

# AMG Yacktman I YACKX

Adapting, not compromising.

## Morningstar's Take YACKX

**Morningstar Rating** ★★★★★

**Morningstar Analyst Rating** Gold

### Morningstar Pillars

Process	+	Positive
Performance	+	Positive
People	+	Positive
Parent	○	Neutral
Price	○	Neutral

### Role In Portfolio

Core

### Fund Performance YACKX

Year	Total Return (%)	+/- Category
YTD	-11.33	4.18
2019	17.66	-7.38
2018	2.69	11.22
2017	18.23	2.29
2016	11.20	-3.61

Data through 5-31-20

9-13-19 | by Kevin McDevitt

AMG Yacktman continues to make the best of a difficult environment. It retains its Morningstar Analyst Rating of Gold.

Not compromising its standards has meant holding a lot of cash for this fund. Comanagers Stephen Yacktman and Jason Subotky are not strict value investors, but they are very valuation-conscious. If they can't find enough attractive investment opportunities, they will let cash build. That has been the trend since December 2011, when cash fell to 3% of assets. It declined from 12.4% that March as Yacktman and Subotky put cash to work following the midyear correction. Since then the trend has been mostly upward as the market has rallied and price multiples have increased. As a result, cash stood at nearly 30% of assets as of June 2019.

That big cash stake helped the fund weather 2018's fourth-quarter correction far better than most peers. It fell just 3.8% versus the Russell 1000 Value Index's 11.7% decline. What's more, the fund hasn't been penalized nearly as much as one might think for having such a big chunk of assets on the sidelines. True, the fund's 10.9% annualized return since 2011 did lag the index by 1 percentage point through August 2019, but the trade-off was more than favorable on a risk-adjusted basis thanks to its excellent risk management. Its Sharpe ratio--a measure of risk-adjusted results--was 1.22, far outpacing the index's 0.99. Moreover, the fund captured only 60.6% of the index's downside during that stretch while it captured 76.4% of the index's gains.

Neither has the team been standing still, despite cash being greater than 20% over the past three years. Rich valuations have sent Yacktman and Subotky overseas in search of opportunities, where price multiples are generally lower. The fund's foreign equity stake has grown to 16.8% of assets from 2% in March 2015. Top holding Samsung has been in the portfolio since June 2017, but the team added two German companies in the first quarter, specialty chemicals company Brenntag and Aquaphor lotion-maker Beiersdorf.

The greatest risk is opportunity cost, but the fund has delivered on a risk-adjusted basis.

**Process Pillar** + Positive | Kevin McDevitt 09/13/2019

This fund sometimes gets the high-quality label, but price and valuation are what matter most. The team's preference for companies with strong free cash flows, reasonable debt, high returns on capital, and modest cyclicality makes high-quality companies the default. However, if the price is right, management will buy value-oriented or cyclical names, often coming out of a recession and a bear market. The team thinks of stocks as junior bonds and compares their free-cash flow

yields with those of AAA rated corporates. Once a stock is in the portfolio, the team is reluctant to sell because high-quality companies tend to compound capital at attractive rates. This leads to low turnover. On the other hand, if the team cannot find cheap stocks to buy, it will let cash build to 20% or more of assets. This patience and discipline earn a Positive Process rating.

Capacity isn't an issue given the portfolio's low turnover and current focus on liquid large-cap stocks. But the fund has grown too big to invest meaningfully in small and mid-caps as it did in the late 1990s. Back then, the fund loaded up on small and mid-caps given their compelling valuations versus large caps. The team likely wouldn't have the flexibility to invest meaningfully in such stocks now even if valuations became attractive. That's especially true if the team plans to maintain its relatively concentrated portfolio.

This concentrated fund has a conservative side. It had 44.5% of its assets in its top 10 holdings as of June 2019, more than double that of the S&P 500. Plus, the fund sticks to just a few sectors, given the team's preference for companies with competitive advantages that aren't very economically sensitive. (Though the team will buy cyclicals if the price is right.) This has led to big stakes in consumer-oriented and technology shares. Branded consumer staples and discretionary stocks represented about a fourth of the equity portfolio versus about 18% of the S&P 500.

But the fund has marshaled its defenses as valuations have risen. The portfolio's average price multiples have mostly dropped below the index's, but its holdings tend to be of higher quality. This shows in the shifting balance between staples and discretionary stocks. Since peaking at nearly 31% of the equity portfolio in March 2009, economically sensitive discretionary stocks dropped to just 4.2% by June 2019. The team has maintained a big overweighting in recession-resistant staples such

as Procter & Gamble PG, which were 20.1% of the June 2019 portfolio. Moreover, cash grew to nearly 30% of assets in June 2019, near the high end of the fund's historical range.

Rich U.S. valuations have sent the fund overseas, where price multiples are generally lower. The fund's foreign equity stake has grown to 16.8% of assets from 2% in March 2015.

**Performance Pillar** Positive | Kevin McDevitt 09/13/2019

This fund's long-term returns earn a Positive Performance rating. Since the fund's 1992 inception, its 10.3% annualized return beats the S&P 500's and Russell 1000 Value Index's 9.7% return through July 2019. The fund has an even bigger lead since Stephen Yacktman was named a comanager at year-end 2002. Since then, the fund's 10.7% annualized gain beats the S&P 500's 9.7% and Russell 1000 Value Index's 8.8%.

Management aims to maximize risk-adjusted results over a full market cycle. This attention to risk shows in its preference for high-quality companies, valuation consciousness, and a penchant for big cash stakes when equity valuations get stretched. Despite maintaining a relatively concentrated portfolio, the fund's 15-year standard deviation is in line with the S&P 500's with far lower downside capture.

As with most highly differentiated funds, this one goes through dry spells. It has been left for dead more than once, including during the late 1990s and mid-2000s, and again in 2012-15. While the managers are not deep contrarians, their value leanings and the concentrated portfolio can leave it out of step with the broader market, especially in the latter stages of bull markets when the team often gets defensive. But this defensiveness led to outstanding relative returns during the 2000-02 and 2008 bear markets and 2011 and 2018's corrections. It has made up on the downside for gains lost during rallies.

**People Pillar** Positive | Kevin McDevitt 09/13/2019

This fund ensured continuity when its advisor, Yacktman Asset Management, sold itself to Affiliated Managers Group AMG in 2012. That deal locked in the fund's three managers, as each signed a 10-year employment contract as part of the agreement. The team also retained full investment authority, so there wouldn't be any change in the fund's strategy.

That's encouraging considering Don Yacktman, Stephen Yacktman, and Jason Subotky's long-term investment success. Don Yacktman officially stepped down as a comanager in May 2016 but remains as an advisor. This move reflects the fact that his son Stephen and Subotky have managed the fund day-to-day for the past several years. Those two do not have an independent record of their own, but they have ample experience. This earns the fund a Positive People rating. Stephen has worked on the fund since 1993 and has been a comanager since year-end 2002. Subotky has been a comanager since year-end 2009 and has been with the firm since 2001. Both have more than \$1 million invested in the fund.

The team strengthened its bench when it hired Adam Sues in August 2013. After less than a year with the firm, Sues was named sole manager of AMG Yacktman Special Opportunities YASLX in June 2014. They hired Brandt Dusthimer as an analyst in April 2015. He has a strong tech background, having worked for five years as a software engineer.

**Parent Pillar** Neutral | 05/08/2019

AMG has some attractive features that led to a Parent rating upgrade in March 2019 to Positive from Neutral. However, a recently announced CEO change reignites a previous concern about the team's stability, leading to the return of a Neutral Parent rating.

In March 2014, Jeff Cerutti became CEO of AMG Funds, a role that was created for him and that was eliminated following his departure in June 2018. In March 2018, Nate Dalton succeeded longtime Affiliated Managers Group CEO Sean Healey, following his diagnosis of ALS. After only 11 months in the role and as the public company has recorded weaker earnings results, Dalton will

be succeeded by current CFO and president Jay Horgen.

Some positives remain. AMG has maintained its attractiveness as a partner by continuing to allow its affiliates considerable autonomy in both investment decisions as well as business decisions. AMG can accommodate different needs of its partners, but its core function has endured. It continues to acquire equity interests in boutique asset managers, often acting as a facilitator in the transfer of wealth for a boutique's founders. It has historically partnered with some of the industry's stronger boutiques, such as AQR (which operates most independently of AMG) and Yacktman (which uses virtually all of AMG's services), as well as Tweedy, Browne (which is somewhere in between).

**Price Pillar** Neutral | Kevin McDevitt 09/13/2019

This fund's fee-level peer group changed to large-cap institutional after parent AMG raised its minimum initial investment to \$100,000 in October 2016. While the fund's 0.75% prospectus expense ratio would be below-average relative to its former large-cap no-load peers, it lands in average territory among its institutional peers. As a result, the fund receives an overall Morningstar Fee Level of Average and a Neutral Price rating.

The fund's low turnover keeps brokerage commissions, as a percentage of net assets, below those of the large-value Morningstar Category average.

**Average annual returns (%)<sup>12</sup> (as of 03/31/20)**

	Inception	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Incpt
YACKX (Class I)	07/06/92	-21.68	-21.68	-14.49	1.52	3.96	7.82	9.37
S&P 500® Index	-	-19.60	-19.60	-6.98	5.10	6.73	10.53	8.99
Russell 1000® Value Index	-	-26.73	-26.73	-17.17	-2.18	1.90	7.67	8.65

**Expense Ratios (gross/net):** Class I 0.75% / 0.75%

**Top Ten holdings (%)<sup>3</sup>**

Holding	% of Net Assets
Samsung Electronics Co Ltd Preferred	9.21
Bollore SA	4.44
Johnson & Johnson	3.33
PepsiCo Inc	3.25
Microsoft Corp	3.20
Continental AG	3.20
Walt Disney Co	3.03
Fox Corp, Class A	3.02
Procter & Gamble Co	2.70
Booking Holdings Inc	2.68
TOTAL %	38.06

<sup>1</sup> Returns for periods less than one year are not annualized.

<sup>2</sup> The performance information shown for periods prior to June 29, 2012, is that of the predecessor to the Fund, The Yacktman Fund, which was reorganized into the Fund on June 29, 2012, and was managed by Yacktman Asset Management LP with the same investment objective and substantially similar investment policies as those of the Fund.

<sup>3</sup> Mention of a specific security should not be considered a recommendation to buy or a solicitation to sell that security. Holdings are subject to change.

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## Disclosure

*Investors should carefully consider the fund's investment objectives, risks, charges, and expenses before investing. For this and other information, please call 800.835.3879 or download a free prospectus. Read it carefully before investing or sending money.*

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Any sectors, industries, or securities discussed should not be perceived as investment recommendations. Any securities discussed may no longer be held in the Fund's portfolio. It should not be assumed that any of the securities transactions discussed were or will prove to be profitable, or that the investment recommendations we make in the future will be profitable.

The Fund is subject to risks associated with investments in mid-capitalization companies such as greater price volatility, lower trading volume, and less liquidity than the stocks of larger, more established companies.

The Fund is subject to risks associated with investments in small-capitalization companies, such as erratic earnings patterns, competitive conditions, limited earnings history and a reliance on one or a limited number of products.

Companies that are in similar businesses may be similarly affected by particular economic or market events; to the extent the Fund has substantial holdings within a particular sector, the risks associated with that sector increase.

The Fund invests in value stocks, which may perform differently from the market as a whole and may be undervalued by the market for a long period of time.

The S&P 500<sup>®</sup> Index is a capitalization-weighted index of 500 stocks. The S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Russell 1000<sup>®</sup> Value Index is a market capitalization weighted index that measures the performance of those Russell 1000<sup>®</sup> companies with lower price-to-book ratios and lower forecasted growth values.

Unlike the Fund, indices are unmanaged, are not available for investment and do not incur expenses.

All holdings and sector/region allocations are subject to review and adjustment in accordance with the Portfolio's investment strategy and may vary in the future, and should not be considered recommendations to buy or sell any security. The Portfolio is actively managed; therefore holdings may not be current.

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