JANUS

Time to Invest in Change

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What to Tell Your Clients:

Change-factor investing provides opportunities.

- After significant multiple expansion over the last two years, a catalyst to lift all stocks broadly is unlikely.
- The best remaining opportunities for equity investors may lie with companies enacting positive, material changes to their business.
- Companies undergoing dramatic change can see significant stock price appreciation as market sentiment toward the company turns positive.
- After five years of slow economic growth, we are seeing more shareholder-friendly boards forced to make the types of changes that can spark a change in market sentiment.

After significant multiple expansion over the last two years, some of the best remaining opportunities for equity investors may lie with stocks that are due for a change in market sentiment as the company enacts dramatic changes to its business. Dan Kozlowski, Portfolio Manager of the Janus Contrarian Fund, explains how a slow-growth economic environment has forced more companies to make the types of changes that can reshape their long-term destinies, and outlines where he is seeing some of the most promising change opportunities emerge.

Companies making big changes offer attractive opportunities in today's market

When the going gets tough, the tough get going. We believe the old adage is true for a number of companies in today's slow-growth economic environment, and will be important for investors seeking to maximize equity return potential going forward.

Slow economic growth over the last five years has put pressure on many corporate boards to get creative and affect real, often dramatic, changes to grow their per share profitability. We believe the companies making those sweeping changes will provide some of the best investment opportunities in the current market environment.

Easy monetary policies and a stabilizing (albeit slow-growing) economy have provided a supportive backdrop for stocks, and equities have enjoyed a strong run since the beginning of 2013. Now that multiples have broadly expanded, it is hard to envision a catalyst that will dramatically lift all stocks.

Instead, we believe the push driving further stock-price appreciation must come from within. The remaining opportunity set in equities is limited to those companies that grow earnings to justify their current multiples, or companies that experience a shift in market sentiment caused by the company rewriting its long-term destiny.

The good news, at least for contrarian investors who seek stocks that are due for a change in market sentiment, is that a greater number of companies have been encouraged to make the sweeping changes required to reshape a business, and the sentiment around it.

Without the tailwind of a roaring economy, boards have taken a harder look at their businesses. We've seen an increase in the number of companies divesting noncore assets, changing management teams or making acquisitions that consolidate the industry in which the company operates. We expect these companies to provide outsized returns in an environment where stocks are more fairly valued and there is little impetus for a broader market push.

A slow-growth economy has forced more companies to enact big changes

One of the most prominent examples of how bad economics can force positive, material change is in the airline industry. Airline companies have been a major theme in our portfolio because we think consolidation in the industry will be a long-term game changer for these companies.

Continued on next page

About the Manager:

Dan Kozlowski, CFA, joined Janus in 1999 and has been managing the Janus Contrarian Fund since 2011.

Janus Contrarian Fund: Portfolio Snapshot

- **Avoid Consensus:** We believe non-consensus ideas that are underfollowed, underappreciated, and undervalued provide asymmetric risk/reward profiles.
- **An Opportunistic Portfolio:** By concentrating on companies undergoing change, we anticipate that the catalysts for stock price appreciation are already in motion and provide potential growth drivers for the Fund.
- **Change Presents Opportunities:** A contrarian investor must have the discipline to not only invest in non-consensus ideas but also to sell those same ideas once they reach consensus.

Rising fuel costs, destructive price wars and a weak economy that dampened flight demand grounded major airlines for years. But these headwinds were an impetus for economic rationality among the major airlines. Since 2008, we've seen several large airline mergers consolidate the industry. As of 2014, the four largest airlines operate 85% of all domestic flights, compared to 58% in 2003.

Consolidation has reduced industry-wide capacity. With less capacity, major airlines have pricing power for the first time in decades. As dynamics for the industry have changed, stock prices for major airlines have risen considerably. Since the beginning of 2012, the NYSE Arca Airline Index is up roughly 220%, compared to a 79% return for the S&P 500 Index.

We see positive change in the specialty pharmaceutical industry, and through European restructuring

The weak economy has played a hand in forcing positive change within many other companies and industries. The European Crisis forced restructuring and union concessions at many large companies, making them more profitable and competitive. In the U.S., shareholder activism in the industrials sector is high, and new management teams are improving the fundamentals for many companies.

Though less tied to the general economy, we're seeing big changes among specialty pharmaceutical companies as well, where merger and acquisition activity is consolidating the industry and new, financially-minded CEOs are taking out costs and making research and development spending less risky for their companies.

In a world where a slow economy forces companies to create their own avenues for growth, we expect to see more shareholder-friendly boards make major changes to their businesses to remain competitive. And in a market environment where valuations for most stocks have already risen considerably, we would expect these companies to be top performers.

Please consider the charges, risks, expenses and investment objectives carefully before investing. For a prospectus or, if available, a summary prospectus containing this and other information, please call Janus at 877.33JANUS (52687) or download the file from janus.com/info. Read it carefully before you invest or send money.

Investing involves risk, including the possible loss of principal and fluctuation of value.

Past performance is no guarantee of future results.

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There is no assurance that the investment process will consistently lead to successful investing.

The transportation industry can be significantly affected by changes in the economy, fuel prices, labor relations, insurance costs and government regulation.

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NYSE Arca Airline Index measures the performance of highly capitalized companies in the global airline industry.

S&P 500® Index is a commonly recognized, market capitalization weighted index of 500 widely held equity securities, designed to measure broad U.S. equity performance.

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