has a "long-term growth orientation," Dearborn said.

"Our pattern is that during choppy and down markets we tend to do better, and in rip-roaring, bull markets we tend to have to huff and puff and try to keep up," Dearborn said.

The firm invokes this history: From 1990 to 2009, during the years in which overall market returns were positive, the S&P gained 285 percent, while Lodestar's return on stocks was only 254 percent. During the years in which overall market returns were negative, the S&P was down 83 percent, while Lodestar was down less, 53 percent. For the entire period, the S&P's cumulative return was 383 percent, while Lodestar's was 439 percent.

During the tech bubble that began in late 1999, Lodestar's conservative approach seemed especially slow.

Ganchiff compared success in this period to throwing darts at stock listings in a newspaper to pick the profitable ones. "During that time I recall clients saying, 'What do I need you for? I could train my dog to do this, there's no talent involved,'" said Ganchiff, who was working then at Chicago Title & Trust Co.

"It was difficult to the extent that the market was going straight up and we were going up, but not straight up," Dearborn said.

But the recession cured all that. Dearborn said the recession has reinforced his confidence in Lodestar's approach, especially in light of Lodestar's clientele. "We were just sticking to a fundamental approach of wanting high-quality, liquid assets that were bought at good prices, and with a long-term orientation," Dearborn said.

Lodestar was founded in 1989 by William Goldstein, an experienced asset manager who had previously directed Prescott Asset Management of Prescott, Ball & Turben, a unit of Kemper Corp.

Lodestar initially had 25 clients and about \$30 million in assets under management. Since then, the firm has grown to have over 350 clients and still more than \$700 million.

At the low end, Lodestar customers must have \$1 million in investable assets. At the high end, some family groups have \$40 million. There are five advisers and a total of nine employees at the firm.

Lodestar is small. Chicago-based William Blair & Co. at the end of 2009 managed more than \$36 billion in assets and Goldman Sachs Group Inc managed \$871 billion.

Lodestar's sole source of revenue is fees on assets under management, which makes "a very pure business model," Dearborn said. Because the firm does not provide brokerage service and thus has no incentive to encourage trading, "we have no conflicts of interest with our clients."

Generally, Lodestar has a management fee of 1 percent.

Lodestar competes with bigger firms by having a relationship-driven approach. "All of our work on behalf of our clients is very personal, very customized. No two individuals are exactly alike," Dearborn said.

He said the firm has to pressure some clients to meet even once a year. "That would not be our preference. Our preference would be to get together two, three, four times a year and review," Dearborn said.

Wilson said she greatly appreciates the way Lodestar advisers connect with their clients. "They always answer the phone," she said. Wilson also said they get together every year to re-evaluate her goals for the following year.

Wilson also said Lodestar develops relationships with clients that extend beyond financials. "We do talk about things outside of what x,y,z stock is doing," she said. She even gives restaurant advice to Dearborn because she lives in the city.

Lodestar's marketing strategy reflects its conservative investment approach – reserved. "We don't have a big marketing presence. We've grown by word of mouth, and networking with our clients and other service providers," Dearborn said.

Despite a conservative calling card, Lodestar does consider foreign investment. "As much as we focus on the core investment approach that we have, we're not averse to having some international exposure," Dearborn said, citing more efficient opportunities such as exchange-traded funds. "We're doing more of that than we used to, but it's still a minor portion of what we're doing," Dearborn continued.

According to Ganchiff, about 20 percent to 25 percent of Lodestar's portfolio is in foreign investments.

In sticking to core beliefs, Lodestar is aware of the risk that foreign investing presents. Ganchiff cited some of the difficulties of international investing including sporadic earnings announcements, currency risk, and in some countries the intertwining of the private enterprise sector and government, where business might rise and fall with the rapport the business sector has with the government.

Roughly half of the money that Lodestar manages is in equity investments. The other half is in fixed income, and Lodestar is not changing its high-quality approach in the future regarding bonds. Lodestar is reluctant to invest in non-investment grade bonds.

"Our view on the fixed income is that it's really there to moderate the risk of the equities," Dearborn said. "If we're going to be nuancing our investment approach over time, it's probably going to be on the equity front."



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