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Local Currency Emerging Markets Debt Manager Search

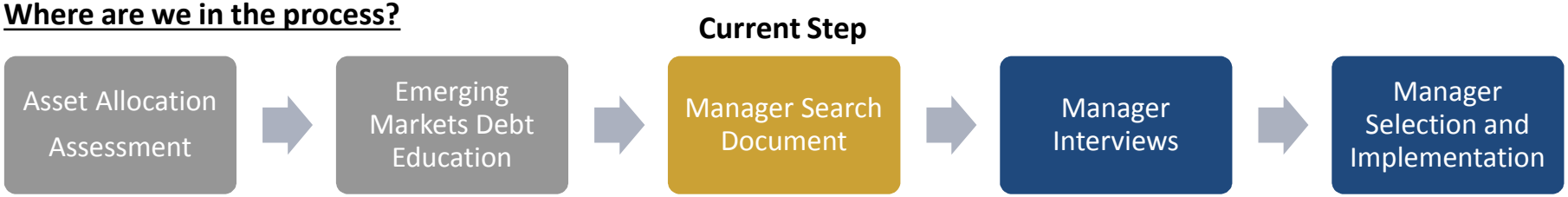
Howard County Retirement Plans

April 2015

EXECUTIVE SUMMARY

- This presentation serves as a continuation of the Committee's exploration of local currency emerging markets debt as an asset class available to help increase diversification within the Retirement Plans.

Where are we in the process?



OVERVIEW OF SEARCH CRITERIA

- After being presented with an asset allocation study, the Committee asked Summit to provide educational material on emerging markets debt as well as a list of high quality managers. In selecting managers for consideration, Summit pulled from two overlapping groups:

  (1) Managers from the entirety of the local currency universe who passed a rigorous set of screens, and
  (2) Summit's previously established Top Tier list.

RECOMMENDATION

- Summit recommends the Committee interview Colchester, Investec, and Lazard for Howard County's local currency emerging markets debt allocation.
- Colchester's high conviction, real yield focused process represents a differentiated approach well suited for taking on a less efficient asset class.
- If the Committee would prefer a more relative value centric/lower tracking error option, both Investec and Lazard have solid strategies.
  - While Lazard lacks assets in its commingled vehicle, it has offered an extremely attractive founder fee (55 bps).

SCREENING PROCESS

- The following process was used to assess the universe of investable managers:

Quantitative and Qualitative Screening of Universe

Starting Point:
Local Currency Universe
(68 Open Strategies)

Wrong Benchmark
(-22 Strategies)

Total AUM Under $1B
(-29 Strategies)

3-Year Excess Return >0
(-8 Strategies)

Qualitative Issues
(-6 Strategies)

3 Strategies Passed All Of The Screens:
Colchester, Investec, and Lazard

Summit's Current Top Tier List

Colchester

Gramercy

Investec

Pictet

Standish

Excluded From Search:
Gramercy – Lack of Assets/Asset Growth
Standish – Loss of Assets

4 Strategies Included in Search:
Colchester, Investec, Lazard*, and Pictet

*While not on Top Tier, Lazard is currently on Summit's 2nd Tier.

MANAGER OVERVIEW

- Colchester
  - Pro: Real yield focused product with high conviction positions; exceptional performance in both up and down markets.
  - Con: Not the cheapest option even as a commingled fund; growing fast due to performance; shorter dedicated emerging markets debt track record; high conviction positions can lead to greater tracking error.
- Investec
  - Pro: Relative value focused product with a broad opportunity set; rigorous, regimented process; greater emerging markets FX experience; emerging market based (South Africa) firm.
  - Con: Not the cheapest option even as a commingled fund; newer product launched after original product (Broad) closed due to capacity constraints in illiquid, off-benchmark allocations.
- Lazard
  - Pro: Relative value focused product; solid track record since moving over from HSBC; PM is an industry veteran; Summit negotiated fee of 55 bps extremely attractive for the asset class.
  - Con: Commingled fund is new and has yet to be seeded; group's strength is Total Return/Blended strategies.
- Pictet
  - Pro: Ability to utilize developed markets in times of stress has led to solid downside protection.
  - Con: Not the cheapest option even as a commingled fund; will typically underperform in up markets; sizable institutional mutual funds can lead to swings in AUM.

SIDE-BY-SIDE COMPARISON

Emerging Markets Local Currency Debt					
	As of 12/31/2014	Colchester	Investec	Lazard	Pictet
Firm	Headquarters Location	London, England	London, England	New York, New York	London, England
	Firm Assets	$31.7B	$112.4B	$178.4B	$151.6B
	Ownership	51% employee owned; 49% other ownership	15% employee owned; 85% owned by Investec Ltd/Investec Plc	100% Publicly Held	100% owned by Banque Pictet & Cie
Product	Product Inception Date	December 2008	July 2006	December 2010	August 2006
	Product Assets	$6.0B	$8.8B	$3.6B	$9.9B
	Vehicle(s) Available	SA, CF	SA, CF	SA, CF	SA, CF
	Separate Account Minimum	$75M	$200M	$100M	$150M
	Commingled Fund Minimum	$2M	$10M	$1M	$500,000
	Mutual Fund Minimum	N/A	N/A	N/A	N/A*
Characteristics	Security Screening Approach	Bottom-Up	Combined	Combined	Combined
	No. of Securities	29	160	111	244
	Portfolio Turnover	35%	65%	64%**	66%
	Average Quality	A	BBB	BBB	BBB
	Yield to Maturity	6.48%	7.34%	7.01%	6.60%
	Duration Band Around Index	-20% to +25%	± 2 Years	2 to 6 Years	± 0.5 Years

*US mutual fund available for altered local emerging markets debt index.
**3Q2014

STATISTICAL SUMMARY

As of 12/31/2014	Colchester	Investec	Lazard	Pictet	JPM GBI-EM Global Diversified Unhedged
3 Year Performance:					
Annualized Return	3.3%	0.7%	0.9%	-0.1%	0.1%
Annualized St. Dev	9.0%	9.7%	9.8%	9.2%	9.5%
Sharpe Ratio	0.36	0.07	0.09	-0.02	0.00
Tracking Error	1.6%	1.0%	0.7%	0.6%	N/A
Info Ratio	1.94	0.65	1.20	-0.31	N/A
Batting Average	75.0%	75.0%	75.0%	33.3%	N/A
Up Market Capture	107.7%	110.4%	107.1%	97.5%	N/A
Down Market Capture	66.4%	101.1%	95.4%	100.2%	N/A
5 Year Performance:					
Annualized Return	4.5%	3.1%	N/A	2.6%	2.6%
Annualized St. Dev	9.9%	10.9%	N/A	10.0%	10.4%
Sharpe Ratio	0.44	0.27	N/A	0.25	0.24
Tracking Error	2.3%	1.5%	N/A	0.8%	N/A
Info Ratio	0.81	0.30	N/A	-0.05	N/A
Batting Average	65.0%	65.0%	N/A	40.0%	N/A
Up Market Capture	103.5%	110.2%	N/A	97.7%	N/A
Down Market Capture	79.1%	105.8%	N/A	97.8%	N/A
7 Year Performance:					
Annualized Return	N/A	5.2%	N/A	5.0%	4.0%
Annualized St. Dev	N/A	12.6%	N/A	11.1%	11.6%
Sharpe Ratio	N/A	0.37	N/A	0.40	0.31
Tracking Error	N/A	2.2%	N/A	1.6%	N/A
Info Ratio	N/A	0.51	N/A	0.59	N/A
Batting Average	N/A	60.7%	N/A	53.6%	N/A
Up Market Capture	N/A	113.6%	N/A	100.7%	N/A
Down Market Capture	N/A	103.0%	N/A	88.3%	N/A
10 Year Performance:					
Annualized Return	N/A	N/A	N/A	N/A	6.7%
Annualized St. Dev	N/A	N/A	N/A	N/A	10.5%
Sharpe Ratio	N/A	N/A	N/A	N/A	0.49
Tracking Error	N/A	N/A	N/A	N/A	N/A
Info Ratio	N/A	N/A	N/A	N/A	N/A
Batting Average	N/A	N/A	N/A	N/A	N/A
Up Market Capture	N/A	N/A	N/A	N/A	N/A
Down Market Capture	N/A	N/A	N/A	N/A	N/A

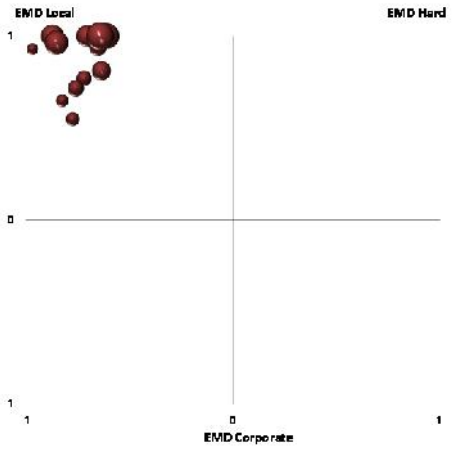
PERFORMANCE RETURNS

Manager vs Benchmark					
As of 12/31/2014	1 year	3 years	5 years	7 years	10 years
Colchester	-3.02%	3.25%	4.48%	N/A	N/A
Investec	-4.57%	0.69%	3.08%	5.15%	N/A
Lazard	-4.80%	0.92%	N/A	N/A	N/A
Pictet	-5.36%	-0.12%	2.59%	4.97%	N/A
JPM GBI-EM Global Diversified Unhedged	**-5.72%**	**0.07%**	**2.63%**	**4.01%**	**6.65%**

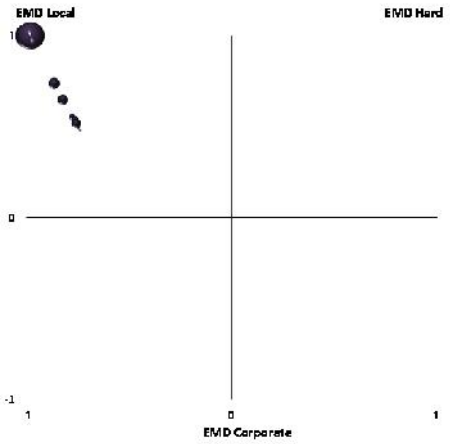
Calendar Year Return										
	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005
Colchester	-3.02%	-6.20%	21.01%	-1.53%	14.85%	26.54%	N/A	N/A	N/A	N/A
Investec	-4.57%	-9.43%	18.11%	-2.27%	16.66%	31.47%	-7.09%	20.40%	N/A	N/A
Lazard	-4.80%	-7.88%	17.21%	-1.35%	N/A	N/A	N/A	N/A	N/A	N/A
Pictet	-5.36%	-9.64%	16.52%	-0.38%	14.50%	25.06%	-1.21%	16.93%	N/A	N/A
JPM GBI-EM Global Diversified Unhedged	**-5.72%**	**-8.98%**	**16.76%**	**-1.75%**	**15.68%**	**21.98%**	**-5.22%**	**18.11%**	**15.22%**	**6.27%**

STYLE ANALYSIS, ROLLING 3-YEAR PERIODS

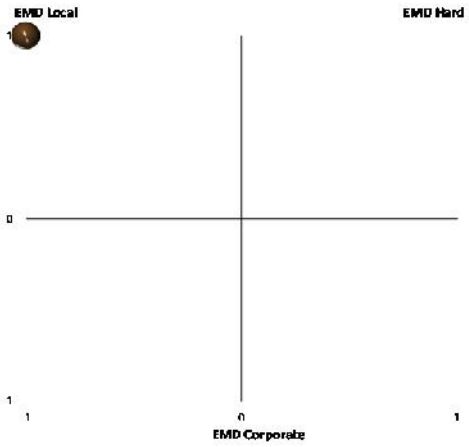
Colchester



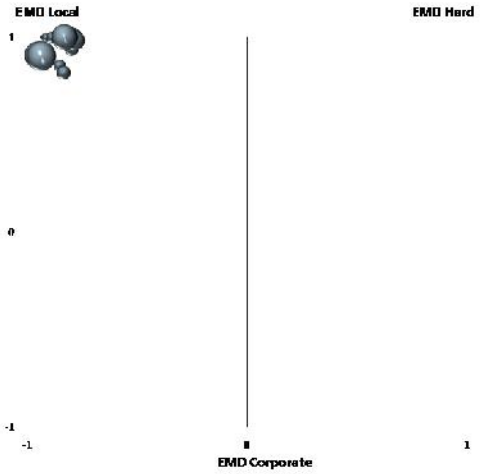
Investec



Lazard



Pictet



INTERVIEW RECOMMENDATION

- Given the diversifying aspect of the asset class versus current allocations, manager-specific biases do not have a significant influence on correlations. Therefore the managers Summit is recommending to interview are based mainly on Summit's conviction level in the manager.

- Why Colchester?
  - Summit finds Colchester's high conviction, real yield focused approach is unique in the emerging markets debt space and well suited for taking advantage of a less efficient asset class.

- Why Investec or Lazard?
  - As with most high conviction styles, Colchester will tend to run a higher tracking error versus the benchmark. A more relative value centric option, such as Investec or Lazard, will maintain a tighter tracking error band.
  - What Investec and Lazard add is a more expansive, out-of-benchmark opportunity set versus Colchester, which allows them to maintain much of the alpha potential of Colchester's higher conviction style.
    - While Lazard lacks assets in its commingled vehicle, it has offered an extremely attractive founder fee (55 bps) and the strategy already has $3.6B in separate accounts.

POOLED VEHICLE REVIEW

	Colchester	Investec	Lazard	Pictet
Type of Fund	3c7	LLC	LP	LLC
Assets	$436 million*	$1.6 billion	$0 million	$1.1 billion
Fee	75 bps on first $25M 65 bps on next $25M 40 bps thereafter (includes admin/custody)	75 bps** (includes admin/custody)	55 bps on all assets** (includes admin/custody)	78 bps on all assets; Capped at 100 bps (includes admin/custody)
Allowable Clients	ERISA & Non-ERISA	ERISA & Non-ERISA	ERISA & Non-ERISA	ERISA & Non-ERISA
Liquidity	Monthly (10 business days notice)	Daily (5 business days notice)	Daily Withdrawals; Twice Monthly Subscriptions (5 business days notice)	Monthly (3 business days notice)
Lock-Ups	None	None	None***	None
Entry/Exit Fees	Anti-dilution levy of 15 bps may apply	Anti-dilution levy of 15-30 bps may apply	None***	2.0% redemption fee if held less than six months
Gate on Redemptions	None	None	None	None

*This is for the US sleeve of the fund. The total fund has $1.9 billion.
**Summit negotiated fee schedule.
***A short-term trading fee can be applied to withdrawals within 30 days of contribution.

APPENDIX

COLCHESTER GLOBAL INVESTORS – LOCAL MARKETS DEBT FUND

FIRM DETAILS

Address: 20 Savile Row
London, UK

Phone: 44 (20) 7292.6920

Asset Class: Emerging Markets Debt - Local

Benchmark: JPM GBI EM Global Diversified

Founded: 1999

Ownership: 51% employee owned; 49% owned by Silchester International Investors

Assets Under Management: $31.7 billion

PRODUCT DETAILS

Inception: December 2008

Assets Under Management: $6.0 billion

Vehicles Offered: SA, CF

Commingled Fund Minimum: $2 million

Portfolio Managers/Dual Role PMs: 3

Avg. Yrs of Experience: 32

Avg. Yrs at Firm: 13

Research Analysts: 5

Avg. Yrs of Experience: 14

Avg. Yrs at Firm: 4

Fee Schedule (CF): 0.75% on first $25 million
0.65% on next $25 million
0.40% on balance

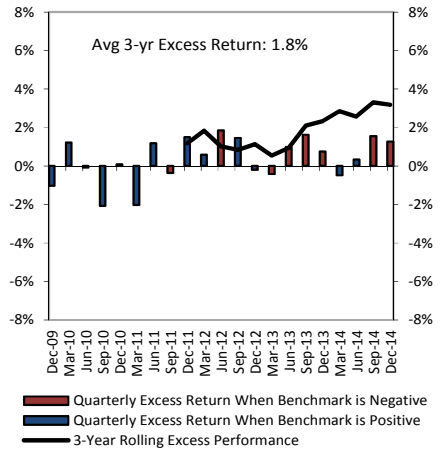
(Performance-based fees are not available)

CHARACTERISTICS

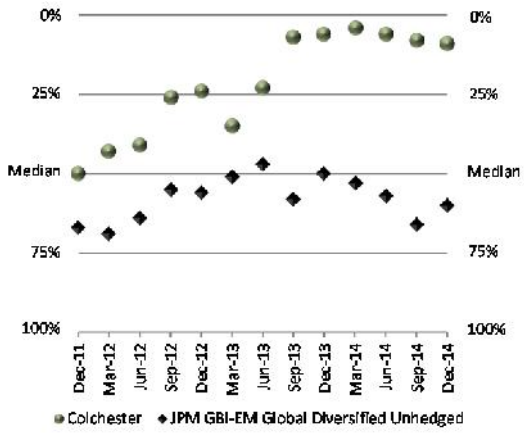
	Portfolio	Benchmark
# of Bonds:	29	195
Portfolio Turnover:	35%	N/A
Avg Credit Quality:	A	BBB
Min Credit Quality:	BBB	BB
Duration:	4.8 yrs	4.9 yrs
Last 3 Years:		
Information Ratio:	1.9	N/A
Sharpe Ratio:	0.4	0.0

ROLLING PERFORMANCE AND RANKINGS

Three-Year Rolling/Quarterly Excess Performance vs. JPM GBI EM Global Diversified Index



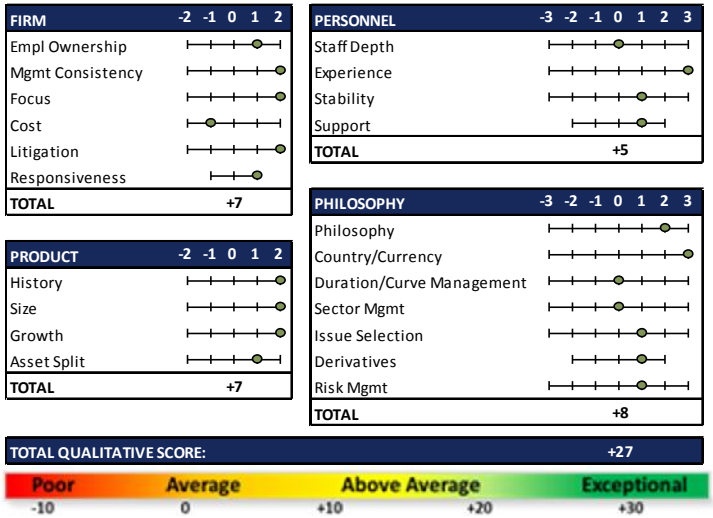
Manager vs. EM Local Currency Universe Rolling Three-Year Periods



QUALITATIVE OVERVIEW

- Colchester opened its doors in 1999 to focus solely on global bond investing. Silchester International Investors is a minority owner at 49% and Colchester's investment team owns the balance. Ian Sims, CIO, retains 50% of the employee ownership. Colchester manages standard and customized composites in global, international, TIPS, emerging markets local currency, and hedged/unhedged debt mandates.
- All products are managed by a single investment team headed by Ian Sims. He has over 30 years of investment experience and is supported by Keith Lloyd, Deputy CIO, and Kathryn Elsby, PM, who have been with the firm since 2000. Idrissa Boly is the Investment Officer primarily assigned to conduct fundamental research on EMD.
- Colchester's philosophy rests on the belief that bonds should be evaluated on the inflation-adjusted income they generate. They believe that countries with high real yields and strong fundamentals can produce superior returns. Their opportunity set is limited to local nominal and inflation-linked sovereign bonds. Colchester seeks to build concentrated, benchmark agnostic portfolios. This philosophy will generate higher tracking error (500 bps).
- The process begins with a forecast of various countries' future inflation based on money supply, exchange rates, capacity utilization, and commodity pricing. They overlay their real yield conclusions with an assessment of the overall health of the countries. Model portfolios for each investable country are created to determine the allocations to nominals and inflation-linkers. A mean-variance optimizer then helps to determine final allocations to each country and currency. Maximum exposure to inflation-linkers and non-investment grade is limited to 30%.

QUALITATIVE RANKING



COLCHESTER GLOBAL INVESTORS – LOCAL MARKETS DEBT FUND

Key Differentiator: Boutique firm dedicated to investing in sovereign bonds through an inflation-forecasting process.

- **Investment Thesis:**
  - **Real Yield Emphasis** – Colchester follows a philosophy highlighted by its concentration on identifying and investing in higher real yield countries with healthy fiscal situations, which they believe can produce superior returns.
  - **Global Sovereign Focus** – As a true boutique manager, Colchester packs a punch with its experienced team and fundamental focus on global bond investments. They firmly believe the sovereign bond market provides ample opportunity for alpha generation and do not venture into non-sovereigns.
  - **Stable and Seasoned Senior Team** – The senior team has a long history in international fixed income dating back to their days at Hill Samuel and Delaware International Investors. Ian Sims, CIO, and his two other senior portfolio managers average over 30 years in the investment industry, a bulk of that within global fixed income.
  - **Respected Partner Firm** – They have a solid, well-established partner in Silchester International Investors, a well-respected player in the international equity market. The ownership structure remains stable with Silchester a minority owner at 49% and Colchester's investment team owning the balance.
- **Risks/Concerns:**
  - **Concentrated Approach** – With investments in less than 10 countries and only 20-30 holdings, their concentrated approach can lead to higher tracking error. Mitigating some of this concern, Colchester invests in the most liquid countries in the JPM GBI-EM GD Index and can completely hedge or have naked currency exposures.
  - **Modeling Limitations** – Historically 70% of the process has been quantitative and this carries with it some data and modeling risks as statistics provided by emerging countries are sometimes unreliable. To alleviate modeling errors, Colchester has added PMs in the recent past and increased travel to allow for a qualitative overlay and data verification/customization.
- **Performance Review and Expectations:**
  - Colchester again solidly outperformed the JPM GBI-EM Global Diversified Index, adding 126 bps of excess return in the fourth quarter. For 2014, the strategy delivered an excess return of 311 bps. Currency selection provided the boost in the fourth quarter, adding 146 bps to performance. Underweights to the Russian Ruble, Colombian Peso, and Polish Zloty were major contributors. Colchester observes that the pace of recoveries is not equal across countries with the US showing encouraging signs of strength compared to Europe and Japan slowing or stagnating. 2015 will see increasing divergence in emerging markets as rate increases in the US expose poorly run countries. Understanding the drivers of the differences in economic growth and the response function of central banks will be critical to performance.
  - Excess return expectations are 150-200 basis points over a market cycle; Colchester's higher quality portfolio should help performance if local rates are to suffer another sell off over the near term.

INVESTEC ASSET MANAGEMENT – EM DEBT LC DYNAMIC

FIRM DETAILS

Address:	25 Basinghall Street London, England EC2V 5HA
Phone:	00 44 207 597 2000
Asset Class:	Emerging Markets Debt - Local
Benchmark:	JPM GBI EM Global Diversified
Founded:	1991
Ownership:	15% employee owned; 85% owned by Investec Ltd/ Investec Plc

Assets Under Management: $112.4 billion

PRODUCT DETAILS

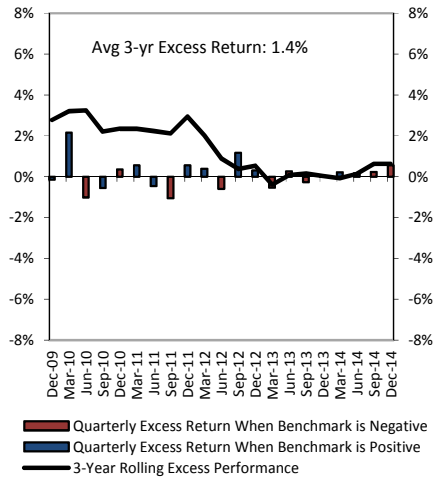
Inception: July 2006
Assets Under Management: $8.8 billion
Vehicles Offered: SA, CF
Commingled Fund Minimum: $10 million
Portfolio Managers/Dual Role PMs: 9
Avg. Yrs of Experience: 14
Avg. Yrs at Firm: 8
Research Analysts: 9
Avg. Yrs of Experience: 7
Avg. Yrs at Firm: 5
Fee Schedule (CF)*: 0.75%
(Performance-based fees are available)

CHARACTERISTICS

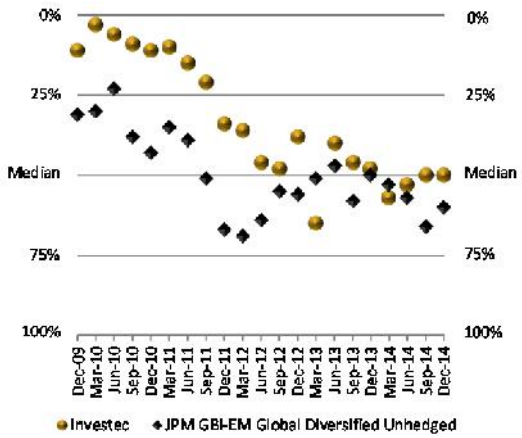
	Portfolio	Benchmark
# of Bonds:	160	195
Portfolio Turnover:	65%	N/A
Avg Credit Quality:	BBB	BBB
Min Credit Quality:	BB	BB
Duration:	4.8 yrs	4.9 yrs
Last 3 Years:		
Information Ratio:	0.7	N/A
Sharpe Ratio:	0.1	0.0

ROLLING PERFORMANCE AND RANKINGS

Three-Year Rolling/Quarterly Excess Performance vs. JPM GBI EM Global Diversified Index**



Manager vs. EM Local Currency Universe Rolling Three-Year Periods**



QUALITATIVE OVERVIEW

- Established in 1991 in South Africa, Investec Asset Management (IAM) is a subsidiary of Investec Group, which is publicly listed in London and South Africa. 15% of IAM is owned by senior professionals at the firm. Investec has been investing in emerging markets for 15 years.
- Peter Eerdmans and Werner Gey van Pittius head the 18-member EMD team. Along with PMs and analysts for both sovereign and credit, other key individuals include a currency strategist and five traders. The EMD Local team leverages broader firm resources in equity, commodity, and developed debt markets. The PMs, who average 14 years experience, have been unchanged since inception and specialize by region.
- Investec primarily employs a bottom-up process to identify relative value opportunities. Their top-down view determines beta exposure and is utilized to verify conviction in bottom-up ideas. Quantitative tools support the team's decision-making process. Currency decisions are distinct from bond recommendations. The strategy can short currencies and invest in non-index securities.
- The process considers changing macroeconomic fundamentals, valuations, and market price behavior to identify opportunities. Fundamental research studies inflation risks, drivers of economic growth, central bank policies, and politics. Valuation analysis is based on inflation, G3 and local yields, and country and currency risks. Market behavior emphasizes technical factors, such as investor positioning and supply and demand. The proprietary research is combined in a scorecard with varying weights to different factors. Diversification, top-down views, and experience determine trades. Regional PMs have broad ownership of idea implementation within respective regions.

QUALITATIVE RANKING

FIRM	-2 -1 0 1 2
Empl Ownership	
Mgmt Consistency	
Focus	
Cost	
Litigation	
Responsiveness	
TOTAL	+5

PERSONNEL	-3 -2 -1 0 1 2 3
Staff Depth	
Experience	
Stability	
Support	
TOTAL	+7

PRODUCT	-2 -1 0 1 2
History	
Size	
Growth	
Asset Split	
TOTAL	+6

PHILOSOPHY	-3 -2 -1 0 1 2 3
Philosophy	
Country/Currency	
Duration/Curve Management	
Sector Mgmt	
Issue Selection	
Derivatives	
Risk Mgmt	
TOTAL	+12

TOTAL QUALITATIVE SCORE: +30

Poor (-10) | Average (0) | Above Average (+10, +20) | Exceptional (+30)

*Summit Negotiated Fee Schedule
**Performance prior to the start of 2011 reflects the EM Debt LC Broad composite. Performance thereafter reflects the EM Debt LC Dynamic Composite.

INVESTEC ASSET MANAGEMENT – EM DEBT LC DYNAMIC

Key Differentiator: Bottom-up, relative value manager who utilizes a broad opportunity set and expertise in EM currencies to generate alpha.

- **Investment Thesis:**
  - **Local EMD Focus** – With the vast majority of assets managed by this team tied to EMD local mandates, EMD is an important source of revenue. Additionally, its large AUM in EMD assets has enabled Investec to build the intellectual capacity needed to invest broadly within the asset class. This helps avoid the need to consistently overweight large EM markets, such as Brazil.
  - **Currency Management** – Compared to other managers, Investec has greater experience in analyzing FX in emerging markets and managing currency risk. Their models are tailored for use with developing currencies, rather than G7 FX.
  - **Decentralized Decision Making** – Peter Eerdmans heads the group, but regional PMs are ultimately responsible for their recommendations. Each region has unique attributes and the team setup allows for taking advantage of infrequent opportunities to exploit inefficiencies in periods of momentum or contrarian/deep value trends.
  - **Alignment of Interest** – Senior investment and non-investment staff purchased 15% of Investec Asset Management in 1Q2013. An additional 5% is available for purchase over the next six years. The new equity ownership structure is a significant step toward retaining key professionals over the long-term and aligning remuneration of senior professionals with growth of client portfolios.
- **Risks/Concerns:**
  - **Short-Term Currency Exposure** – Relative currency positioning can include absolute negative currency views. While long-term currency trends can be additive, it is difficult to consistently generate alpha from currency tilts in the short-term. This can increase volatility of the portfolio over shorter time periods.
  - **Lesser Product –** Investec's EMD Local Dynamic strategy was launched in late-2010, but the investment process is very similar to their other strategy called "EMD Local Broad", which has eight years of history. The primary distinction between the "Dynamic" and the closed "Broad" strategy is that the "Broad" strategy can opportunistically invest 2-3% of the portfolio in highly illiquid securities.
- **Performance Review and Expectations:**
  - The strategy outperformed the JPM GBI-EM Global Diversified Index by 55 bps in the fourth quarter. 2014 outperformance wrapped up at a stellar 115 bps, despite the tough environment for emerging markets debt managers. In general, currency selection (+76 bps) drove the outperformance in the fourth quarter with positioning in Chile, Turkey, India, and China all producing at least 20 bps of excess return. Investec is running neutral to defensive posture (beta) currently on emerging markets currencies given oil related volatility and dollar headwinds. Duration is similarly being held at a neutral posture (beta) as Investec looks for greater clarity in battle between already low yields and a supportive inflation outlook.
  - Excess return expectations are 100-200 bps over the long-term; opportunistic investing in hard currency corporates and non-index countries will likely be impactful on short-term returns.

LAZARD ASSET MANAGEMENT – EMERGING LOCAL MARKETS BOND

FIRM DETAILS

Address:	30 Rockefeller Plaza, 57th floor New York, NY 10112
Phone:	212.632.6000
Asset Class:	Emerging Markets Debt - Local
Benchmark:	JPM GBI EM Global Diversified
Founded:	1970
Ownership:	100% Publicly held (Lazard Ltd.)

Assets Under Management: $178.4 billion

PRODUCT DETAILS

Inception: December 2010
Assets Under Management: $3.6 billion
Vehicles Offered: SA, CF
Commingled Fund Minimum: $1 million
Portfolio Managers/Dual Role PMs: 3
Avg. Yrs of Experience: 21
Avg. Yrs at Firm: 4
Research Analysts: 34
Avg. Yrs of Experience: 12
Avg. Yrs at Firm: 5
Fee Schedule*: 0.55%

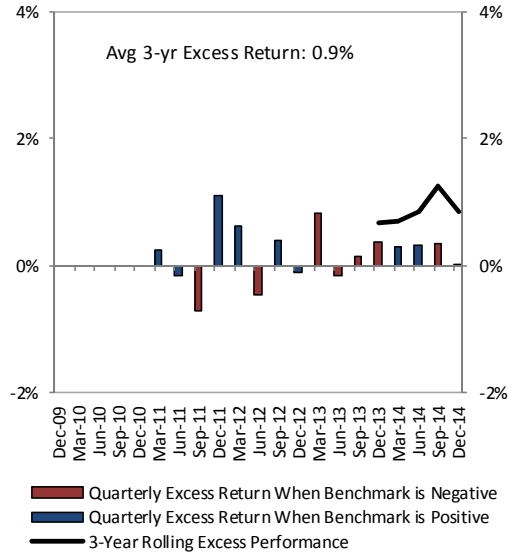
CHARACTERISTICS

	Portfolio	Benchmark
# of Bonds:	111	195
Portfolio Turnover:	64%**	N/A
Avg Credit Quality:	BBB	BBB
Min Credit Quality:	BB	BB
Duration:	4.8 yrs	4.9 yrs
Last 3 Years:		
Information Ratio:	1.2	N/A
Sharpe Ratio:	0.1	0.0

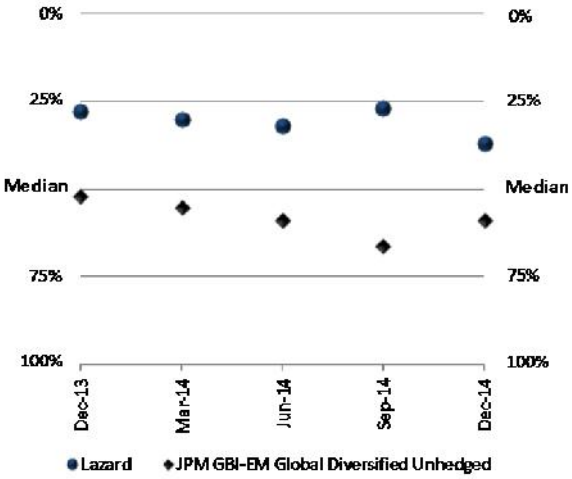
*Summit Negotiated Fee Schedule
**3Q2014

ROLLING PERFORMANCE AND RANKINGS

Three-Year Rolling/Quarterly Excess Performance vs. JPM GBI EM Global Diversified Index



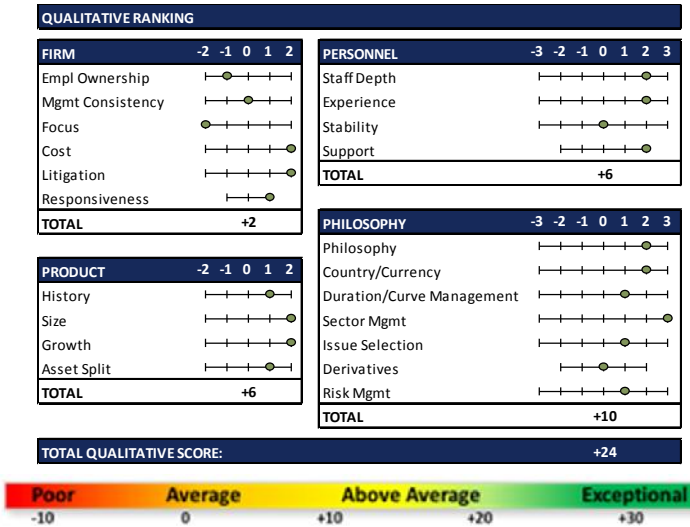
Manager vs. EM Local Currency Universe Rolling Three-Year Periods



QUALITATIVE OVERVIEW

- Lazard Asset Management is a subsidiary of Lazard Frères & Co. LLC. The parent organization is a limited liability corporation that is, in turn, held by Lazard Ltd., a publicly-traded company (LAZ). Over 100 employees currently have a vested interest in the firm.
- Denise Simon heads the Emerging Markets Debt (EMD) group and is primarily responsible for local markets. Arif Joshi, co-PM, covers hard currency sovereign and corporate products, while George Varino is the client PM. Simon and Joshi joined Lazard in late 2010 from HSBC Asset Management, where they ran a similar suite of products. The team currently manages EMD strategies, including hard, local, blend, corporate, and absolute return mandates.
- Lazard employs global macroeconomic signals to exploit cyclical trends and structural inefficiencies in EMD. Fundamental data in developed and emerging markets, risk indicators, and valuation determines positioning. The universe is broad and includes quasi-sovereign, corporate, and inflation-linked securities in local and hard currencies. Maximum out-of-benchmark and derivative exposures are 40% and 50%, respectively.
- Fundamental variables reviewed include growth metrics, inflation trends, external accounts, and global fiscal and monetary forecasts, while risk metrics analyzed are risk sentiment, liquidity, and productivity. Expected returns for country and currency are developed with consideration for volatility. Instrument selection is based on forecast for different portions of the yield curve, derivative vs. cash bond spread, and valuation of nominal, inflation-linked, and credit securities. Portfolios are stress tested for different scenarios, including spike in risk aversion, surprise in global growth and Eurozone dynamics, and large changes to commodity prices.

QUALITATIVE RANKING



LAZARD ASSET MANAGEMENT – EMERGING LOCAL MARKETS BOND

Key Differentiator: Seasoned PM team with the pulse of the broad EM universe.

- **Investment Thesis:**
  - **Seasoned Senior Team** – While the lead PMs, Denise Simon and Arif Joshi, have only been at Lazard since 2010, they started managing EMD together at Atlantic Advisors (subsequently bought by HSBC 2005) over 10 years ago. They have the distinction of being one of the first groups to launch a Total Return-style EMD fund. This alternative benchmark-agnostic framework is a distinction versus most EMD managers.
  - **Full EMD Suite** – Lazard offers a full suite of EMD products (hard currency, local currency, blend, total return, and corporate) and utilizes a single team to manage them all. This single team approach help facilitate a consistent view and recognizes the cross-currents of information in emerging markets.
  - **Meaningful Out-to-Index Opportunity Set** – Lazard makes use of inflation-linked, corporate, and quasi-sovereign bonds. The existence of a full EMD suite means the team is already aware of the broader EMD opportunity set.
  - **Separate Currency and Bond Decision** – Lazard manages currency and bond exposures to the index separately creating a richer in-index opportunity set.
  - **Attractive Fee Schedule** – Summit's negotiated fee of 55 bps all-in is attractive for the asset class, especially for an established manager of EMD assets.
- **Risks/Concerns:**
  - **Analyst Pool –** When Denise and Arif left HSBC in 2010, they brought none of their analysts. While the assembled team of eight dedicated EMD analysts does have an average of 13 years of experience, they have had less opportunity to work together than some other managers.
  - **Lazard Element** – Lazard's presence brings an aggressive market effort and, often times, rapid asset growth. This could challenge the strategy's ability to access smaller, more niche opportunities as well as its ability to shift active tilts. Additionally, as Lazard is primarily an equity firm, the degree of focus on fixed income may not be the same as at a boutique or fixed income centric manager.
  - **No Assets In Commingled Fund** – Currently, Lazard has no assets in its commingled fund. Given its separate account minimum of $100MM, Lazard may have difficulty managing the fund to mirror the current composite if the fund's asset level is low.
  - **Not Headline Product** – The team has made its name managing Blend and Total Return products and considers sector rotation, only a minor factor in a dedicated sector product, a major alpha driver in its other offerings.
- **Performance Expectations:**
  - Excess return expectations are 100-200 basis points over a market cycle.

PICTET ASSET MANAGEMENT, LTD. – EMERGING LOCAL CURRENCY DEBT

FIRM DETAILS

Address:	Moor House, Level 11 120 London Wall London, England EC2Y 5ET
Phone:	20 7847 5000
Asset Class:	Emerging Markets Debt - Local
Benchmark:	JPM GBI EM Global Diversified
Founded:	1980
Ownership:	100% owned by Banque Pictet & Cie

Assets Under Management: $151.6 billion

PRODUCT DETAILS

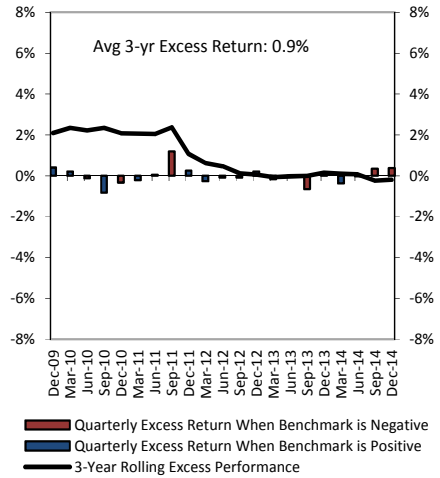
Inception: August 2006
Assets Under Management: $9.9 billion
Vehicles Offered*: SA, CF
Commingled Fund Minimum: $500,000
Portfolio Managers/Dual Role PMs: 5
Avg. Yrs of Experience: 19
Avg. Yrs at Firm: 9
Research Analysts: 4
Avg. Yrs of Experience: 11
Avg. Yrs at Firm: 4
Fee Schedule (CF)**: 0.78% on all assets
(Performance-based fees are available)

CHARACTERISTICS

	Portfolio	Benchmark
# of Bonds:	244	195
Portfolio Turnover:	66%	N/A
Avg Credit Quality:	BBB	BBB
Min Credit Quality:	BB	BB
Duration:	4.8 yrs	4.9 yrs
Last 3 Years:		
Information Ratio:	-0.3	N/A
Sharpe Ratio:	0.0	0.0

ROLLING PERFORMANCE AND RANKINGS

Three-Year Rolling/Quarterly Excess Performance vs. JPM GBI EM Global Diversified Index



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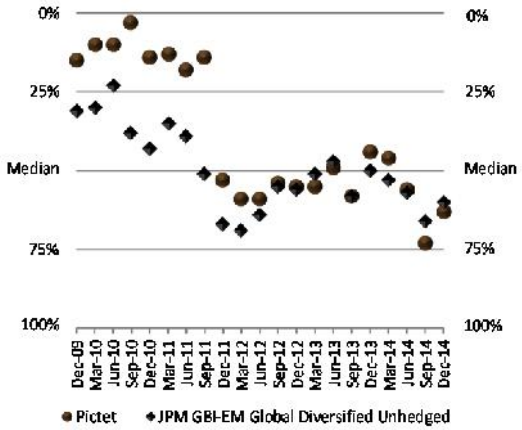
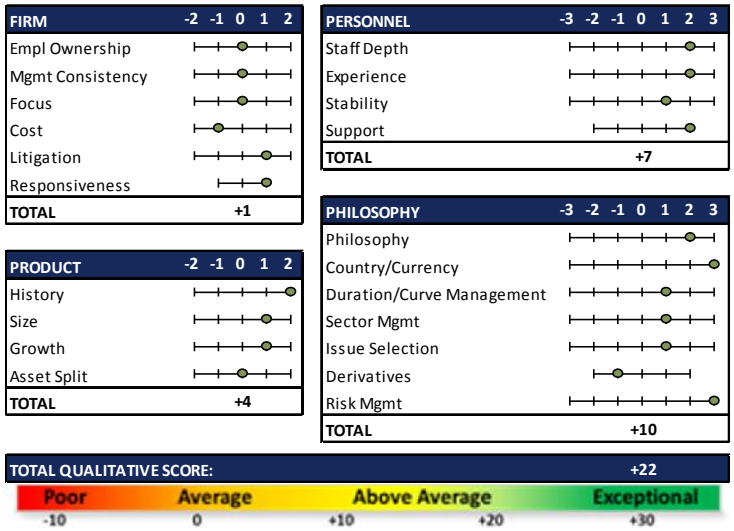


QUALITATIVE OVERVIEW

- Pictet Asset Management (PAM) is wholly owned by the Swiss bank, Pictet & Cie. The bank was founded in Geneva in 1805 and is one of Switzerland's largest private banks. PAM manages $150 billion in assets encompassing equity, fixed income, and alternatives. Most of their assets are contained in institutional mutual funds.
- Simon Lue-Fong leads the emerging markets debt team. Simon joined PAM in 2005 and has 23 years of investment experience. The five portfolio managers are divided up by regional expertise with each also conducting research. The team is supported by four portfolio analysts and four dedicated EMD traders.
- PAM follows an active approach to emerging markets debt where top-down and bottom-up analysis are equally utilized. The team does not rely on one alpha-generating strategy to come in and out of favor and will aim to outperform in all market conditions by adapting strategies. Currencies and interest rates are seen as two separate decisions.
- PAM splits their process into two distinct stages. Stage one involves developing their outlook on a macroeconomic level and deciding on regional/country allocations. The team utilizes its own Risk Aversion Index and Country Analysts Depository model to help with this stage. Stage two looks at medium/short-term catalysts to determine currency and interest rate biases and the timing of trades. The portfolio has the flexibility to add value through non-benchmark trades (30% max). This includes developed market and sector trades. When opportunities are less attractive, neutral exposures are maintained.

QUALITATIVE RANKING



*Mutual Fund managed to an adjusted benchmark exists.
**Total expense ratio is capped at 1.00%. The Commingled Fund has a 2% redemption fee if assets are withdrawn within 6 months after the initial funding.

PICTET ASSET MANAGEMENT, LTD. – EMERGING LOCAL CURRENCY DEBT

Key Differentiator: Decentralized team adjusts strategy beta to market cycles to help protect during risk-off environments.

- **Investment Thesis:**
  - **Process Adapts to Market Risk** – Due to the team's experience in various market cycles for both developed and emerging markets, Pictet modifies the portfolio to suit the different variations in the economy. For example, exposures to the rates and currencies of developed markets were increased in 2008 as Pictet's top-down view indicated greater market risk. As liquidity dried up and the volatility of risk assets increased, Pictet's positioning resulted in top percentile performance in 2008.
  - **Critical Mass of Local Assets** – Pictet's emerging markets debt assets total around $20B with 50% in their Local Currency Emerging Markets Debt strategy. The asset size provides Pictet leverage in scheduling meetings with government officials and allows the strategy to participate in small and large issues.
  - **Regionally Focused Teams** – Although the investment staff works closely to execute a consistent process, the group is split by region. Investment personnel have the latitude to develop regional research, consistent with the broader framework, and are responsible for trade recommendations within their universe. Due to the specialization, analysts develop deep expertise and incentives are directly tied to the performance of the individual and team.
- **Risks/Concerns:**
  - **Fund Assets** – A majority of the assets are tied to non-US mutual funds, which have ballooned over the past few years. Total assets from US investors are low, but growing. A large institutional base would lower substantial fluctuations in revenue that can arise from fund flows.
  - **Key Man** – Pictet hired Simon Lue-Fong to head the emerging markets team in 2005. He has made several changes to the staff and is ultimately responsible for the strategy's process and returns. Although the other senior investment personnel are qualified, Simon Lue-Fong has the most experience and is key to the successful implementation of the strategy.
  - **Non-Index Exposure** – The non-benchmark exposures, which are limited to 30%, can contribute to volatile excess returns. Pictet has invested in non-benchmark countries, currencies, and sectors.
- **Performance Review and Expectations:**
  - The strategy outperformed the JPM GBI-EM Global Diversified Index by 37 bps in the fourth quarter, bringing 2014 outperformance to 33 bps. The primary source of outperformance was positioning in EM currencies, which added 64 bps of excess return. An underweight to EM currencies in general and, specifically, the currencies of commodity dependent countries (Brazil, Columbia, and Chile) was additive. Other performance drivers were fairly muted with exposure in local rates, particularly an underweight to Turkey, costing 16 bps versus the benchmark. Looking to 2015, Pictet is positive on Asian, manufacturing based economics and underweight to more commodity dependent countries. Pictet is negative on EM currencies given the current trend in the US dollar. Overall, Pictet sees considerable idiosyncratic opportunities arising in 2015.
  - Excess return expectations are 100-200 bps over the long term.

CORRELATION MATRIX – VERSUS CURRENT FIXED INCOME MANAGERS

3 Year Correlation	Dodge & Cox Core Fixed Income	PIMCO Total Return Full Authority	State Street Global Advisors U.S. TIPS
Colchester Global Investors Limited	0.6315	0.5952	0.5078
Investec Asset Management	0.6387	0.5770	0.4904
Lazard Asset Management LLC	0.6316	0.5693	0.4866
Pictet Asset Management Ltd	0.6582	0.5993	0.5206

5 Year Correlation	Dodge & Cox Core Fixed Income	PIMCO Total Return Full Authority	State Street Global Advisors U.S. TIPS
Colchester Global Investors Limited	0.6067	0.6170	0.4343
Investec Asset Management	0.6106	0.6038	0.4235
Lazard Asset Management LLC	N/A	N/A	N/A
Pictet Asset Management Ltd	0.6081	0.6112	0.4574

CORRELATION MATRIX – VERSUS FIXED INCOME INDICES

3 Year Correlation	Barclays US Aggregate	Barclays US Corporate High Yield	Barclays US Universal	JPM EMBI Global Diversified	JPM GBI-EM Diversified Unhedged
Colchester Global Investors Limited	0.4291	0.8004	0.5486	0.8663	0.9831
Investec Asset Management	0.4119	0.8080	0.5365	0.8611	0.9833
Lazard Asset Management LLC	0.3913	0.8109	0.5175	0.8377	0.9866
Pictet Asset Management Ltd	0.4284	0.8086	0.5506	0.8511	0.9850

5 Year Correlation	Barclays US Aggregate	Barclays US Corporate High Yield	Barclays US Universal	JPM EMBI Global Diversified	JPM GBI-EM Diversified Unhedged
Colchester Global Investors Limited	0.2488	0.7600	0.4189	0.8593	0.9839
Investec Asset Management	0.2362	0.7703	0.4106	0.8624	0.9825
Lazard Asset Management LLC	N/A	N/A	N/A	N/A	N/A
Pictet Asset Management Ltd	0.2586	0.7410	0.4251	0.8485	0.9864

CORRELATION MATRIX – VERSUS EQUITY INDICES

3 Year Correlation	Russell 1000	Russell 2000	MSCI EAFE-ND	MSCI EAFE Small Cap-ND	MSCI EM-ND
Colchester Global Investors Limited	0.6272	0.4569	0.8025	0.7325	0.8700
Investec Asset Management	0.6199	0.4539	0.8077	0.7500	0.8963
Lazard Asset Management LLC	0.6296	0.4669	0.8146	0.7687	0.9039
Pictet Asset Management Ltd	0.5876	0.4203	0.7924	0.7408	0.8899

5 Year Correlation	Russell 1000	Russell 2000	MSCI EAFE-ND	MSCI EAFE Small Cap-ND	MSCI EM-ND
Colchester Global Investors Limited	0.6487	0.5716	0.7816	0.7642	0.8617
Investec Asset Management	0.6548	0.5779	0.7903	0.7730	0.8786
Lazard Asset Management LLC	N/A	N/A	N/A	N/A	N/A
Pictet Asset Management Ltd	0.6163	0.5380	0.7704	0.7637	0.8594

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