



Four decades of investing with Gordon Crawford

After 41 years at The Capital Group, Gordon Crawford will retire in December, handing over his portfolio responsibilities to the next generation of managers. In the following Q&A, Gordon talks about his early years in the business, his pivotal role covering the media and entertainment industry, and his outlook for the developed and emerging markets.

As you look back at your career, will you share some examples of your most successful investments?

My most successful investment involved one of the executives that I have an enormous amount of respect for, John Malone. John for years headed up Tele-Communications (TCI), which was the biggest cable company in the business. In the early 1990s, he decided to spin off Liberty Media, which was a collection of TCI's programming and cable network assets, and he did it in typical John Malone fashion. It was a very complicated split-off, not a spinoff. They set up an exchange ratio between Liberty and TCI that people didn't understand. The prospectus was daunting. John put low valuations on the assets, because none of them were traded publicly. I thought it was an enormously attractive situation.

We decided we still loved TCI. We didn't want to give up our ownership, so we went out in the open market and bought enough TCI shares to submit into this split-off so that we would own about 15% of Liberty Media, as well. And then we actually bought some rights and thought maybe we would ultimately own 18% or 19% of Liberty Media.

Two days before the deal closed, I got a call from John Malone because he knew what I was doing. He said, "Gordy, less than half the people are going to exercise their rights to trade into the split-off, so you're going to own 43% of Liberty Media." I talked to our lawyers and we figured out that, although the ownership limit was 20%, we were only going to have about 12% of the votes. For that reason they let us go ahead with it and, on day one, we owned 43% of Liberty Media. For a couple of months the stock almost never had a down day because everybody that owned it had jumped through hoops to get there, so there were no sellers. People finally figured out how valuable, and



Gordon Crawford is a portfolio counselor on several mutual funds in the American Funds family, including The Growth Fund of America, SMALLCAP World Fund and The New Economy Fund. Since he joined Capital in 1971, Gordon has also been an investment analyst, covering the media/entertainment and insurance industries.

undervalued, these assets were. Over the next few years the stock went up, I think, 20 times. It was an enormously successful investment.

In the interest of being fair and balanced, which investment didn't work out so well?

I've made some mistakes in my career. One example is Time Warner, which at one time was the greatest media and entertainment company on Earth and we had done very well with it. Then in 2000, America Online announced the merger with Time Warner. I did not foresee the collapse of AOL. Part of it was due to fraud, but a lot of it was my not recognizing that AOL's dial-up Internet business was about to get seriously hurt by the advent of broadband, which was controlled by the cable companies. And so we ended up losing a lot of money on it during that time period, from the top to when it bottomed.

What are your thoughts on the media and entertainment industry after following it for so many years?

I was very fortunate to cover media and entertainment throughout most of my career. It's a dynamic field that is always being transformed by technology, which makes it very exciting. You can go all the way back to 1456 when Johannes Gutenberg invented the movable-type printing press, to Thomas Alva Edison inventing the movie camera, the projector and recorded music devices, to radio and television fundamentally changing the industry again. There is constant change and innovation.

When I entered the investment management business in the early 1970s, cable television — which was a retransmission business offering service for \$6 a month — had just started creating its own programming. You had Home Box Office in 1978 and WTBS with Ted Turner, and then CNN in 1980.

I was fortunate enough to be there at the birth of an industry. Nobody else followed these companies and they were growing rapidly. And then, of course, next came the VCR, and then the DVD, and the home video business was born. That ended up being 50% of the business of movie companies.

So there has always been this dynamic change. We've seen it in spades during the last 10 years with the Internet, again, just completely reshuffling the deck in media and entertainment, decimating some industries, such as recorded music and newspapers, and creating new companies with stratospheric market caps. It has always been a fascinating, rapidly evolving industry and I've been very lucky to have spent 40 years intimately involved with it.



Gordon Crawford in 1971

Covering the media and entertainment industry, you developed close relationships with executives and became a confidant and a sounding board. Can you talk about some of those experiences?

There were a number of times in my career when somebody would come to me and either bounce a deal idea off me or ask for an introduction to someone. When that happened, we would freeze trading in the stock until whatever I knew became public information.

One good example of that was when my wife and I were fishing at Ted Turner's ranch one August. Ted got a call from Jerry Levin, the head of Time Warner, saying he wanted to fly out the next day to talk. It was kind of a fun story because my wife and Jane Fonda got to drive out and pick him up while Ted and I went fishing. Then after lunch, Ted comes running down the hill, with all these buffalos behind him, announcing that he's agreed to be purchased by Time Warner. Of course, I immediately called our legal department and told them to freeze trading on Time Warner, Turner Broadcasting and Liberty. We ended up being frozen for about a month and a half, because they didn't announce the deal for quite some time.

Let's talk about The Growth Fund of America. What has it been like managing GFA from its formative years to today?

It has been an amazing journey. Obviously I'm biased, but I think it is a truly great fund. People who look at it today don't realize where the fund came from. When we took control of GFA on December 1, 1973, it had \$12 million in assets — \$12 million, not billion — and a tax loss carryforward of \$16 million, which was bigger than its asset base.

The track record for the whole period controlled by Capital has been truly remarkable. GFA had a great run from 1982 to 1999.

Figures shown are past results for Class A shares and are not predictive of results in future periods. Current and future results may be lower or higher than those shown. Share prices and returns will vary, so investors may lose money. Investing for short periods makes losses more likely. Fund results are for Class A shares and reflect deduction of maximum sales charge of 5.75%. For current information and month-end results, visit americanfunds.com.

Part of it was just a great bull market, but I think in that 18-year period we had two down years and they were both about 5%. And then we had nine years when the fund was up more than 20% — sometimes as much as 30% or 40% — so it was an extraordinary period.

What really put GFA on the map was the year 2000. In 1999, GFA was up about 45%. It held a lot of technology stocks, and we did an amazing pivot and sold a lot of our tech. We went very defensive and raised cash. And so in the calendar year 2000, GFA ended with a 7% gain while the S&P 500 index declined 9% and the average Lipper multi-cap growth fund lost 12%. As a result of that, even though the next two years were down years, GFA basically went from \$30 billion in assets to \$200 billion at its peak.

Then 2008–2009 came along. Our shareholders were very disappointed in GFA's performance during that down market, and understandably so. We were not happy with it either. GFA basically went down in line with the market. That is after people watched us in 2000 go up 7% in a market that lost 9%.

I think people misunderstand why GFA declined. It's not because it was a \$200 billion fund, and it's not because the system was broken. It was simply that in 2008–2009 every single group of stocks matched the broader market's decline. It was a total across-the-board wipeout and, unless you held cash, there was really nowhere to hide.

When a group of stocks becomes overvalued, we tend to get out of them. In 2000 you could sell tech, telecom and media, buy defensives, and stock-pick your way out of a down market. From 1980 to 1982, when oil stocks were 30% of the index, you could stock-pick your way out of a down market, which we did. You could stock-pick your way out of the "Nifty Fifty" market in 1973–1974. But you couldn't stock pick your way out of 2008–2009.

We are having a very good year in 2012. I still believe The Growth Fund of America is a great fund with a great group of managers.

What prompted us to get out of technology in 2000? Was it a decision by one particular analyst, or a group of managers?

It was everybody. I remember one of my great pals, Jim Martin, our semiconductor analyst, pounding the table at one meeting, saying this is a train wreck waiting to happen, based on what he saw as rampant triple ordering in the semiconductor business. In the spring of 1999, I spoke to a business school class at Stanford and I compared the Internet bubble — which hadn't yet burst— with the railroad bubble of 1840 in the U.K. The similarities were amazing. There was a crazy bubble in railroad stocks, with its own jargon, like all the Internet jargon. People who didn't get it were ridiculed. There was capital flowing into the industry — and then there was a huge collapse. In the end, the railroads did change the way business was done in the U.K. and around the world, just like the Internet is changing things today. But there was a bubble and the bubble needed to be corrected.



Gordon Crawford (R) in Geneva, with David Fisher and Nilly Sikorsky in 1979.

Did we not see the housing bubble with quite the same clarity?

We talked about it. We didn't own any housing stocks, but we didn't do a good enough job connecting the dots of how the housing market's collapse was going to impact the banking industry. Typically you would buy bank stocks in a down market because of their yields. But nobody anticipated what happened in 2008–2009, which was that we came close to a total breakdown of the global financial system. We certainly should have figured it out better than we did.

Let's turn to your views on developed markets versus emerging markets. Can you talk about your perspective on that?

For the last 30 years, the major developed democracies of the world have been living beyond their means, building up massive amounts of debt and making health care and pension promises they can't possibly keep. They are just borrowing money, as

individuals and as governments. Alexis de Tocqueville wrote that a democracy can never last. The reason is that, once voters figure out that they can elect people who will grant them largess from the public treasury, all they will do is choose politicians who will grant them largess from the public treasury. So he concluded that it will inevitably end up in a wrecked fiscal policy and the end of democracy.

I think we have been building toward that in the last 30 years. The global financial crisis was a giant wakeup call for the United States, Western Europe and Japan. It's a call that has largely gone unheeded. Very little has been done to address the debt issue. The world's major central banks have helped kick the can down the road by flooding the system with liquidity, blowing out their balance sheets. It has helped keep everything afloat and given us a false sense of security.

We are saddling our grandchildren with a ridiculous amount of debt. It's a scandal, really, and we are just not doing anything about it. My generation has decided that they are going to grant themselves all this largess, and they are going to pay very low rates of real taxes and borrow the difference, so we're heading for a disaster. There is a piper that must eventually be paid. I don't know if it's going to be this year or five years from now, but eventually we are going to have to get real about bringing some discipline back into the system.

So that's what I am very concerned about. I think even if we muddle through, we are going to be facing five or 10 years of very low global growth in the developed world, as opposed to the growth we've experienced for the last 30 years, which we all know now was achieved through leveraging up the system.

And the outlook for emerging markets?

The emerging markets are in better shape. They have lower levels of debt at the household level, at the corporate level and at the governmental level. Asia went through a terrible period in the late 1990s, and they all got religion. Most of those countries have a debt-to-GDP ratio of 40%, not 100%. Their consumer populations are relatively unlevered. They have growing populations. They have large middle classes moving up the disposable income ladder. They are all different, but I think it's a fair bet that if you look at GDP or some other metric for Brazil, India, China, Russia, Indonesia and other countries today and then look again 20 years from now, those countries will account for a much bigger part of the global economy than they do today. If you can invest some money there and not look at it every day, 20 years from now I think you will be happy to have had assets in emerging markets.

How does that view influence your portfolio positioning?

My world view informs everything I do. I am a tailwind investor. I love finding what I think will be an enduring secular trend. It might be the growth of cable TV in the early days, or the Internet today. There have been plenty of times when I felt a whole industry was attractive, like cable, and we owned virtually every company in it. I prefer good management, but even with bad management, if there is a strong enough tailwind, it can lift the entire industry.

I am never going to be 100% in cash. That wouldn't be appropriate, and it's not what our shareholders want from us. So I am always trying to find great companies like Amazon and Google — companies that have compelling products and services, that are taking so much global market share that even in a struggling developed world they are growing rapidly and profitably. I have steered away from companies that don't have that dynamic. I want companies that can do well in a poor environment. In the emerging markets, I like companies that are focused on middle-class consumers in domestic markets, as opposed to exporters, which I think are going to have a difficult time.



Gordon Crawford (L) with Bill Grimsley in 1991

How are we preparing for your departure in the funds that you manage?

It's very simple. It's one of the beauties of our Multiple Portfolio Manager System. If I was the sole portfolio manager of SMALLCAP World Fund and I decided to retire and somebody had to step into my shoes, there would be total chaos and a very unpleasant transition period. But SMALLCAP World Fund has more than a dozen portfolio managers, and 35% to 40% of the fund is managed by the analysts. When I take the elevator down for the last time, there will be nary a ripple. My little slice of the fund will be taken over by other people and the shareholders won't even notice I'm gone.

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Let's go back for a moment and start at the beginning. How did you come to The Capital Group?

Well, I almost didn't come to Capital. I was at the University of Virginia Graduate Business School — now the Darden School — working on my MBA. From the moment I started business school, I knew I wanted to be a securities analyst. I had already worked four years on Wall Street, and I worked part time at the Institute for Chartered Financial Analysts in business school.

I interviewed with all of the usual suspects: T. Rowe Price, Fidelity, Goldman Sachs, Morgan Stanley. Both my wife and I were bartending to put me through school. We had a child. One day, I stopped by the school on my way to my bartending job, and I bumped into my finance professor. He said, "You're not signed up for Capital?" And I said, "Who is Capital?" He said, "It's a great, small, private investment management company. Go home, call in sick, get a suit on, and I'll try to convince these guys to stay." They did stay, and the rest is history.

What happened during the interview that made you decide Capital was the right place for you?

It wasn't the first interview that sealed it for me. It was the second. Unlike all the other companies that interviewed me, Capital invited my wife to come along. We spent an entire day in Los Angeles meeting virtually everybody involved in the investment process at Capital. We had dinner with David Fisher and his wife. They showed my wife around L.A. and I just fell in love with the people and the culture.

My wife went home early and I had more interviews at other firms. When I arrived back at my apartment in Charlottesville, before I could say hello to my wife or hug my kid, I had a call from Capital's head of human resources. He offered me a job and I said yes on the spot. My wife almost fainted, because we hadn't discussed it. The HR person said, "Well, I haven't told you how much you're going to make," and I told him, "I don't care, I want the job."

What made you decide to stay for 41 years?

Capital is the best place to manage money in the business: a privately held company with a conservative nature and a sound balance sheet. That creates an enormous comfort zone, even in difficult times. I remember the crash of October 1987, when the stock market went down 20% in one day. There was tremendous fear. I called friends who worked for hedge funds and small investment management companies, and they didn't know if their businesses would survive. They were running scared. At Capital, we had a history of investing in our capabilities during down markets, and we had a sound balance sheet. So I spent my time thinking about what stocks I wanted to buy for our clients.

I never wanted to work for a company where I would feel like I wasn't proud of any decision that was made if I read about it in the Los Angeles Times or the New York Times or The Wall Street Journal the next day. And in 41 years, I have never been put in that situation. Our decisions have always been of the highest ethical order and always focused on achieving solid, long-term results for our clients. It never occurred to me to work anywhere else. I've been extremely fortunate to work here and I've never looked back.

Here are The Growth Fund of America's average annual total returns for Class A shares with all distributions reinvested for periods ended September 30, 2012, assuming payment of the 5.75% maximum sales charge at the beginning of the stated periods:

1 year: +20.57% 5 years: -1.12% 10 years: +8.08% Expense ratio: 0.68%

The expense ratio is as of the fund's prospectus available at the time of publication.

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from a financial professional and should be read carefully before investing.

Past results are not predictive of results in future periods.

Securities mentioned by Mr. Crawford in this publication are owned in the following funds he manages. Here is a listing of those securities, along with the percentage of assets in each fund and the top 10 holdings for each fund (as of 9/30/2012):

The Growth Fund of America — Securities mentioned: Amazon 3.3%, Google 2.2%, Liberty Media 0.4%, Time Warner 0.3%. *Top 10 holdings*: Amazon 3.3%, Apple 2.9%, Gilead Sciences 2.9%, Comcast 2.7%, Home Depot 2.4%, Google 2.2%, Oracle 2.1%, Philip Morris International 1.7%, EOG Resources 1.3%, Costco Wholesale 1.2%.

The New Economy Fund — Securities mentioned: Amazon 1.3%, Google 0.1%, Liberty Media 0.7%, Time Warner 0.6%. *Top 10 holdings:* Apple 2.4%, Gilead Sciences 2.1%, Galaxy Entertainment Group 2.1%, Hologic 1.8%, Crown Castle International 1.8%, Samsung Electronics 1.7%, Comcast 1.7%, Baidu 1.6%, AIA Group 1.4%, Amazon 1.3%.

SMALLCAP World Fund — Securities mentioned: Liberty Media 0.5%. Top 10 holdings: ENN Energy Holdings 1.2%, Pharmacyclics 1.1%, Regeneron Pharmaceuticals 1.0%, InterOil 1.0%, AAC Technologies Holdings 0.9%, Mr Price Group 0.9%, Ophir Energy 0.8% Virgin Media 0.8%, Iululemon athletica 0.7%, Raia Drogasil 0.7%.

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