

# Diversified Target Return Fund

November 2011

**L**ooking to profit from the outperformance of consistently strong active equity managers who are able to outperform in a broad variety of market environments.

## It all starts with selection...

For us, fund manager selection is key. The best way for us to access opportunities are via specialist teams that are dedicated to one particular activity. The input from these specialist teams helps us identify the best opportunities from a broad range of asset classes. At present, the manager selection component accounts for 70% of the Diversified Target Return Fund's portfolio. This is spread across traditional asset classes, such as equities and bonds, but also some non-traditional areas such as infrastructure, aviation and mezzanine finance.

## ...but market movements can cause falls in even the best strategies.

As we have seen this summer, diversification and manager selection alone are not enough to protect a portfolio as broad directional moves in the markets are the key driver of return. Looking at equities for example, only ten funds in the IMA UK All Companies Sector have delivered positive returns so far this year<sup>1</sup>, despite the fact that almost all the managers we met have justifiably told us they had picked strong, well-positioned and well-financed businesses, all of which were apparently well prepared to weather the ongoing market volatility.

<sup>1</sup>Source: Trustnet. As of 19 October 2011 based on net returns with income reinvested.

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## So it's all about consistency...

The key issue is to find managers who offer consistency of return across both time and different market conditions. However, our research shows that many managers swing from top to bottom in the rankings depending on what the market is focusing on. This means their performance is a result of their investment style, rather than active management.

## ...which can be identified and then isolated using market hedges.

By focusing on managers who we consider to be able to provide consistent returns in different market conditions, we reduce the need to make a call on the type of market we are in. The selection of managers is really only the starting point of our investment process. Once we identify an investment where we expect to see consistent outperformance, we will take a long position in the fund and a corresponding short position in the underlying index. This results in a position which has the capacity to deliver positive returns regardless of underlying market direction.

## Accessing outperformance without the market risk

While we do believe that manager selection is important, it is crucial to

remember that it does not provide an insight into market direction. As such our approach in the Diversified Target Return Fund differs from our competitors in the way that we access top-performing managers – its our job to provide exposure to these opportunities without being reliant on the market going up to generate consistent returns.

Please note the value of investments and any income will fluctuate and is not guaranteed (this may be partly due to exchange rate fluctuations). Investors may not get back the full amount invested.



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