BUSINESS INSIDER

We interviewed Wall Street's 7 top-performing investors to get their secrets for success — and their best ideas for 2020

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December 16, 2019

- **Business Insider spoke with the seven best-performing large-cap fund managers of the year, based on a trailing one-year basis through the end of September.**
- **The fund managers outlined which thematic and single-stock strategies paid off for them this year, and they laid out their top trades and ideas for 2020.**

If you followed only financial-news headlines in 2019, you might assume the market had a tough year. Recession fears flared, trade-war tensions ebbed and flowed with ferocity, and corporate earnings growth slowed.

Yet the benchmark S&P 500 was still up 19% year-to-date through the end of September. Thank the Federal Reserve and its overt willingness to continuing stimulating an economic expansion that's already the longest in history.

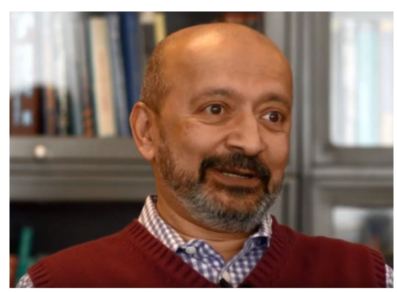
But even amid a robust market environment that saw every major stock index climb for the year, a handful of fund managers stood out as the cream of the crop. These were the people and firms that were still able to outperform, even though equities and other risk assets were so strong across the board.

Presented below are the results of our discussions with these investing heavyweights, who broke down their methodologies, what they did right, and what their attack plan would be going forward.

The managers are arranged in decreasing order of trailing one-year return, through September 30.

Ajay Dravid and Rufus Rankin, portfolio managers, AXS Alternative Growth Fund (EEHIX)

The top-performing fund managers of the year crushed the market without picking a single stock.



Ajay Dravid

Amid double-digit gains for equities, their $21.3 million fund beat the market through its mix of broad exposure to the S&P 500 and use of alternative hedging strategies.

Dravid and Rankin adopt a differentiated take on the traditional long-short equity strategy in that they do not take positions in individual companies.

Instead, their investing rests on four pillars. The first is a long-only strategy that seeks returns that match the S&P 500's through equity index futures. This part is outsourced to traders who they think have the best prospects of producing superior returns.

The second pillar is a diversifier strategy that complements these returns through trading programs that have low correlations to the market.

Third, they have a hedge strategy with quantitative trading programs that dynamically adjust their exposure to equities so as to limit their downside when the market falls. And finally, they invest in fixed-income assets including money-market funds, exchange-traded funds, and Treasurys.

Their goal is to outperform the market over the long run and to be down less than the market in times of stress. It's essential that they beat the market, since they waive their management fee for a year if they fail to outperform on a trailing-three-year basis.

One-year return: 19.3%. Biggest holdings (as of 9/30): Interest rate futures (41.7%), equity index futures (16.4%), energy futures 10.2%

What worked in 2019:

"The best-performing strategy was the dynamic hedges, which is very interesting. In a period when the stock market went up nearly 20% over the first nine months of the year, normally the dynamic hedges would not give positive performance. They would normally tend to be flat to down because they are designed to perform when the stock market is going down. But this year, there were enough periods of volatility or small corrections during which these dynamic hedging strategies did very well."

What's ahead in 2020:

"A: We don't know. B: We don't care.

"If the market keeps going up, we know that part of our strategy will be up. If the market goes down, that part of the strategy will be down.

"You could classify this as a view-free strategy. Ajay and I are not taking views on what we think is going to happen over the next quarter or year and adjusting the portfolio. We're not bearish, we're not bullish. We're trying to really stick to our knitting here."

Joe Hudepohl, the lead manager of Eaton Vance's Atlanta Capital Focused Growth Fund (EAALX) and Calvert Equity Fund (CSIEX)


Atlanta Capital

The saying goes that the best defense is a good offense. But counterintuitively, playing defense was perhaps the best way to play the stock market in 2019. That has helped produce sterling results for Eaton Vance, a firm that stresses quality stocks above all else. In a period that included some dramatic market losses and a major rally in 2019, Eaton Vance has three of the 10 best-performing large-cap hedge funds this year, as well as two of the top eight managers.

Hudepohl is the lead manager of two of those funds. And one, the Atlanta Capital Focused Growth Fund, was also one of the best performers of 2018. Hudepohl's two top funds have some stocks in common, which helps explain their similar performance. The focused growth fund has 25 stocks and has $288 million in assets, while the Calvert Equity Fund contains 60 stocks and other assets and has $3.5 billion in investments. Hudepohl is part of his firm's growth equity team, which manages $4.2 billion in assets across several funds. He says Eaton Vance defines quality as "consistent growth and stability in earnings" and that deliver steady returns that will compound over time.

One-year return: 18.9% (EAALX), 18.7% (CSIEX). Biggest holdings (as of 9/30): EAALX — Visa (8.2%), Alphabet (7.2%), Danaher (5.7%), Microsoft (5.5%), Thermo Fisher Scientific (5.2%)
CSIEX — Visa (4.7%), Microsoft (4.6%), Danaher (4.6%), Alphabet (4.5%), Thermo Fisher (4.4%)

What worked in 2019: "If you look at last 12 months, tech probably would have showed up largely because of Visa and Mastercard had been two contributors. Those have been in the portfolio for a number of years and really playing that long-term trend for a movement from cash to credit usage and those being the two dominant players. Healthcare has been very strong for us over the last nine to 12 months. And that was actually driven by Danaher, which is in the life-sciences space. Fantastic business. Thermo Fisher is in that group as well. Another one that's been fairly strong for us is American Tower. That actually shows up in under REITs even though you don't really own it for the sake of a traditional REIT in terms of income gathering. It's really a long-term play on the growth in wireless data usage."

What's ahead in 2020: "The underlying philosophy of the firm is high-quality investing. And that's been kind of the mantra for the last 50 years. We like compounders, or businesses that are pretty consistent and that you can compound with over time. The majority of our excess return over the last 12 months has been driven by less downside capture in the market. So I think the number we've been looking at, depending on the portfolio, roughly 75% to 80% of our downside of our outperformance in the last 12 months has come from downside protection. We don't try to predict macro trends. We're bottoms-up, fundamental long-term investors, and so we don't try to predict that … My guess is volatility will continue, somewhat like we've seen in the last 12 months, which again, I think is generally favorable towards high quality businesses and the businesses that we focus on."

Chip Reed, lead manager of the Eaton Vance Atlanta Capital Select Equity Fund (ESEAX)

Reed acknowledges that his Atlanta Capital Select Equity Fund has "some odd ones" because of its focus on quality above sector makeup, growth, the economic cycle, and other considerations. But in a volatile year marked by lingering trade tensions and uncertainty that flared up without warning, that formula is working well. Reed says the fund, which had $1.1 billion in assets as of September 30, focuses exclusively on companies that generate strong earnings and cash flows and aren't taking on any debt. Above all, he says that the firm is trying to avoid outsize losses and that the best way to do that is to find the companies that are delivering the most consistent results. Reed is part of Atlanta's core equity team, which manages $18.5 billion in assets.


Eaton Vance

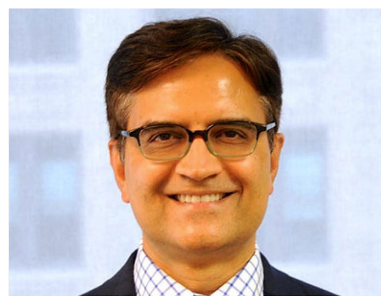
One-year return: 16.2% Biggest holdings (as of 9/30): Ball Corp. (7.7%), TJX (6.1%), White Mountains Insurance Group (5.9%), Fiserv (5.6%), Teleflex (4.6%)

What worked in 2019: "It's really about the consistency in the earnings of the companies that we invest in. And clearly this year has been a year where higher quality issues have outperformed. Most managers will tell you they're high quality and they'll talk about things like the business model and a competitive advantage and management. And those are all true, but they're fairly soft and subjective. We like to fall back on the earnings consistency over a full cycle and kind of 10 years of history. Surprisingly, the best performer year to date was Ball Corp. … I don't think most portfolio managers on their list as their largest single holding. They make aluminum cans. Specialty cans is kind of their niche. Think of the Coke-shaped aluminum can you may have seen, or the skinny can for a White Claw is a good example, where they've been able to capture newer markets."

What's ahead in 2020: "If you look over a 12-month period, the market, even though we're hitting new highs, it's not up a whole lot. It's actually kind of been flat, and I think that's kind of the environment that we're going to see going into next year. There's a lot of things that could go wrong: trade, Brexit, negative rates around the world. There's a lot of things that can go wrong real quick. Meanwhile the economy is OK. It's not great, it's not bad, it's just kind of a muddle through. I think that's what's led the shift to higher quality this year and it really plays into our strong suit: Being defensive in a market that could go wrong at any minute."

Vijay Chopra, lead manager of the Copley Fund (COPLX)

Chopra oversees $105 million as the lead manager of the Copley Fund. Since Chopra has been at the helm of the fund, his focus has been to identify large-cap companies with strong fundamentals that have a robust history of paying and growing dividends. It's the firm's bread and butter. He employs a combination of top-down and bottom-up research when it comes to stock selection, with the latter holding a larger weight in the decision-making process. He starts by examining the universe of investable securities that meet the criteria mentioned above and then whittles down the possible purchases until he arrives at just a few names. From there, business models are examined, quality is assessed, and a final decision is made.


Dr. Vijay Chopra

It's a very low-turnover, long-term, fundamental approach to managing capital — and it's been quite literally paying dividends.

Today, the Copley Fund is heavily allocated to the utilities sector, encompassing more that 62% of the firm's assets.

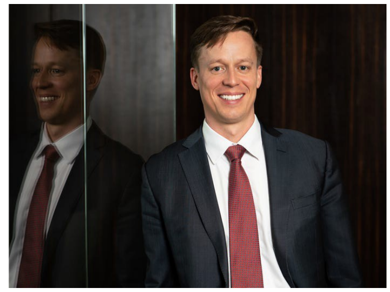
One-year return: 16.1% Biggest holdings (as of 9/30): NextEra Energy (20.1%), Dominion Energy (7.3%), Exxon Mobil (7.2%), DTE Energy (7%), Arthur J. Gallagher & Co (6.9%)

What worked in 2019: "This year has been a great year, but the style of the fund lends itself to long-term outperformance. It's a conservative, all-weather fund with an emphasis on total return. We look at dividend growers that are quality, so we make sure that the dividend growth will be persistent and long-term. We believe that in the long term fundamentals are we rewarded, and so we invest based on that."

What's ahead in 2020: "Right now we feel that there's a turnaround in the macro environment. The PMI indices have started to turn up. We also follow GDP revisions, and those have bottomed and are sort of trending up — and you can see the upturn in Asia and in some other parts of the world. In the US, the consumer is holding up nicely — and the fact that the Fed has been cutting rates this year would mean that next year you'll see the positive impact that it has on economic growth. We are positioning for a slight cyclical recovery. We're not saying that it's going to be a very strong recovery, but just compared to what we've had in the last year or so. We're expecting a turnaround, so we're being more pro-cyclical in our approach."

Brian Yacktman, portfolio manager, YCG Enhance Fund (YCGEX)

Yacktman opened the doors to YCG Funds, his Austin, Texas-based firm, right around the market top in 2007. He survived the crisis and has since come a long way, delivering market-beating returns on one-, three-, and five-year bases. Yacktman attributes his success to a strategy of finding "boring," high-quality stocks that stand the test of time while avoiding those that are being chased by impatient investors. In his view, the behavioral tendency of wanting to get rich quickly leads to a systemic overpricing of popular, low-quality stocks and a systemic underpricing of the boring, higher-quality companies. He determines "quality" using a few yardsticks. They include strong pricing power through which a company can grow its sales volumes without requiring lots of capital and high insider ownership so that executive incentives are aligned with the company's success.



Nisa Hunt; YCG Funds

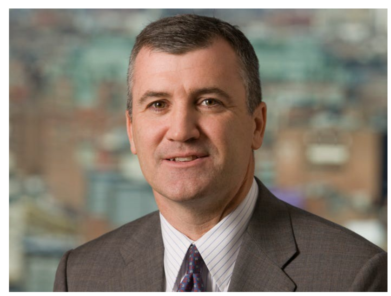
One-year return: 15.8% Biggest holdings (as of 9/30): Mastercard (6.1%), Moody's (5.3%), CBRE Group (5.3%), Wells Fargo (5.2%), Aon (5.11%)

What worked in 2019: “The one that surprised us — more than beaten our expectations by far — is MSCI. It is just a juggernaut. They're the gold standard for international indices. Even though it's wildly outperformed our expectations and is up 70% over the last 12 months, I still think that it's a great long-term buy. We've owned it since 2012."

What's ahead in 2020: “The biggest concern I probably have is that all of these low rates have led to a debt binge and loaded up asset prices everywhere — in private equities, public equities, and venture capital. And so you could have an impending corporate-debt crisis. You don't want companies that are reliant on capital markets. Before WeWork collapsed, I was saying, 'It'd be crazy to invest in that thing.' I'd say the same thing about Netflix, Tesla — these are companies that people get really excited about. But they're reliant on the kindness of capital markets."

Donald Kilbride, lead manager of the Vanguard Dividend Growth Fund (VDIGX)

For 15 years, Kilbride — the lead manager of Vanguard's Dividend Growth Fund — has applied a rather simple and straightforward philosophy to investing with stunning results. It all comes down to the notion of value creation and value distribution — and Kilbride has a nose for sniffing out the firms that do it best. Kilbride's fund is rather concentrated with positions in only 42 stocks, all of which are held with firm conviction. Not only is he looking for companies that are making smart investment decisions and growing returns on capital, but he also has a keen eye on prioritization of these companies to return that value to shareholders. It's a notion that can be discerned from the company's dividend payout history.



Donald Kilbride

He looks for a long history of dividend growth with a payout ratio in the "sweet spot" of 30% to 60%, employs a bottom-up, "brick-by-brick" approach to stock picking. Kilbride generally focuses his attention on large-cap, US-based issues with low volatility and operating models that aren't overtly capital intensive. Today, the Vanguard Dividend Growth Fund's net assets tip the scales at a whopping $39.5 billion.

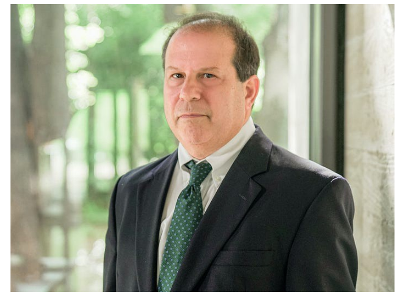
One-year return: 14%. Biggest holdings (as of 9/30): Coca-Cola (3.77%), Medtronic PLC (3.68%), McDonald's (3.59%), Nike (3.50%), Johnson & Johnson (3.21%)

What worked in 2019: "We try not to let the environment overly influence how we're building this portfolio. We don't spend a heck of a lot of time, if any, trying to figure out big complicated questions like macro. We try to solve simpler questions like dividend growth. As you look at the fund you can see there's a lot of healthcare. There's a lot of exposure to the consumer and specific areas of the industrial sector like transportation and aerospace. We actually are unlike a lot of investors in that we don't seek change. Most investors go out and find things that they think are mispriced and then they hope, or they expect, or in some cases they force change. That can be a good way to invest, but that's really not what we do. We to identify things that we think are so powerful and so time-tested that they don't need to change in a material way."

What's ahead in 2020: "The one sector that's of some particular interest to us is healthcare, for the obvious reasons. Healthcare has been a little bit weaker in terms of price, owing to a little bit of a preelection year, concerns about what might change in the healthcare system, and that has had the effect of putting pressure on healthcare stocks generally. That tends to be a good time to lean into these, and that's sort of what we're doing. If you have a quality orientation like we do, with a dividend focus like we do, given demographics and all that, there's probably no better industry that fits what we do looking forward than healthcare."

Rich Eisinger, portfolio manager, Madison Investors Fund (MINVX)

Even before attending business school, Eisinger was reading books about Warren Buffett's investing strategy. It's no surprise that, as head of Madison's US equity team, he has an approach shaped by one of Buffett's popular tenets: Think about investing as buying an ownership stake in a business and not as a stock trade. Eisinger and his team have three main guidelines when picking stocks. First, they seek out companies with strong and sustainable competitive advantages that can generate steady cash flow.



Madison Investments

Second, they look for management teams that allocate capital wisely, for example by not buying back their shares at high prices. And third, they seek to buy companies trading at a discount to their assessed intrinsic value. Each analyst then draws up a strictly one-page report on each qualifying stock, ranking them on a scale of one through five. Every company that lands in the portfolio scores at least three.

One-year return: 13.5%. Biggest holdings (as of 9/30): Alphabet (5.3%), Lowe's (5.1%), Brookfield Asset Management (5%), US Bancorp (4.8%), PPG Industries (4.8%)

What worked in 2019: "Buffett's company is in the portfolio — and that's a 5. Another '5' in the portfolio is Brookfield Asset Management. They're involved in infrastructure, hydroelectric power, and commercial real estate. They're also an alternative asset manager, so they create funds for the institutional marketplace that contain a lot of the assets in these areas."

What's ahead in 2020: "We don't really try to predict the economy, but we see a slower global growth environment. Europe and China are facing macroeconomic headwinds. This is bleeding into the US in some areas, particularly industrials. "I read recently that more than 85% of global central banks are still in the easing process. So that's obviously fuel for the stock-market fire."