

# These stars made it to 15%-a-year club

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Returning an average of 15 per cent or more over the past 10 years is a notable achievement for a mutual fund. And a rare one. Only 13 funds did it for the 10-year period ended Dec. 31.

That's out of about 900 retail investment funds with 10-year track records. (Ignored for the purpose of this ranking are funds that report returns before deducting management fees.)

The current members of the exclusive 15 per cent club range from diversified funds in mainstream categories, to industry-sector funds and hedge funds. Clearly, the road to riches has many routes.

While 10-year returns are meaningful, they are still subject to what analysts call end-date bias. If you relied solely on 10-year returns for fund selection, you'd be overlooking some potentially strong future performers that have done poorly over the past 10-year period.

For instance, funds specializing in Asian markets have been laggards during the 1997-2006 period. The Morningstar Asia Pacific Rim Equity Index of fund performance lost an annualized 0.3 per cent, and the Morningstar Asia Pacific Rim ex-Japan fund index has an average return of only 1.8 per cent. With China's emergence as an economic superpower, returns over the next 10 years may be much better.

Generally, funds investing in Canadian stocks outperformed those holding United States and other foreign stocks over the past 10 years. This won't always happen. Over the next 10 years, the opposite could well be true, as has often been the case.

For all these reasons, the top performers are not to be looked at as a "buy" list. Still, some useful insights can be gleaned from the latest 10-year winners.

Low fees give managers a head start. Management expense ratios, or MERs, varied widely among the 13 top performers, but low fees are a characteristic of four of the five funds specializing in Canadian stocks. Chou RRSP, Phillips Hager & North Dividend Income, Saxon Small Cap and Sceptre Equity Growth all are no-load funds with MERs well below the peer group medians. (The exception was Hillsdale Canadian Performance Equity, with an 18.5 per cent return and a pricey 2.78 per cent MER.)

Smart picking was the main reason for the lofty returns earned by these funds, which have managers who include Allan Jacobs of Sceptre Investment Counsel Ltd., the Morningstar 2006 manager of the year. Nonetheless, low fees gave Jacobs and others a head start on their costlier competitors.

High returns can mean high risk. The overall winner over the past 10 years is Front Street Special Opportunities Canadian, an aggressive specialty fund with investments that include small, thinly traded companies.

Its annualized return was a high-flying 23.1 per cent. But investors might want to pack an air-sickness bag. The fund's one-month returns have ranged between a 33.1 per cent gain and a 26.3 per cent loss.

Also risky are sector-specific funds. CIBC Energy and Dominion Equity Resource, which are among the top 10-year performers, have capitalized on the energy boom. But commodity cycles work both ways, and these funds are bound to have lean periods, too.

Hedge funds may have a place. Before considering a hedge fund that employs alternative strategies such as short-selling or leveraging, however, you should have the core-equity and fixed-income categories covered. Even then, hedge funds are not for everyone. The funds are best suited for wealthier and more sophisticated investors.

Among the hedge-fund success stories is Goodwood Fund, a long-short-equity fund managed in Toronto by Peter Puccetti. The fund, aimed at only wealthier investors, celebrated its 10th birthday in 2006 and ended the year as the second-highest performer of any retail investment fund over 10 years, with an annualized 21.8 per cent return.

Better still, unlike some crap-shoot-style funds, Goodwood was one of the best performers on a risk-adjusted basis. Good for Goodwood. As with any fund, good performance isn't just about returns. It's also about keeping the ride from being too bumpy.

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