

Brown Capital Mgmt Small Co Instl BCSIX

Morningstar Rating

★★★★★

Kudos

- Strong long-term record.
- Impressive aftertax returns.
- Seasoned management team.

Risks

- Management is willing to hold huge stakes in sectors such as technology and health care.
- Streaky returns.
- Success here will depend on management's continued ability to identify firms with sustainable competitive advantages.

Strategy

This fund's managers search for promising growth businesses that they can invest in for the long haul. Because the managers look for companies with \$250 million or less in operating revenue, the fund holds everything from micro- to mid-cap names. The fund sports huge weightings in volatile sectors such as technology and biotech.

Management

Keith Lee leads the management team of Robert Hall, Kempton Ingersol, and Amy Zhang. Lee has been with Brown Capital Management since 1991.

Inside Scoop

At this small-growth fund, the managers aren't afraid to make sizable long-term bets on the stocks and industries they like. Turnover is very low, and their record is good over the long run, but investors should be prepared for jumpy relative-return rankings.

Role in Portfolio

Supporting Player

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Year	Total Return (%)	+/-Category
YTD	25.79	6.80
2009	—	—
2008	-30.14	11.41
2007	21.17	13.58
2006	15.67	4.86

Data through 07-31-09

Morningstar's Take | 07-14-09 | by John Coumarios

Patience is a virtue at Brown Capital Management Small Company.

This fund traffics in one of the most volatile areas of the market, but it manages to keep a lid on risk. True, its 30% decline in 2008 was significant, but it was still better than 97% of its small-growth peers. Managers Keith Lee, Robert Hall, Kempton Ingersol, and Amy Zhang control risk by holding firms with sustainable competitive advantages and low relative levels of debt.

Although many managers say they buy companies that they deem to have sustainable competitive advantages, this fund's management team proves it with its minuscule portfolio turnover. Managers should hold highly profitable stocks almost indefinitely, and this fund does, with turnover that has averaged 11% per year over the past decade. Basically, this turnover number implies that the managers are holding on to stocks for nearly a decade. In 2003 and 2004, the fund's turnover was 1% each year, and it has never reached 30% in a year over the past decade.

Confidence in the ability of a firm to post high profits year after year means holding some firms with high price/earnings ratios. For example, Green Mountain Coffee Roasters' GMCR P/E ratio has averaged 43 over the past five years. The stock's profits have been enough to support its prodigious price, however, with net income increasing from around \$6 million in 2003 to around \$41 million for the trailing 12 months through March 2009. Most of that dramatic increase has come over the past year, though, with the advent of single-cup coffee makers for the home and with the firm's products now being sold in Wal-Mart WMT. This fund's managers deserve kudos for showing patience before the firm's fundamentals improved.

This fund will look sluggish relative to its peers when lower-quality stocks are the darlings, but investors shouldn't be fooled by that. It's one of the best funds in this space.

John Coumarios is a fund analyst with Morningstar.

Important Disclosure Information

Performance shown is for the period ended June 30, 2009. The performance information quoted above represents past performance, which is not a guarantee of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted.