

*Extract from...*

## **Corporate Access, Investor Targeting and Stock Selection:**

*Targets Should Have Low But Some Industry Exposure*

By Brendan Fitzpatrick, Founder, Fitzcores LLC

### Executive Summary

Corporate investor relations officers (IROs) and corporate access professionals at investment banks often seek potential new investors based on the assumption that high current exposure to an industry predisposes an investor to make a subsequent investment in the same industry. However, our research shows nearly the opposite – ***the amount of exposure a fund has in an industry is negatively correlated with subsequent investment in that industry provided a fund has at least some exposure to the industry.***

We attribute our findings to the fact that most actively managed funds are both diversified across industry and selective (hold a relatively small number of securities). For a fund manager to purchase a stock in an industry already represented in the fund, he or she would need to sell the fund's current exposure to maintain industry diversification and the count of fund holdings.

***A misunderstanding of how portfolio managers construct their funds can result in a substantial misallocation of time preparing for and participating in meetings that don't result in the investor purchasing the security.***

Many professionals in the corporate access realm encourage engagement between C-suite executives and non-owning fund managers that have high exposure to a security's industry. Their broadly shared assumption is that a fund manager with high exposure to an industry likes the industry, is familiar with it, and can be convinced to make another investment in it. Corporate executives, meanwhile, may believe their company compares favorably to a fund's current holding in their industry and that a face-to-face meeting can convince the fund manager to switch horses. Regardless of the reason, adherents to this approach are likely to experience disappointing results. Their performance would likely improve significantly if they would simply change their focus to fund managers who have low but some exposure to a security's industry.

### Appendix: Industry Exposure and Subsequent Industry Initiation

The table below shows the frequency of initiation by funds in an industry based on funds' prior year exposure to that industry. For comparison purposes, the values shown are relative to the rate of initiation for 'All' groups combined. For example, for the advertising/marketing services industry, funds with 1<sup>st</sup> quartile industry exposure initiated in the industry at 2.8x the rate for all funds, while funds with 4<sup>th</sup> quartile industry exposure initiated in the industry at 0.5x the rate for all funds. It follows that funds with 1<sup>st</sup> quartile exposure to the advertising/marketing services industry initiated at 5.6 times the rate of funds with 4<sup>th</sup> quartile exposure (2.8/.5).

Due the large number of industries included in our study (below), we used conditional formatting to highlight results – green for relatively high initiation frequency (greater than two times “All”), red for relatively low initiation frequency (less than .75 times “All”), and clear for neutral.

### Details by Industry

Industry	Level of Exposure (Quartile)						Quartile 1st > 4th
	None	1st	2nd	3rd	4th	All	
ALL industries (median)	0.5	2.8	2.2	1.5	1.0	1.0	*
advertising/marketing_services	0.8	2.8	2.2	1.0	0.5	1.0	*
aerospace_&_defense	0.3	2.1	2.2	1.6	0.9	1.0	*
agricultural_commodities/milling	0.6	2.7	2.8	0.7	2.0	1.0	*
air_freight/couriers	0.7	2.2	1.8	0.8	0.7	1.0	*
airlines	0.6	3.1	2.2	2.0	1.3	1.0	*
alternative_power_generation	0.6	3.9	2.1	2.3	1.5	1.0	*
aluminum	0.8	4.6	2.4	0.9	1.6	1.0	*
apparel/footwear	0.5	2.1	1.5	0.8	1.0	1.0	*
apparel/footwear_retail	0.4	2.7	2.3	1.4	0.6	1.0	*
auto_parts:oem	0.5	1.7	2.3	1.2	0.7	1.0	*
automotive_aftermarket	0.8	2.8	2.3	0.1	0.9	1.0	*
beverages:_alcoholic	0.5	1.8	1.4	1.1	3.6	1.0	positive
beverages:_non-alcoholic	0.6	3.2	1.6	1.5	1.0	1.0	*
biotechnology	0.3	2.3	2.0	2.3	1.3	1.0	*
broadcasting	0.5	5.0	4.1	2.4	0.9	1.0	*
building_products	0.5	3.1	2.1	2.3	0.6	1.0	*
cable/satellite_tv	0.9	2.4	1.1	0.4	1.5	1.0	*
casinos/gaming	0.4	4.9	4.0	2.2	1.1	1.0	*
chemicals:_agricultural	0.7	1.6	3.3	0.9	1.1	1.0	*
chemicals:_major_diversified	0.5	4.3	1.9	0.9	0.5	1.0	*
chemicals:_specialty	0.4	2.1	1.4	1.1	0.7	1.0	*
coal	0.6	4.4	4.0	3.0	2.2	1.0	*
computer_peripherals	0.5	2.3	2.8	2.9	1.1	1.0	*
computer_processing_hardware	0.4	3.4	2.2	1.8	1.8	1.0	*
construction_materials	0.7	2.7	1.9	0.6	0.3	1.0	*
containers/packaging	0.4	2.7	2.8	1.2	0.9	1.0	*
contract_drilling	0.7	3.1	2.7	1.5	1.1	1.0	*
data_processing_services	0.4	2.6	3.7	1.6	0.7	1.0	*
department_stores	0.6	5.2	2.8	2.4	0.2	1.0	*
discount_stores	0.8	4.1	2.0	2.7	0.0	1.0	*
drugstore_chains	0.8	2.5	3.1	1.5	0.6	1.0	*
electric_utilities	0.3	1.5	1.3	1.6	1.6	1.0	neutral
electrical_products	0.4	1.8	1.7	0.8	1.1	1.0	*
electronic_components	0.5	3.2	1.9	1.4	1.0	1.0	*
electronic_equipment/instrument	0.5	2.7	1.3	1.4	0.6	1.0	*
electronic_production_equipment	0.5	3.4	2.0	1.2	1.1	1.0	*
electronics_distributors	0.9	3.2	1.6	1.1	0.0	1.0	*
electronics/appliance_stores	0.9	3.6	3.5	0.0	1.2	1.0	*
electronics/appliances	0.5	3.9	1.8	1.5	1.7	1.0	*

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## Details by Industry (cont.)

Industry	Level of Exposure (Quartile)						Quartile 1st > 4th
	None	1st	2nd	3rd	4th	All	
ALL industries (median)	0.5	2.8	2.2	1.5	1.0	1.0	*
engineering & construction	0.3	2.2	1.3	2.0	1.1	1.0	*
environmental services	0.8	5.2	0.4	1.2	0.5	1.0	*
finance/rental/leasing	0.4	3.2	2.2	1.8	0.8	1.0	*
financial conglomerates	0.9	5.7	1.7	1.8	0.0	1.0	*
financial publishing/services	0.6	6.3	4.5	1.0	1.6	1.0	*
food distributors	0.7	3.5	3.1	1.1	0.9	1.0	*
food retail	0.4	2.1	2.2	2.8	1.0	1.0	*
food: major diversified	0.6	2.2	2.3	1.2	0.9	1.0	*
food: meat/fish/dairy	0.7	2.7	2.6	1.1	0.8	1.0	*
food: specialty/candy	0.4	1.7	2.0	1.4	1.1	1.0	*
forest products	0.5	4.7	3.3	4.4	2.5	1.0	*
gas distributors	0.6	3.4	2.2	1.1	0.9	1.0	*
home furnishings	0.6	4.1	3.4	1.8	1.5	1.0	*
home improvement chains	0.7	2.9	1.8	2.2	0.6	1.0	*
homebuilding	0.4	2.1	2.7	1.8	1.3	1.0	*
hospital/nursing management	0.5	4.4	2.5	1.2	0.8	1.0	*
hotels/resorts/cruise lines	0.6	2.6	3.7	1.5	0.8	1.0	*
household/personal care	0.4	2.2	1.6	1.3	0.8	1.0	*
industrial conglomerates	0.9	4.3	2.4	0.5	0.7	1.0	*
industrial machinery	0.2	1.1	1.4	1.6	0.9	1.0	*
industrial specialties	0.5	3.6	2.3	1.1	0.9	1.0	*
information technology services	0.2	1.4	2.1	1.6	0.9	1.0	*
insurance brokers/services	0.6	4.1	3.4	2.1	1.1	1.0	*
integrated oil	0.4	1.6	1.4	1.2	1.2	1.0	*
internet retail	0.6	2.7	1.7	1.1	0.3	1.0	*
internet software/services	0.3	2.0	1.7	1.1	0.9	1.0	*
investment banks/brokers	0.5	2.8	2.2	2.0	0.7	1.0	*
investment managers	0.5	3.2	2.4	1.3	0.7	1.0	*
investment trusts/mutual funds	0.8	7.0	8.4	3.2	2.8	1.0	*
life/health insurance	0.8	2.8	1.9	2.1	0.9	1.0	*
major banks	0.9	2.8	1.4	2.5	0.7	1.0	*
major telecommunications	0.5	2.6	3.1	1.2	1.2	1.0	*
managed health care	0.4	2.4	2.8	1.9	1.0	1.0	*
marine shipping	0.4	2.1	3.0	3.4	1.9	1.0	*
medical distributors	0.4	2.5	3.5	1.3	1.4	1.0	*
medical specialties	0.2	1.2	1.8	1.6	1.0	1.0	*
medical/nursing services	0.5	1.6	2.5	2.6	1.3	1.0	*
metal fabrication	0.6	4.8	2.8	1.9	0.3	1.0	*
miscellaneous	0.8	8.7	6.9	2.1	2.1	1.0	*
miscellaneous commercial services	0.3	1.3	1.5	1.6	1.0	1.0	*
miscellaneous manufacturing	0.6	4.8	1.9	1.9	0.1	1.0	*
motor vehicles	0.4	1.6	1.4	2.4	1.5	1.0	*
movies/entertainment	0.7	2.6	2.4	1.3	0.6	1.0	*

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	None	1st	2nd	3rd	4th	All	
ALL industries (median)	0.5	2.8	2.2	1.5	1.0	1.0	*
multi-line_insurance	0.4	3.5	1.7	1.6	0.8	1.0	*
office_equipment/supplies	0.6	3.8	13.7	3.7	3.6	1.0	*
oil_gas_pipelines	0.5	3.1	3.3	2.5	3.8	1.0	neutral
oil_gas_production	0.5	1.9	2.5	1.5	1.6	1.0	*
oil_refining/marketing	0.4	2.7	2.3	1.8	1.8	1.0	*
oilfield_services/equipment	0.4	4.7	4.1	2.3	1.6	1.0	*
other_consumer_services	0.4	2.9	3.1	1.4	0.6	1.0	*
other_consumer_specialties	0.9	2.2	1.4	1.6	0.7	1.0	*
other_metals/minerals	0.5	2.4	2.0	0.9	1.2	1.0	*
other_transportation	0.5	3.3	2.4	1.0	0.7	1.0	*
packaged_software	0.2	0.8	1.8	1.6	0.8	1.0	neutral
personnel_services	0.5	6.8	3.3	1.8	1.4	1.0	*
pharmaceuticals:_major	0.3	1.2	1.7	1.2	0.8	1.0	*
pharmaceuticals:other	0.7	7.5	2.5	3.3	3.7	1.0	*
precious_metals	0.5	2.5	2.5	2.0	2.0	1.0	*
property/casualty_insurance	0.4	5.7	3.5	2.3	0.2	1.0	*
publishing:_newspapers	1.0	2.8	1.5	1.7	0.0	1.0	*
pulp_&_paper	0.9	2.6	2.7	0.6	1.2	1.0	*
railroads	0.7	3.3	1.9	1.3	0.6	1.0	*
real_estate_development	0.3	2.2	1.9	1.9	1.2	1.0	*
real_estate_investment_trusts	0.1	0.9	1.9	1.5	2.5	1.0	positive
recreational_products	0.5	4.8	3.2	1.3	1.6	1.0	*
regional_banks	0.7	4.4	2.3	1.4	0.0	1.0	*
restaurants	0.4	2.3	2.4	1.4	0.7	1.0	*
semiconductors	0.3	1.1	1.4	1.4	1.4	1.0	neutral
services_to_the_health_industry	0.8	4.7	2.5	1.0	0.0	1.0	*
specialty_stores	0.4	1.4	2.0	1.6	0.9	1.0	*
specialty_telecommunications	0.6	3.1	3.1	3.2	0.5	1.0	*
steel	0.5	3.2	1.9	1.2	1.3	1.0	*
telecommunications_equipment	0.6	1.7	1.3	1.5	1.4	1.0	*
textiles	0.7	3.5	6.8	0.9	2.7	1.0	*
tobacco	0.5	5.3	2.7	2.5	2.0	1.0	*
trucking	0.4	3.7	3.1	1.9	2.0	1.0	*
trucks/construction/farm_machinery	0.4	2.6	1.3	1.7	0.7	1.0	*
water_utilities	0.9	1.8	1.1	0.5	2.0	1.0	neutral
wholesale_distributors	0.4	2.1	1.8	1.9	0.8	1.0	*
wireless_telecommunications	0.4	2.1	1.9	1.2	1.7	1.0	*

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