

The Thrilling 36

I set the bar really high and only 36 funds made the cut.

09-04-2020 | by Russel Kinnel

It's time to unveil the Thrilling 36. It's an extremely selective annual list focused on the most important data points for achieving investment success. With more than 8,000 funds out there, you can be super choosy. So, I raise the bar on some crucial metrics, and each year, somewhere between 20 and 50 funds pop out. I don't make any changes to the metrics, so the results are simply the output of screens and not influenced by my opinion. For example, fees have proved to be the best predictor, followed by manager investment. Here are the screens:

- 1 | Expense ratio in the category's cheapest quintile.
- 2 | Manager investment of more than \$1 million in the fund.
- 3 | Morningstar Risk rating below the High level.
- 4 | Morningstar Analyst Rating of Bronze or higher.
- 5 | Parent rating better than Average/Neutral.
- 6 | Returns above the fund's category benchmark over the manager's tenure for a minimum of five years. In the case of allocation funds, I also used category averages because benchmarks are often pure equity or bond and therefore not a good test.
- 7 | Must be a share class accessible to individual investors with a minimum investment no greater than \$50,000.
- 8 | No funds of funds.

For the expense ratio, I use the prospectus adjusted expense ratio. This figure excludes costs that are not collected as fees by the manager such as leverage, shorting costs, or

brokerage commissions. The reason is that it gives us a true apples-to-apples comparison. That's not to suggest that those kinds of costs don't matter. They do matter, but, as they are not collected by the fund company and tend to bounce around, they are more noise than signal.

The Morningstar Risk measure is the risk adjustment used for the Morningstar Rating. It's based on the utility theory of risk and penalizes downside volatility more than upside. I throw out high-risk funds because our studies of Morningstar Investor Returns suggest people have a harder time using high-risk funds well. It's based on a fund's three-, five-, and 10-year records and is measured relative to category peers.

I have not excluded funds closed to new investors. The people who bought them in the past want to know if they still qualify. I have marked those funds as closed in the table. You'll notice that some institutional share classes made the test. That's because they are available for a minimum of \$50,000 or less. Also, there are A shares--yes, a full load can undermine that fee edge, but all of the listed funds are available for no-load as well. Even when sold through full-service brokers, A shares often are sold with no front load or a reduced front load depending on the amount invested.

As you look at the list, you may notice how much it looks like past lists. From last year's list of 34, 28 funds are back this year. I take that as a good sign that these advantages endure and these funds have the potential to serve investors well over a long stretch.

Name	Ticker	Category	Morningstar Analyst Rating	Parent Pillar	Prospectus Adjusted Exp Ratio %	Manager Tenure (Longest, Years)	Return Above Benchmark Annualized Basis Points
American Funds American Balanced	ABALX	Allocation—50% to 70% Eq	Silver	High	0.59	21.5	119
American Funds American Mutual	AMRMX	Large Value	Gold	High	0.61	14.5	144
American Funds Capital Income Bldr	CAIBX	World Allocation	Silver	High	0.61	28.5	160
American Funds Capital World Gr&Inc	CWGIX	World Large Stock	Silver	High	0.78	14.4	63
American Funds Growth Fund of Amer	AGTHX	Large Growth	Silver	High	0.65	26.7	108
American Funds Income Fund of Amer	AMECX	Allocation—70% to 85% Eq	Silver	High	0.58	28.5	152
American Funds New Perspective	ANWPX	World Large Stock	Gold	Positive	0.76	19.6	300
Baird Aggregate Bond	BAGIX	Intermediate Core Bond	Gold	Above Avg	0.30	19.8	48
Baird Core Plus Bond	BCOIX	Intermediate Core-Plus Bond	Silver	Above Avg	0.30	19.8	70
Baird MidCap	BMDIX	Mid-Cap Growth	Bronze	Above Avg	0.82	19.6	62
Baird Short-Term Bond	BSBIX	Short-Term Bond	Gold	Above Avg	0.30	15.9	39
Dodge & Cox Global Bond	DODLX	World Bond	Gold	High	0.45	6.2	138
Dodge & Cox Income	DODIX	Intermediate Core-Plus Bond	Gold	High	0.42	31.5	34
Dodge & Cox Stock	DODGX	Large Value	Gold	High	0.52	28.5	141
Fidelity Diversified International	FDIVX	Foreign Large Growth	Bronze	Above Avg	0.75	19.3	85
Fidelity Low-Priced Stock	FLPSX	Mid-Cap Value	Silver	Above Avg	0.52	30.6	218
Fidelity Select Health Care	FSPHX	Health	Gold	Positive	0.70	11.8	345
Fidelity Total Bond Fund	FTBFX	Intermediate Core-Plus Bond	Gold	Positive	0.45	15.6	25
Harbor Capital Appreciation	HACAX	Large Growth	Silver	Positive	0.67	30.2	173
JPMorgan Hedged Equity	JHOAX	Options-Based	Silver	Positive	0.85	6.6	277
Meridian Growth	MRIGX	Small Growth	Bronze	Above Avg	0.87	6.8	66
Primecap Odyssey Aggressive Growth	POAGX	Mid-Cap Growth	Gold	High	0.64	15.7	212
Seafarer Overseas Gr and Income	SIGIX	Diversified Emerging Mkts	Silver	Above Avg	0.89	8.4	245
T. Rowe Price Mid-Cap Growth	RPMGX	Mid-Cap Growth	Gold	High	0.74	28.1	300
T. Rowe Price Mid-Cap Value	TRMCX	Mid-Cap Value	Gold	High	0.78	19.6	93
T. Rowe Price New Asia	PRASX	Pacific/Asia ex-Japan Stk	Bronze	Positive	0.94	6.1	171
Vanguard Capital Opportunity	VHCOX	Large Growth	Gold	High	0.44	22.4	554
Vanguard Dividend Growth	VDIGX	Large Blend	Gold	High	0.27	14.4	67
Vanguard Energy	VGENX	Equity Energy	Bronze	High	0.32	8.2	184
Vanguard Equity-Income	VEIPX	Large Value	Silver	High	0.27	16.6	119
Vanguard Health Care	VGHAX	Health	Gold	High	0.27	12.2	3
Vanguard Primecap Core	VPCCX	Large Blend	Gold	High	0.46	15.6	98
Vanguard Primecap	VPMCX	Large Growth	Gold	High	0.38	35.1	280
Vanguard US Growth	VWUSX	Large Growth	Bronze	High	0.39	9.8	97
Vanguard Wellesley Income	VWINX	Allocation—30% to 50% Eq	Gold	High	0.23	13.5	138
Vanguard Windsor	VWNDX	Large Value	Bronze	High	0.30	7.9	41

The 8 Newbies

Let's start with a look at our eight new entrants.

American Funds American Mutual (AMRMX)

This strategy certainly captures American Funds' strengths. The firm does a great job with dividend-focused portfolios. It targets an income level but doesn't take too much risk to achieve it. In the 2020 bear market, some equity-income funds' exposure to heavily indebted companies and the economy burned them. But this fund's emphasis on quality and a modest cash stake limited losses to 29.5% compared with 34.4% for the FTSE High Dividend Yield Index. The fund's year-to-date 3.9% loss puts it in the top 5% of large-value funds. Going back to the longest-tenured managers' 2006 start date, the fund is well ahead of its peers and Morningstar Category benchmark. Moreover, seven of the fund's eight managers have more than \$1 million invested.

JPMorgan Hedged Equity (JHQAX)

This fund has the sort of record that alternative managers imply they will produce but then fail to deliver. It holds up well in down markets and has performed consistently in most years. The fund follows a systematic process for buying and selling options on the S&P 500 index, which serves to curb losses at the price of limited gains. The fund is up 5.4% for the year to date and has gained 7% annualized since its 2013 inception.

Meridian Growth (MERDX)

Managers Chad Meade and Brian Schaub are seasoned small/mid-growth investors who seek stable growers with competitive advantages. They have had a lot of success with that approach here and before at Janus. The portfolio is a little quirky. It has a big tech weighting like you'd expect but also a sizable investment in industrials and consumer cyclicals. They were careful to keep the fund from growing too big and closed it in 2014.

Primecap Odyssey Aggressive Growth (POAGX) and Vanguard Capital Opportunity (VHCOX)

This pair of closed funds from Primecap made this list for many years but fell off when the risk ratings were High. The funds certainly qualified on return measures, as they've

run circles around the index. Now their risk ratings have dipped to Above Average, ironically amid one of their worst calendar-year performances. Travel stocks have singled the funds this year, but we still rate them Gold, and four of the five managers have more than \$1 million invested in the Primecap fund and three out of five are over \$1 million in the Vanguard fund. (I own both of these.)

Vanguard Health Care (VGHGX)

This fund returns to the annual list after a short absence. Returns have been neck and neck with the benchmark, so it's kind of prone to popping on and off the list depending on when we run the numbers. Despite this, the fund's strengths are dependable. At 0.32%, it is a bargain for a sector fund. Jean Hynes and a deep team at Wellington runs it with a sensible strategy of looking for innovators with competitive advantages but tempering that with valuation discipline.

On Sept. 3, the fund's rating was placed under review on news that manager Jean Hynes will become the CEO of subadvisor Wellington Management Company on June 30, 2021, when current CEO Brendan Swords retires. Hynes, who became a comanager on this strategy in 2008 before taking over as the sole skipper in 2013, will remain at the helm going forward. Watch for our updated rating to come shortly.

Vanguard U.S. Growth (VWUSX)

It's great to see this fund enjoying a day in the sun. Vanguard had a rough go of subadvisor selection here, but things have settled a bit. The fund now has a solid lineup of five subadvisors: Baille Gifford, Jackson Square, Jennison, Vanguard's Quantitative Equity Group, and Wellington Management. It's a strong group, and it is enjoying a great year, with a 29% gain so far in 2020. The fund has long had low fees, but the subadvisors are finally settled and functioning well. Knock on wood.

Vanguard Windsor (VWNDX)

I didn't expect to see this fund make it through. Like most deep-value funds, this one has had some low points, and this year it even lost as much as the average large-value fund. But it does boast a good pair of subadvisors in Wellington and Pzena. David Palmer took over as lead manager on

Jan. 1, 2019, but the fund still passes the five-year hurdle because Richard Pzena's tenure goes back to 2012. And of course, it has low costs. Strong years like 2019 and 2017 were enough to push returns ahead of the benchmark going back to Pzena's 2012 start date. This fund definitely requires some patience.

16 stalwarts

Now that I've highlighted the new additions, let's look at 16 funds that were in the first edition of this list in 2012 and that illustrate its strength. Each has a great team of investors behind it that has stuck to its principles. The funds look very similar to how they looked eight years ago.

American Funds American Balanced (ABALX) and American Funds Income Fund of America (AMECX) illustrate two things in American Funds' wheelhouse: income and reach. The firm does a great job of providing a good yield in a well-designed strategy that avoids taking on too much risk. Combine that with their managers' long tenure and the deep bench from which they can draw to replace retirees and you have very dependable vehicles.

American Funds New Perspective (ANWPX) and American Funds Growth Fund of America (AGTHX) also reflect the firms' global reach packaged in a fairly low cost vehicle.

American Funds American Mutual (AMRMX) and Primecap Odyssey Aggressive Growth (POAGX) have the unusual distinction of being on the newbies list and on the founding list as they fell out recently only to come back as fees and risk levels moved back under the line. (Vanguard Primecap (VPMCX) and Vanguard Primecap Core (VPCCX) have also been mainstays since the beginning.)

Dodge & Cox Income (DODIX) and Dodge & Cox Stock (DODGX) were on the first list and this one. Analysts and managers make a career of working at the firm helping the funds stay true to their philosophy and process over time.

Fidelity Low-Priced Stock (FLPSX) manager Joel Tillinghast just continues to produce for investors.

Fidelity Total Bond (FTBFX) has been a dependable, though aggressive, strategy under Ford O'Neil.

Harbor Capital Appreciation (HACAX) has been a great growth fund for a long time thanks to subadvisor Jennison. A deep group of analysts and managers back longtime lead manager Spiro "Sig" Segalas, bolstering our faith in this fund even when he retires.

Vanguard Dividend Growth (VDIGX) and Vanguard Equity-Income (VEIPX) show that American isn't the only shop with some skill in income-driven equity investments. They benefit from Vanguard's low costs and the enduring strength of Wellington Management Company. Vanguard Energy (VGENX) isn't an income play, but it has likewise benefited from the combination of low costs and Wellington investment savvy.

The Dominant Fund Companies

Having low costs, strong corporate culture, skilled managers, and strong performance is no easy feat. That's why just a few fund companies dominated the list. These are the fund industry's version of competitive advantages, and they are very hard to achieve. You can see the long-term focus of all these firms and their managers. So many have more than \$1 million invested because they are there for the long haul and truly believe in the process and their colleagues.

Vanguard has the most funds with 10, followed by American with seven, and Fidelity and Baird with four. T. Rowe Price and Dodge & Cox each landed three funds on the list.

Who Fell Out?

American Funds AMCAP (AMCPX) and American Funds Global Balanced (GBLAX) both still pass the performance test, but this time they came up a hair short on the fee test.

Dodge & Cox Global Stock (DODWX) suffered a brutal first half of 2020, and it now lags its benchmark since inception.

Vanguard Wellington (VWELX) and Vanguard GNMA (VFII) fell out because they no longer have managers with tenures of five years or more.

Vanguard Explorer (VEXPX) no longer has a manager with more than \$1 million invested since Ken Abrams, of subadvisor Wellington, retired. Daniel Fitzpatrick, his successor at Wellington, does have between \$500,000 and \$1 million invested.

T. Rowe Price Capital Appreciation (PRWCX) actually wasn't on the list last time, either, but because I always get a lot of questions about it: The fund missed the expense ratio screen by 4 basis points. Don't worry, we still rate it Gold.

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Results as of September 30, 2020

Fund name	Inception date	Average annual total returns (%)				Expense ratio (%)
		One year	Five years	10 years	Lifetime	
American Balanced Fund® (ABALX)	7/26/75	2.78	8.20	9.17	10.36	0.59
American Mutual Fund® (AMRMX)	2/21/50	-1.27	9.54	10.25	11.37	0.61
Capital Income Builder® (CAIBX)	7/30/87	-6.29	3.97	5.31	8.43	0.61
Capital World Growth and Income Fund® (CWGIX)	3/26/93	3.74	8.08	7.63	9.95	0.78
The Growth Fund of America® (AGTHX)	12/1/73	24.54	15.48	14.01	13.62	0.65
The Income Fund of America® (AMECX)	12/1/73	-4.03	6.15	7.26	10.46	0.57
New Perspective Fund® (ANWPX)	3/13/73	18.11	13.01	11.20	12.23	0.76

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

Investment results assume all distributions are reinvested and reflect applicable fees and expenses. Returns greater than one year were annualized. Expense ratios are as of each fund's prospectus available at the time of publication. When applicable, investment results reflect fee waivers and/or expense reimbursements, without which results would have been lower. Please see capitalgroup.com for more information.

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If used after December 31, 2020, this article must be accompanied by a current American Funds quarterly statistical update.

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