

Take Note

UK EQUITY FUND (RIC) – MANAGER CHANGES

We have enhanced the manager line-up by removing Fidelity and Threadneedle and hiring Morley Fund Management and RCM Capital Management into the Fund.

Changes to the Fund

Fidelity's and Threadneedle's weights have been redistributed across the newly hired managers (RCM 15%; Morley 10%) and existing managers (Standard Life's weight goes up from 15% to 20%; the RIC II UK Equity Plus allocation goes from 3% to 5%).

Reasons for the changes

Our manager research process has concluded that organisational changes to the UK equity teams at both Fidelity and Threadneedle introduce greater uncertainty in the future performance of each manager's UK equity product held within the Fund. In the meantime, we have higher confidence in the UK equity products of Morley and RCM which we are already using in some of Russell's other UK equity funds.

The growth of the UK Equity Fund has allowed us to increase the allocation to the RIC II UK Equity Plus Fund to 5% as originally indicated when we first made an allocation to it in May 2006.

Morley Fund Management

Morley Fund Management is the UK-based asset management business of Aviva plc, one of the world's largest financial services groups, with over £162bn of assets managed worldwide and £34bn in UK equity strategies as at 30 September 2006.

Morley's process is driven by a bottom-up stock picking approach to identify long-term growth opportunities. Fund manager David Lis is a pragmatic investor and extends his stock selection process beyond the FTSE All Share, taking into consideration opportunities in the Alternative Investment Market (AIM) and Fledgling markets. Consequently, portfolios tend to have a growth and small/mid cap bias.

Stock selection is the primary driver of added value for this manager. In the first instance, Lis seeks to identify companies with a long-term record of consistent, above-average profitability or earnings growth. However, he is not an out-and-out growth investor and therefore uses a variety of additional criteria to select stocks including: emerging growth – young or blue-sky companies with the prospect of dynamic growth; value – undervalued stocks across the whole of the market; special situations – recovery stories; 'Best of Breed' - the best companies in their sector with a sustainable competitive advantage; and top-down – holdings influenced by macroeconomic views on the market. Additionally, for a manager with a growth bias he also possesses a keen appreciation of valuation.

Morley's modular approach to fund management, which encompasses a focus on growth, value, special situations, smaller companies and income, means that Lis is able to construct portfolios using the expertise of Morley's analysts and portfolio managers to create an aggressive 'best ideas' portfolio. This will consist of between 25 and 40 stocks. With over 30 years' experience in the industry, Lis has developed his own growth oriented but pragmatic approach to investing, and our favourable view of this product is primarily based on his ability to maximise the potential of the team and act as the final decision maker.

RCM Capital Management

RCM Capital Management LLC was founded as Rosenberg Capital Management in 1970. It is now an independent subsidiary of Allianz Global Investors.

RCM's UK High Alpha equity product is a concentrated strategy with a co-management structure. Large cap is managed by Mark Lovett, who has 17 years' investment experience, while the mid cap component is run by Trevor Green (13 years' investment experience). The product's key strength is the insight of these two experienced investors.

A broad range of market perspectives are considered within a decision-making process that is seeking to uncover mis-valued growth stocks. Lovett and Green are comfortable building portfolios concentrated in such stocks and use detailed bottom-up, fundamental analysis to build conviction. Their valuation methodology uses a hybrid approach that incorporates earnings multiples, price to cashflow and enterprise value among other measures. The firm's extensive research resource supports this effort.

Whilst RCM's product will experience high benchmark-relative volatility, we are comfortable that the risk measurement by the manager is fully embedded into the portfolio construction process and the sell discipline is implemented robustly.

Impact on the Fund

The Fund's characteristics are not expected to change significantly, although there will be a small reduction in the number of holdings. We are also enhancing the return potential of the Fund. While both managers have approaches which result in more growth-oriented portfolios, RCM maintains a quality growth bias of predominantly large cap stocks driven by a bottom-up process, while Morley's pragmatic approach will lead to a focus on the smaller end of the universe and will be driven at times by top-down perspectives.

Changes to manager weights in the UK Equity Fund (RIC)

Manager	Mandate	Previous Fund Weight (%)	New Fund Weight (%)
Fidelity	Contrarian/Growth Bias	10	-
GMO	Active Quantitative	15	15
Majedie	Adaptive Stock Picker	15	15
Threadneedle	Macro-driven Aggressive	22	-
Bernstein	Focus on valuation Fundamental research	15	15
Standard Life	Quantitative screen Fundamental research	15	20
Select Holdings	"Best Ideas"	5	5
RIC II UK Equity Plus	High Alpha Fund	3	5
Morley	Pragmatic Stock Picker	-	10
RCM	Quality Growth	-	15

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