American Express CEO Must Fix Funds, Investors Say

New York, Oct. 28 (Bloomberg) -- American Express Co.'s Kenneth Chenault says his sons used to tell strangers to switch to the company's credit cards. Now, the 10- and 12-year-old boys ask people if they have a financial plan, he says.

Chenault, 51, needs all the help he can get attracting customers to American Express Financial Advisors. The 11,000-broker network has generated 16 percent of net income since January 2001, less than half its annual contribution the previous five years. The unit's share of the U.S mutual fund market has fallen to 11th this year from seventh in 1998, according to Financial Research Corp.

The chief executive appointed Jim Cracchiolo, who cut $1 billion in costs from American Express's credit-card and travel operation in a former job, to overhaul the Minneapolis business. Cracchiolo has hired portfolio managers from Fidelity Investments, started 14 new funds, and tapped outside firms such as Gabelli Asset Management Inc. to try to lift below-average returns.

``We haven't seen evidence of the turnaround there yet,'' said R. Lynn Yturri, who helps manage $149 billion in assets, including American Express shares, at Banc One Investment Advisors in Scottsdale, Arizona. ``They've been coming up short.''

Chenault needs to bolster financial planning profits as corporate-card and travel clients pare spending and the economy shows scant signs of picking up, some investors say. American Express stock is down 34 percent since he took over in January 2001, damaged in part by the Sept. 11 terrorist attacks that curtailed air travel and forced 3,000 employees from the company's headquarters for nine months.

American Express said third-quarter profit was $687 million, or 52 cents a share, beating the 51-cent average estimate of analysts polled by Thomson First Call. Net income was more than double the same quarter last year as credit-card customers spent more.

Sales in the financial planning operation rose 22 percent to $14 billion as sales of annuities more than doubled to $2.66 billion. Still, the unit's track record, including a $1 billion write-off for the company's own investments in junk bonds last year, hurts efforts to add new money to the $191.6 billion in assets managed for 2.5 million clients, some investors say.

The average return for the 18 American Express stock funds with three-year track records lags 55 percent of all equity funds, according to Bloomberg data. Bond investments fared worse -- with the average return for 15 bond funds lagging 88 percent of peers.

Chenault said the division, which also sells insurance and retirement planning, needs time to reverse course.

``The key thing is investment performance,'' he said in an interview. ``We need to demonstrate that year in and year out.'' He's put his trust in Cracchiolo, a 44-year-old Brooklyn native who most recently more than doubled American Express loans outside the U.S. as president of the international card and travel unit from 1998 to 2000.

Cracchiolo spends at least a day a week in New York and keeps an office in the World Financial Center, a change from predecessor David Hubers. The executive brings ``a sense of urgency'' to his task, said Chenault, who highlights his own priorities to groups of employees with the story about his sons.

Under Hubers, a Minnesotan who ran American Express Financial Advisors for seven years before retiring in 2000, the division posted annual earnings growth of at least 10 percent as the Standard & Poor's 500 Index averaged an annual 16 percent return.

``In the 1990s, we had strong momentum supported by the tailwinds of the economic markets,'' said Brian Heath, the executive who oversees the financial advisers. ``That may have created a bit of complacency when we got hit by more difficult markets.''

To win more support from advisers who work for American Express as franchisees and have had the option since 1999 to sell thousands of rival funds, Cracchiolo is replacing money managers and starting funds focused on value stocks and small-cap growth companies.

Zurich Scudder Investments' Ted Truscott joined as chief investment officer last year. Nick Thakore, Robert Ewing, and Doug Chase left Fidelity in February to oversee $12 billion in equity assets and a $25 million hedge fund from American Express's first Boston office.

At Fidelity, the biggest U.S. mutual fund company, the worst-performing of those managers' funds beat 71 percent of competitors in the 12 months through February, according to Bloomberg data.

``When the markets do return, they're in a far better position to show better performance,'' said David Katz, chief investment officer at Matrix Asset Advisors Inc., which manages $750 million, including more than 325,000 American Express shares.

Cracchiolo is also trying to attract the cash of investors reluctant to put money in stocks or bonds. Customers who keep at least $25,000 in his new integrated investment and bank account get a break on fees. Choices for depositors now include a high-yield savings account and more than one money market option.

He's also encouraging more American Express cardholders to invest with the company. Some advisers now spend weekends talking to shoppers in the stores of Costco Wholesale Corp., a credit-card partner.

Still, it's going to take more than ``Be Confident'' hats and pens to get many to recommend American Express funds to their clients, some advisers said.

``I can't bet my practice on it,'' said Charlie Hamowy, a New York-based American Express adviser who estimates he put about 1 percent of new client money into American Express products in the last year.

Advisers such as Hamowy say they might feel differently if early signs of progress hold. The average American Express stock fund rose 2.6 percent in the last three months, beating the 2.2 percent increase for the average equity fund, according to Bloomberg data.

``We've made some aggressive changes here," Cracchiolo said in an interview. ``If the Financial Advisors unit does not return, then we'll have to make some different decisions."

--Helen Stock in the New York newsroom, or at (212) 318-2315, or at hstock@bloomberg.net. Editors: Kassenaar, *Serafino, Kassenaar, *Dickson.

Story illustration: For selected functions related to the company's earnings and stock performance, click on {AXP US <Equity> CNP10320720102 <GO>}. To see the average return for American Express funds, type {FPC <GO>}, click on 98 and change the fund family to AXP.