THE LEARNING EXPERIENCE CONTINUES: CSULB'S SMIF PROGRAM ENTERS ITS THIRD DECADE

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ABSTRACT

The Student-Managed Investment Fund (SMIF) at California State University, Long Beach, was launched in 1994 with one portfolio worth $50,000. In the two decades since then, the program has grown to include three portfolios with a combined value of more than $250,000, managed on behalf of three different clients, and it has provided learning experiences for the advisors of the program as well as for its student portfolio participants. This paper describes the evolution and growth of the SMIF program over the course of its first two decades and discusses the ongoing organizational, educational, and investment-management challenges it faces as it strives to best meet the challenge of preparing its students for their post-graduate careers.

Keywords: Student-Managed Investment Fund

INTRODUCTION

As increasing proportions of undergraduates in America are drawn toward business majors, from approximately one in seven students in 1970 to more than one in five students today, the relevance and efficacy of undergraduate business education has come under increasing criticism. One bright spot in business education that has risen to meet the challenge of better preparing our students to face the real world of business are student-managed investment funds, or SMIF programs, which have become increasingly prevalent throughout the country as well as internationally. As an example of such a program, and to illustrate a number of the issues involved with such programs, this paper describes the evolution of the SMIF Program at California State University, Long Beach (CSULB), which serves as the backdrop for providing a discussion of some of the benefits and challenges, in terms of both investment performance and the educational process, that a SMIF-type program can face.

OVERVIEW OF SMIF-TYPE PROGRAMS

A little over twenty years ago, when the SMIF Program at CSULB was first established, there were only a handful of such programs throughout the country, and CSULB's was the first such program to receive approval by the Chancellor's office for the California State University (CSU) system. In the two decades since then, there has been an explosion of such programs throughout the country, and internationally as well.

As discussions among panelists discussing SMIF-type programs at various conferences in the intervening decades have shown, though, there is no one "right way" to structure a SMIF program. Rather, there is a wide variety of different ways, along a wide variety of dimensions, in which such programs can be structured and operated. A key distinguishing characteristic, of course, is the size or amount of "assets under management" for the fund (or funds) the students manage, with the largest programs managing millions of dollars and the smallest managing as little as ten thousand dollars or less. But while having a larger fund obviously offers more prestige and cachet for the students, the smaller funds still require many of the same decisions to be made and much of the same work to be done and thus still can provide much of the same educational experience.

Other dimensions along which SMIF-type programs can differ and which can have a more substantive effect on the learning experience include:

- Whether the fund is equity-only, fixed-income-only, or a mix of equity and fixed-income. Equity-only (often "stock-picking") funds are probably the most common, but funds that invest in both equities and fixed-income are becoming increasingly numerous.
- Whether the use of ETFs is allowed (or even required), or if investment must be made in individual (single-firm) securities.
- Whether the use of derivatives is allowed. (Typically, they are not.)
- How frequently trades are allowed to be made. Some funds allow only one set of trades to be made per semester, typically near the end of the semester, while other funds (especially the "stock-picking" types of funds) allow trades to be made pretty much any time that the students agree on them. The most common arrangement is a maximum of once per week or once per class meeting, assuming that the trade meets with the approval of the students (and the faculty advisor).
- The amount of oversight over trade decisions and actual trading. With most funds, a majority of the students (or a majority of the students on the "investment committee") must agree to a given trade before it can be made. The faculty advisor will typically have veto power over any decisions the students make (and may sometimes have a vote, as well), but most advisors express their opinions on the issue during the students' deliberations, but then typically allow the students to proceed with the decisions they make – and to live with the consequences of those decisions – unless they would violate the investment policy statements for the fund.
- How restrictive the investment policy statement for the fund is, how many and what kind of constraints it places on the students' activities, and how highly structured versus flexible the program itself is.
- Whether the program is structured as a for-credit class or as a club or other extracurricular organization. If it is structured as a class, then additional questions include: Is it a one- or a two-semester course? Is it an honors course, for which students have to apply, or is enrollment open to anyone who is interested (subject to meeting the prerequisites, if any)? Can students take the class multiple times? If it is structured as a class, does the advisor give lectures, and are the students given tests and / or other assignments to complete, or is managing the portfolio the sole activity and responsibility of the class?
- And, finally, the size of the program, in terms of number of student participants. Some, probably most, programs, especially the honors-type programs, are restricted to a small handful of students, while others may have dozens of students who participate, in one way or another.

CREATION OF THE SMIF PROGRAM AT CSULB

The Student-Managed Investment Fund (SMIF) program at the California State University, Long Beach (CSULB) was launched in 1994 with one portfolio worth $50,000. The money to fund this portfolio came from two adjunct Finance faculty members, Wes Seegers and Norm Coulsen, both of whom were successful businessmen who became teachers in order to give something back and donated all the salary they earned from teaching back to the department until a sufficient amount had accumulated to start the program. However, with little experience from other SMIF-type programs to draw upon at the time and with a perception that students could not be trusted to make responsible investments, the CSU Chancellor's office was wary of allowing students to manage a part of the university's endowment, so they faced the prospect of the program's creation with quite a degree of trepidation.

After a number of years of organizational efforts and back-and-forth discussions between the donors, the chair of the Finance department, the dean of the College of Business Administration, and the Chancellor's office, the program was finally launched in Fall 1994. In order to assuage the Chancellor's office's many reservations, the donors had to provide assurances that they would not sue the university if the students lost money on any of their investments, and the program itself was structured in a very conservative way. First off, to ensure that the students were as serious as possible and would devote an adequate amount of time to their analysis before making decisions, it was structured as an honors-type program with a one-day-per-week class.

Information letters and application forms were sent out to all MBA students and all undergraduate finance majors, and interested students had to have completed the basic introductory finance and investments courses and apply and go through an interview process before the 12-16 successful applicants were chosen. The students who were chosen were sorted into three or four teams of four students each with whom they would do all the research and conduct all the analysis necessary for the class and then present the results of their efforts to the rest of the class for discussion and voting. The class started out with a $50,000 portfolio and were required to go through an in-depth three-stage top-down approach before they could start investing it, with economic and market analysis coming first, after which the asset allocation was discussed and voted upon by the class, followed by sector and industry analysis and then finally individual security selection, which was to include individual stocks and individual bonds. Of these, the analysis and selection of the portfolio's fixed-income securities came first, so that the portfolio could start accruing interest from these holdings.

Because of the steep learning curve underlying all of these steps of analysis, it could be near the end of the fall semester by the time the fixed-income portion of the portfolio was fully invested and the students could finally turn to the equity portion of the portfolio. The analysis of potential equity securities for the portfolio included in-depth fundamental analysis of the underlying company and an estimate of the value, following multiple approaches, of that company's stock and the derivation of a target price, three to five years out, for it. Typically, quite a few stocks would need to be analyzed before one could be found that would be approved by the class as a whole for inclusion in the portfolio (and by the advisor, who had veto power over any selections made, and by the end of the spring semester typically only a fraction of the portfolio had been successfully invested. Part of this was by design, to limit the amount of risk faced by the portfolio.

Other aspects of the program that were designed to limit risk included diversification guidelines (e.g., no more than 10% of the portfolio could be invested in any one security – so a minimum of ten securities would be necessary to fully invest the portfolio) as well as the requirement for a 10% stop loss order for any security purchased for the portfolio (which had the consequence that the students restricted themselves to stocks that exhibited relatively low enough volatility levels so that they would be less likely to be stopped out). More significantly, so that the portfolio would not face the risk of loss during the summer when the students were not there to oversee it, the portfolio was liquidated at the end of the year and returned to cash. Of course, this policy had the side-effect that, even though the students were required to anticipate what a proposed position would be worth in three to five years, they know that they only had until the end of the spring semester (typically only a few months away even for the earliest positions that were put into the portfolio) for any possible gains from the position to be realized.

This was in contradiction to the typical financial advice to refrain from equity investments for such a short investment horizon, and this further encouraged a sense of conservatism among the students. After the holdings were liquidated, the final responsibility for the students was to design, write, and submit an annual report documenting their year's activities and the portfolio's gains and losses for the year. After that, the portfolio account would be returned to $50,000 (with either excess funds above that amount withdrawn or the amount of any shortfall added from a "SMIF Overflow" account – funded by continuing donations from the original donors – to bring the portfolio back up to $50,000), and the entire process would start all over again for the following year.

GROWTH OF PORTFOLIOS UNDER MANAGEMENT

Given the burdensome responsibilities of overseeing the program, a co-director of the program was added in Fall 2001, with the director and the co-director each getting one course (three unit)'s worth of teaching credit per semester for their participation with the program. In addition to his advice and guidance to the students, the co-director also participated in and developed ties with one of the two local CFA societies, the CFA Society of Orange County (CFAOC) (formerly known as the Orange County Society of Investment Managers, or OCSIM). This involvement led to the creation of the CFA Society of Orange County Foundation (CFAOCF) and the first major expansion of the SMIF program's responsibilities. The CFAOCF was established with a two-fold responsibility – to provide scholarships for worthy local investment students and to provide an added element of realism to investment-management students, such as our SMIF students, through the establishment of an annual request-for-proposal (RFP) competition, with the right to manage an additional portfolio for the following calendar year dependent upon its outcome.

As part of this competition, the students had to submit an in-depth written response to the RFP and then make an oral presentation to the Foundation's Investment Policy Committee. During the first year of the competition, in Fall 2003, the students were "awarded" a $100,000 virtual portfolio to manage for the 2004 calendar year, the responsibility for which was split between the 2003-2004 SMIF class, for the first part of 2004, and the 2004-2005 class for the latter part. Starting from the Fall 2004 competition, donors provided the use of their portfolios for the competition and the students gained the right to manage an additional real-money portfolio of as much as $100,000, the management of which was always split between two year's classes. Starting in Fall 2005, following recruitment efforts by both CFAOCF representatives and the CSULB SMIF program directors, additional universities also started to participate in the annual RFP competition – first California State University – Fullerton, then University of California – Irvine, and finally also Chapman University – competing for portfolios ranging from a virtual portfolio (for the fourth-place team) to real-dollar portfolios ranging from $25,000 up to as much as $100,000.

After a number of years of managing two separate portfolios, the original SMIF portfolio and a CFAOCF portfolio, and reporting to two separate oversight bodies – the CSULB foundation's Investment and Finance Committee and the CFAOCF's Investment Policy Committee, respectively – with regard to their performance, the students of the 2008-2009 SMIF program made a presentation to the board of directors of the 49er Shops – the non-profit corporation that runs the university's bookstore and on-campus concessions – regarding the possibility of managing part of their investment portfolio. The presentation was successful, and, on January 1, 2011, the SMIF students began managing a third portfolio of $100,000 on behalf of the 49er Shops. This brought the SMIF program's assets under management up to over a quarter of a million dollars. At around the same time, an advisory board was created for the SMIF program, and these two developments together brought two additional sets of reports and presentations the SMIF students would need to make throughout the year.

EVOLUTION OF THE CLASS STRUCTURE AND PORTFOLIO COMPONENTS

To accommodate these additional administrative responsibilities, as well as the other consequences of the event of the Great Recession and its aftermath, a number of adjustments were instituted. Because the SMIF students' responsibilities now continued year-round and did not allow for lengthy delays between the start of the school year and the placement of investment securities in the portfolio. This led one of the students, Reuben Conceicao, who had been on the team that had made the presentation to manage a portfolio for the 49er Shops, to stay on as a research assistant for the year following his graduation to develop a new quantitative strategy (described in [1]) to assist the students in determining their target asset allocation more quickly. In addition, and in conjunction with these efforts, the use of ETFs as investment securities was allowed, so that it would be easier for more of the portfolio to be filled out more quickly.

Simultaneously, the class structure underwent changes, as well. Due to budget cuts, along with the retirement of the program's founder, the college reduced its support of the program down to a single program administrator, while the number of students enrolled in the program was increased from around 16 to 20+ students. Unfortunately, as a consequence of the Great Recession, there was also a dramatic reduction in the number of finance students enrolled in the college and, concomitantly, in the number of applicants for the SMIF program, so that it was difficult to maintain the honors aspects of the programs, since almost all applicants were accepted and ongoing efforts had to be made to find enough applicants to fill up all the available positions.

However, this led to somewhat of a "silo" effect among the teams, which, in combination with somewhat of a free-rider effect among some of the weaker students, led to a few classes that, overall, were much less productive and effective than would be desired. Part of this problem has been ameliorated by the rebound in finance enrollments in recent years, which has concomitantly provided a larger pool of more qualified candidates. In addition, the team structure was reverted back to a task-based structure (in which tasks are assigned to teams based on the upcoming portfolio responsibilities) rather than a function-based structure (in which each team has fixed responsibilities for which it and it alone is responsible). Moreover, in an effort to reduce the reliance on any one approach and to take the greatest advantage of being housed in an academic environment, as part of their research efforts the students task themselves with reading and presenting to the rest of the class various Financial Analyst Journal and similar articles, such as [2]-[7], for discussion about whether and how the ideas in such papers can be used to improve the students' portfolio management activities. Finally, there has been a renewed emphasis in bringing the analysis down to the level of individual stocks rather than relying on ETFs to fill out the equity portion of the portfolio.

SUCCESS OF PROGRAM

Overall, the time, expense, and effort that has been devoted to the program to appear to have borne fruit and been successful. Within the program itself, the students have all expressed surprise at how much they have learned about investments and the investment-management process over the course of the academic year. More importantly, once the students leave the program and graduate, quite a few have been able to go on to good jobs in a variety of capacities out in the "real world," whether engaged with educational programs at Bloomberg, working in institutional development at Western Asset

Management and PIMCO, or engaged in security analysis or portfolio management for the Capital Group.

SOURCES OF PROGRAM FUNDING

Unfortunately, all of these beneficial results do not come free, and there have been a number of sources of funds that have supported various activities and expenses related to CSULB's SMIF program. The largest source of funds, of course, has been the college's general funds, out of which is funded the regular salaries for the program director (and, formerly, the co-director, as well), including one course per semester for the SMIF class itself and, in addition, one course's worth of assigned time for the various SMIF-related administrative activities that are engaged in throughout the year. The dean's office also provides the supplies for some of the SMIF students' presentations over the course of the year, as has the 49er Shops. On a larger scale, the college also currently pays for one, and at times has paid for two, Bloomberg terminals, for which the SMIF students get first, though not exclusive priority. Additional funds are provided, on an annual grant basis, by CSULB's Instructionally Related Activities Board, which paid for the acquisition of the first Bloomberg terminal as well as student travel to the RISE Symposium and now the Q-GAME Forum. A final source of funding has been the SMIF Advisory Board, which has donated money for SMIF student scholarships and supplies and has made additional pledges toward increasing our number of Bloomberg terminals.

CURRENT STATUS AND FUTURE DIRECTIONS

As both the college's budget and the pool of dedicated finance students have slowly recovered from the lean years following the Great Recession, CSULB's SMIF program is slowly becoming stronger. More of its alumni are reaching higher positions of greater responsibility and authority and they are starting to be able to provide greater levels of support as well as keep the program informed of current industry trends, such as an increased emphasis on Socially Responsible Investing (SRI) and Environmental / Social / Governance (ESG) guidelines, such as those our advisory board has recently required our students to start following. Another ongoing challenge is how best to integrate the economic and the quantitative analysis that the students conduct into one coherent process. Regardless, the program must and will keep innovating to keep providing the best education and preparation possible for our students.

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