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Silvercrest's Silver Lining

By Robert Milburn

Last June, Silvercrest Asset Management Group (ticker: SAMG) went public --a fast-growing money manager led by the former Donaldson, Lufkin & Jenrette veteran G. Moffett Cochran. In many ways it was a great year for the upstart firm, which manages $8.1 billion in private-client assets. In September, after total assets rose 48% a year on average since its founding in 2002, Silvercrest finally reached Penta's 2013 list of Top 40 Wealth Managers ("Seeking Higher Returns," Sept. 16).

In November, however, the 63-year-old chief executive passed away. Cochran had, for the past decade, been quietly battling pancreatic cancer. The market reacted in its unsentimental way—Silvercrest's shares closed the week up almost 1% after the announcement. A month later, smooth as silk, the board selected Cochran's carefully groomed heir, Rick Hough, who had risen through the ranks over 11 years and in 2010 was named chief operating officer.

Therein is a lesson in dignified succession planning—both on a corporate and personal level. None of Silvercrest's 402 wealthy clients have left since Cochran's passing.

That's because Cochran had for a long time carefully planned his succession. When last spring the firm went on its initial-public-offering roadshow, investors peppered Cochran, asking, "What's your succession plan?" Known for his Southern drawl and dry sense of humor, Cochran pointed to Hough and said, "Here's my succession plan," adding, "but not yet."

One semiretired investment banker deeply loyal to Cochran—let's call him James—explained why he is staying on at Silvercrest after doggedly following Cochran from bank to bank for the past 20 years. James was among Silvercrest's first clients and had referred friends and family to the firm, among them his sister and mother, while also tapping Silvercrest for his numerous trusts.

"The transition was very comfortable, even in

New CEO Rick Hough: "We're delivering what we say we are."

Evan Kafka for *Barron's*

(over please)

a very uncomfortable situation," says James. He viewed the "seamless" passing of the baton as a testament to Cochran's and Hough's management skills. He has also warmed up to Hough, saying, "As a client, I trust Moffett's judgment and agree with everyone at Silvercrest that [Hough] is the right guy to take the company forward."

James is still active in a number of private companies, and his diversified Silvercrest portfolio is structured to counterbalance these concentrated private-equity type investments. "What I like about Silvercrest is that they never overpromise but always overdeliver, and I know I can sleep well at night because of that," he says.

James is partially and obliquely referring to the track record of Silvercrest's managed equity portfolios. Among Silvercrest's primary in-house offerings are a half-dozen equity strategies run by portfolio manager Roger Vogel, 57, and his five-person team. Vogel's strategy is

All Silvercrest's equity funds have outperformed their Russell benchmarks.

to find underappreciated stocks, project their earnings growth, and discount those estimates into current-day dollars. Vogel and his analysts manage about $5.3 billion in assets.

As of Dec. 31, 2013, all of their equity funds and strategies have significantly outperformed their respective Russell benchmarks, net of fees, since they were launched between 2002 and 2005. Among Silvercrest's star performers are its Equity Income fund, which produced 11.4% annual returns, versus 8.21% for its Russell benchmark, and its Focused Value, which produced 10%, versus the Russell's 7.8%. For more on Vogel, and a few of his stock picks, see our sidebar to the right.

Those results explain why the relatively small firm caught the attention of CalSTRS, the $176 billion California public pension fund, which handed a $400 million equity mandate to Silvercrest. Such a vote of confidence is doubly reassuring to family clients, since CalSTRS performs top-level due diligence before allocating funds to managers; institutional investors, generally, constitute about 11% of Silvercrest's discretionary assets. "We tell our private families and clients that they're getting institutional-quality investment management. We're delivering what we say we are," Hough says.

It became clear to Hough that Cochran had bigger plans for him when, in 2007, Hough became the youngest partner at the firm and was installed as one of five on Silvercrest's executive committee. "I learned at the knee of one of the best," he says. Hough, now 44, has spent half of his working life at Silvercrest. Previously, he was the founding director of Children's Scholarship Fund, a nonprofit that provides private-school funding for low-income children, a charity founded by the private-equity heavy Ted Forstmann. Hough spent five years establishing the organization's nationwide presence.

Hough concedes he's a bit of a wonk, and revels in statistics and marketing minutiae. If anything, he prefers to be behind the scenes delicately fine-tuning Silvercrest's operations rather than acting as the gregarious oracle and client contact that many families crave. "I'm not the No. 1 client-facing guy on any of the portfolios," he says.

That role, more often than not, falls on Albert Messina, the manager who is also the spokesman for all of the client-advisors on Silvercrest's four-man executive

Vogel's World

Roger Vogel, who heads Silvercrest's equity value team, says recent declines in the stock market were mere profit-taking after last year's strong showing; the volatility surrounding the Fed's tapering, just short-term noise. "I've yet to recall one of my companies come to me saying they're allocating capital based on whether they think the Fed is tapering or not." The economy is improving, he says, and if valuations remain reasonable, "we shouldn't talk ourselves out of being bullish."

When *Barron's* last chatted with Vogel, we were nearing the one-year anniversary of the market bottom ("How to Catch Lightning," Feb. 22, 2010). Vogel's three stock picks outperformed tremendously; after one year, the stocks shot up by 42%, 90%, and 127%, respectively. Vogel here provides Penta readers with three more plays:

AmerisourceBergen (ABC)
This wholesaler of branded and generic drugs is part of "an oligopoly of sorts," says Vogel, competing with Cardinal Health and McKesson. Cash-flow is stable, and the firm consistently reports double-digit earnings growth. "We expect that to continue over the next five years," he adds. An aging population and a wave of generics in 2015, which are more profitable than branded drugs, will continue to drive earnings growth. In September 2013, the company signed a 10-year joint venture to distribute drugs to Walgreen that will also drive profitability. Add in a 1.4% dividend yield and the stock looks tasty. Recent price: $68.58; fair value: $80.

M/A-COM Technology Solutions (MTSI)
"This pick is the highest on our risk/return spectrum," Vogel says. The analog semiconductor maker's products are used in radio-frequency and microwave devices. It was acquired by Tyco Electronics and AMP Inc., and got lost under their joint umbrella. In 2009, it was bought by John Ocampo, a semiconductor investor and now MTSI's chairman. New products are in development, and the company's recent acquisition of Mindspeed Technologies extends its presence to Asia. Its gross margin jumped by 2.6 percentage points in the latest quarter, evidence it's recovering. If management does its job, Vogel expects MTSI's multiple, now 12 times Silvercrest's forward 12-month earnings estimate, to approach competitor Hittite Microwave's multiple of 24. Recent price: $16.96; fair value: high-$20s.

Hillenbrand (HI)
"It used to be Batesville Caskets, a death-care company, which is still a very good cash-flow business but with very little room for growth," says Vogel. Hillenbrand acquired a string of industrial machine-makers, and its customers now include the Frito-Lay unit of PepsiCo, Kimberly-Clark, and ExxonMobil. Revenue has diversified to about 60% industrial and 40% funerary. Vogel expects "organic revenue growth of 4% to 6% over the next few years." Operating margins should climb by two percentage points. Management is also expected to de-lever its balance sheet, which all told should add $3.00-per share in earnings growth. Dividend yield: 2.7%; recent price: $29.49; fair value: $40. —RM

committee. Messina, a born raconteur, relishes telling stories about his clients, many of whom have loyally followed him and Moffett for more than 20 years. Messina recalls a female client whose father passed away. It was 1986. She inherited $8 million, which she gripped with an iron fist, and an unhappy Messina was instructed to invest her money only in bonds. In 1987, the infamous Black Monday set off a worldwide crash, and Messina's client panicked, but he managed to persuade her not to sell everything.

The portfolio eventually righted itself, as Messina patiently educated his client. But for her, the experience was a revelation, and she followed him to Silvercrest and entrusted him with her children's accounts. Whenever there's a downturn, this now-savvy investor calls him, insisting, "Don't sell a thing! We're going to ride through this."

Silvercrest's six acquisitions have added more than $4 billion in assets over the past decade. As COO, Hough handled the last three deals himself. The purchase of Ten-Sixty Asset Management a year ago brought in-house hedge fund due-diligence and risk-analytics expertise; the purchase of Milbank Winthrop added commodity and fund-of-fund capacity. These deals round out Silvercrest's services, but don't expect Hough to expand the firm into more ancillary services.

Future acquisitions are likely to add pins to the map. Headquartered in midtown Manhattan, Silvercrest has posts in Boston; Charlottesville, Va.; and a small office in Los Angeles with two employees. In the near term, Hough plans to build the capacity of the Boston and L.A. offices, making it easier to service Silvercrest's 70-plus California-based clients.

The IPO last year allowed the firm to buy out Vulcan Capital—the private-equity firm of Paul Allen, co-founder of Microsoft—from its Silvercrest L.P. holding; it owned 26.8% of Silvercrest after buying a stake in 2007. Post-IPO, Silvercrest L.P. became a secondary share class owned by 37 Silvercrest principals (along with Cochran's estate), which controls 54% of the company. Now, instead of being a target for acquisition, Silvercrest has the paper to go shopping itself. "On day one," says Hough, "Moffett wanted to make this a public company so that it could continue to operate as an independent firm."

So Hough is now on the hunt for acquisitions that will help the firm more easily service its wealthy clients, with an average assets under management of $20.3 million, spread out across 43 states. But geographic expansion has to be manageable for the firm's 93 full-time employees, Hough insists, adding, "I think other firms have made the mistake of going to too many cities, and creating a lot of small offices that may or may not be profitable." It can also be difficult to unwind commitments and lock-ins once a firm has made hasty acquisitions.

So he is treading carefully, bypassing retirement resorts like Palm Beach, Fla., and Scottsdale, Ariz., and looking for firms in strategically important but often underserved regions. "We want to be in financial money centers, not merely where the wealthy congregate. Think about where the Federal Reserve banks are." In particular, he likes Chicago, Miami, San Francisco, Dallas, Houston, and even Minneapolis/St. Paul, which he calls "a very wealthy city that is underserved by firms like ours."

Hough is actually rather amusing on the subject of acquisitions. "We are not a supermarket, and we don't pretend that we are going to walk your dog," he says, before railing against acquisitive wealth managers who "acquire firms on a seemingly negative financial basis," then stuff client portfolios with proprietary offerings only to "sell these teams when the next deal comes along." Demonstrating that he shares Cochran's wit, Hough dryly adds, "I don't want to rent a business."

Whatever he buys with his post-IPO war chest, the key for Hough, personally, is to keep Cochran's legacy alive and growing, well into the future. "Moffett's ego was such that he believed this was our firm, and he wanted it to live beyond him," Hough says. And that, precisely, is what the new chief executive intends to do.