

THE INVESTMENT MANAGEMENT SERVICE

Date Issued: [Date Issued]

[Client Name]

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**1.** WELCOME MESSAGE

**A message from Investment Director, Adrian Gough**

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**“Our objective is to be the advisor of choice for ambitious organisations, high net worth individuals and other professionals.”**

RSM Tenon Group PLC is a public company on the main list of the London Stock Exchange.  Being one of the most progressive and entrepreneurial professional services firms in the UK, it has a dedicated focus on delivering the highest quality and closest personal service to its clients.  RSM Tenon Financial Management Limited was also voted IFA of the year 2009 by a leading industry magazine, Money Marketing.

The achievement of your financial objectives takes time, knowledge and expertise, which very few individuals have.  That is why achieving the financial success that matches your personal success may sometimes seem elusive.  It is that knowledge, expertise and time that RSM Tenon Financial Management Ltd. brings to their clients to assist them achieve these.

RSM Tenon Financial Management Limited advise clients who have combined assets of over £3billion currently under management and advice.

* Tax
* Investment
* Retirement
* Planning and structuring
* Philanthropy
* Trusts and estate planning

Our advice is delivered in an integrated way by a qualified and experienced relationship manager.

Our investment consulting is bespoke and targeted specifically at the needs of high net worth families, for whom we provide strategic asset allocation advice and portfolio management services.

Please read it carefully and let us know if you have any questions.

**2. OUR INVESTMENT PROCESS**

**Investment Philosophy**

When managing clients’ assets we follow certain methodologies that over time we have found work very well.

* We apply modern portfolio theory rather than guesswork or gut feelings to portfolio construction. This allows us to apply clear mathematical principles to our investment decisions
* We believe absolutely in a diversified asset strategy – this reduces risk and delivers more consistent returns
* Our investment recommendations are always clear and based on an analysis of the risks and rewards and how any changes will integrate with your existing investments
* We have a whole of market approach to the selection of investment managers
* Total underlying costs incurred in meeting your objectives should be minimised

**Modern Portfolio Theory**

Modern Portfolio Theory is the term used to describe a mathematically based investment process using the principles set out by Harry Markowitz and Bill Sharpe in their Nobel Prize Winning Investment Theory. For each asset class we estimate expected levels of risk and return based on historical performance, risk premiums and forward looking views. These estimates are then used to determine the most efficient mix of assets for each portfolio. At the core of this process is a belief in efficient markets where, over the longer term, risk is in line with reward. The following chart shows our long term risk and return forecasts for each asset class.

**Diversification**

The old adage of not having all of your eggs in one basket is as sensible today as it has always been. When building a portfolio it is very useful to understand just how different or similar a range of investments are to each other. The statistical measure of similarity is ‘correlation’. Correlation is measured on a scale of -1 to +1.

Two investments with a correlation of -1 are termed negatively correlated and will usually move in opposite directions. To use a simplistic example, in the wet and cold winter months you would expect sales of umbrellas to flourish and sales of ice cream to flounder i.e. their returns are negatively correlated.

Investments with a correlation of +1 are positively correlated and will usually move in the same direction. Using a similar example, in our cold and wet British winter you would expect sales of both umbrellas and wellington boots to flourish i.e. their returns are positively correlated.

Finally, investments with a correlation of zero are uncorrelated and it is impossible to predict how they will move versus each other. For example, sales of wellington boots and children’s crayons could be expected to show little correlation.

The following chart illustrates this.



Some investments have high levels of positive correlation, such as UK and US equities: We can be fairly certain of a fall in the UK stock market if the US stock market falls overnight.

Introducing alternative investments is the key to diversification. The following table shows how little correlation some alternative investments are to the UK stock market:

* UK Gilts - 0.18
* Commercial Property +0.25
* Hedge Funds - 0.09
* Commodities +0.10

The key to effective diversification is to have a range of investments that have correlations as low as possible. From the table above we can see that two of the four investments are positively correlated, whilst the other two are negatively correlated. But, they are all a long way from a correlation of +1.0 (where the investments could be expected to move in an identical way to the UK stock market).

**The benefits of Diversification**

Diversifying your portfolio into alternative assets WILL reduce risk. Even adding very high risk assets such as commodities can reduce portfolio risk if the weightings are correct. The following chart demonstrates this concept using ten years of historical data. Starting with a 25% equity / 75% bond portfolio we can see the average annual return over 10 years is 7.4% and risk is 7.3%. By adding a 10% commercial property weighting, portfolio risk reduces and return reduces a very small amount. If we add a 10% hedge fund weighting, return increases and portfolio risk reduces. These additions might seem straightforward as both of these asset classes are lower risk, however, if we add a 5% weighting to commodities, a high risk asset class, again we see a reduction in risk and an increase in return.

Might there be reasons not to diversify? The major reason would be that a diversified investment strategy should be expected to under-perform a strongly rising stock market.

**Model Portfolios**

We maintain model portfolios for all of our core investment strategies. This allows us to more efficiently manage our clients’ portfolios, attribute risk and monitor any deviations. Each model has a detailed investment objective which, together with appropriate constraints and risk controls, ensures maximum opportunity for expectations to be achieved.

Our model portfolios are managed by the firm’s Investment Committee who meet regularly to ensure portfolios are performing in line with expectations, review performance of investment managers and agree new asset classes or changes in policy. The firm also has a governance and oversight board, the members of which are responsible for risk management and performance oversight.

**Whole of Market Approach**

We believe that no single manager will be effective at managing money in all asset classes. Consequently, we operate an open architecture approach to investment management, choosing the world’s best managers wherever they may be.

Our universe of investment options includes Boutique Investment Managers, UK Unit Trusts and OEICs, offshore funds, and funds listed on any recognised investment exchange. We are NOT restricted to the funds available on a particular IFA or stockbroker investment platform.

*Whole of Market – Key Benefits*

* Access to some of the worlds most talented and experienced investment professionals
* Risk control through diversification across asset classes, styles and managers
* Much reduced stock specific risk
* Monitoring your investment managers against strict buy and sell criteria
* Competitive total expense ratio

**Manager Selection and De-selection**

We have a detailed process for the selection, monitoring and de-selection of investment managers. It is designed to put managers on watch and to trigger recommended sales in the event of excessive risk or poor performance relative to the market or peers. This analysis is applied to all managers.

All manager appointments are made against these criteria and of particular importance are:

* A consistent track record
* Excellent risk adjusted returns
* Management tenure
* Good communication links with the manager
* Risk controls

The following chart illustrates our manager selection process, starting with over 53,000 manager options which are refined down to c.30 managers who would be used in your portfolio.

**53,311**

**Number of Managers**

**25-35**

**57**

**120**

**150**

**Process**

**Resource**

Investment

Approved List

Qualitative Due Diligence

Quantitative Analysis

Database, contacts, clients

ARC Profiler System

Skill and experience overlay

Research

Manager visits and independent due diligence reports

**Manager Blending**

Selecting good managers is only half of the process. Very little benefit is obtained by ‘diversifying’ risk by using four managers who all follow very similar investment strategies. The key is to choose good managers and then blend these managers together to deliver a mix where overall risk is reduced. The following chart shows how this works in practice.

The black line represents the ‘Capital Markets Line’ which is all of the possible mixes of two asset classes; Cash and Equities. Any fund above the line is delivering a superior level of risk adjusted return. Our two funds, 1 and 2 are both very good. If we were to blend these funds together in a 50/50 mix, the return of the blend would be the average of the two, as we might expect. The risk of the blend, however, would NOT be the average. This is because the funds are not perfectly correlated. In this example, the funds are approximately 50% correlated and we can see a significantly reduction in risk by blending the funds together in a portfolio.



**What happens in practice?**

Your portfolio is monitored on a regular basis with a detailed review of every fund and manager included in your portfolio on at least a monthly basis. Where we detect undesirable risk or return trends we will investigate further and, where appropriate, make changes.

Our investment committee meets on a monthly basis to review markets and the outlook for risk and return of the various asset classes. We buy in independent research and this forms the thrust of our asset allocation decision making.

In summary, this is a proactive investment management service but where change is not made for changes sake.

**3. YOUR PORTFOLIO**

You have completed our psychometric risk profile questionnaire and we suggest our **[Client Investment Type]** Strategy as the most effective mix of the various asset classes to meet your risk and return requirements.

All of our lower risk strategies have an absolute return objective. By this we mean a targeted return above the current Bank of England Base Rate. Our higher risk models have a more directional return profile. **Our [Client Investment Type] Strategy is designed to deliver a return of [Strategy Return Over Base] per annum above the long term average of the Bank of England Base Rate (after all fees) over a rolling [Strategy Time Horizon] year period.**

**Asset Allocation**

We believe the MOST important investment decision is to determine the most effective asset allocation mix and a large number of studies have been conducted into whether asset allocation adds value to the investment process. The latest of these “Does Asset Allocation Policy Explain 40, 90 or 100 Percent of Performance?” by Roger Ibbotson and Paul Kaplan confirmed the results of previous studies – that around 90% of performance is determined by asset allocation.

[Allocation Chart Header]:

*[Allocation Chart]*

[Allocation Chart Caption]

*[Allocation Comparison Chart]*

INSERT COMMENT ON ASSET ALLOCATION HERE

[Stress Crash Header]

[Stress Crash Text]

*[Stress Test Market Crash Chart]*

ADD COMMENTS ON COMPARATIVE PERFORMANCE

**How does Performance Compare?**

Higher risk usually means higher return. How would a diversified mix of assets have performed during the post-credit crunch bear market rally, and over a longer period such as the last ten years? [Stress Market Rise]

*[Stress Test Market Rise Chart]*

ADD COMMENTS ON COMPARATIVE PERFORMANCE

**This analysis is somewhat hypothetical as these ‘shock’ events will certainly not be replicated in their original form again. However, it does serve to illustrate the potential impact of higher levels of risk in a portfolio and the potential benefits of diversification. The past performance shown above does not represent any maximum or minimum gains or losses and future ‘shocks’ could, potentially, see even bigger losses.**

**Note: Value of investments call fall as well as rise and past performance is no guide to future performance.**

The following chart compares the ten year performance of the recommended approach vs [Comparison Chart Header]

*[Ten Year Return Chart]*

**Rolling Return Charts**

Ten year return charts are very good at showing how a portfolio would have performed had your money been invested at the beginning of the ten year period. However, what would the performance be if your funds were invested on alternative dates? One way of looking at this is to use rolling return charts. The following three charts show rolling returns over one three and five years. These charts are slightly complex but basically, choose a date on the horizontal axis and the ‘value’ of the various lines at that date shows the compound performance for the appropriate time period.

*[Rolling Return 1yr Chart]*

*[Rolling Return 3yr Chart]*

*[Rolling Return 5yr Chart]*

Another way of exploring risk is to look at ‘drawdowns’ or falls in value. The following chart shows ALL falls in value [Drawdown Chart Text] The chart allows you to see both the magnitude of falls in value and, perhaps more importantly, the time taken to recover.

*[Drawdown Chart]*

ADD COMMENTS ON DRAWDOWN CHARTS

The following table details our current investment recommendations. Please note these are subject to change as the funds are monitored on an ongoing basis. Expected yield and income is an estimate and is not guaranteed.

*[Model Table]*

**4. OUR CLIENT APPROACH**

A successful relationship depends upon a number of things:

* A clear understanding of your goals and aspirations – what are you striving to achieve, when and why – how important are these objectives and what are the priorities?
* Regular communication between Consultant and client
* Risk – how much risk do you want to take? How certain do you want to be that your goals will be achieved?

We will provide yearly reviews where we will:

* Review your goals and objectives
* Agree any changes to your strategy
* Agree short term cash flow needs
* Discuss the performance of your portfolio and agree necessary changes to our approach or the managers used

We will send regular statements which will include information on asset allocation, transactions and a full income statement.

We provide secure internet access to your portfolio allowing you to view real time valuations.

After the end of the tax year we send a comprehensive tax pack to you or your tax advisors (if you are not using RSM Tenon for tax compliance) detailing all income received and capital gains realised during the tax year.

**5. FEES & CHARGES**

**Fund Fees**

The investment funds that we purchase on your behalf all have management charges. Some of these funds also have performance related fees. All fees are detailed in the enclosed fund fact sheets, We work hard to reduce costs and one of the ways we achieve this is to negotiate rebates on management fees from the fund managers. **ALL trail commission, rebates and retrocessions received from fund managers will be credited to your portfolio as a cash credit each quarter.** These commissions can be as much as 0.75% of the fund value and by crediting them back to the portfolio we significantly reduce the total cost of managing the portfolio. **We estimate that the aggregate charge levied by the funds in your portfolio, net of these rebates, will be [Strategy Aggregate Charge] per annum.** This figure excludes performance fees because all performance fees are bespoke to the fund. We do not know what the performance of the fund will be and, therefore, cannot illustrate the impact of these fees. They are, in essence, a payment to the fund manager for achieving certain levels of out-performance and are fully described in the attached fund fact sheets.

**Dealing and Custody Charges**

All assets will be custodied on the SEI platform, the cost of which is 0.25% per annum. This includes all dealing, execution and custody costs.

When purchasing collective investment schemes we are able to deal on institutional terms thus **significantly** reducing the cost of purchase.

**6. SUMMARY AND CONCLUSION**

We hope you have found this report interesting. Our aim has been to demonstrate a clear investment process based on sound principles, robust risk controls, proven process and depth of experience.

**7. RISK WARNINGS**

Although levels of risk are closely monitored, any investment carries risks. Amongst those you should consider are:

* **A large proportion of investments are made into offshore or unlisted funds which are not regulated by the Financial Services Authority. Investors in these funds are not covered by the Financial Services Compensation Scheme nor do they have the right of recourse to the Financial Ombudsman Service.**
* **Some asset classes, particularly private equity, hedge funds and alternative bond funds, have limited liquidity which tends to tie up capital for extended periods of time. A number of these funds allow only quarterly redemptions and sometimes have extended notice periods. These funds may not be appropriate if you might require sudden access to a significant proportion of your portfolio.**
* Part of your portfolio would provide exposure to funds which invest in property and land, which can be difficult to sell; so you may not be able to sell/cash in this investment when you want to. The investment provider may have to delay acting on your instructions to sell your investment. This delay could be very significant; **historically, we have seen redemption delays of over twelve months.**  These funds may not be appropriate if you might require sudden access to a significant proportion of your portfolio. The value of property and land is generally a matter of a valuer’s opinion rather than fact.
* **While your capital is being transferred it will be out of the market. This means that if the markets rise while your transfer remains pending you will not benefit from any growth in capital or income.**
* Part of your portfolio would provide exposure to funds which invest in higher yielding bonds. Companies issuing higher yielding bonds are more likely to default on the loan.
* Many funds have a, ‘redemption gate’ of around 10% of the fund value. Where total redemptions in a given time frame exceed the, ‘gate’ managers have the ability to pro-rata redemptions for that time period. This would have the effect of delaying redemption of part of your holding in such a fund. We sometimes invest in smaller boutique funds where the aggregate investment from clients forms a relatively large part of the fund. Holdings in such funds are more likely to trigger the redemption gate than holdings in very large funds. The redemption terms of all the funds we propose to purchase on your behalf are detailed in the fund fact sheets which are attached to this report.
* A diversified investment strategy (where your portfolio is invested in a wide range of asset classes) can be expected to underperform against strongly rising equity markets.
* Past performance is not an indication of likely future performance.
* Investments can go down as well as up and you may not get back the amount you originally invested. Projected investment returns are merely an estimate, not a forecast and certainly not a guarantee.
* There is no guarantee that by transferring your funds to an alternative investment arrangement you will benefit from better returns than could have been achieved with your existing investment managers.
* Taxation legislation may change and therefore impact on any income and investment returns you receive.
* Investment Strategies have been running since 1 February 2007. All of the back-testing and stress testing referred to in this report has been compiled using the performance of the indices which represent the asset allocation of the strategy.
* The investments we are suggesting are for your anticipated investment term. It is impossible to predict the way in which the economy and the financial markets may develop during that period. If inflation, interest rates or investment performance were to change significantly this could affect your needs, the possible returns and our recommendations.