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In Deep

Using leverage, fund managers and investors try to land the big one.

The Classics

By Ilana Polyak

For clients with a long-term horizon, Mark Rosenbaum and Jana Basden say that nothing beats good ol' asset allocation.

With markets suffering from their worst performance in decades, it might be easy to try something a little more innovative than stocks, such as short positions, puts—anything to avoid further damage. But for one money-management firm in Portland, Ore., classic asset allocation still holds plenty of appeal.

"My sense is that the market is heading up over time," says Mark Rosenbaum, managing partner of Rosenbaum Financial. "We don't want to time the market, and we try to diversify to the greatest extent possible."

The Silo Approach

You would expect such a belief in the long-term possibility of markets from a firm that started in 1957 when Rosenbaum's father, Fred, began selling life insurance and other insurance products to local business owners.

Mark and the elder Rosenbaum started the current company in 1982 and called it Rosenbaum & Rosenbaum. Together, they expanded into other areas, such as executive compensation, estate planning, and benefits management, including pensions. They later changed the name to Rosenbaum Financial to better reflect the broader nature of their expanding business.

As more capabilities were added and the firm expanded into these different areas, Rosenbaum added staff who had the relevant areas of expertise. Investments were a natural offshoot of this progression, as clients then needed help managing pension assets. Much of the company's growth stems from the investment side now.

Today, the firm aims to manage all aspects of a client's financial life, so it is moving away from this silo system into a more integrated model. In addition to being registered investment advisors and stockbrokers, the associates are also charter life underwriters.

"The client will have one main contact at the firm, but we're getting to the point where they are also comfortable speaking with different members of the team," Rosenbaum says.

The Investment Side

Jana Basden handles investments for the firm. Basden's background is in security selection and stock trading, but she also has a certified financial planner designation.

Rosenbaum and Basden pit various market segments against one another to find the best prospects among different securities. They emphasize investments that have had significant outperformance over time and look for those that can continue to outperform for the next 20 years or so. Today, the portfolio tilts more toward international stocks than it has in many years, with about a 30% weighting. That reflects Rosenbaum's view that the recovery, just like the downturn, will be global. Domestic stocks add another 50%, and alternative investments make up the balance.

In the past, Rosenbaum and Basden maintained positions in emerging markets and Europe, but today they emphasize Europe's more-established economies, such as Switzerland. The alternative portion of the portfolio, which has always included real estate, now includes timber, agriculture, and metals.

The firm makes a point of not betting on or against any particular sector or region. "Take our commodities or alternative positions," Rosenbaum says, "We've got 50% in North America and 50% outside."

At the same time, there is a smattering of small and large caps and emerging markets, all in the conviction that these segments will be contributors to performance in the long run. "We believe that there is a historical reason to suggest that small caps will perform well, but there is just as much of a case to be made that emerging markets will provide accelerated performance in comparison to the U.S. in coming out of the recession," Rosenbaum says.

Because of that approach, their portfolios are benchmarked against the MSCI World Index.

Mark Rosenbaum, managing partner, and **Jana Basden**, certified financial planner, Rosenbaum Investments

How they caught our eye: Basden manages funds of funds for the firm's clients using research from Morningstar Direct, an institutional product.

Career path: Rosenbaum began an insurance career in 1977 after attending Lewis and Clark College in Portland, Ore. He founded Rosenbaum Financial in 1982 with his father. Basden started her career in 1981 with Merrill Lynch and worked for Charles Schwab, Bidwell & Co., Banc of America, and Allstate.

Personal: Mark Rosenbaum, 51, is married with two children, ages 21 and 24. Jana Basden, 46, has two children, ages 24 and 25.

Favorite mutual funds: Oppenheimer Commodity Strategic Real Return QRAAX, Delaware Emerging Markets DEMAX, Meridian Growth MERDX

Fund of Funds

The portfolios consist mostly of closed-end and open-end mutual funds. Basden begins her search for funds with Morningstar Direct, a product that allows her to screen through Morningstar's global investment database and analytics. It is most often used by institutional investors. Using Direct "may be fairly unusual for an independent advisor," she says.

Each of the positions makes up at most 8% or 9% of assets to ensure that risk is spread around and to optimize diversification. Basden has several criteria in mind as she's composing the portfolio. For example, when she evaluates a fund's performance, she wants to make sure that it reflects the record of the current manager, not a predecessor.

She's also a stickler for style purity because, with an average portfolio of 24 funds, she wants to be sure that the funds are performing well in concert with one another. "If you're a large-cap manager and you're doing well because you're padding your fund with small-cap names, that's going to mess me up because I've already got small caps elsewhere in my portfolio," she says.

And the returns must be in proportion of the amount of risk a manager takes, she says. "I will not invest in a fund with a great return if the manager is betting the farm for it." But Basden doesn't shy away from risk as long as her clients are rewarded for it.

And she doesn't write off low-rated funds. "For example, both of the commodity funds I have are 1-star funds," she says. "But they invest very differently than the other funds in the category."

What Doesn't Make the Cut

Basden also has strict criteria for dropping funds, though poor performance alone isn't an automatic sell signal. "I had a mid-cap fund that struggled for a couple of years," she says, "but that was because it wasn't participating in the market bubbles. Now, it's doing great."

But a manager change is enough to put her on immediate notice, because there's no indication that the fund will continue to be managed as before. Another red flag is a fund that hews too closely to an index. There is no point in paying higher fees for indexing, she reasons. She's also soured on exchange-traded funds. Advisors have increasingly gravitated toward ETFs, believing that they provide more transparency, liquidity, and lower cost than their open-end brethren. Though Basden likes the ETF structure in theory, in practice, she has had difficulty including them in her portfolios.

"ETFs do have much lower expense ratios," she says. "But they have the problem of trading at a premium to net asset value. That's more true of some of the ETFs that deal with international markets."

That might be due to time-zone disparity, but it is worrisome enough that Basden has all but eschewed ETFs. She includes just four such offerings now. Her criterion is that they "must be the best option for the category." For example, she uses ETFs for investing in the 30 stocks that make up the Dow Jones Industrial Average, as well as timber stocks and stocks of firms domiciled in Switzerland.

Long-Term Perspective

By sticking with a classic asset-allocation model, Rosenbaum and Basden believe that they can create portfolios that are responsive to changing market conditions. But their focus is on the long term.

Rosenbaum is quick to point out that the firm's portfolios are only appropriate for clients with a long time horizon, especially considering the current crisis. "Any client that needs their money in the next seven to 10 years, we will not put them into the market," he says.

Ilana Polyak is a freelance financial journalist.