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Fund of Information

Does Your Mutual Fund Own Too Much Apple?

Apple's success has made it a market behemoth—which means it's taking up a larger portion of many funds. Perhaps too large.

By Avi Salzman
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No one could call Apple a "problem" for investors in the past two years. The stock has doubled in that time, and its $740 billion valuation is now twice as large as the second-biggest company by market value, ExxonMobil.

And yet, today it's fair to call Apple (ticker: AAPL) a problem for many fund managers and individual investors. The stock represents such an enormous weight in many indexes that managers must tiptoe gingerly around it: Apple constitutes 3.9% of the Standard & Poor's 500 index, which means money managers who track their performance against the S&P take a big risk if they don't own a similar weighting. Apple looms even larger for technology fund managers who compete against the Powershares QQQ ETF (QQQ), in which the stock has a 14% weighting. Even investors looking for broad diversification have to account for Apple; it constitutes 3.3% of the Russell 3000.

Of the mutual funds that own Apple, the average stake is 3.3% of assets, and the average large-stock fund holds a 3.9% position, according to Morningstar.

Apple's size creates a problem for investors looking to manage their risks. "It's made a lot of people money, but it's also become a very large part of some people's portfolios," says Robert Goldsborough, a funds analyst at Morningstar. "That's the antithesis of diversification."

It's even a risk for a manager who decides not to hold Apple. Investors are likely to question anyone with a limited weighting. "If a fund manager has a different opinion, that manager had better be really good at what he or she picks," Goldsborough says. A relatively small group has managed to beat the market despite not holding Apple: 53 large-stock funds have steered clear of the behemoth in the past three years and still beaten the S&P 500, according to Morningstar.

Owning a heavy weighting in Apple without reducing the rest of the fund's technology exposure can double the problem, notes Chris Cook, a portfolio manager at Ohio-based Beacon Capital Management. "If something bad happens to Apple it will drag the whole sector down," he says.

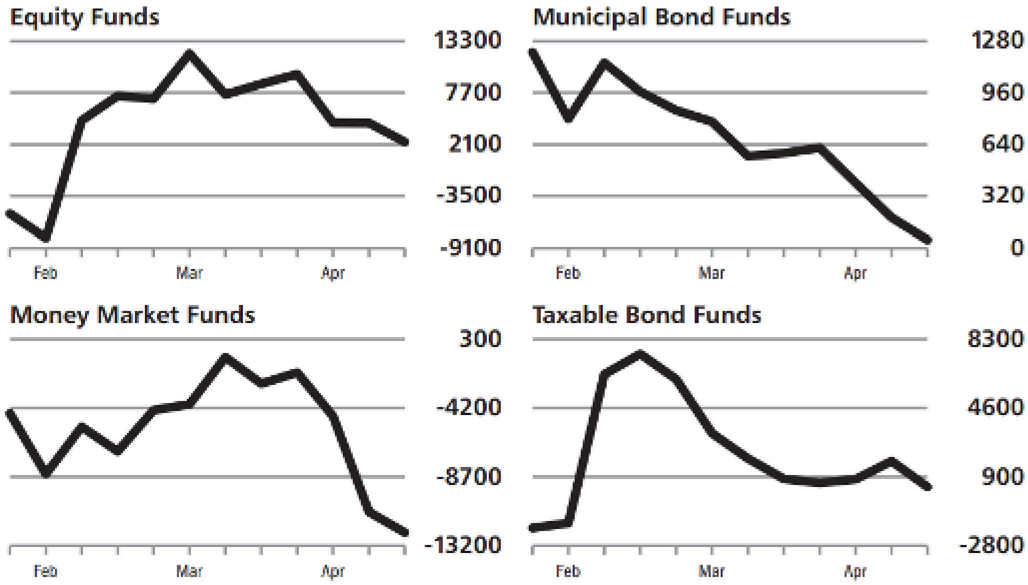
AS PROBLEMS GO, of course, Apple's a pretty good one to have. Not only does the company continue to produce innovative products and break sales records, its growing dividend (now yielding 1.5%) has made the stock more attractive to value investors. And at less than 15 times forward earnings, it doesn't look pricey.

But given the company's dependence on finding hot new products, it's also arguably more vulnerable to a pullback than former behemoths like General Electric (GE) or ExxonMobil (XOM), which Apple supplanted in 2011 as the world's largest public company. For instance, Apple slumped 20% in the two months after it introduced the iPhone 5, and then trailed the market by 25 percentage points in 2013, before its dramatic rebound last year. Apple's product cycles run fast and furious and the periods in between can be filled with doubt as to whether it has lost its mojo, **says John Petrides, a portfolio manager at Point View Wealth Management.**

Even for managers with a deep affinity for Apple, the surge over the past year and a half is starting to give pause. Mark Mulholland, manager of Matthew 25 (MXXVX), says he's cutting his Apple stake to 12% from 14.8% at the end of 2014. It will still be the largest holding in the fund. "It's a great company; it's just not as cheap as it was."

CASH TRACK

Moving Out of Cash: Outflows from money-market funds rose to $12.3 billion from $11.0 billion based on the latest four-week moving average, says Lipper. Equity funds had a $2.4 billion inflow, taxable-bond funds a $364 million inflow, and muni funds a $50 million inflow.



The charts above show four-week moving averages of net cash flow in millions of dollars.

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