

## Riding the Sentiment

*Investors generally look for underperforming stocks that will improve in performance over time and reward them with attractive returns. The strategy adopted by Cookson Peirce Core Equity Fund manager Bruce W. Miller is just the reverse. He follows a proprietary investment process that relies on a judicious and consistent sell discipline, and invests in strong stocks that are outperforming the market and continue to do so.*

**Q: What is your investment philosophy and how it differentiates you from other mutual funds?**

**A:** First and foremost, we are a technical manager and we don't rely on fundamental research. We believe that all the information available is reflected in the decision of every investor to buy, hold, or sell a stock. Therefore, all the information available is priced in the stock, and we need to monitor the price movement rather than the fundamentals.

Our goal is to build a portfolio of strong stocks that will outperform the market by an average of 4% to 6% annually and our track record indicates that we can do this. The strong buy and sell discipline is a key part of our process, because we believe that through buying strong stocks and cutting off the losers quickly, we can build a portfolio that outperforms by nature.

Our philosophy and process were developed by Robert Peirce in the late 1960s, when he analyzed the stock selection techniques of many managers with the idea that there must be a better way to invest than to simply buy

Xerox or IBM, as most managers did at the time. Later, in 1984, he founded the firm together with Jane and Donald Cookson. Since then, we have enhanced our process, but the core philosophy has remained unchanged.

**Q: How that philosophy translates into an investment strategy?**

**A:** We are an all-cap growth manager and we invest predominantly in the U.S. equity market, but we have no bias against owning the ADRs of global titans such as Sony or Siemens. Moreover, many of the U.S. companies we buy have global exposure.

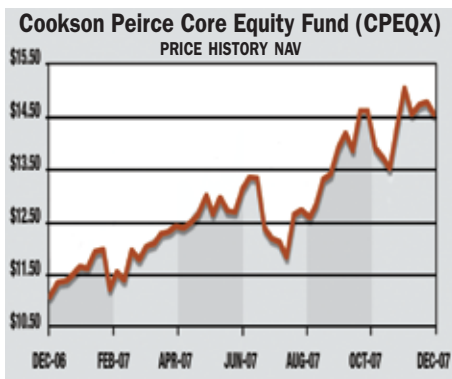
In a nutshell, our strategy is to buy strong stocks, or the stocks that are outperforming the market, and sell them when they start to underperform. A crucial part of our strategy is that we let our winners run. So, when we buy a stock that does well, we continue to hold it until it underperforms. That's just the opposite of what most individual investors do. When they buy a stock that does well, they are happy with the return, sell the winner and, therefore, miss the continued run up.



**BRUCE W. MILLER** is a principal of Cookson, Peirce & Co., Inc. and serves as the firm's Chief Investment Officer.

Miller joined the firm in 1987 as a portfolio manager. He is responsible for the day to day management of all portfolios, and leads the investment committee. He is active in the research efforts of the firm to continuously improve the investment process and results.

Miller graduated from Slippery Rock University with a Bachelor of Science degree in Business with a major in Finance. He continued his education at Kent State University on an assistantship where he received his M.B.A. with a concentration.



We also sell our losers very quickly, before they generate big losses. Unlike most individual investors, we wouldn't wait and hope for the loser to recover to the price we paid. By the law of the large numbers, if you lose 50%, you need to make 100% just to get even, and we don't want any losses that big nor do we want to wait for possibly years for a recovery.

**Q: Since you rely on relative strength, your portfolio reflects the market emotions and beliefs. Does that mean that you are actually supporting the market's sentiment rather than questioning it?**

**A:** We follow the market sentiment and we ride along with it. When the sentiment turns, we turn. Therefore, we'll probably never get the very bottom or the very top in any stock. Our goal is to catch 75% of the upward move because we are waiting for a change

**“We'll probably never get the very bottom or the very top in any stock. Our goal is to catch 75% of the upward move because we are waiting for a change in the sentiment to get in and out of these stocks.”**

in the sentiment to get in and out of these stocks. Typically, we are a little bit late on the buy and a little bit late on the sell, but that's part of our process.

**Q: You mentioned that you have enhanced your system in the past decade. What improvements have you made?**

**A:** Since the 90's, we have added group analysis to our stock selection technique and we use 28 industry groups. The S&P 500 uses nine economic sectors in 67 groups, but we felt that nine is too few and 67 too many. Some examples of our industry groups include automotive, business services, banks, insurance, health care drugs, health care equipment, retail, real estate, and media.

We introduced those industry groups to deal with an inherent problem of the relative strength system. If you want to buy the strongest stock, which is also in the strongest group, you are typically too late. So we calculate the average alpha of the groups, and instead of buying the strongest stock in the strongest group, we buy the strongest stocks in the second quartile of groups. In that way we buy stocks in groups that are not quite recognized and overbought yet, but that still have positive momentum.

We use the industry groups to avoid groups that have been too strong. For example, right now the aerospace and defense group has been on a big run. Although we own many of those stocks, we don't add any new ones because the group is too strong. We still don't sell them at this point, but we aren't purchasing them either. Overall, the group analysis keeps us from chasing stocks.

**Q: Would you explain your research process in more detail? What screens or metrics do you follow**

**to generate ideas and sift through them?**

**A:** Most importantly, we have a disciplined, quantitative process. We're very much bottom-up oriented when looking at the stocks, and top-down in selecting the groups from which to purchase stocks. We regularly update our list and generate the outputs, and we select the strongest stocks to add to the portfolio from the top of that list.

If the top stock belongs to a group that is acceptable, we buy it. If we already own it, we see if there is room for buying more of that stock. If not, we move down to the next stock on the list without looking at the fundamentals. On a weekly basis, we recalculate the alpha and the beta on every stock in our universe and also recalculate group strength.

Our process is not to constantly upgrade the portfolio looking for stronger stocks than the ones we currently own. It is a 'cast out' process, where the sell becomes the reason for the subsequent purchase. So when a stock becomes weak and we sell it, we look for the best stock to replace it with.

It is also important that we analyze our quarterly performance and adopt rectifying measures accordingly. For instance, in the third quarter of 2006 we had our worst relative performance since inception, and our analysis of this performance resulted in a change to the system. We realized that the underperformance was caused by buying stocks too long after they had been rated as buys, or near the peak as they were getting ready to weaken.

Now we move the stocks that have recently become buys to the top of our list because we know that most of the outperformance is generated early after the stock has become a buy. In addition, if stocks that we have held for more than a year have dropped down

to the hold category, we sell them instead of waiting for them to drop down into the sell category. That enhancement has slightly increased the turnover, but has considerably improved our performance.

**Q: Could you provide some examples of stock picks that illustrate your process?**

**A:** Enron Corporation would be a good example of our sell discipline. The company peaked at around \$77 a share and we owned it along the way up. Then the stock started to fall and we sold it at around \$56. Meanwhile, most of the major brokerage houses continued to call it a value 'buy,' even when the stock reached \$28. We sold it at \$56 not because we knew about the problems of the company or the future events, but because of our discipline and because it had become weak relative to the market.

In March/April 2007, we started selling off all the financial stocks because they had become relatively weak. If we had stayed in the financial stocks, our performance would be much worse than it is now. We had also owned many REITs and housing stocks, which were very strong all the way until the end of 2006, when we began selling them.

**Q: How do you approach portfolio construction? Which index are you benchmarked against?**

**A:** We have a diversified portfolio, which typically consists of 20 stocks. We measure the volatility of our universe every week and when it picks up, we'll move up to 25 stocks. If the volatility is at a very high level, we'll move up to 30 stocks. Currently, there are 24 stocks in the portfolio.


We start with equal allocation in those stocks and, as they perform, the winners will become heavier because of their performance, and the losers will

become relatively smaller until we sell them. To minimize the individual stock risk, we have limited our maximum stock position to 5% at the time of purchase. Also, the exposure to any industry group is limited to 20%. Since we manage a growth fund, we allow a maximum of 35% of the money to be invested in high beta stocks.

In terms of benchmarks, we measure ourselves against the S&P 500. Our universe consists of all the S&P 500 stocks and about 300 of the S&P 400 stocks. It also includes 150 stocks that are in neither of those indexes. Those additional stocks represent industries that are not covered, or just stocks that we consider interesting. Nevertheless, the bulk of our selection comes from the S&P 500 index.

**Q: What risks do you perceive and how do you control them?**

**A:** Risk management, as well as our entire investment process, is based on our consistent sell and buy discipline. The key element is that we get out of the stocks before they become big losers. We do not believe in market timing or in building up large amounts of cash in the portfolio. We try to stay with the stocks that we believe will do better than the markets. Since this is a growth portfolio, it can be a little bit more volatile on the downside but, historically, we have done pretty well in bear markets as well.

One of our rules related to risk control is that we reduce the positions when they reach 10% of the portfolio. Another element is that we stay out of the sectors that we believe are going to underperform. We believe that the way to make money is to make bets on sectors and stocks, but we are quantitative, technically oriented, and disciplined in that respect. With a minimum of 20 holdings, I believe that we also have adequate diversification to eliminate systemic risk. 

## Cookson Peirce Core Equity Fund

Symbol	<b>CPEQX</b>
Website	<a href="http://www.cooksonpeirce.com">www.cooksonpeirce.com</a>
Address	Cookson, Peirce & Co., Inc. 555 Grant Street, Suite 380 Pittsburgh, PA 15219-4421
Tel. No.	866.655.2455
Inception	08/03/2005

PORTFOLIO	
Total Net Assets*	\$19.1
Avg Mkt Cap (\$ Weighted)*	\$23,800
Average Price/Earnings Ratio	27.37x
Average Price/Book Ratio	6.27x
Turnover Ratio	115%

INVESTMENT INFORMATION	
New Investment	Open
Min Initial Investment	\$2,500
Min Subsequent Investment	\$500
Min Initial IRA Investment	\$2,500

RISK (AGAINST S&P 500 - 3-YEARS)	
Alpha	N/A
Beta	N/A
R-Squared	N/A
Ann. Std Deviation	N/A
Sharpe Ratio	N/A

RETURNS VS. S&P 500 INDEX		
	CPEQX	Index
1 Year (Cum.)	29.66%	5.49%
3 Year (Ann.)	N/A	8.62%
5 Year (Ann.)	N/A	12.83%

FEES AND EXPENSES	
Max Sales Charge - Front	0.00%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee	1.00%
Total Expense Ratio	2.00%

PORTFOLIO MANAGER	
Bruce W. Miller	2005

\*millions \*\*within 2 months of purchase

Data through: 12/31/2007

Source: Company Documents; Morningstar

Ticker staff searches for mutual funds for their consistency in performance and durability of investment style.

Our interview covers investment philosophy and strategy, research process, portfolio construction and risk control for funds. Through an interview we uncover long-term strategies and processes that help to generate long-term returns.

You can read more on this and other funds at [Ticker.com](http://Ticker.com)