

FRIC US Equity Fund Manager Change

We have enhanced the manager mix of the FRIC US Equity Fund by replacing BGI with John A Levin & Co (Levin) and Systematic Financial Management (Systematic). We have also changed Jacobs Levy Equity Management's (Jacobs Levy's) mandate.

As described in more detail later in this Take Note, these changes can be summarised as below:

- Departing manager, BGI, is an active, quantitative core value manager.
- Levin is a market-oriented manager with a value bias.
- Systematic is a value manager with a modest growth bias.
- We have switched incumbent manager, Jacobs Levy's, mandate from market-oriented to value. This maintains an appropriate exposure to value factors at the total fund level.

Both Levin and Systematic have investment processes that are more aggressive than BGI's and we believe their addition will increase the fund's future performance. The number of stocks in the fund will fall by approximately 20%. While this increases the level of risk in the fund, US equity market volatility has fallen significantly over the last five years. This climate has given us the opportunity to include more aggressive managers in the fund while keeping within the fund's forecast tracking error range. One of the advantages of multi-manager is that, even in a lower-volatility environment, we can find dynamic investment processes that will benefit fund performance.

Who is John A Levin & Co?

John A Levin & Co (Levin) is a boutique US equity manager. It runs approximately \$9 billion in US equities and \$7 billion in this market-oriented product. Levin also has around \$4 billion in hedge fund strategies.

Levin prefers large, stable companies. It analyses cashflow to find stocks trading at a discount to their market value - giving it a value bias. Levin's investment process is built on fundamental, qualitative research: careful company assessment, a full examination of financials and in-depth direct discussions with both company management and customers. Levin keeps this research process dynamic; the research team only comprises ten people but they have a wealth of experience - an average of 14 years. This experience is a key benefit and the foundation of Levin's qualitatively-oriented process. It brings ideas to the portfolio that are likely to be different to those of Jacobs Levy and Systematic.

Levin is also strongly aware of downside risk and has a strict sell-discipline. It does not like deep value stocks that carry significant risk of bankruptcy (the 'value trap'). Any adverse development in actual or perceived fundamentals, or falls in the price of a stock at any time after purchase triggers a re-examination of the stock with a view to selling it.

However, Levin does have an aggressive investment process. Firstly, it runs a more concentrated, higher conviction portfolio than the other value managers in the fund, typically holding around 55-70 stocks. Secondly, it likes to take contrarian views to the rest of the market - preferring companies that other managers may not hold. Levin also uses ideas generated by its hedge fund business, which provides another input into its investment process.

Who is Systematic?

We know Systematic very well, having a longstanding relationship with this manager in some of our other funds. Systematic has a bottom-up process that screens the market using traditional value indicators, such as low price/earnings, price/book and price/sales ratios, as well as a range of other value indicators. However, in our view, one of the most compelling elements of Systematic's process is that the manager combines this low valuation approach with a focus on positive earnings surprises as a signal of fundamental company improvement - a strategy normally employed by growth managers. In itself, this is not unusual; the other value managers in the fund also look at earnings. However, Systematic places more emphasis on this than other value managers. Therefore, Systematic could also perform well in growth environments where markets reward earnings momentum.

Modifying Jacobs Levy's mandate

Coincident with this change in managers, we have changed quant manager, Jacobs Levy's mandate from market-oriented to value. As Levin and Systematic have growth elements to their processes, this change in Jacobs Levy's mandate will help the fund maintain an adequate exposure to stocks that will perform well in a strong value market.

Jacobs Levy's process covers a larger number of stocks than our other value managers. Its process is highly sophisticated; 70 different models incorporating a huge level of detail. It also has a greater focus on investor behaviour than the other managers in the fund, quantifying investor risk tolerance, herd behaviour patterns and overreaction to corporate announcements. Jacobs Levy runs the most complex process in the fund and has a broader investable universe - therefore it finds opportunities across the entire market.

Summary

In summary, Levin relies on high quality company research and has a market-oriented process with a bias to value. It also runs a more concentrated, higher conviction portfolio, giving it a more varied return pattern. Jacobs Levy has the most complex process and greater market coverage. Systematic focuses its research effort on specific areas, but is talented at spotting earnings surprises - something that can help its performance in both value and growth environments.

Manager weights

Manager	Previous Fund Weight	New Fund Weight
Montag & Caldwell	13%	12%
Ark	10%	13%
Turner	16%	18%
Suffolk	12%	12%
MFS	16%	12%
Jacobs Levy	11%	13%
BGI	22%	0%
John Levin	0%	13%
Systematic	0%	7%