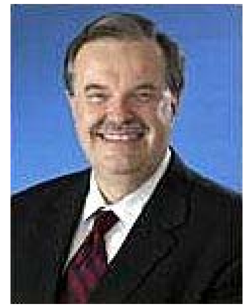
RIA Profile: R.W. Rogé and Company



R.W. Rogé and Company manages $250 million from its offices in Bohemia, NY (a community on the south shore of Long Island), including $25 million in two internally managed mutual funds. Ron Rogé, the founder and CEO, is an often-quoted authority on the advisory business, and we spoke with him about his firm's investment strategy, economic outlook, and the automation challenges he faces.

With 250 clients, the average client size is $1 million, but relationship sizes vary from a few hundred thousand to $20 million. Of the ten people in the firm, seven are professionals, including three portfolio managers, three CFPs, and one paraplanner. Schwab's PortfolioCenter is run in-house for portfolio accounting, SunGard's PlanningStation is used for financial planning, along with Goldmine for CRM and Quickbooks for internal accounting. Rogé believes the firm's competitive edge derives from a thoroughly documented set of procedures – which encompass everything from operations to investment selection – and not from its technology platform. He noted that, like many advisors, he employs a "best of breed" combination of applications, but lacks any systematic integration between those applications.

Risk Assessment and Model Portfolios

Rogé has found that most advisors in the industry use the initial client meeting as an opportunity to sell their services. He rejects this approach, instead using the meeting to facilitate a needs analysis. Prior to the meeting, Rogé and his team will send out a package of information, outlining the firm's investment approach. In the initial two hour meeting, he is able to collect about 80% of the data needed from each client, and will have a good outline of the client's goals and needs, which are then refined over time. Rogé uses a "very old program" that was developed by the American Management Association for risk tolerance assessment. Although the program was not designed for investor risk analysis, Rogé has found that, over the last 20 years, it has produced consistently accurate results. Once the risk assessment is complete, the client is assigned to one of six model portfolios. That portfolio is then customized to meet the unique needs of each client.

Rogé relies on active management for 100% of the assets managed, and does not use any index funds or ETFs. The bulk of assets are invested in actively managed mutual funds, with about $40 million in individual bonds and the $25 in the two Rogé mutual funds. Mutual fund selection begins with the identification of candidate funds, either through quantitative screening (using Morningstar and Value Line) or through the recommendation of peers and industry experts. Rogé has gained a reputation for recognizing skillful managers while funds are still small, even though those funds may have high expense ratios, and cites the Artisan Mid Cap (ARTMX) and Artisan International (ARTIX) funds as examples [Ed Note: ARTIX is among the most popular funds in the Advisor Perspectives universe; ARTMX would be ranked 31st among U.S. mid-cap funds in the AP universe]. Rogé explained that this success comes from a highly detailed due diligence process, which includes as many as 65 essay questions that a candidate manager must answer. Following the questionnaire is an on-site visit or a conference call, which is used to clarify the responses to any of the questions. Once selected, a fund is ranked for preference within a given sector or strategy. Most investments will be in one of the 30 funds that are ranked first on the preference list, but overweighting or other concerns allow Rogé to invest in second or third preference funds.

Rebalancing is generally quarterly, although portfolios are reviewed daily and an over- or underweighting in an asset class or sector can trigger an ad hoc adjustment. Many of the funds used have transaction fees, and Rogé will not rebalance unless the benefits outweigh the costs of those fees.

Investment Strategy and 2007 Priorities

Rogé describes his investment approach as having a "deep value" orientation with a strong emphasis on global economic issues. The value orientation is evident from his reliance on First Eagle Overseas (SGOIX) and the Third Avenue (TAVFX) funds [Ed. Note: SGOIX is the 21st most popular fund in the AP universe*; TAVFX is the 2nd most popular fund among US mid-caps].

At the beginning of 2007, Rogé identified three priorities for the firm's investment strategy. First, Rogé decided to place a greater emphasis on large cap stocks. When asked how this was faring, Rogé explained that "we are not quite there yet. It will take six months to a year to implement a change like this, which we prefer to do slowly." Rogé added that, from 2002 to mid-2006, he had let small caps run and had become extremely over-weighted. They gradually began to cut back on small caps in mid 2006 and watched small caps continue to perform well for a year and a half. Rogé believes that small caps are more interest rate sensitive and, given his concern about entering a recession (more about this below), believes that they are less attractive than mid and large caps. The second goal for 2007 was to move out of individual bonds and into bond funds (mostly the Loomis Sayles Bond Fund (LSBDX), primarily because of the need for greater diversification, but also because the administrative cost of managing individual positions was eroding returns [Ed. Note: LSBDX is the 2nd most popular US long-term bond fund*]. Rogé has lowered his exposure to individual bonds from $80 million to the current level of $40 million. The third goal was to utilize mutual funds with a more concentrated focus, such as the Oakmark Global Select, Fairholme, and Third

Avenue funds. Rogé describes himself as a "big fan of focused funds, even though they exhibit greater volatility." Rogé is able to mitigate the volatility by employing a mixture of concentrated funds.

Non-US investments are approximately 30% of assets managed, and Rogé will increase this allocation for his more aggressive clients. Over the last three years, he has cut back on his exposure to emerging markets, from approximately 18% to 8% of non-US assets. No separately managed accounts or alternative investments are used. Rogé has ruled out alternatives for their lack of transparency and lack of academic studies showing hedge funds outperform mutual funds. When asked whether his larger clients are looking for hedge funds or similar opportunities, Rogé explained that a number of his larger clients came to him because they wanted to get out of alternatives.

The Rogé Partners and Rogé Select Opportunity Funds

A truly distinctive aspect of R.W. Rogé's approach is the utilization of two internally managed, open-ended publicly traded mutual funds. The first is the Rogé Partners fund (ROGEX), which Rogé describes as a fund of mutual funds. It was started approximately three years ago, with the goal of providing an opportunity for friends and family of the firm's clients to invest alongside Rogé's clients. The ROGEX fund holds many of the same funds as are in the typical Rogé client portfolio. Someone who cannot meet the minimum account size to become a wealth management client can still utilize Rogé's investment strategy. As of September 5, 2007 ROGEX has beaten the S&P by over 400 basis points on an annualized basis since its inception, while maintaining a similar level of standard deviation risk and a beta of approximately 1.0. A second fund was introduced in July – the Rogé Select Opportunity Fund (RSOFX) – which uses a focused approach, investing in 30-40 stocks globally with Rogé's deep value philosophy. Much of the funds daily management is handled by Rogé's son Steve, who has a solid track record as an analyst and stock picker. Ron Rogé likes to focus his efforts on portfolio strategy and manager selection.

Rogé's Long Term Outlook

For advisors, Rogé sees that Wall Street layoffs are allowing individuals to start new advisory and hedge fund businesses and are creating a more competitive environment for RIAs. SEC regulation has added $70-80 thousand of annual compliance expenses. Compliance is outsourced, and Rogé has separate compliance officers for the firm and for the internally managed funds, and sees compliance expenses as an increasingly challenging hurdle.

With respect to the volatility in today's markets, Rogé's firm does not have any meaningful exposure to collateralized debt, either through individually owned bonds or through bond funds. In fact, he sees opportunity in securities now trading at attractive valuations. Many securities that were on the firm's watch list are now candidates for purchase. Rogé added that he sees "bargains, but not in any particular sector, although some financials look attractive as do health care stocks."

Rogé's greatest concern is with the state of the global economy and specifically with the possibility of a recession. He monitors economic data and believes there is a better than 50% chance that the U.S. economy will come close to or enter a recession in next year. "If the Federal Reserve steps in now and begins to lower rates we may avoid a recession, but that will present longer term problems for the U.S. dollar," Rogé noted, "which has gone down 30% in the last seven years. But this will have other effects, and I am most worried about long term inflation." Rogé said that the positive side of the weaker dollar is the impact it will have on reducing the trade deficit, but he also worries that use of outsourced labor (from places like China and India) may artificially reduce the inflation numbers that are reported. "We have real inflation that is not showing up in the numbers," Rogé said.

* Note: In the AP listings of most popular mutual funds, the symbol shown is the first symbol alphabetically among all share classes. SGOIX is listed as FESGX and LSBDX is listed as LBFAX. See for a more complete explanation.