



## Greener Pastures

By Rob Wherry

Dale Harvey left the burdens of managing \$20 billion for Capital Group to form his own boutique inspired by Thomas Jefferson.

Dale Harvey didn't like being popular. In the mid-2000s, Harvey found himself managing \$20 billion in mutual fund assets for Capital Group, the parent firm of American Funds. Harvey had built up solid records running diversified sleeves of several team-managed funds such as Washington Mutual *AWSHX*, *SMALLCAP World SMCWX*, and American Balanced *ABALX*. His work hadn't gone unnoticed by investors and his colleagues. Each morning, it seemed, he came into the office to find that the lead manager on the funds had earmarked more inflows for him to invest.

Most managers wouldn't mind having such a problem. But Harvey considered it a burden.

For starters, he often couldn't build full positions in the out-of-favor companies he preferred without tripping over restrictions on how many of the outstanding shares he could buy. Investing millions of dollars at a time, he also ran the risk of artificially popping stock prices. Most concerning to Harvey, though, was the idea of buying stocks he didn't have high conviction in.

"I had to put the money to work. I was managing \$20 billion, but I didn't have \$20 billion [worth of] good ideas," he says. "I would buy all the shares I was allowed to buy, and it was just a half position."

To Harvey, it became clear there was just one solution: leave the firm he had called home for 16 years. What he was contemplating was a drastic step, both on a personal level and from the perspective of his employer. Manager turnover is low at Capital Group, which is reflected in the fact that 91% of its almost \$1

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#### Dale Harvey

trillion in retail mutual fund assets are run by managers with tenures greater than 15 years.

"It's like being a professor," says Harvey of his former employer. "Nobody ever leaves."

Always a contrarian, Harvey gained inspiration for taking such a leap from a somewhat odd source: Thomas Jefferson. Growing up in Virginia, he knew well the story of Jefferson and Monticello, the plantation that served as the third president's home for most of his life. Harvey, though, found himself reminiscing about Jefferson's lesser-known estate, a retreat 100 miles away called Poplar Forest that Jefferson used to escape the crowds at Monticello.

The parallels were obvious to Harvey—his new firm would be his version of Poplar Forest, with him and a small team of analysts running money far from the glare of the spotlight. To carry the analogy further, Harvey would be free to invest in a portfolio of stocks that were largely off the beaten path. The kicker: Poplar Forest would make a great name for the new firm.

#### Breaking Away

Poplar Forest Capital opened its doors in October 2007, just as the economic downturn was starting to take hold. While the timing could have been better, the firm wasn't entering uncharted territory. The mutual fund world is filled with examples of managers who have broken off of large fund companies in order to start their own firms. DoubleLine, Marsico, Wintergreen, Yacktman, and IVA are

all firms that fit such a description. Like the managers behind those firms, Harvey was attracted to the idea that he could pick stocks without anybody looking over his shoulder.

The firm he built and the fund that followed in 2010 were in many ways significant departures from his time at Capital Group. For one, Harvey decided against using a team-managed approach and hired just four analysts. Poplar Forest Partners PFPFX is a concentrated portfolio of 25 to 35 stocks built without regard to the market cap or the sector weightings of the S&P 500. At Capital he ran diversified sleeves of funds that had more than three times the holdings.

"I had 80 investments, but I only wanted 30," he says.

Harvey, though, didn't alter his value-investing strategy, which was partly formed from his admiration for John Neff, the legendary Wellington manager who ran Vanguard Windsor VWNDX for 31 years. Harvey favors attractively priced mid- and large-cap stocks that are underperforming because of what he considers short-term execution problems. To avoid value traps, candidates must have strong balance sheets, sustainable free cash flows and a history of paying dividends.

Ultimately, he wants to own firms that can generate a 15% annualized total return over a three-year period. A catalyst can often help spur that growth. While most candidates fit that bill, Harvey does reserve a small portion

of the portfolio for riskier plays such as firms going through reorganizations or stocks down the market-cap spectrum. These holdings are usually kept to small position sizes to minimize risk.

The emphasis on bottom-up research and Harvey's contrarian bent are apparent from the resulting portfolio. As of March 31, the fund had no exposure to materials, utilities, REITs, and telecommunication stocks, which account for 12% of the S&P 500 Index. Technology stocks, a growth-fund staple, soaked up a large 25% of assets versus 10% for the average large-value peer. In addition, the fund's top 10 positions held 43% of assets compared with 26% for peers.

#### Patience Leads to Results

Poplar Forest Capital could have failed as quickly as it opened. At the time, Harvey was managing a \$40 million private account that held his own money and cash from a few outside investors that included his ex-colleagues and friends from his Harvard Business School days. He made a prescient call to mostly avoid financials, which helped him stem losses in the account its first year in existence.

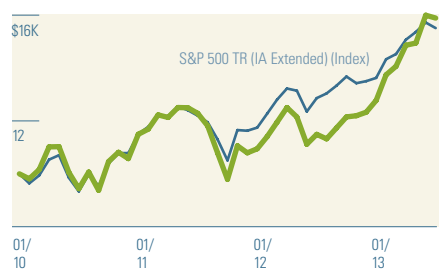
The mutual fund also ran the risk of flaming out early on. Harvey got off to a so-so start in 2010, posting a 15% gain that slightly trailed the S&P 500. While picks in the consumer discretionary and tech sectors such as Time Warner TWC and TE Connectivity TEL led the way that year, the gains from those stocks were partly offset by health-care names such as Baxter International BAX, whose shares

# Undiscovered Managers



Dale Harvey

## Poplar Forest Partners PFPFX



**Category**  
Large Value

**Expense Ratio (%)**  
1.25

**Morningstar Rating**  
★★

**3-Yr Annl Total Rtn (%)**  
18.96

**Minimum Investment**  
\$25,000

**3-Yr Total Rtn % Rank Cat**  
13

Data as of June 30, 2013

dropped 30% on a product recall and a slump in profits.

The next year, Harvey built a 25% exposure to financial-services firms such as Bank of America BAC and Citigroup C. But those shares tumbled in 2011 as investors ditched financials amid the sovereign debt crisis in Europe and the debt ceiling debate in the United States. The fund's 4.8% loss that year trailed the average peer by four percentage points. Such a lackluster showing could have sounded the death knell for a young fund, but investors didn't head for the exits.

"We were straightforward and explained [the performance] to shareholders," he says. "It was the same thing with tech stocks in the 1990s. There were a couple of years there when I looked like a chump. I was early then, but I was correct."

That was the case this time around, too. Harvey's conviction in his stock selection is apparent in the fund's low 29% turnover rate, which is one third the peer group average. Indeed, he mostly held the financials that were laggards in 2011 and watched them rebound the next year. The fund's 17% return in 2012 landed in the top quartile of the peer group.

The fund's strong performance has continued into 2013, driven largely by its overweight to tech stocks and in particular Hewlett-Packard HPQ, which at 5% of assets is the fund's largest position.

Harvey originally bought HP at around \$24 a share in 2011 as the stock dipped in the wake of the Autonomy merger. This was before beleaguered chief executive officer Leo Apotheker was fired and replaced by Meg Whitman, the former CEO of eBay EBAY. From Harvey's perspective, the cheap share price meant investors weren't even assigning a value to the firm's printer and computer business. He largely stuck by the underwater position, trimming it briefly in 2012 in order to offset capital gains in the portfolio. But he jumped back in earlier this year in time to catch an upswing in the shares propelled by decent second quarter earnings and a rosy outlook for the rest of the year.

"Once Meg was in place, all the pieces were in place," he says. "The board has learned its lesson."

Harvey hasn't gotten all his picks right, though. The fund's biggest detractor this year through June 11 was cruise ship line Carnival CCL, whose shares have stumbled in the wake of a major wreck and several onboard, high-profile mishaps. The fund still owns the shares, but Harvey has cut the position.

"Senior management hasn't responded to the incidents well. They were like the Keystone Cops," he says. "Did they run their costs too thin? It's hard to answer that."

## Building a Legacy

Poplar Forest Partners has gained an annualized 14.8% since its inception in 2010, which represents a two-percentage-point margin of victory over its average large-value peer. That record has slowly gotten it some attention from investors.

"We couldn't get behind a startup," says Michael Hatch, a financial advisor with Sterling Group in Pasadena, Calif., who looked at investing in the fund early on but waited a few years before doing so. "We needed to make sure the firm gelled."

Not everyone is ready to jump in, though. "When you are at a big firm like American Funds, there is a lot that helps you," says Anton Bayer, founder of wealth management firm Up Capital Management in Granite Bay, Calif. Bayer has researched the fund, but has yet to invest. "It is helpful to know [Dale] came from a successful career. But I was hesitant about being an early investor."

While Harvey is happy to have investors, he isn't interested in running as much money as he did at American Funds. Indeed, he says the strategy's optimal size is \$5 billion to \$7 billion, including the fund and other accounts. He also says he isn't interested at the moment in launching additional funds that could attract assets.

"I always want to be a boutique," he says. More importantly, he wants Poplar Forest Partners to endure in much the same way Jefferson's legacy has. "He focused on creating institutions that were long-lasting." ■■

Rob Wherry is the associate editor of *Morningstar Advisor* magazine.

*The fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The summary and statutory prospectuses contain this and other important information and can be obtained by calling (626) 304-6000 or by visiting [www.poplarforestfunds.com](http://www.poplarforestfunds.com). Read carefully before investing.*

**Mutual fund investing involves risk. Principal loss is possible. The fund may invest in debt securities which typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. The fund invests in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods.**

***Poplar Forest Partners Fund***

**Average Annual Total Returns as of December 31, 2017**

	<b><u>4Q 2017</u></b>	<b><u>1 Year</u></b>	<b><u>3 Years</u></b>	<b><u>5 Years</u></b>	<b><u>Since Inception</u></b>
<b>Poplar Forest Partners Fund:</b>					<b>(12/31/09)</b>
I Shares	5.56%	6.80%	6.80%	7.90%	15.11%
A Shares No Load	5.50%	6.53%	6.53%	7.63%	14.82%
A Shares With Load	0.22%	1.21%	1.21%	5.81%	13.65%
S&P 500 Index	6.64%	21.83%	21.83%	11.41%	15.79%
Morningstar Large Value Category	5.99%	15.94%	8.65%	13.33%	NA

Expense Ratio A Shares: 1.29% Gross; 1.25% Net of fee waiver

Expense Ratio Institutional Shares: 1.04% Gross; 1.00% Net of fee waiver

The net expense ratio is applicable to investors.

*Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the fund may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 877-522-8860. Investment performance reflects fee waivers. In the absence of such waivers, total returns would be reduced. Performance data shown for Class A with Maximum Sales Charge reflects the Class A maximum sales charge of 5.00%. Performance data shown for Class A without Sales Charge does not reflect the deduction of the sales load. If reflected, the load would reduce the performance. \*The Adviser has contractually agreed to waive a portion or all of its management fees and/or pay Fund expenses (excluding acquired fund fees and expenses, interest, taxes and extraordinary expenses) in order to limit the Net Annual Fund Operating Expenses to 1.25% and 1.00% of average daily net assets of the Fund's Class A shares and Institutional Class shares, respectively until April 6, 2018.*

As of December 31, 2017, the Poplar Forest Partners Fund's 10 largest holdings accounted for 47.34% of total fund assets. The Fund's 10 largest holdings at December 31, 2017 were:

<b>ABBOTT LABORATORIES</b>	<b>5.49%</b>
<b>LINCOLN NATIONAL</b>	<b>4.85%</b>
<b>AMERISOURCEBERGEN</b>	<b>4.70%</b>
<b>CITIGROUP</b>	<b>4.65%</b>
<b>ZIMMER BIOMET HOLDINGS</b>	<b>4.60%</b>
<b>MSC INDUSTRIAL DIRECT</b>	<b>4.59%</b>
<b>BANK OF AMERICA</b>	<b>4.52%</b>
<b>RELIANCE STEEL &amp; ALUMINUM</b>	<b>4.45%</b>
<b>DEVON ENERGY</b>	<b>4.22%</b>
<b>TAPESTRY</b>	<b>4.14%</b>

Fund holdings and sector allocations are subject to change at any time and are not recommendations to buy or sell any security.

Free cash flow is revenue less operating expenses including interest expenses and maintenance capital spending. It is the discretionary cash that a company has after all expenses and is available for purposes such as dividend payments, investing back into the business or share repurchases.

The S&P 500 Index is a market-value weighted index consisting of 500 stocks chosen for market size, liquidity, and industry group representation. It is not possible to invest directly in an index.

The Morningstar Large Value Category Average includes funds with similar investment objectives.

References to other mutual funds should not be considered an offer of those securities.

The Growth of \$10,000 chart illustrates the performance of a hypothetical \$10,000 investment made in the Fund since its inception on 12/31/09. It assumes reinvestment of dividends and capital gains, but does not reflect the effect of any applicable sales charge or redemption fees. This chart does not imply any future performance.

The Poplar Forest Partners Fund is distributed by Quasar Distributors, LLC.