Skandia
for the international investor

principles of investment

produced in association with

Skandia
Investment Management

understanding multi-manager funds

This factsheet provides an overview of multi-manager funds.

why invest in multi-manager funds?

Choosing the right fund is difficult. The options available to an investor are almost limitless. In the UK alone there are over 2,000 registered funds to choose from and there are thousands of offshore funds registered in places such as Luxembourg and the Irish Republic available to investors throughout the world.

Additionally new funds are constantly being launched, making it difficult to keep track of which funds and fund managers are the best at any one time.

Not all fund managers will be capable of delivering consistent outperformance, leaving the investor at risk of potentially choosing yesterday's stars rather than tomorrow's.

Making the right choice for a portfolio and then refining it and reshaping it over the years takes time, information and skill.

Fund managers need to be selected and monitored to ensure they remain at the top of their game – and replaced when they do not. Few private investors have the resources to do this properly.

Multi-manager funds offer investors access to a wide range of fund managers, together with dedicated experts to select and monitor them on the investors behalf.

what are multi-manager funds?

A multi-manager fund offers you access to multiple funds through a single fund; as a result multi-manager funds can increase the potential for diversification and so reduce the overall level of risk.

The job of the 'multi-manager' is to have an in-depth knowledge of funds and fund managers, in the same way a fund manager should have a comprehensive knowledge of shares.

Multi-managers use this expertise to select the appropriate funds in each asset class and region with the aim of further reducing risk, resulting in a focused portfolio with plenty of potential to outperform.

Some of the various methods used to achieve this are more sophisticated than others, but in general terms the tasks are as follows:

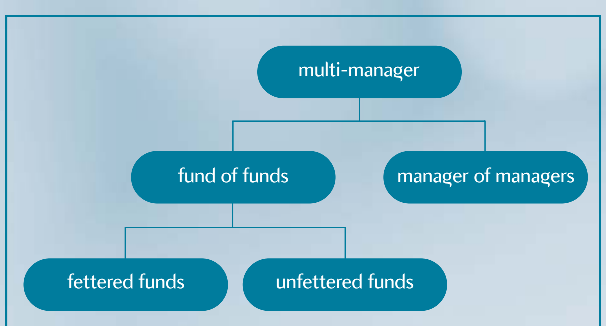
1. **Asset Allocation** – decide the correct allocation between regions and asset types.
2. **Fund manager selection** – select appropriate experts in their respective field.
3. **Monitoring and managing the managers** – the multi-manager will keep track of all fund changes (for example investment style changes, fund group mergers and changes of fund managers).

types of multi-manager funds

The term 'multi-manager fund' can refer to two main types of funds, 'fund of funds' and manager of managers', as shown in the diagram below.

Fund of funds

A fund of funds aims to create a blend of the most appropriate investment funds to meet a defined objective.



There are two different types of fund of funds: **fettered** (in-house) and **unfettered**.

Fettered fund of funds only invest in funds managed by the same fund group. Therefore a fettered fund of funds provided by Skandia would invest exclusively in funds provided by Skandia.

Unfettered funds, on the other hand, have the freedom to invest in funds provided by other fund groups.

> 'Nearly 85% of all UK fund of funds are unfettered funds.'
>
> Source: New Star, December 2004.

Some groups will take this even further and will set an in-house rule that excludes them from investing in any of their company's funds, ensuring all investments are external.

Fund of funds can provide a number of advantages:

- A high level of diversification through just one multi-manager fund – with the reassurance that the underlying funds are being constantly monitored.
- Fund of funds can be tax efficient. They are actively managed, meaning the fund manager will buy and sell funds to achieve the overall objective. If funds were bought and sold in this way by a private investor (resulting in a gain on the investment) the investor may, in certain countries, be liable to tax on the gain.
- Minimises paperwork investors receive the paperwork for the multi-manager fund, not all the underlying funds.
- The individual funds within the fund of funds can be bought and sold almost immediately – they are flexible to change.

However, the multi-manager cannot specify how the underlying funds are operated. This can lead to asset overlaps between funds if the different underlying managers pursue similar investment strategies.

This leads us to one of the advantages of the second type of multi-manager fund – 'manager of managers' funds.

Manager of managers funds

In this case, rather than investing directly into specific funds, the manager of managers appoints the underlying fund managers who buy assets directly.

A separate instruction or segregated mandate is issued to each of the appointed managers outlining the parameters in which the money is to be managed, as shown below.

For example, the manager of managers may have specific instructions as to the amount of risk that a proportion of the fund is to be exposed to or on the general investment style.

If a fund manager is not performing satisfactorily against the requested mandate they can be replaced. In this way the fund is actively managed by the manager of managers with the aim of achieving optimum performance within the overall objective.

Manager of managers funds often have a broad asset allocation – though they have different risk profiles. For example, there are many 'cautious', 'balanced' and 'aggressive' portfolios, which may work well as core funds within a diversified portfolio.

In general terms, the core advantages for manager of managers funds are the same as for fund of funds:

- Portfolio diversification.
- Simplicity – the opportunity to achieve a diversified portfolio through only one fund.

and finally...

Multi-manager funds offer a convenient way to access a wide range of fund managers. Spreading investments across a wide range of managers decreases the likelihood of a fall in value across the whole portfolio.

At the same time, cautious, balanced and aggressive multi-manager funds make it simple to adapt a portfolio to suit an investor's changing circumstances. There are also a growing number of more specialist funds, such as those that offer investments in a specific region or asset class, but still retain the access to multiple managers.

A financial adviser will be able to recommend multi-manager funds that are suitable for your individual needs and defined risk profile.

www.royalskandia.com

Calls may be monitored and recorded for training purposes and to avoid misunderstandings.

Royal Skandia Life Assurance Limited (an incorporated company limited by shares) Registered number: 24916
Registered and Head Office: Skandia House, King Edward Road, Onchan, Isle of Man, IM99 1NU, British Isles
Phone: +44 (0) 1624 655 555 Fax: +44 (0) 1624 611 715
Authorised by the Isle of Man Government Insurance and Pensions Authority Authorised and regulated by the Financial Services Authority for business conducted in the UK. Some of the FSA's rules do not apply to non-UK based insurers. FSA Register number: 142309

Skandia Life Ireland Limited Registered No: 309649 Ireland
Registered Office: Arthur Cox Building, Earlsfort Terrace, Dublin 2, Ireland
Head Office address: Skandia Ireland, Regus House - 4th Floor, Harcourt Road, Dublin 2, Ireland. Skandia Life Ireland Limited is regulated by the Irish Financial Regulator. Skandia Ireland products are only available in certain countries within the European Economic Area.