FPA Crescent FPACX

A good hurdler.

Morningstar's Take FPACX

Morningstar Rating	★★★★★
Morningstar Analyst Rating	Gold

Morningstar Pillars

Process	Positive
Performance	Positive
People	Positive
Parent	Positive
Price	Negative

Role In Portfolio
Supporting

Fund Performance FPACX

Year	Total Return (%)	+/- Category
YTD	5.15	-0.67
2016	10.25	2.91
2015	-2.06	-0.13
2014	6.64	0.43
2013	21.95	5.47

Data through 5-31-17

5-22-17 | by Dan Culloton

FPA Crescent can clear the hurdles between it and its goals and still deserves a Morningstar Analyst Rating of Gold.

Expenses are the biggest and most obvious hurdle. The fund has never been cheap and likely never will be; the managers argue they offer a hedge fund-like philosophy and approach for less than hedge fund fees. Precious few alternative or traditional strategies, however, have been able to overcome higher-than-average fees over the long term, but so far this fund has been the exception. It has delivered excellent results after fees for 24 years, and for most of that time fees were much higher than they are now. Expenses here have dropped 43% since 2009, and, while they're still above average, they are lower now than they have ever been.

Asset size is another potential hurdle. With more than $20 billion under management here and in similar strategies, its management team's ability to invest in the small- and mid-cap stocks that helped it years ago is limited. Flows into the fund, however, have turned negative in recent years, which actually alleviates some asset bloat concerns. There also are more people involved: Manager Steve Romick now has two comanagers and eight analysts contributing.

Romick and his team also apply the same eclectic, contrarian style that shoots for equitylike returns with less than equitylike risk by watching and waiting for the right price and place to deploy cash across the capital structure.

Patience and strict value standards remain the fund's edge. Romick remains pessimistic about valuations in general but hasn't gone on strike. The fund still had a lot of cash on hand at the end of 2017's first quarter--38% of assets--but he still thought financials stocks were relatively inexpensive after their post-U.S. election rally. The team also had been snooping around the healthcare sector after its weak 2016. The fund's helping of high-yield bonds remained small, less than 6% of assets, after taking profits on some energy and basic materials sector issues it had picked up earlier in 2016. This approach has helped the fund achieve its goals over time.

Process Pillar Positive | Dan Culloton
05/22/2017
This fund ranges across asset classes, market caps, sectors, geographies, and public and private markets in pursuit of equitylike returns with less risk. The managers, who can also short securities, are absolute value investors who view risk as the possibility of suffering permanent loss, not of underperforming a benchmark or peer group. They seek securities trading at substantial discounts to their estimated worth and stockpile cash when they can't find them. This flexible approach earns a Positive Process Pillar rating.

The fund's asset allocation varies based on where value resides. In the late 1990s and early 2000s, it favored small caps that had lagged in the 1990s' bull market. In 2008, it turned to high-yield and distressed debt, believing they were cheaper than stocks. In 2009, the fund shifted to moderately priced blue chips.

Macroeconomics influence but don't drive the process. The fund raised cash in the mid-2000s, when the credit boom neared its peak. Concerns that loose monetary policy has inflated asset prices have guided the fund into cash again in recent years.

The fund's size makes it harder to invest in small- and mid-cap stocks and limits the impact of its illiquid investments. But the team also is deeper, and the fund has expanded its tool kit by lifting its limits on overseas investments and individual short positions.

This fund found itself preparing for the opportunity to pounce in early 2017. The managers found the stock and bond markets dearly priced for the most part and trimmed some of the positions they entered in the latter half of 2015 and early 2016, primarily among energy high-yield bonds and some financials stocks.

The portfolio, however, maintained significant positions in financials companies. Veteran manager Steve Romick said they still looked relatively inexpensive even after their post-election rally. The Trump administration's trade, tax, and financial regulation agenda looked more uncertain at the start of 2017's second quarter, but stocks like Bank of America BAC and Ally Financial ALLY still were not expensive and had more capital and less debt than they did before the 2008 financial crisis, he said.

The fund's high-yield stake in early 2017 remained below 6% of assets as its managers trimmed some bonds and found little else to get excited about. The fund has, however, stayed creative and opportunistic on the margins, making a private loan to the troubled Sears Canada alongside private equity firms such as KKR and TPG. The managers expect an internal rate of return of nearly 12% on the loan.

The portfolio remains an interesting mix of the opportunistic and cautious with such positions balanced by a large, nearly 40% cash stake.

Performance Pillar Positive | Dan Culloton
05/22/2017
The fund's stated mission is to deliver equitylike returns with less risk than the stock market-- a hurdle it has far exceeded since inception--and earns a Positive Performance Pillar rating. Its 10.4% annualized gain from its June 1993 launch through April 30, 2017, beats the S&P 500 by 1 percentage point per year, while its standard deviation, a measure of volatility, was 31% lower than the index's.

FPA Crescent has won by not losing. With an oft-heavy cash stake, it will lag in some rallies. From its 1993 inception through the end of April 2017, it captured 69% of the S&P 500's gains in upturns. However, it was able to preserve those gains in rough environments, suffering just 46% of the index's losses in downturns. Over longer stretches, performance has been consistent. In 167 rolling 10-year periods from its birth through the end of April 2017, the fund has beaten the allocation--50% to 70% Morningstar Category average 100% of the time and the S&P 500 89% of the time.

It fares well on both an absolute and risk-adjusted basis against rivals and benchmarks with 60%/40% stock/bond mixes. Its Morningstar Risk-Adjusted Return of 6.5% annualized from inception through April 2016 beats the 4.5% of Vanguard Balanced Index VBIAX, which passively invests in the total stock and bond markets.

People Pillar Positive | Dan Culloton
05/22/2017
Steve Romick has led FPA Crescent since its 1993 inception, compiling a stellar record along the way. The fund isn't a one-man show, though. Analysts and investment committee members Brian Selmo and Mark Landecker have been comanagers since June 2013. Selmo is also research director for the Crescent team, overseeing about eight analysts with an average FPA tenure of more than three years. In total, 11 investment professionals works on this fund, which earns a Positive People Pillar rating.

FPA targets experienced analysts, but it takes pains to ensure its hires share the firm's distinctive investment style. Selmo, for example, had founded his own asset-management firm and was an analyst at value shop Third Avenue before joining in 2008. Landecker worked at Kinney Asset Management and Arrow Investments before joining in 2009.

Romick collaborates with other managers at the firm. In total, FPA has nearly 30 investment professionals with an average tenure with the firm of seven years. Romick's role at FPA has grown as former partner Bob Rodriguez stepped back and then retired in 2016, though FPA Crescent remains the only mutual fund he manages. He, Landecker, and Selmo also run a hedge fund, separate accounts, and a piece of Litman Gregory Masters Alternative Strategies MASFX. Each manager invests more than $1 million here.

Parent Pillar Positive | Dan Culloton
04/13/2017
FPA has changed but still earns a Positive Parent Pillar rating.

This is no longer Bob Rodriguez's shop; the outspoken legend retired in 2016. Steve Romick, FPA Crescent FPACX manager and managing partner with CFO J. Richard Atwood, is now its public face. He's no less zealous a contrarian than Rodriguez, though he expresses himself less vehemently and is more apt to nurture investor expectations than leave them to form their own.

The same is true of FPA. It still would, as former First Eagle Global SGENX manager Jean Marie Eveillard said, "rather lose half of our clients than half of our clients' money." But it’s more likely to try to convince clients to stay during fallow periods. In addition to naming successors and restructuring funds in recent years as key managers retired, the firm also expanded client service and started hosting biennial investor days. Like other active managers, the firm has seen outflows in recent years.

A core of committed capital and virtues remain, however. Investors still run FPA for investors. They eat their own cooking and charge reasonable fees. They're focused on the long term, disdain trendy fund launches, avoid regulatory snafus, and write smart and engaging shareholder letters. The firm’s focus on achieving good absolute long-term returns via high-conviction, bottom-up strategies also hasn’t wavered.

Price Pillar Negative | Dan Culloton
05/22/2017
FPA Crescent is expensive relative to its category and gets a Negative Price Pillar rating. Its 1.07% annual price tag, according to its most recent prospectus, though lower than in the past, remains above the category average and median. Outsourcing accounting and administration has shaved some basis points off this fund's levy, but assets have grown to more than $17 billion from $1.3 billion in this fund in 10 years. Shareholders have benefited in the form of lower administrative costs, but the fund's flat 1% management fee limits the extent they will profit from improving economies of scale.

You should consider the Fund's investment objectives, risks, and charges and expenses carefully before you invest. The Prospectus details the Fund's objective and policies and other matters of interest to the prospective investor. Please read this Prospectus carefully before investing. The Prospectus may be obtained by visiting the website at www.fpafunds.com, by calling toll-free, 1-800-982-4372, or by contacting the Fund in writing.

Average Annual Total Returns

As of Date: 3/31/17	Since 6/2/93	20 Years	15 Years	10 Years	5 Years	3 Years	1 Year	YTD	QTR	Market Cycle Performance 10/10/07-3/31/17	Market Cycle Performance 3/25/00-10/9/07
FPA Crescent Fund	10.42	9.19	8.49	7.02	8.47	5.27	14.19	3.37	3.37	6.75	14.70
S&P 500	9.31	7.86	7.09	7.51	13.30	10.37	17.17	6.07	6.07	6.74	2.00
MSCI ACWI	-	-	-	-	8.37	5.08	15.04	6.91	6.91	2.84	-
60% S&P500/ 40% BBgBarc US Agg	8.02	7.17	6.39	6.52	8.94	7.38	10.26	3.95	3.95	6.06	3.97
CPI	NA	2.13	2.10	1.73	1.27	1.10	2.45	0.30	0.30	1.66	2.75

Periods greater than one year are annualized. Performance is calculated on a total return basis which includes reinvestment of all distributions.

* The Fund commenced operations on June 2, 1993. The performance shown for periods prior to March 1, 1996 reflects the historical performance of a predecessor fund, FPA assumed control of the predecessor fund on March 1, 1996. FPA Crescent Fund's objectives, policies, guidelines, and restrictions are, in all material respects, equivalent to those of the predecessor fund.

Market Cycle Performance reflects the two most recent market cycles (peak to peak) defined as a period that contains a decline of at least 20% from the previous market peak over at least a two-month period and a rebound to establish a new peak above the prior market peak. The current cycle is ongoing and thus presented through the most recent quarter-end. Once the cycle closes, the results presented may differ materially.

Past performance is no guarantee of future results and current performance may be higher or lower than the performance shown. This data represents past performance and investors should understand that investment returns and principal values fluctuate, so that when you redeem your investment it may be worth more or less than its original cost. The Fund's expense ratio as of its most recent prospectus is 1.11%. A redemption fee of 2% will be imposed on redemptions within 90 days. Current month-end performance data may be obtained at www.fpafunds.com or by calling toll-free, 1-800-982-4372.

Please see important disclosures at the end of the commentary.

Important Disclosures

The views expressed herein and any forward-looking statements are as of the date of the publication and are those of the portfolio management team. Future events or results may vary significantly from those expressed and are subject to change at any time in response to changing circumstances and industry developments. This information and data has been prepared from sources believed reliable, but the accuracy and completeness of the information cannot be guaranteed and is not a complete summary or statement of all available data.

Portfolio composition will change due to ongoing management of the Fund. References to individual securities are for informational purposes only and should not be construed as recommendations by the Fund, the portfolio managers, or the Distributor. It should not be assumed that future investments will be profitable or will equal the performance of the security examples discussed. The portfolio holdings as of the most recent quarter-end may be obtained at www.fpafunds.com.

Investments in mutual funds carry risks and investors may lose principal value. Stock markets are volatile and can decline significantly in response to adverse issuer, political, regulatory, market, or economic developments. The Fund may purchase foreign securities, including American Depository Receipts (ADRs) and other depository receipts, which are subject to interest rate, currency exchange rate, economic and political risks; these risks may be heightened when investing in emerging markets. Small and mid-cap stocks involve greater risks and may fluctuate in price more than larger company stocks. Short-selling involves increased risks and transaction costs. You risk paying more for a security than you received from its sale.

Interest rate risk is the risk that when interest rates go up, the value of fixed income securities, such as bonds, typically go down and investors may lose principal value. Credit risk is the risk of loss of principal due to the issuer's failure to repay a loan. Generally, the lower the quality rating of a security, the greater the risk that the issuer will fail to pay interest fully and return principal in a timely manner. If an issuer defaults the security may lose some or all of its value. The return of principal in a bond investment is not guaranteed. Bonds have issuer, interest rate, inflation and credit risks. Lower rated bonds, callable bonds and other types of debt obligations involve greater risks. Mortgage-backed securities and asset-backed securities are subject to prepayment risk and the risk of default on the underlying mortgages or other assets. Derivatives may increase volatility.

Value securities, including those selected by the Fund's portfolio managers, are subject to the risk that their intrinsic value may never be realized by the market because the market fails to recognize what the portfolio managers consider to be their true business value or because the portfolio managers have misjudged those values. In addition, value style investing may fall out of favor and underperform growth or other styles of investing during given periods.

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FPA Crescent Fund was rated against the following numbers of US Fund Allocation – 50% to 70% Equity funds over the following time periods: 3 stars out of 724 funds in the last three years, 4 stars out of 651 funds in the last five years, and 5 stars out of 428 funds in the last ten years. Past performance is no guarantee of future results.

The Morningstar Analyst Rating™ is not a credit or risk rating. It is a subjective evaluation performed by Morningstar's manager research group, which consists of various Morningstar, Inc. subsidiaries ("Manager Research Group"). In the United States, that subsidiary is Morningstar Research Services LLC, which is registered with and governed by the U.S. Securities and Exchange Commission. The Manager Research Group evaluates funds based on five key pillars, which are process, performance, people, parent, and price. The Manager Research Group uses this five pillar evaluation to determine how they believe funds are likely to perform relative to a benchmark, or in the case of exchange-traded funds and index mutual funds, a relevant peer group, over the long term on a risk-adjusted basis. They consider quantitative and qualitative factors in their research, and the weight of each pillar may vary. The Analyst Rating scale is Gold, Silver, Bronze, Neutral, and Negative. A Morningstar Analyst Rating of Gold, Silver, or Bronze reflects the Manager Research Group's conviction in a fund's prospects for outperformance. Analyst Ratings ultimately reflect the Manager Research Group's overall assessment, are overseen by an Analyst Rating Committee, and are continuously monitored and reevaluated at least every 14 months. For more detailed information about Morningstar's Analyst Rating, including its methodology, please go to global.morningstar.com/managerdisclosures/.

The Morningstar Analyst Rating (i) should not be used as the sole basis in evaluating a fund, (ii) involves unknown risks and uncertainties which may cause Analyst expectations not to occur or to differ significantly from what they expected, and (iii) should not be considered an offer or solicitation to buy or sell the fund.

Index Definitions

The S&P 500 Index includes a representative sample of 500 hundred companies in leading industries of the U.S. economy. The Index focuses on the large-cap segment of the market, with over 80% coverage of U.S. equities, but is also considered a proxy for the total market.

MSCI ACWI Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI consists of 44 country indices comprising 23 developed and 21 emerging market country indices.

Barclays Aggregate Index provides a measure of the performance of the U.S. investment grade bonds market, which includes investment grade U.S. Government bonds, investment grade corporate bonds, mortgage pass-through securities and asset-backed securities that are publicly offered for sale in the United States. The securities in the Index must have at least 1 year remaining in maturity. In addition, the securities must be denominated in U.S. dollars and must be fixed rate, nonconvertible, and taxable.

The Consumer Price Index (CPI) is an unmanaged index representing the rate of the inflation of U.S. consumer prices as determined by the U.S. Department of Labor Statistics. The CPI is presented to illustrate the Fund's purchasing power against changes in the prices of goods as opposed to a benchmark, which is used to compare the Fund's performance. There can be no guarantee that the CPI will reflect the exact level of inflation at any given time.

60% S&P500/ 40% Barclays Aggregate Index is a hypothetical combination of unmanaged indices and comprises 60% S&P 500 Index and 40% Barclays Aggregate Index, the Fund's neutral mix of 60% stocks and 40% bonds.

Indices are unmanaged, do not reflect any commissions or fees which would be incurred by an investor purchasing the underlying securities. Investors cannot invest directly in an index.

The FPA Funds are distributed by UMB Distribution Services, LLC, 235 W. Galena Street, Milwaukee, WI, 53212.