



Know What You Own

by Glenn E. Atkins, CFA

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That's sounds very much like that old real estate mantra, Location, Location, Location, and with good reason. In any investment portfolio it's important to know what's in it. This is particularly true when it comes to mutual fund portfolios.

Mutual funds have been at the front of the investment news cycle for months now. Scandals, fees and the privileged few dominate the news flow. Let's forget about that for now and look at mutual funds strictly from an investment perspective.

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Mutual funds are great for the very small investor (generally less than \$100,000) who needs diversification and for 401(k) type plans. But the phenomenon we see over and over again is that many mutual funds hold many of the same stocks, thereby denying the investor the full benefits of diversification that should be afforded to them.

Just for fun I picked ten of the largest fund companies (actually the first ten I thought of) and then picked one fund from each family that I thought represented that family's "flagship" fund. Maybe it was the flagship fund and maybe it wasn't and I really don't know because this is not a scientific study anyway. I then examined the top ten holdings of each of these ten funds.

The funds were Fidelity Magellan (FMAGX), Janus Fund (JANSX), Strong Large Cap Core (SLCRX), American Funds Investment Company of America (AIVSX), Aim Constellation (CSTGX), Dreyfus Large Cap Value (DLCVX), Federated Large Cap Growth (FLGAX), Franklin Large Cap Value (FLVAX), Putnam Voyager (PVOYX), and the T. Rowe Price Blue Chip Growth (TRBCX) fund. We

could have the debate of whether these funds are apples-to-apples and whether they are all comparable, but we'll save that for later. Actually, it might not matter whether they are alike or not.

The following number of funds held the following stocks among their top-ten holdings:

<u>Stock</u>	<u>Top 10 Holdings Held By # of Funds</u>
Pfizer	7 of 10
Microsoft	6 of 10
Gen. Elec.	5 of 10
Citigroup	5 of 10
AIG	4 of 10
Cisco	4 of 10
Intel	3 of 10
Johnson & Johnson	3 of 10
BankAmerica	3 of 10
Wal-Mart	3 of 10

In the mutual fund companies' defense, if you're a large fund, it's hard not to own most of these stocks. The fact is most large funds are so big they have to own these stocks because they can't buy and sell smaller stocks without moving the market.

If you're an investor and you blindly pick these ten funds or ten others, however, you might not be nearly as diversified as you thought. Back to the debate thing I mentioned above. The fact is you could probably cherry-pick ten funds that had all or nearly all the same top ten holdings. Conversely, you could pick ten funds that were nothing alike. That's the point – the debate of whether these funds are alike or different doesn't really matter. What matters is you must deliberately choose funds that are not alike. That way you have a good cross-section of market sector coverage and little in the way of overlapping top ten holdings. This actually may be harder than it sounds. You could just invest your portfolio in individual stocks or hire a money manager to build your own private "mutual fund" with no duplicate holdings. 