

THE RATHBONE  
INVESTMENT  
MANAGEMENT PROCESS





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HERITAGE, STABILITY,  
STEWARDSHIP & TRUST.





## ABOUT RATHBONES

Rathbone Investment Management is one of the UK's largest and longest established providers of high-quality discretionary investment management services to individuals, families and their advisers, as well as trustees and charities.

We are part of Rathbone Brothers Plc, an independently-owned FTSE 250 company.

As a client of Rathbones you can expect to benefit from:

- A direct relationship with the person managing your investments. This means your requirements are properly understood and reflected in the construction and management of your portfolio, by someone who has responsibility for all investment decisions on an ongoing basis.
- The skills and experience of your investment manager which are supported by substantial research, insight and ideas generated through the Rathbone investment process.
- Independent ownership and thinking, meaning your investment manager is free to select the most appropriate investment opportunities from across the market, covering the full spectrum of asset classes, to meet your specific needs.
- Efficient administration systems and technology which are essential to ensure the smooth running of your portfolio and give you total peace of mind.

## INTRODUCTION

As a client of Rathbones you can expect a truly bespoke personal service, backed by a well-researched investment process, designed to deliver appropriate risk adjusted returns.

Your investment manager takes time to understand your specific requirements, constructing a bespoke portfolio to reflect your preferences. On an ongoing basis, you will receive regular updates and have direct access to your investment manager during business hours. This means we are able to respond to any changes in your requirements, as well as changes in market conditions, in an effective way.

Our investment process is fundamental to the service we provide, guiding the thinking of our investment managers yet allowing enough flexibility to ensure that your individual needs are met. It is constantly evolving and we continue to invest in the people and resources required to ensure it remains robust, flexible and capable of meeting a variety of needs.

As alternative asset classes and investment products such as hedge funds and structured products have become more accessible and available to individual investors, we have invested significant resource to ensure we can incorporate this growing range of options effectively.

Investment professionals from across our business participate in the investment process. The outputs of this process are derived from our combined expertise and experience, and help to ensure that the investments selected are suitable for our clients. Our internal performance monitoring and risk control processes ensure that the quality of service and fulfilment of client objectives can be achieved.

Our service to you is underpinned by our investment process. This document explains:

- how the investment process works;
- our internal structure that supports the investment process;
- the range of inputs to the investment process; and
- how our investment managers apply the outputs to construct and manage portfolios.

Our investment process also supports fund managers in managing a range of Rathbones multi-asset unit trusts which are available for investors with £1,000 or more to invest.

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## OUR INVESTMENT PHILOSOPHY

Central to our investment philosophy is our belief that deciding on a basic structure or asset allocation provides a vital framework and guidance when managing funds for our clients. This structure will vary according to each client's individual requirements and will alter over time as economic conditions and prospects for asset classes change, altering their correlations to each other. The investment/risk profile of each individual's requirements is regularly assessed to ensure the portfolio is matched to the client's needs.

We believe in pragmatism, using a variety of funds with varying investment styles and philosophies that we believe are suitable to the market environment prevailing at the time of investment. It is essential to consider the liquidity of all of our holdings in a variety of market conditions and how sensitive our investment choices might be to market movements, whether they are individual equities, bonds or collective funds.

These considerations reflect the importance of managing risk. This is also a major consideration in the use of alternative investments sourced to complement and offset the risks and return profiles of other more traditional investments.

We believe that it is crucial to source investments on an open market basis using our in-house research teams. Importantly this means that in-house funds and individual holdings are only ever selected on merit.



# HOW THE INVESTMENT PROCESS IS STRUCTURED

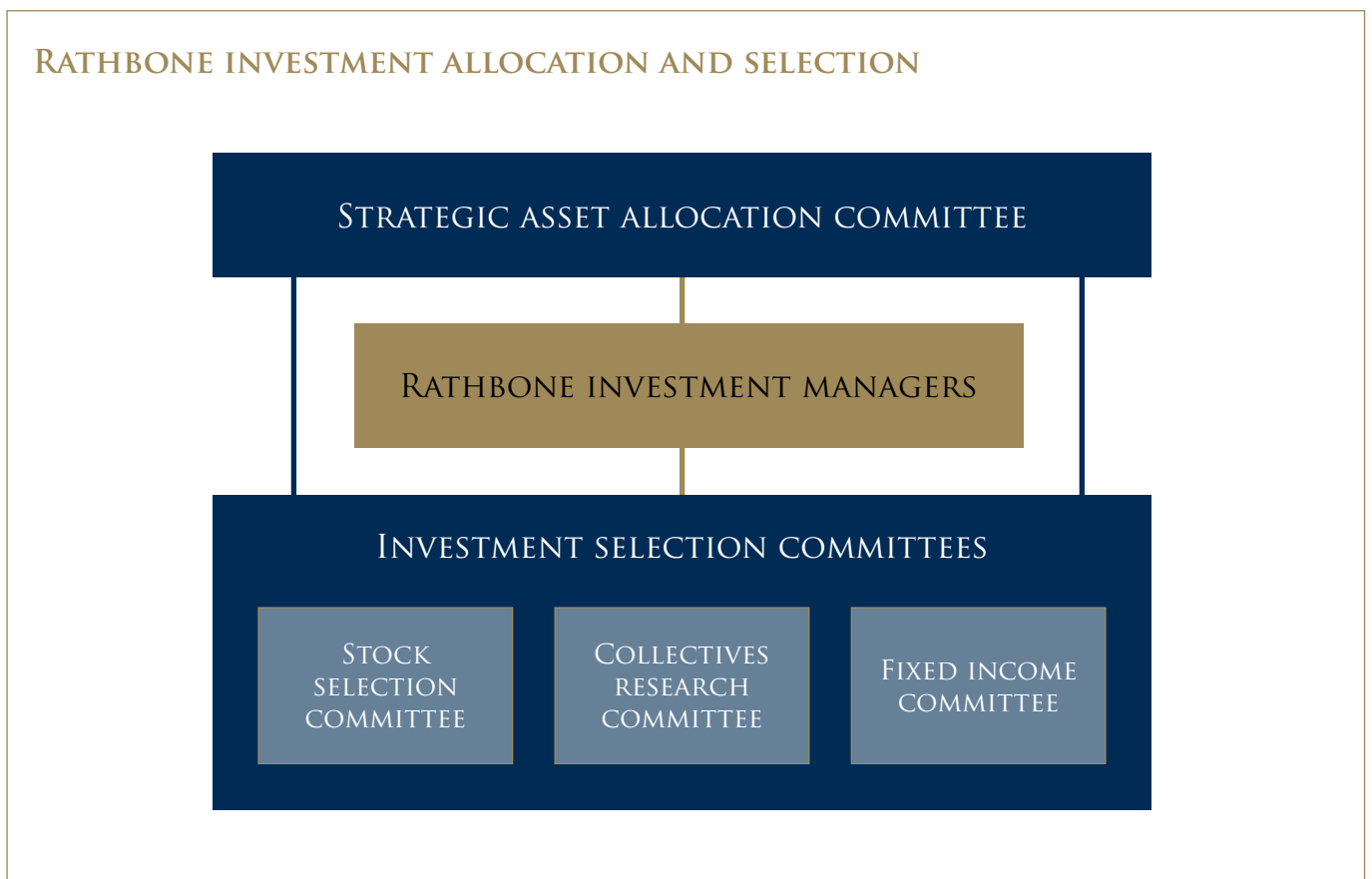
There are two parts to our investment process:

- asset allocation; and
- investment selection.

Asset allocation is the process of deciding which asset classes and strategies to include in a portfolio and the proportions to be allocated to each area. Asset classes that can be incorporated into our process include cash and fixed interest, equities, property and commodities. We also consider alternative strategies such as hedge funds, private equity and structured products.

Investment selection refers to the specific investments that are used to make up a portfolio. These may include direct equities and fixed income or collective funds.

Our investment managers are free to make the final asset allocation decisions as well as investment selection for individual clients. However, they are supported by the work of four investment committees: the strategic asset allocation committee, the stock selection committee, the fixed income committee and the collectives research committee. The work of these committees supports our investment professionals in forming an opinion about the state of the world economy and the investment opportunities available. The committees provide input and help in decision making, and output that is practical and relevant for your particular needs.



## ASSET ALLOCATION

A portfolio structure does not change substantially unless your needs change, the mandate previously agreed changes or, alternatively, if our fundamental long-term view on asset classes has altered. We make tactical changes to portfolios to reflect over – or under-valuations of the various asset classes. The initial stage of the asset allocation process involves formulating a view on the outlook for the various asset classes.

These views incorporate macroeconomic issues such as:

- the geopolitical background;
- economic growth expectations;
- central bank policy;
- interest rates;
- inflation; and
- liquidity.

These factors are analysed in tandem with asset class specific information such as risk premiums, volatility, credit spreads, earnings growth, cash flow, dividend growth and valuations.

## RATHBONE ASSET ALLOCATION PROCESS



This process is driven by Rathbones' strategic asset allocation committee, the membership of which is drawn widely from across Rathbones, incorporating a range of investment professionals with distinct skills and expertise in key areas. The committee's work is well resourced and is supported by our own in-house research team, with intelligence drawn from external strategists and economists. The committee meets monthly with major meetings held quarterly.

## STRATEGIC ASSET ALLOCATION COMMITTEE STRUCTURE

### STRATEGIC ASSET ALLOCATION COMMITTEE



#### CHAIRMAN

**Hugh Adlington**  
Investment director



#### UK EQUITIES

**Julian Chillingworth**  
Chief investment officer

Macro summaries and analysis; model performance; key statistics, data and charts



#### REGIONAL REPRESENTATIVE

**Julian Rathbone**  
Investment director



#### MACRO

**David Coombs**  
Investment director



#### ANALYST

**Rashpal Sohan**  
Asset allocation analyst



#### FIXED INCOME

**Bryn Jones**  
Fixed income fund manager



#### INTERNATIONAL EQUITIES

**Clive Hexton**  
Investment director



#### ANALYST

**Elizabeth Savage**  
Research director



#### PROPERTY

**Chris Sutton**  
Investment director



#### ALTERNATIVE ASSETS

+ input from practitioners  
**Rupert Heggs**  
Investment director



#### ANALYST

**Mona Shah**  
Research analyst

## OUTPUTS

### INVESTMENT MANAGEMENT REPRESENTATIVES (rotational)



**Richard Lanyon**  
Head of investment management



**Ivo Clifton**  
Head of charities



**Jonathan Giles**  
Managing director  
Rathbone Investment Management International



**Andrew Hess**  
Investment director



**Malise Reid-Scott**  
Investment director



**Nicola Day**  
Investment director



**Jane Sydenham**  
Investment director

## KEY INPUTS AND OUTPUTS INCLUDE:

### Inputs

- External views and opinions from investment strategists, policy-makers, surveys and economists form the foundation of the debate.
- We use economic research from the following strategists: Bank Credit Analyst, Macro Research Board, Wolfe Trahan and Capital Economics. Each group utilises distinct methodologies to arrive at their conclusions which prevents confirmatory bias. More detail on the providers of economic research is provided in appendix one.

- Executive members of the committee are responsible for specific investment areas. They submit a summary of views ahead of the meeting highlighting the risks and opportunities.
- Our in-house asset allocation analyst collates a data book of information including model performance data, macro data, statistics and information.

### Outputs

- Changes are implemented to Rathbones' asset allocation models.
- Detailed minutes are produced.
- Changes are communicated directly to Rathbone investment managers via email and the weekly investment meeting.

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## ASSET ALLOCATION MODELS

The strategic asset allocation committee manages six models to assist your investment manager in constructing a suitable portfolio in-line with your requirements. These models act as a guide and reference point for a variety of bespoke client mandates. Your investment manager is not compelled to fit your portfolio to a model and we believe that every client will ultimately need an individual combination of assets suitable for their circumstances.

The models aim to produce an effective risk-adjusted combination of assets. We produce models to cover both relative and risk controlled strategies. Your investment manager will discuss their differences and agree a suitable approach in-line with your preferences.

### RELATIVE RETURN

There are three traditional models designed to meet the broad requirements of growth, income or a balanced portfolio, which is a blend of the growth and income models. They relate to, but are not identical to, industry standard indices constructed by the Association of Private Client Investment Managers and Stockbrokers (APCIMS).

- The growth model is a fairly aggressive model where the weightings are increased and decreased more actively than the other two models. This is the most equity-biased model and has the biggest allocation to developing markets.
- The balanced model is more evenly divided between income and growth-oriented investments. It has exposure to a broad range of asset classes but has smaller allocations to alternative assets when compared to the strategic growth and total return models.
- The income model, as the name suggests, is primarily designed to generate more regular cash flows than the growth and balanced models and usually has a greater bias towards fixed interest holdings.

### RISK CONTROLLED STRATEGIES

In addition, three further models have been produced with the aim of moving beyond the more traditional approach taken by the APCIMS models which are dominated by equities (although APCIMS has in recent years introduced property and hedge funds and reduced equity exposure to a limited extent).

More traditional models focus on the nature of return and whether that return is derived from growth or income. An additional dimension is revealed if we also look more closely at risk and the correlation between different asset classes in helping to achieve diversification.

An expanding pool of alternative assets suitable for private clients has, in recent years, enabled a more diversified approach to constructing portfolios than in the past.

The enhanced growth model aims to generate capital growth over the medium to long term. The investment objective for this model is to add 2% above a benchmark comprising 70% MSCI world equity index/30% MSCI emerging markets index. This model reflects the importance of emerging markets and our views of their share in global growth in the next decade. This model incorporates a greater emphasis on equities and retains a multi-asset approach, making use of fixed income and alternative investments to control risk.

The strategic growth model aims to generate attractive returns relative to equity markets with lower volatility over the medium-term. The benchmark for this model is CPI (Consumer Price Index) plus 5%. This model incorporates a wider range of asset classes and introduces a greater exposure to structures and securities that are less correlated to each other.

The total return model is more risk-averse and provides tax efficient total returns without experiencing significant downside volatility. The benchmark for this model is LIBOR (London inter bank offer rate) plus 2%.

## INVESTMENT SELECTION

Once the asset allocation is decided, your investment manager needs to select specific investments with which to populate your portfolio. Recommended lists are produced by the three investment selection committees to assist investment managers in this task.

Our whole-of-market approach allows us to select the best investments available in each asset class across all markets without any conflicts of interest. The investment selection process is tailored to the particular characteristics of each asset class. We look at:

- Fixed interest stocks and bonds.
- Equities.
- Collective funds (open and closed ended, onshore and offshore).
- Hedge funds.
- Structured products.
- Private equity.
- Property.
- Commodities.
- Cash.

Definitions for all of these asset classes are provided in the glossary.

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## EQUITY SELECTION PROCESS

Our process places great emphasis on internally-generated ideas. These arise through meetings with companies and sector analysts, the expertise of the managers of our unit trust range, and the considerable experience of our private client investment managers. These ideas are drawn together through our stock selection committee. This comprises 15 individuals representing a broad range of investment styles and levels of experience, drawn from London, Liverpool and other regional offices.



## STOCK SELECTION COMMITTEE



### CHAIRMAN

**Julian Chillingworth**  
Chief investment  
officer



**Clive Hexton**  
Investment director



**Gary Street**  
Investment director



**James Douglas  
Withers**  
Investment manager



**David Hough**  
Investment director



**Alex Turnbull**  
Investment director



**Tim Eliot-Cohen**  
Investment director



**Richard Lanyon**  
Head of investment  
management



**George Viney**  
Investment analyst



**Helen Gerrard**  
Investment director



**Adrian Maxwell**  
Investment manager



**Charles Wilcox**  
Investment director



**Simon  
Heathcote-Amory**  
Investment manager



**Andrew Sanders**  
Investment director



**Tim Woodhead**  
Investment director

The committee generates three recommended lists for Income, Growth and Balanced models as well as a watch list. The watch list comprises a number of favoured stock ideas but with valuations above our view of fair value. For a stock to

be added to a list it needs a proposer and then a simple majority of votes amongst the committee members. The Chief Investment Officer has a casting vote in the case of a tie. The key criteria we look for in companies are detailed below:

<b>Themes</b>	External influences which may favourably affect a particular company or sector.
<b>Management</b>	A focus by management on delivering shareholder value.
<b>Growth</b>	Strong market position, with products that are market leaders, with visible and sustainable growth in earnings, cash flow and dividends. The ability to improve and maintain margins is a crucial part of this analysis.
<b>Financials</b>	We pay particular attention to the balance sheet and associated cash flow analysis including an understanding of operational and financial gearing for each company.
<b>Catalyst</b>	This can include company restructurings, new management, new products, acquisitions, disposals, changes in legislation, cyclical and interest rate and exchange rate sensitivities.
<b>Value</b>	Value plays an important part in our selection process. Measures include P/E, yield, dividend cover and dividend growth, price to cash flow, EV/EBITDA and price to book value.

The committee meets bimonthly and ideas are communicated through email, our weekly investment meeting and regular updates of our recommended lists.

The committee is attempting to generate long-term ideas rather than short-term trading positions, as we feel this is more appropriate to our investment style. This is particularly important if you have capital gains restrictions or when considering the overall cost or managing your portfolio to match your risk appetite.

## RESEARCH

We aim to cover the largest 150 UK companies internally, and more detailed research is carried out on specific situations outside of this primary universe. This includes regular meetings between our in-house research team and company management.

In addition, we utilise third-party research from brokers and sell-side analysts. The forecasts produced by analysts are useful in so far as they provide a starting point for our own house view.

As mentioned above, third-party research is also received and this flow of information is assisted by Rathbones' independent status (ie not being part of a large bank with a corporate broking arm). Sources include:

External research sources for equity and fixed income		
ABN AMRO	HSBC	Panmure Gordon
Barclays Capital	Investec	RBS
Citigroup	JP Morgan Cazenove	Redburn Partners
Collins Stewart	Liberum Capital	Sanford Bernstein
Credit Suisse	Mirabaud Securities	Share Capital
Deutsche Bank	Morgan Stanley	Société Générale
Evolution	Nomura	South China Research
Fox-Pitt Kelton	Numis	UBS Warburg

# FIXED INCOME SELECTION PROCESS

The fixed income committee is responsible for providing core recommended lists in Sterling, US Dollars and Euros. In addition, given the nature of bond markets, and that some

instruments are not traded on recognised exchanges, the committee monitors dealing, execution, valuation, pricing and general market trading conditions.

## FIXED INCOME COMMITTEE



**CHAIRMAN**  
**Bryn Jones**  
Fixed income fund manager



**Karen McCusker**  
Investment director



**Alex Turnbull**  
Investment director



**Tim Ford**  
Portfolio manager



**Will McIntosh-Whyte**  
Investment manager

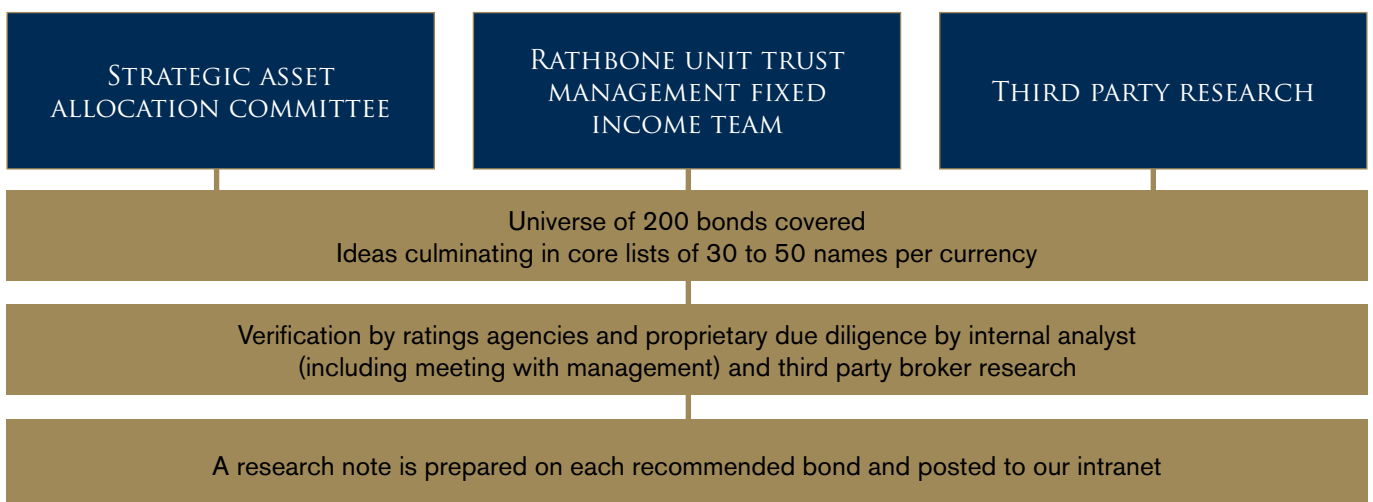


**Mark Waring**  
Dealer



**Noelle Cazalis**  
Credit analyst

The committee meets monthly in order to review the recommended lists. There are three key inputs to the decision making process:



The fixed interest investment universe incorporates G7 Government and investment grade (above Fitch's 'BBB' rating) corporate bonds – financial and non financial. This will include the following instruments:

- Conventional fixed income (bonds with a fixed yield).
- Index linked (bonds with a yield linked to inflation).
- Floating rate note (bonds with a variable yield linked to a money market rate eg, LIBOR).
- Senior (bonds with a superior claim on the assets of insurers).
- Subordinated (bonds with a lesser claim on the issuers' assets and income).
- Asset backed (bonds secured by loans to a company for purchases on credit).

When analysing bonds for inclusion on a recommended list, we consider both micro and macroeconomic factors which include:

### MICRO (CREDIT RISK ANALYSIS)

This includes consideration of:

- Financial ratios eg, interest cover, leverage to free cash flow.
- The ranking of a particular asset in the capital structure of the entity.
- Quality of company management.
- The attitude of company management to bonds.
- Credit agency outlook for the company/country.
- Quality of collateral.
- Strength of covenants.
- Liquidity levels.
- Valuation levels.

### MACRO (ECONOMIC RISK ANALYSIS)

- Sensitivity of fixed interest vehicle to interest rate cycle.
- Effectiveness of total return in relation to clients' differing tax status.
- Prevailing default rates.
- Demand and supply, and the impact this has on pricing.
- Prevailing level of new issues.
- Regulatory issues eg, changes in tax treatment of certain assets.
- Sector issues and opportunities.
- The outlook for inflation and the impact this has on real yields.

Our fixed income committee meets monthly and outputs are communicated to our investment managers via email, our intranet site and at our weekly investment meeting.



# COLLECTIVES RESEARCH

The selection of collective investment funds is a key part of our investment offering and a significant percentage of our assets under management. Our whole-of-market approach means that we source funds from across a broad investment universe comprising both traditional and alternative investment strategies. We may invest your portfolio in a range of different structures including open and closed ended funds, both on and offshore.

A recommended list is maintained by the collectives research committee which comprises research analysts and investment managers who specialise in particular investment areas. This approach allows broad coverage of available investment opportunities, twinned with rigorous, in-depth research and due diligence. There is much interaction between the investment analysts who possess detailed technical knowledge, and experienced investment managers who are answerable to you for investment decisions. This ensures that committee recommendations are always made with your needs in mind.

## QUARTERLY COLLECTIVES COMMITTEE

Plus representatives from sub-committees



**CHAIRMAN**

**David Coombs**  
Investment director



**Gerry Lawlor**  
Assistant to head of operations



**Richard Smeeton**  
Director



**Hugh Adlington**  
Investment director



**Elizabeth Savage**  
Research director



**Chris Sutton**  
Investment director



**James Hedley**  
Investment director



**Mona Shah**  
Research analyst



**Tessa Pilkington**  
Research assistant

UK equities including long/short	Developed equities including long/short	Asia, emerging commodities and resources including long/short	Macro, fixed income, credit and fixed income derivatives, hedge and absolute return funds	Exchange traded funds, structured products	Private equity, property and infrastructure
<b>Tim Johnson</b> long only <b>James Cooke</b> long only <b>Stephen Bennett</b> long/short <b>Tim West</b> smaller companies <b>Malise Reid-Scott</b> investment trusts <b>Mona Shah</b> <b>Elizabeth Savage</b> <b>David Coombs</b>	<b>Mona Shah</b> Europe <b>James Blossie-Lynch</b> US <b>Simon Dewar</b> Global <b>Tim Ford</b> Japan <b>Amos Nelson</b> specialist <b>Glen Johnson</b> investment trusts <b>Elizabeth Savage</b> <b>David Coombs</b>	<b>James Hedley</b> Asia <b>James Ward</b> emerging <b>Simon Heathcote-Amory</b> investment trusts <b>Rupert Heggs</b> commodities <b>Amos Nelson</b> commodities <b>Christopher Bullock</b> ethical <b>Mona Shah</b> <b>Elizabeth Savage</b> <b>David Coombs</b>	<b>Bryn Jones</b> fixed income <b>Will McIntosh-Whyte</b> fixed income <b>Charles Sargent</b> fixed income <b>Hugh Adlington</b> macro/TAA <b>Andrew Hess</b> macro/TAA <b>Mona Shah</b> <b>Elizabeth Savage</b> <b>David Coombs</b>	<b>Hugh Adlington</b> <b>Chris Sutton</b> <b>Mona Shah</b> <b>Elizabeth Savage</b> <b>David Coombs</b>	<b>Tim West</b> private equity <b>Chris Sutton</b> property <b>Alex Dow</b> property <b>Alex Turnbull</b> infrastructure <b>James Petit</b> infrastructure <b>Liz Davis</b> property equity <b>Mona Shah</b> <b>Elizabeth Savage</b> <b>David Coombs</b>

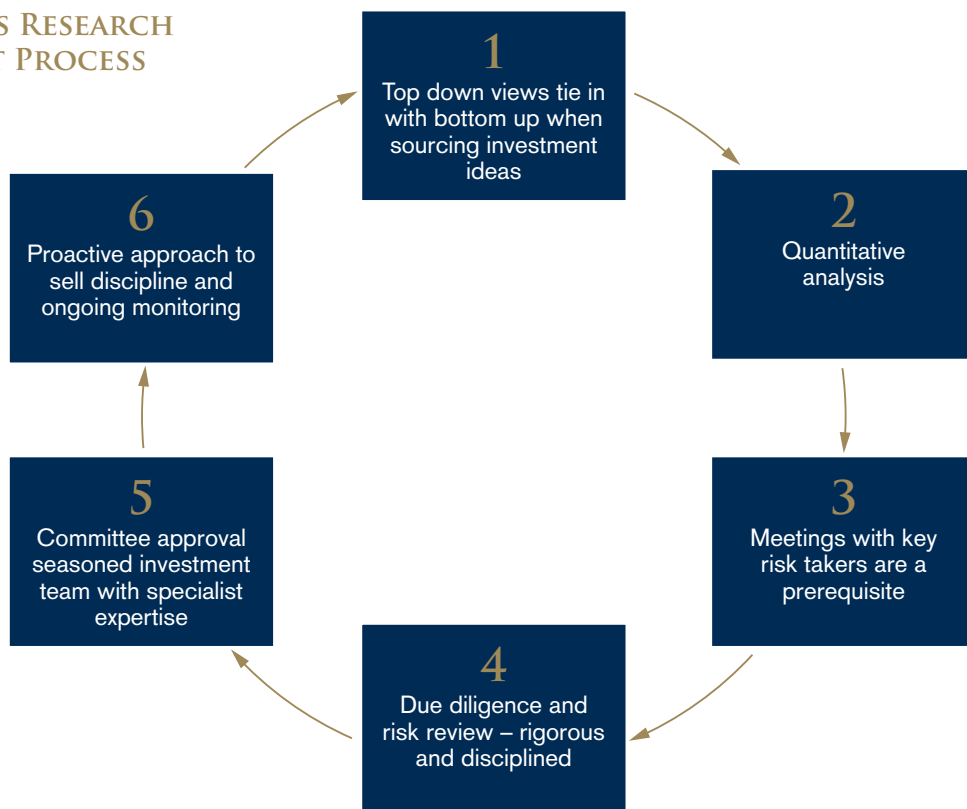
The thinking of our collectives committee is informed by six sub-committees which focus on specific sectors.

The investment and operational areas covered by the collectives research committee are wide ranging, therefore, sub-committees focus on specific investment areas. Our committee structure reflects an increasing convergence between traditional and alternative investment strategies and is designed to harness the skills and experience of the committee members. This means that committee members do not work in silos and have their ideas questioned and debated. The research analysts and committee Chair attend all sub-committee meetings to ensure that the investment process is applied consistently.

## OBJECTIVES OF THE COLLECTIVES RESEARCH COMMITTEE

- Identify the best funds with a variety of risk, return and correlation characteristics.
- Source funds that have consistently outperformed or met their benchmarks with the lowest level of risk.
- Identify alternative investments, including hedge funds and structured products, that have demonstrated that they can reduce the overall risk of a portfolio, as they often lower correlation to both equity and fixed income markets, when combined with traditional asset classes.
- Look for fund structures that are tax and cost efficient and have appropriate liquidity.
- Identify funds and conduct thorough due diligence to ensure robust risk management processes, strong corporate governance and independent, reputable counterparties.
- Monitor the performance of recommended investments on an ongoing basis.

## COLLECTIVES RESEARCH INVESTMENT PROCESS



**1 Sourcing ideas:** The output from the strategic asset allocation committee steers the bottom up research effort by identifying particular geographic areas, industry sectors or investment strategies that are likely to outperform in the future. This ensures that fund selection is forward-looking and not simply reliant on past performance. Specific investment ideas are sourced through industry contacts, conferences and referrals. We also subscribe to third-party investment and analytics software which enables us to screen the universe according to various risk and return metrics. Specifically we are looking for 'best of breed' investment funds across the risk/return spectrum. We are always mindful of the regulatory, tax and liquidity requirements of our clients when sourcing investment ideas.

**2 Quantitative analysis:** For traditional long funds we first review returns over three years on a discrete basis. This is broken into 12 quarters. Any manager who has outperformed in at least eight quarters out of 12 is worthy of further analysis. Next we assess this short list of funds based on 10 risk measures with particular attention to those which measure absolute losses, volatility and relative risk versus the benchmark.

The combination of performance and risk data is scored and all funds are ranked.

As many alternative investments such as hedge funds follow unconstrained investment mandates, it is not meaningful to measure their performance against a benchmark. For these funds we first seek to understand the investment objective and the nature of the strategy employed. The performance track record is then assessed in the context of the market environment and the likely effect of this on the strategy. With this in mind we analyse the track record for the overall risk/return and correlation profile of the fund.

Those long only and alternative investment funds with strong risk-adjusted returns will progress to the next stage of due diligence.

**3 Manager meeting:** No fund can be considered for the recommended list until we have conducted at least one meeting with the underlying fund manager/key risk taker. At the meeting we examine in detail the investment objective and how it relates to the investment strategy and its inherent risks. We seek to understand the opportunities for the strategy, why the manager has an edge in exploiting such opportunities and whether this is sustainable. We also seek to identify the best and worst market environment for the strategy and examine the solidity of the fund manager's business infrastructure and team. Follow-up meetings are common to ensure a thorough understanding of the strategy employed.

**4 Due diligence:** This part of the fund selection process is designed to draw out the weaknesses of the investment strategy and fund manager's business. We use a proprietary due diligence questionnaire to answer key questions and examine in more detail operational and investment risk. Red flags include a lack of transparency, conflicts of interest,

liquidity or asset/liability mismatches, inconsistencies in the story and inappropriate fees. We look at business risk to consider the overall profitability of the firm, the experience, background and reputation of the individuals, in some cases obtaining references. We also investigate operational risk by looking at a fund's formation and structure, controls, segregation of responsibilities and counterparties. The final stage of due diligence includes a document review, checking the terms of the investment in the prospectus, due diligence questionnaire, marketing literature and financial statements. Suitability of the structure for your portfolio is determined by checking the liquidity, tax structure and regulatory controls. If everything is satisfactory then a detailed research note is completed and the fund is submitted to the sub-committee for approval.

**5 Approval by committee:** The collective research committee maintains a list of recommended investments. When an investment is submitted for approval the committee debates its merits and drawbacks and decides whether the fund should be added to the list.

If the committee decides to add the fund to the list then we will seek to negotiate terms with the fund provider. Fees levied by fund management houses can impact performance numbers markedly over the long-term. The scale of our business enables us to negotiate competitive fees and where available we seek to hold institutional units which attract lower fees, reducing the costs of managing your portfolio.

The recommended list is posted on our intranet and any changes are articulated via email and at our weekly investment meeting. Investments on the recommended list are clearly labelled according to their investment mandate and expected risk and return. This assists investment managers to select the most appropriate funds for individual client portfolios. When a fund is added to the recommended list the committee will arrange a follow up meeting to allow Rathbone investment managers the opportunity to meet the manager first hand.

**6 Ongoing monitoring:** The due diligence process does not stop once an investment has been approved. Regular meetings are conducted with the investment managers of all funds and products on the recommended list. The sub-committees meet every six weeks to assess the performance of the recommended funds against their benchmarks and peer groups. The committees take a proactive, forward-looking approach when monitoring investments. We check a number of risk metrics including volatility and correlation and look for change or deviation from the investment objective. Strong positive performance can be a warning sign as it can indicate an increase in risk taking and be the precursor to negative performance. We also monitor the size of assets under management as a fund that is too large may see returns erode over time and we also check for changes to the business such as departure of personnel or change of ownership. Some investments may be removed from the recommended list simply because a better alternative has been sourced.

# BUILDING YOUR PORTFOLIO

These are some of the most important issues that we discuss with our clients:

- Lifestyle and objectives.
- Capital growth or preservation.
- Absolute or relative return.
- Appetite for risk versus the return objectives.
- Income requirement.
- Time horizon.
- Tax position.
- Large holdings.
- Ethical concerns.
- Inheritance considerations.

Our view on strategic asset allocation guides investment managers in the long-term structure of an investment portfolio. Your overall portfolio structure is generally revisited only when there is a significant change in your circumstances – such as the need to rebalance after major price movements or a change in your brief/mandate.

Your portfolio structure will be tailored to your requirements. Consideration will be given to objectives, risk tolerance and any special circumstances. We believe that time spent with you and the information you give us is essential to the full understanding of the investment mandate specific to your portfolio.

Having established your objectives and risk requirements, your investment manager will begin to build a bespoke portfolio. We can draw on the various in-house model portfolios to which we have referred previously in this document, as well as using the recommended lists for each of the asset classes covered.

Our service does not stop here. You can expect your investment manager to regularly review the asset allocation and holdings within your portfolio, taking appropriate action to ensure the portfolio is managed in line with your mandate.

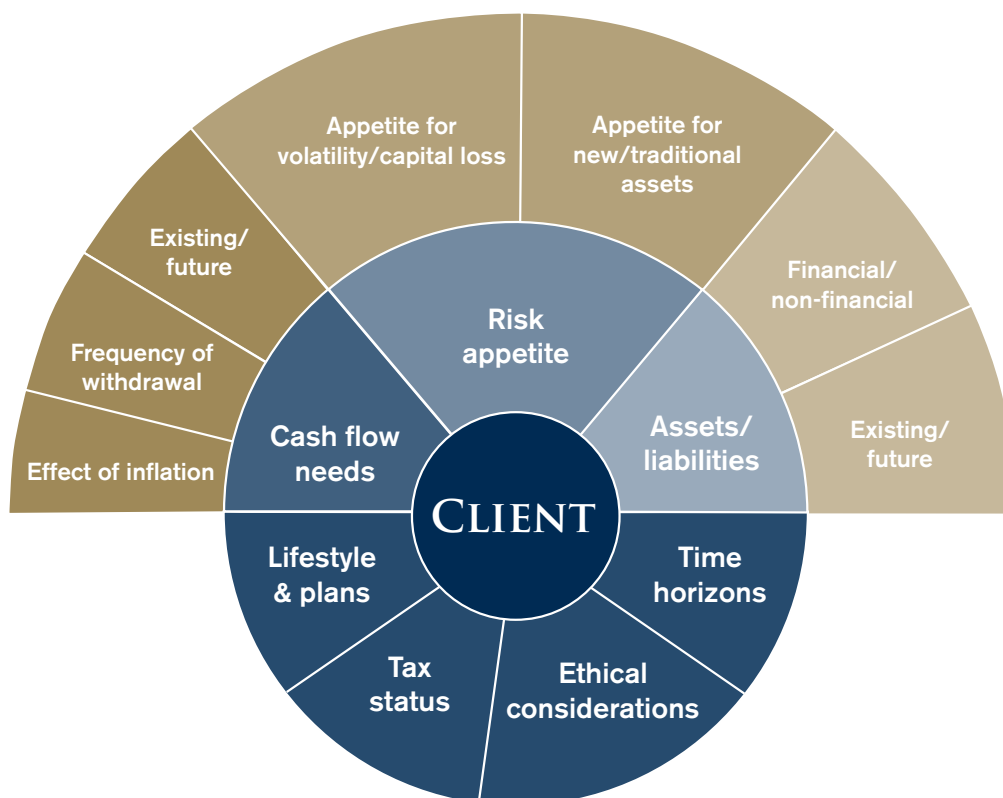
Whether the assets to be managed by Rathbones are part of a series of mandates or are a self-contained entity, we rely on a continual dialogue with you to discuss circumstances as they develop, so that your portfolio can be managed accordingly.



# ESTABLISHING YOUR INVESTMENT OBJECTIVES

We base your investment mandate on your specific needs and preferences. It is important to emphasise that our models are not intended to restrict your investment manager's flexibility to meet your individual needs and it is not necessary to adhere to our model portfolios. Rather, your investment manager will use them for guidance when constructing a portfolio. This allows your investment manager to create the most suitable portfolio for your circumstances.

Your investment manager will maintain an awareness of the risk/reward characteristics of each asset class and the effect these can have on the overall balance of the fund. In some cases we are asked to manage a pure equity or fixed interest fund, so an asset allocation process becomes less relevant. However, the flexibility of our investment process means that your investment manager is able to manage a range of different mandates in the most effective way.



## CONTROL PROCESS

The latitude we allow our investment managers to construct portfolios and select investments on your behalf is counterbalanced by rigorous checks, monitoring and audit trails at different levels within Rathbones.

Each month an independent review of sample portfolios and client files is carried out. We examine the validity of the regulatory documentation and the investment policy specified by each client, and confirm that it matches that adopted by their investment manager. At the same time we check that the stock selection is suitable for each client and service standards and investment returns are measured and noted.

Each quarter, the performance of all portfolios managed by each of our investment managers is analysed and we review any whose returns fall outside, either above or below, our predetermined tolerances. Those that fall outside this banding require a written explanation from the investment manager concerned.

All new investment management trainees are required to obtain the Chartered Institute for Securities and Investment diploma or the Chartered Financial Analyst diploma, and investment managers at all levels regularly receive training on investment, regulations and other topical issues in order to maintain and improve professional standards.

## APPENDIX ONE

### ECONOMIC RESEARCH GROUPS

We pay for economic research from five independent groups. These are detailed below. In each case their economists visit Rathbones for regular internal meetings as well as providing written updates. These views form an integral part of the debate at our Strategic Asset Allocation meetings and are summarised by our research team and circulated to all fund managers on a regular basis.

#### CAPITAL ECONOMICS

A leading independent UK macroeconomic research consultancy, employing more than 15 economists and providing research on the US, Europe, Asia, Latin America and the UK. Founded in 1999, under the leadership of Roger Bootle (one of Europe's most prominent economists), they have gained a reputation for original and insightful research, particularly as they believe in 'telling it as they see it'. Capital Economics' philosophy is broad-based and pragmatic, and their contrarian view has seen them deliver some of the most accurate forecasts in recent years.

#### BCA RESEARCH GROUP

A Montreal based independent research provider covering investment strategy, economic analysis and forecasts for the global financial markets. Founded in 1949 as The Bank Credit Analyst, it became well-known for its interest rate and yield curve analysis, but has expanded to cover international trends and strategies, global economic developments, commodities, foreign exchange, equities and fixed income securities. BCA employs a number of proprietary indicators in their analysis. Rathbones is primarily advised by Peter Berezin, Managing editor and member of the BCA research team. Mr. Berezin joined BCA after spending three years as Vice president and Senior global economist with Goldman Sachs in New York. Prior to this, he spent seven years with the IMF.

## MACRO RESEARCH BOARD (MRB)

MRB Partners is a newly-formed (2010) independent investment research and consultancy firm, specialising in providing top-down global asset allocation advice to investment managers around the world. MRB aims to provide investment strategy and recommendations by identifying key structural and cyclical themes driving the global economy and asset markets, utilising rigorous and comprehensive proprietary forecasting models and indicators, while leveraging the extensive experience of their senior staff. MRB has differentiated itself by providing Rathbones with a more personalised asset allocation service based on a deep understanding of our asset allocation and investment process. We work closely with Peter Perkins, one of the key founding partners, who was previously employed by BCA.

## WOLFE TRAHAN

Wolfe Trahan & Co. is a leading Wall Street research boutique led by Ed Wolfe and François Trahan. François joined the firm in February 2010 as Chief investment strategist, allowing the firm to expand into portfolio strategy and quantitative analysis. François is considered to be one of the pre-eminent strategists and quantitative analysts and employs a unique, objective and disciplined method of analysing the US, global economy and financial markets, relying on the disciplined use of leading economic indicators (conventional leading economic indicators, including proprietary ones) with the aim of making recommendations for equity markets, sectors, style and individual stocks. Compared to other strategists, Trahan's research directly correlates with markets and portfolios rather than remaining embedded in pure economic analysis.

# APPENDIX TWO

## GLOSSARY OF INVESTMENT TERMS

### ABSOLUTE LOSS

A monetary loss incurred by an investor, where there is no prospect of recovery, eg, where a company goes bankrupt, and the sum invested is not recoverable.

### ALTERNATIVE INVESTMENTS

Alternative investments include investments that may not trade publicly on an organised exchange. Examples include partnership funds, which focus on private equity and hedge funds and can include any non-traditional asset class, including works of art, horses, antiques, classic cars and fine wines.

Two alternative assets that have become increasingly attractive for investment managers looking after private clients are structured products and hedge funds or funds of hedge funds.

- **Structured products** – There is no universal definition for this term, as it covers many different types of investment. Broadly, structured products aim to provide the investor with a preset and expected return based on various assumptions about how markets will perform in future. To do this, they often use futures and options. Most structured products have a fixed life so investors know when they will mature. Many will have some degree of inbuilt capital protection, typically promising a minimum return of 100% of the original investment made at the time of issue. Some will fix a return of less than this but should, therefore, offer greater potential for high returns.
- **Hedge funds** – The term 'to hedge' means to manage risk. To do this the underlying hedge funds can employ techniques such as shorting (selling stock they do not own), leveraging (using borrowed money to buy investments) and the use of futures and options. They can also invest in different asset classes such as currencies, commodities and loans. A common aim is to produce an overall return that is not closely correlated to, and is less volatile than, that of traditional assets such as equities or bonds. Many hedge funds do not do this and therefore extra care needs to be taken when selecting this type of holding.

### APCIMS

Association of Private Client Investment Managers and Stockbrokers.

## BENCHMARK

A benchmark provides a standard against which the performance of an investment strategy or portfolio can be measured. Benchmarks are compiled by a range of financial institutions and trade bodies to cover specific markets, investment types and so on. The appropriate benchmark will depend on the strategy of that portfolio and the type of assets within it. For example the FTSE 100 or FTSE All-Share benchmarks are common for UK equity portfolios. For private client investment portfolios it is common to use the FTSE/APCIMS indices or benchmarks. These benchmarks incorporate a range of asset types – equities, bonds, even ‘alternative investments’ – that would typically make up a private client portfolio. There are several Private Investor Indices for various portfolio models (growth, balanced and income) and they are published every weekend on the databank page of the Financial Times’ Money & Business section. Rathbones’ growth, income and balanced models are all compared against the FTSE/APCIMS<sup>1</sup> private investor indices.

Where there is no benchmark appropriate for an investor’s strategy, it may be necessary to develop one based on combining a number of pre-existing benchmarks.

Our multi-asset unit trusts and Rathbone Investment Management International funds are benchmarked to target returns at cash +2% and CPI +5% over the longer term. The Rathbone Enhanced Growth Portfolio is benchmarked on average, 2% above the returns from a combination of 70% MSCI world equity index and 30% MSCI emerging markets index over the long-term with a volatility targeted to be 100% of equity volatility. There is no specific yield target. The aim is to target a return over a minimum of five years but ideally over ten years and above.

## BESPOKE PORTFOLIO MANAGEMENT

If your portfolio is managed on a bespoke basis, then your investment manager is choosing and buying or selling a range of individual assets for your portfolio, based on their view of what is appropriate for you after discussing and agreeing your needs, risk profile, time horizon and so on. It means your portfolio will differ from other portfolios managed by your investment manager and from those managed by their colleagues. Often, the alternative is to have an investment manager place your portfolio in a single or a combination of a small number of collective investments.

## CASH

Refers to bank balances, or other deposit based investments.

## COLLECTIVE INVESTMENTS/FUNDS

These are investment funds (sometimes referred to as managed funds or mutual funds) such as unit trusts, open-ended investment companies (OEICs), or investment trusts that pool the money of many investors. They invest in a spread of stocks and shares to give investors a well-diversified, professionally managed portfolio. This means they are generally lower risk than individual shares, and they are particularly useful in enabling you to invest in more specialised areas, notably overseas markets and smaller companies.

- **Investment trusts** – An investment trust is a company listed on the Stock Exchange. Since it is a listed company, dividends are paid in a similar way as an individual equity. The underlying share price of the investment trust is subject to supply and demand and may not accurately reflect the underlying value of the assets the company owns (which might range from property to other companies’ stock depending on the investment aim or objective). These individual companies can therefore trade on premiums or, more typically, discounts to their underlying assets; ie the share price might rise to a level that values the company (the share price multiplied by the number of shares in issue) at a higher level than the assets it owns (a premium) or they might fall so that the company is valued at less than the assets it holds (a discount). Being a listed company they have the power to borrow (gear) which increases the assets available for investment, but also the risk.
- **Unit trusts/OEICs** – These are similar to investment trusts in that they are diversified portfolios of shares or bonds, but they are known as open-ended. This means that when investors want to buy into the fund, new units are created; and when they wish to withdraw their money, the units are cancelled in exchange for their cash value. The price of each unit is directly linked to the value of the underlying assets and therefore trades at asset value with no discount or premium as in investment trusts.

## COMMODITIES

Commodities describe investments in a raw material or primary agricultural products that can be traded eg, water, coffee, gold, copper.

## CONSUMER PRICE INDEX (CPI)

The principal measure of UK inflation which excludes housing costs.

## CORRELATION

Correlation describes how the behaviour of two variables, usually different assets, are related.

<sup>1</sup>APCIMS – Association of Private Client Investment Managers and Stockbrokers. See [www.apcims.co.uk](http://www.apcims.co.uk)

## FIXED-INTEREST INVESTMENTS

Fixed-interest investments pay a set rate of return agreed at the outset. Their stability means they are often part of the portfolios of an investment manager's clients. They are relatively low risk and predictable, which is helpful for investors looking for income.

- **Gilts or UK government stocks** – These are the safest form of fixed interest since they are guaranteed by the Government. Conventional gilts pay a fixed rate of interest until the Government buys back the stock on a preset date at a preset price. If held to that date, the return they pay is therefore completely predictable and fixed. Their price, however, can rise and fall in the market, mainly depending on interest rates and inflation. Index-linked gilts are particularly low-risk investments since their return is linked to inflation. The income from them is also indexed but usually modest, which makes them attractive to investors who dislike risk and don't need income.
- **Corporate bonds** – These have similar characteristics to gilts. They are guaranteed by the underlying company rather than the government so are higher risk than gilts but give similar types of return. They'll normally have a higher yield (income return) than gilts, reflecting their higher risk. If a company performs badly or goes bankrupt, the holders of a bond would have priority over ordinary shareholders in receiving repayment or income.

## FUND OF FUNDS

A fund of funds is an investment fund whose strategy is to hold a portfolio of other investment funds, rather than investing directly in shares, bonds or other securities. In this way it achieves more diversification for investors with the aim of reducing risk.

## FUTURES AND OPTIONS

Futures are a financial contract obliging the buyer to purchase an asset (or the seller to sell an asset), such as a physical commodity or a financial instrument, at a preset future date and price. They are often used to hedge or to speculate on the price movement of the underlying asset. For example, a producer of corn could use futures to lock in a certain price and reduce risk (hedge). On the other hand, anybody could speculate on the price movement of corn by going long or short using futures. The main difference between options and futures is that options enable the holder to buy or sell the underlying asset at the expiry date, while the holder of a futures contract must fulfil its terms. In reality, few of the underlying goods specified in futures contracts are ever delivered.

(Please note Rathbones does not currently deal directly in futures and options.)

## INSTITUTIONAL FEES

The rates charged for the purchase of certain assets eg, unit trusts, which are often lower than those charged to a private investor, based on the volume of the asset being purchased over time.

## LIBOR - LONDON INTERBANK OFFER RATE

The interest rate that London banks charge each other for loans, usually over a one month or three month basis, six month or one year basis. These rates are often used as a benchmark for bank rates all over the world.

## PRIVATE EQUITY

Money that is invested in companies that are not publicly traded on the Stock Exchange, or money invested in publicly traded companies as part of a buyout to render them private companies.

## PROPERTY

Property refers to investment in bricks and mortar property funds and securities.

## RELATIVE RISK

The level of risk of loss in relation to the risks being taken.

## SHARES, ALSO KNOWN AS EQUITIES

When you buy shares in a company you become a partial owner of it. The main benefit as a shareholder is to receive a share of the profits of that company, usually as a dividend. If the company performs well and increases its profits, the dividend should rise. The share price should increase as well, giving the prospect of capital gains. Shares are risk investments and their value can go down as well as up, as can the income you get from them (the dividend). You should view shares as a medium-term to long-term investment. It is important to spread investment risk across a range of companies, sectors and markets to reduce the risk of losing out if any one company or sector performs badly.

## VOLATILITY

Volatility measures the relative rate at which the price of an asset moves up and down over time.

## FURTHER INFORMATION

The Association of Private Client Investment Managers and Stockbrokers has a directory of members (of which Rathbones is one). Write to 22 City Road, Finsbury Square, London EC1Y 2AJ, call 020 7448 7100 or go to [www.apcims.co.uk](http://www.apcims.co.uk).

The Financial Services Authority regulates all discretionary investment management companies. It also offers information for private investors at [www.moneyadvice.service.org.uk/yourmoney/](http://www.moneyadvice.service.org.uk/yourmoney/)

Many of the national newspapers have weekly personal finance or money sections that offer advice, and most of their websites also offer information about personal finance.



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## IMPORTANT INFORMATION

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