

Guinness Atkinson Global Innovators (IWIRX)

A Mutual Fund Observer 'Star in the Shadows' Fund

By David Snowball, Publisher



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Fund name Guinness Atkinson Global Innovators (IWIRX)

Objective and Strategy The fund seeks long term capital growth through investing in what they deem to be 30 of the world's most innovative companies. They take an eclectic approach to identifying global innovators. They read widely (for example *Fast Company* and MIT's *Technology Review*, as well as reports from the Boston Consulting Group and Thomson Reuters) and maintain ongoing conversations with folks in a variety of industries. At base, though, the list of truly innovative firms seems finite and relatively stable. Having identified a potential addition to the portfolio, they also have to convince themselves that it has more upside than anyone currently in the portfolio (since there's a one-in-one-out discipline) and that it's selling at a substantial discount to fair value (typically about one standard deviation below its 10-year average). They rebalance about quarterly to maintain roughly equally weighted positions in all thirty, but the rebalance is not purely mechanical. They try to keep the weights "reasonably in line" but are aware of the importance of minimizing trading costs and tax burdens. The fund stays fully invested.

Adviser Guinness Atkinson Asset Management. The firm started in 1993 as the US arm of **Guinness Flight Global Asset Management** and their first American funds were Guinness Flight China and Hong Kong (1994) and **Asia Focus**(1996). Guinness Flight was acquired by Investec, then Tim Guinness and Jim Atkinson's acquired Investec's US funds business to form Guinness Atkinson. Their London-based sister company is Guinness Asset Management which runs European funds that parallel the U.S. ones. The U.S. operation has about \$460 million in assets under management and advises the eight GA funds.

Managers Matthew Page and Ian Mortimer. Mr. Page joined GA in 2005 after working for Goldman Sachs. He earned an M.A. from Oxford in 2004. Dr. Mortimer joined GA in 2006 and also co-manages the Global Innovators (IWIRX) fund. Prior to joining GA, he completed a doctorate in experimental physics at the University of Oxford. The guys also co-manage the **Inflation-Managed Dividend Fund** (GAINX) and its Dublin-based doppel-ganger **Guinness Global Equity Income Fund**.

Strategy capacity and closure Approximately \$1-2 billion. After years of running a \$50 million portfolio, the managers admit that they haven't had much occasion to consider how much money is too much or when they'll start turning away investors. The current estimate of strategy capacity was generated by a simple calculation: 30 times the amount they might legally and prudently own of the smallest stock in their universe.

Active share 96. "Active share" measures the degree to which a fund's portfolio differs from the holdings of its benchmark portfolio. High active share indicates management which is providing a portfolio that is substantially different from, and independent of, the index. An active share of zero indicates perfect overlap with the index, 100 indicates perfect

independence. The active share for Global Innovators is 96, which reflects a very high level of independence from its benchmark MSCI World Index.

Management's Stake in the Fund The managers are not invested in the fund because it's only open to U.S. residents.

Opening date Good question! The fund launched as the Wired 40 Index on December 15, 1998. It performed splendidly. It became the actively managed Global Innovators Fund on April 1, 2003 under the direction of Edmund Harriss and Tim Guinness. It performed splendidly. The current team came onboard in May 2010 (Page) and May 2011 (Mortimer) and tweaked the process, after which it again performed splendidly.

Minimum investment \$5,000, reduced to \$1,000 for IRAs and just \$250 for accounts established with an automatic investment plan.

Expense ratio 1.45% on assets of about \$100 million, as of August 1, 2014. The fund has been drawing about \$500,000/day in new investments this year.

Comments Let's start with the obvious and work backward from there.

The obvious: Global Innovators has outstanding (consistently outstanding, enduringly outstanding) returns. The hallmark is [Lipper's recognition of the fund's rank](#) within its Global Large Cap Growth group:

One-year rank	#1 of 98 funds, as of 06/30/14
Three-year rank	#1 of 72
Five-year rank	#1 of 69
Ten-year rank	#1 of 38

Morningstar, using a different peer group, places it in the top 1–6% of US Large Blend funds for the past 1, 3, 5 and 10 year periods (as of 07/31/14). Over the past decade, a \$10,000 initial investment would have tripled in value here while merely doubling in value in its average peer.

But why?

Good academic research, stretching back more than a decade, shows that firms with a strong commitment to ongoing innovation outperform the market. Firms with a minimal commitment to innovation trail the market, at least over longer periods.

The challenge is finding such firms and resisting the temptation to overpay for them. The fund initially (1998–2003) tracked an index of 40 stocks chosen by the editors of *Wired* magazine “to mirror the arc of the new economy as it emerges from the heart of the late industrial age.” In 2003, Guinness concluded that a more focused portfolio and more active selection process would do better, and they were right. In 2010, the new team inherited the fund. They maintained its historic philosophy and construction but broadened its investable universe. Ten years ago there were only about 80 stocks that qualified for consideration; today it's closer to 350 than their “slightly more robust identification process” has them track.

This is not a collection of “story stocks.” The managers note that whenever they travel to meet potential US investors, the first thing they hear is “Oh, you're going to buy Facebook and Twitter.” (That would be “no” to both.) They look for firms that are continually reinventing themselves and looking for better ways to address the opportunities and challenges in their industry. While that might describe eBay, it might also describe a major petroleum firm (BP) or a firm that supplies backup power to data centers (Schneider Electric). The key is to find firms which will produce disproportionately high returns on invested capital in the decade ahead, not stocks that everyone is talking about.

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Then they need to avoid overpaying for them. The managers note that many of their potential acquisitions sell as “extortionate valuations.” Their strategy is to wait the required 12–36 months until they finally disappoint the crowd’s manic expectations. There’s a stampede for the door, the stocks overshoot—sometimes dramatically—on the downside and the guys move in.

Their purchases are conditioned by two criteria. First, they look for valuations at least one standard deviation below a firm’s ten year average (which is to say, they wait for a margin of safety). Second, they maintain a one-in-one-out discipline. For any firm to enter the portfolio, they have to be willing to entirely eliminate their position in another stock. They turn the portfolio over about once every three years. They continue tracking the stocks they sell since they remain potential re-entrants to the portfolio. They note that “The switches to the portfolio over the past 3.5–4 years have, on average, done well. The additions have outperformed the dropped stocks, on a sales basis, by about 25% per stock.”

Bottom Line While we need to mechanically and truthfully repeat the “past performance is not indicative of future results” mantra, Global Innovator’s premise and record might give us some pause. Its strategy is grounded in a serious and sustained line of academic research. Its discipline is pursued by few others. Its results have been consistent across 15 years and three sets of managers. Investors willing to tolerate the slightly-elevated volatility of a fully invested, modestly pricey equity portfolio, [Global Innovators](#) really does command careful attention.

Fund website [GA Global Innovators Fund](#). While you’re there, please do read the [Innovation Matters](#) (2014) whitepaper. It’s short, clear and does a nice job of walking you through both the academic research and the managers’ approach.

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Fund holdings and sector allocations are subject to change at any time, and should not be considered a recommendation to buy or sell any security.

As of 12/31/14, the top 10 holdings of the Global Innovators Fund are: 1. Oracle Corp 3.50% 2. Applied Materials Inc 3.38% 3. H&R Block Inc 3.36% 4. Cisco Systems Inc 3.33% 5. Samsung Electronics Co Ltd – GDR 3.31% 6. QUALCOMM Inc. 3.28% 7. Comcast Corp - A Shares 3.27% 8. Danaher Corp 3.27% 9. L-3 Communications Holdings Inc 3.27% 10. Check Point Software Technologies Ltd 3.26%

Mutual fund investing involves risk and loss of principal is possible. Investments in foreign securities involve greater volatility, political, economic and currency risks and differences in accounting methods. These risks are greater for emerging markets countries. Non-diversified funds concentrate assets in fewer holdings than diversified funds. Therefore, non-diversified funds are more exposed to individual stock volatility than diversified funds. The Fund also invests in smaller companies, which will involve additional risks such as limited liquidity and greater volatility. The Fund may invest in derivatives which involves risks different from, and in certain cases, greater than the risks presented by traditional investments.

The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and it may be obtained by calling 800.915.6566 or visiting gafunds.com. Read it carefully before investing.

A hypothetical growth of \$10,000 from 7/31/04 through 7/31/14 would have produced \$30,609.83 in the Guinness Atkinson Global Innovators Fund and \$20,693.18 in the Morningstar Large-Cap Growth category, which is the Morningstar large blend investment style.

Lipper Analytical Services, Inc. is an independent mutual fund research and rating service. Each Lipper average represents a universe of Funds with similar invest objectives. Rankings for the periods shown are based on Fund total returns with dividends and distributions reinvested and do not reflect sales charges.

As of 12/31/14, the Guinness Atkinson Global Innovators Fund Lipper ranking for the Global Multi-Cap Growth Category* for total returns was: 1 of 500 for 1 year, 1 of 466 for 3 years, 1 of 399 for 5 years and 1 of 278 for 10 years in the Lipper category Global Multi-Cap Growth. *Lipper changed the category Global Innovators Fund to multi-cap growth as of 8/31/14.

The Wired Index Fund had an annualized growth of -5.61% from 12/15/1998 to 4/30/2003, and the Guinness Atkinson Global Innovators Fund had an annualized growth of 9.96% from 5/1/2003 to 4/30/2010.

Standard Deviation is a statistical measure of the historical volatility of a mutual fund or portfolio, usually computed using 36 monthly returns.

The MSCI World Index with net dividends is an unmanaged, free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. The MSCI World Index consists of 24 developed market country indices. This index includes dividends and distributions net of withholding taxes, but does not reflect fees, brokerage commissions, or other expenses of investing.

Margin of safety is a principle of investing in which an investor only purchases securities when the market price is significantly below its intrinsic value. In other words, when market price is significantly below your estimation of the intrinsic value, the difference is the margin of safety. This difference allows an investment to be made with minimal downside risk.

The term "income stream" used here is used synonymously with the word "dividends." The use of the word peers is meant to define all actively managed equity funds.

Average Annual Returns

As of 12/31/14	YTD	1 Year	3 Years	5 Years	10 Years	Since Inception (12/15/1998)
Global Innovators Fund	12.55%	12.55%	25.16%	16.49%	10.58%	7.43%
Morningstar Large-Cap Growth Category Average		9.99%		14.09%	7.68%	

The fund's gross expense ratio is 1.47%

Performance data quoted represents past performance and 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 Funds may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 900-915-6566 and/or visiting www.gafunds.com. Total returns reflect a fee waiver in effect and in the absence of this waiver, the total returns would be lower. Performance data does not reflect the 2% redemption fee for shares held less than 30 days and if deducted the fee would reduce the performance quoted.

Morningstar Rankings represent a fund's total-return percentile rank relative to all funds that have the same Morningstar Category. The highest percentile rank is 1 and the lowest is 100. It is based on Morningstar total return, which includes both income and capital gains or losses and is not adjusted for sales charges or redemption fees. Morningstar ranked the Global Innovators fund in the top 4%, 1%, 1% and 1% out of 1158, 881, 688, and 346 World Stock* funds for the one-, three-, five- and ten-year periods ending 12/31/2014, respectively. *Morningstar changed the Global Innovators Fund category to World Stock in 11/14, and this data is no longer provided for its previous category. **Past performance does not guarantee future results.**

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