



The Rainier philosophy is simple. We invest in quality growth companies at prices that make sense. We believe that rewarding stock performance comes from companies with superior growth, attractive relative valuations, competitive strength, and financial integrity. Our decisions are based on fundamental analysis, which emphasizes bottom-up stock selection by sector specialists. We invest in all major market sectors because we believe that investment opportunities are found in industries that are frequently overlooked.

# Sector Insights

## Focus: Consumer Discretionary

Consumer Discretionary sector specialists: Daniel M. Brewer, Stacie L. Cowell

**Q: How does Rainier use its sector experts to manage a diversified portfolio?**

A: Sector teams consist of two to four people, with each person acting as both analyst and portfolio manager. These are sub-groups within the greater nine person equity team, in which each portfolio manager serves on multiple teams. We maintain a research focus in every area of the market, with a view that growth opportunities exist in all sectors and that market leadership shifts over time. Our sector teams seek to capitalize on that phenomenon. Different nuances exist for companies in different sectors related to the keys to growth, sources of profitability, and appropriate valuation metrics. Our sector teams specialize in understanding the most important factors that will influence price movements of stocks in their areas.

**Q: What are the major industries within this sector?**

A: Consumer discretionary is one of the largest sectors in the market, and diversity within the sector is broad. This is particularly true in the small- and mid-cap world. The retail industry, which represents about of a quarter of the consumer discretionary sector, is the most broadly recognized industry in the group. It includes a wide range of companies, including those that sell clothing, electronics, home goods and groceries. Also represented are manufacturers of footwear and apparel. Other major industries include restaurants, media, lodging,

gaming, leisure, and consumer durables, which includes housing and autos. Online media and e-commerce companies are also included.

**Q: Is there anything unique about investing in the consumer discretionary sector compared to the other sectors of the market?**

A: This sector is different from others in that it sells into a market of individuals, each with his or her own distinct preferences and opinions. Whereas the typical consumer may have a difficult time articulating what differentiates a bank or a pharmaceutical company from its peers, consumers reflect their immediate opinions about restaurants, clothing stores, and the media. To complicate matters, preferences change. Stores and restaurants can be visited on a timely basis to get a read on current trends. Thus, data points are provided on a continuous basis in this area of the market. This data can be helpful, but also misleading, causing some investors to trade fairly aggressively around this short-term information, often without adding any value.

**Q: What do you focus on when analyzing stocks in the consumer discretionary sector?**

A: A commonality among all of the stocks we own in this area is that they are in some way going through a period of business outperformance, or we believe they are poised to outperform.

This often comes in the form of increased sales performance that we believe will be higher than expectations, and higher than others in the stock's respective industry. This sales growth often converts to better than expected earnings growth, providing a catalyst for the company's stock price to move higher.

It's possible that fundamental growth is often most prevalent in early stage companies that have new and innovative concepts. While still in the early stages, a company may be able to grow units at a double-digit rate, and for a period of time, sales rapidly increase. Although increasing the store base is a key driver for a growing company, analysts also focus on how the existing stores are performing. Tracking so-called "same store sales" is the way we gauge how a company is expanding its business with the store base they already have in place.

The drivers for growth are different for mature companies with an established multi-state base of hundreds or thousands of stores. They might be in a phase where they are accelerating top-line growth by flowing incremental products into their store base. Other companies may be emerging from a period in which they had not been managed as optimally as they should have been, and margins have been somewhat depressed. As they progress through a period in which margins recover to industry standards or better, bottom-line earnings growth typically accelerates more rapidly than peers. In this sector, as across the entire portfolio, we seek companies that grow faster than peers, and where growth will likely exceed investor expectations.

**Q: How does the sector typically react during economic cycles?**

A: The consumer discretionary sector is generally considered to be an early cycle group, in that its stock prices often show strength early in an economic recovery. Historically, stocks in this sector begin to move positively well before actual improvement is apparent. This held true in the most recent recovery, when stocks discounted the economic recovery well in advance of an actual earnings recovery. Leisure and retail shares are often the first to move upward, along with durables such as automobiles. Stocks in other groups, notably media companies, move more concurrent with an economic recovery. Companies in this industry are driven largely by advertising revenues, which usually track closer to GDP trends.

**Q: How did the sector perform during the recent economic crisis?**

A: As the crisis unfolded in 2008, consumer spending dropped precipitously. Up to that point the average consumer had been highly leveraged, and it quickly became apparent that the economy was going to go through a period of deleveraging. Employment and income were also plummeting, and the stocks within the sector reacted accordingly. There were comparisons to what performance had been during prior downturns, but this was a unique scenario because it was very much a consumer-led downturn, punctuated by a credit crisis.

Early in 2009, stocks inflected positively in anticipation of an economic recovery. In somewhat classic fashion, many of the companies that rallied first were those that had been under the most pressure in the downturn, some near bankruptcy. It was not the leaders of their respective industries that led the rally off the bottom, but companies whose margins were the most severely depressed. Since the market bottom in April 2009, consumer discretionary stocks have been one of the strongest performing groups in the market, along with technology and cyclical groups such as basic materials and producer durables.

**Q: What major themes do you see in this sector going forward?**

A: As is the case in other sectors, international growth is a consistent theme for companies in the consumer discretionary arena. "Consumerism" is growing globally, and those companies that are able to grow their store base in more than just one market have more significant growth opportunities available to them. Another important theme in this sector is the concept of reaching the consumer in more ways than the traditional method of just providing a physical store. Retail revolves around getting the product to the consumer right at the point they want to buy it, where and how they want to purchase it. These transactions increasingly occur online due to the expansion of e-commerce. Companies have invested heavily in building out their e-commerce capabilities. Having a multi-channel strategy is imperative to staying competitive, particularly for retail companies. Another trend is the gravitation toward "good goods," notably upscale or luxury products, as well as lifestyle and health and nutrition enhancing offerings.

*Next edition: Materials & Processing*

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Mutual fund investing involves risk. Principal loss is possible. Small- and mid-cap companies tend to have limited liquidity and greater price volatility than large-cap companies.

*Performance data quoted represents past performance, which does not guarantee future results. The 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 higher or lower than quoted. Performance data current to the most recent month-end may be obtained by calling 800.280.6111 or by visiting [www.rainierfunds.com](http://www.rainierfunds.com).*

For performance as of the most recent quarter end, click on the strategy name:

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