LFP

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omniport

Portfolio Construction

Objective:

- To have the confidence and conviction to build a well-structured portfolio based on client objectives and agreed strategies
- To demonstrate that Portfolio Construction is not all numbers and science – commonsense factors prevail

Portfolio Construction

Factors to Consider

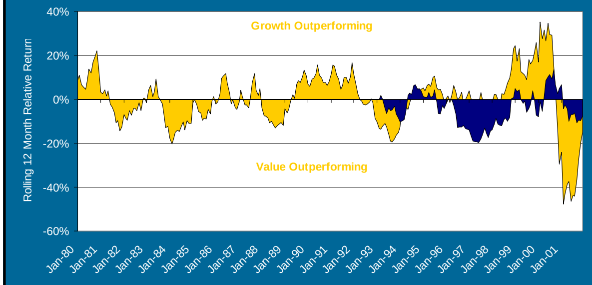
Client's Perspective
Tolerance to volatility
Level of knowledge
Previous experience

Advisor's Perspective – refer to drivers

- Asset Allocation
  Implementation, market timing, tactical shifts
- Time (admin and manager contact)
- Confidence in manager selection
- Fund of Funds/model portfolio approach
- How many managers per asset class ?
- Ask yourself " What role does this fund play in the portfolio?"

Growth vs Value in the Australia

US Value to Growth Cycle (Russell 1000 Growth vs. Value)
Australia SSB Growth vs. Value Overlay



Australia Data Source: Salomon Smith Barney via Mercer Software
US Data Source: Frank Russell
Calculations HSBC Asset management

Why Use Sector Managers ?

- Studies shows clients potentially forgo up to 2% by adopting the balanced approach instead of the sector specialist
- Harness fund manager's strengths and avoid their weaknesses – "best of breed"
- Responsible to clearly defined benchmarks
- Benefit from more focussed manager research

Why Use Sector Managers ?

- Decision to change a manager made easier
- Opportunities for value add and differentiation
- Greater flexibility and responsibility in the strategic asset allocation
- Provides adviser with greater control and ability to limit downside volatility
- IDPS Platforms facilitate this process

Rules of Thumb

When building a portfolio follow these simple rules.

Types of Funds	How Many	Style
Australian Equities	3 Funds (max 4)	Active, high alpha
International Equities	3 Funds (max 4)	Active, high alpha
Listed Property	2 Funds	Active
Fixed Interest	2 Funds	Active/Passive
Mortgage Funds	2 funds	Active fix/var
Diversified Funds		
Growth Funds	3 Funds	Active
Balanced funds	3 Funds	Active
Stable Funds	2 (3 max mtge)	Passive

Hedge Fund Parameters

Maximum holding of "alternative assets"

20% of Growth Component

Blending Managers

- Don't rely on short term performance figures
- Easy sell and gives short term comfort but long term headaches
- The performance over a certain period needs to be analysed in the context of the economic cycle
- A fund manager's style can affect performance

Approved Australian Equities
Ranked Over One Year with Net Assets as at 31 March 1999

Rank	Product Name	1 Year % pa	3 Years %	5 Years % pa	7 Years % pa
1	Merrill Lynch - Imputation Fund	26.0(1)	27.2(1)	16.7(1)	19.4(2)
2	Col First State Mgd Inv - Imputation	25.7(1)	25.6(1)	21.9(1)	24.8(1)
3	BT - Australian Share Fund	25.5(2)	20.4(3)	13.8(4)	18.3(2)
4	ING - Blue Chip Imputation Trust	25.4(2)	23.8(2)	16.4(2)	16.0(3)
5	HSBC - Imputation Growth Trust	20.1(3)	17.1(4)	14.5(3)	17.1(2)
6	Credit Suisse - Australian Shares Fund	17.9(3)	17.8(3)	14.6(3)	
7	Perpetual's - Industrial Share Fund	15.1(4)	23.1(2)	15.6(2)	16.9(3)
8	Advance MultiFund - Imputation Fund	8.1(4)	15.2(4)	12.1(4)	13.5(4)

Approved Australian Equities
Ranked Over One Year with Net Assets as at 31 March 2001

Rank	Product Name	1 Year %	3 Years % pa	5 Years % pa	7 Years % pa
1	Sandhurst - Industrial Share Fund	22.4(1)			
2	Advance MultiFund - Imputation	20.8(1)	9.6(3)	13.3(3)	11.6(3)
3	Perpetual's - Industrial Share Fund	12.5(2)	9.9(2)	16.5(2)	13.2(1)
4	ING - Blue Chip Imputation Trust	10.3(2)	10.4(2)	15.3(2)	12.6(2)
5	Merrill Lynch - Imputation Fund	10.0(2)	11.1(1)	17.5(1)	13.0(2)
6	Col First State Mgd Inv - Imputation	4.8(3)	13.4(1)	18.1(1)	17.6(1)
7	HSBC - Imputation Growth Trust	3.6(3)	9.0(4)	11.6(4)	11.3(4)
8	Credit Suisse - Australian Shares	1.6(4)	9.8(3)	12.9(3)	12.1(3)
9	BT - Australian Share Fund	-8.1(4)	6.8(4)	11.1(4)	9.2(4)

Blending Managers

- Greater diversification is achieved by choosing managers with different styles
- Choose the best in each particular style
- Analysis of style is important to identify any structural biases within the portfolio
- The aim is to produce the highest return while limiting downside volatility
- Greater consistency and less volatility over short and long term

Blending Managers

Focus on the commonsense qualitative factors

- **Quality manager? Yes, on the Approved List**
- Specific Style – Style is not mutually exclusive
- Broad Style – High or Low Alpha
- Stock bias – large, mid-cap, small or non-index holdings
- No. of Stocks
- Fund size and turnover
- International – Currency Management, Country Allocation (indexed, top-down, bottom up etc), Small and/or Emerging Companies

Why Do We Blend Managers ?

- Markets unpredictable and always changing
- Increase expected excess return and maximise risk adjusted returns
- Different managers outperform at different stages of the investment cycle
- No style of funds management is always top quartile – reducing manager specific risk
- Complementing style biases thereby probability of short-term underperformance

Why Do We Blend Managers ?

- Portfolio performance becomes less volatile and more consistent
- Exposure to an underperforming manager reduced with greater style differentiation
- De-emphasise having to pick winners
- Taking focus away from purely performance
- MANAGE THE CLIENT'S EXPECTATIONS

Portfolio Construction

- Pick true to label managers and apply some commonsense diversification
- Do not be baffled by science