Litman Gregory Masters Intl Instl MSILX

A combination of unusual strategies that would be hard to replicate.

Morningstar's Take MSILX

Morningstar Rating	★★★
Morningstar Analyst Rating	Bronze

Morningstar Pillars

Process	Positive
Performance	Neutral
People	Positive
Parent	Positive
Price	Negative

Role In Portfolio
Core

Fund Performance MSILX

Year	Total Return (%)	+/- Category
YTD	19.43	1.55
2016	-4.61	-5.40
2015	-5.52	-3.93
2014	-2.72	2.26
2013	21.47	2.03

Data through 7-31-17

8-17-17 | by Gregg Wolper

The strength of Litman Gregory Masters International's subadvisory lineup, and the distinctive way it's built, earn it a Morningstar Analyst Rating of Bronze despite its undistinguished record and above-average costs.

This fund is managed by a group of subadvisors, each of whom supplies between eight and 15 picks to the portfolio. Unlike many subadvised funds, they are not chosen with traditional diversification in mind, such as filling specific spots in the Morningstar Style Box. Rather, the Litman Gregory overseers look for topnotch managers who they deem effective at managing very focused portfolios and who relish taking on that challenge. If a manager provides some diversification from the rest of the portfolio, so much the better, but that's a secondary consideration.

The number of subadvisors can vary, and in March 2017, Litman Gregory added a sixth: David Marcus of Evermore Global Advisors. The firm said it was impressed with his record using a focused, value approach that leans toward small and midsized companies, often those facing difficult headwinds or with complex structures that even many value investors would shy away from.

This process has paid off for most of this fund's lengthy history, but it had subpar showings in 2015 and the first half of 2016. European banks hurt it in 2015, and then a heavy U.K. weighting suffered when the pound plunged after the mid-2016 Brexit vote. Owning Valeant Pharmaceutical VRX didn't help. Despite bouncing back in the past 12 months, the fund's 10-year ranking is only at the midpoint of the foreign large-blend Morningstar Category through July 31, 2017. For 15 years it has been in the 28th percentile, but in both periods it slightly lags the MSCI ACWI ex-US Index.

This fund is not appropriate for those seeking more conventional managers and a smoother ride. There's reason to think it can outperform in the future, as the current subadvisors are strong and bear no resemblance to index-huggers. There are bound to be bumps along the way, though, and a lower price--it recently rose--would give the fund a better chance of standing out.

Process Pillar Positive | Gregg Wolper
08/17/2017
This fund is managed by multiple subadvisors (typically four to six), each usually receiving an equal percentage of assets to invest in just eight to 15 stocks. The overseers from advisor Litman Gregory do not try to provide broad diversification with their selection of subadvisors--that is, they aren't looking to fill a large-growth slot, a small-value slot, and so on. Rather, they say they look for topnotch managers who are willing to select a small, focused portfolio for this fund and have proven a capability to manage effectively in that format; diversification is a secondary consideration. The fund gets a Positive Process rating.

As of August 2017, the fund has six subadvisors, each managing 16.67% of assets. The current lineup consists of Vinson Walden of Thornburg, investing in a mixture of basic-value names, consistent earners, and emerging franchises; a trio from Northern Cross, following a moderate blue-chip value style; David Herro of Harris Associates, who focuses on stocks trading at steep discounts to their intrinsic value; Mark Little of Lazard, who takes an all-cap relative value approach; a duo from Pictet with a core, all-cap approach; and David Marcus of Evermore Global Advisors, who looks for overlooked, often-complex undervalued situations and leans toward small and midsized companies. Portfolio size and turnover vary depending on the number of managers and whether they've changed in that year.

Although six subadvisors contribute stock picks to this fund, the overall portfolio does not look anything like the indexlike collection a half-dozen managers could potentially provide. One reason is that Litman Gregory intentionally chooses managers willing to break from the pack. The other reason is that the managers each select just a relative handful of stocks for the fund, so they couldn't provide a broad, indexlike collection for the portfolio even if they wanted to.

Thus, while the June 2017 portfolio is broadly exposed to a wide variety of sectors and countries, it shows unusual weightings. For example, it is quite underweight in energy. It also has no utilities or real estate holdings, even though those sectors add up to more than 5% of the foreign large-blend category average. Its consumer cyclical weighting is more than double the category average, with more than 25% of its portfolio there.

Country weightings also stand out. Most notably, with just 6% of its stock portfolio in Japan, the fund holds just one third the category average stake. But these figures aren't static. A year ago, for example, the fund had 26% of its stock portfolio in the U.K., well above the average, but that figure has dropped

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to around 16%, right around the category norm. Overall, the fund owns just 45 stocks, with four of them getting 4% of assets or more.

Performance Pillar Neutral | Gregg Wolper
08/17/2017
After a weak stretch in 2015 and the first half of 2016, this fund's once-outstanding record doesn't look at good as it did before, even with a strong showing in the 12 months through July 31, 2017.

One reason for the setback: Several European financials, considered to be selling at bargain prices by some of the fund's subadvisors, weighed on returns as those stocks have plunged. The portfolio also had a substantial overweighting to the United Kingdom when that country voted in June 2016 to leave the European Union. Although not all U.K. stocks lagged and the British market eventually recovered, the pound declined sharply in the wake of the vote and did not rebound, denting the fund's returns. Another culprit was Valeant Pharmaceuticals VRX: Its share-price collapse took a toll even though roughly half of the position was sold in mid-2015.

The fund had a very strong record prior to that; for example, it had beaten the foreign large-blend category average for five of the six calendar years starting in 2009. Overall, through July 2017 it lands in the middle of the category for the 10-year trailing period and well into the top half for the 15-year period, with a mixed record versus the relevant indexes in those time frames (Multiple subadvisor changes through its history mean those records are only partly relevant.) Overall, the fund gets a Neutral Performance rating.

People Pillar Positive | Gregg Wolper
08/17/2017
This fund is managed by a group of subadvisors, each of whom supplies a small number of stocks (between eight and 15) for the overall fund's portfolio. The makeup of the subadvisor lineup--chosen and monitored by two overseers from Litman Gregory, Jeremy DeGroot and Rajat Jain--has changed substantially over time. Currently, six subadvisors are in place, each running one sixth of the assets. One manager--Harris Associates' David Herro, manager of Oakmark International OAKIX among other funds--has been on board since this fund's 1997 inception. Besides Herro, the lineup includes Vinson Walden from Thornburg (who has comanaged Thornburg Global Opportunities THOAX since 2006 and was named to this fund alongside a now-departed colleague in 2008); Mark Little from Lazard Asset Management (lead manager on Lazard International Strategic Equity LISIX); Howard Appleby, Jean-Francois Ducrest, and James LaTorre from Northern Cross (who have managed Harbor International HAINX since 2009 and worked on it long before then); Fabio Paolini and Benjamin Beneche from Pictet, added on June 30, 2016; and David Marcus of Evermore Global Advisors, added in March 2017. Each of the subadvisors has solid credentials at their main funds, and the Litman Gregory overseers (which included Ken Gregory until 2014) have made thoughtful changes in the lineup over time, so this fund gets a Positive People rating.

Parent Pillar Positive | Gregg Wolper
03/28/2017
Litman Gregory has been a fine steward. Since it first rolled out mutual funds 20 years ago, the firm has stuck with its process of choosing high-quality managers to subadvise mutual funds. The firm offers a limited number of funds run by proven subadvisors that each contribute a small number of their best ideas to the portfolios. As of March 2017, Litman offers four mutual funds, and it expects to add one more this year. It will be the first new launch since 2011. The firm has also kept some key funds small and flexible--the Equity and International funds both closed to new investors in the past at under $1 billion in assets (although both are now open, and the latter is at $1.1 billion). Limiting fund sizes has allowed the firm to keep the number of subadvisors at each fund to a manageable number, rather than adding ever more and winding up with bland portfolios.

The funds fall short in terms of manager investment, although they still look better than most subadvised funds. Two subadvisors (out of a total of 20 across the funds) invest more than $1 million in a fund, one has between $500,000 and $1 million in a fund, and nine others (including the two principals from Litman Gregory) have $100,000 to $500,000 invested in at least one fund. On the fee front, most of the funds look pricey. Still, the quality of the underlying managers has helped the lineup stand out. Two funds earn Morningstar Analyst Ratings of Bronze.

Price Pillar Negative | Gregg Wolper
08/17/2017
This fund's Institutional share class, which holds nearly all the assets, had an expense ratio of 0.99% for 2015 and 2016, but it rose to 1.06% in the April 2017 prospectus. On the bright side, that's lower than it was in 2012, when the fund cost 1.15%. One reason for the decline was a fee waiver, but an additional waiver that was added was allowed to expire, and the fund also suffered large outflows in 2015 and 2016, explaining the rise in the April 2017 prospectus. That level lands on the border between the most-expensive and second-costliest quintiles for institutional shares of foreign large-cap funds. The tiny Investor share class also costs more than the median in its channel. Therefore, the fund receives a Negative Price rating.

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