Premium Drag: When Size Slows Implementation

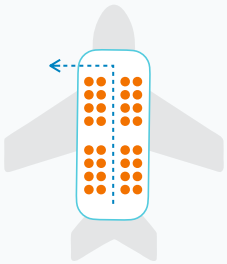
Finding a stock with higher expected returns is only the first step. The portfolio must also buy it. In less-liquid parts of the market, a large manager may need months or years to reach its target weight without pushing the price against itself.

Scale Works Like Deboarding an Airplane

When an airliner reaches the gate, every passenger must exit through one small door. Moving hundreds of passengers through that bottleneck can take 10 to 15 minutes, imposing a cost on everyone onboard. On a private jet, every passenger can be off the plane within a minute. Asset management works the same way. Market liquidity is a scarce resource that must be valued and rationed. Large managers must move more capital through the same limited liquidity. Smaller managers can establish or exit positions more quickly, with less market impact and less opportunity cost. This keeps the portfolio better positioned to capture expected returns.

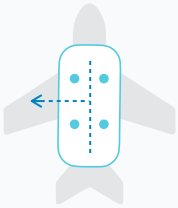
COMMERCIAL AIRLINER
LARGE MANAGER

More capital must funnel through the same limited liquidity. Investors at the back wait longer.



PRIVATE JET
SMALLER MANAGER

Less capital must pass through the market. The portfolio can establish exposure quickly.



Trading Days to Reach Market Weight

Estimated time required to move each portion of the small value universe to its market weight.

	UNDER 1 QUARTER	1 QUARTER TO 1 YEAR	1 TO 2 YEARS	2 TO 4 YEARS	4+ YEARS
NIMBLE FIRM ~$1B in Small Value	100%	0%	0%	0%	0%
LARGE FIRM ~$20B in Small Value	5%	62%	25%	8%	0%
MEGA FIRM ~$50B in Small Value	0%	14%	37%	36%	13%

Scale Creates a Timing Problem

At roughly $50B in small value assets, about half of the eligible stocks are estimated to take more than two years to reach market weight. When managers run multiple strategies, those portfolios compete for the same limited liquidity, further increasing the opportunity cost.

The Drag Works in Both Directions

Slow trading delays both buying stocks with higher expected returns and selling stocks with lower expected returns. Because prices and expected returns change every day, investors must remain nimble to capture the premiums.

Why It Matters

A large manager faces a difficult choice: trade quickly and push prices against the portfolio, or trade slowly and bear the opportunity cost of delayed exposure. Investors face a different choice: hire a manager whose size creates that constraint or hire one with the capacity to act. An unconstrained approach has an inherent advantage over a constrained one.

Illustration assumes trading 2% of average daily volume in each security every trading day. Small value is defined as the smallest 10% of U.S. companies by total market capitalization and the 30% most value companies using price-to-book.
Source: Longview analysis of Russell 3000 constituents as of June 30, 2024.

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