STANLIB
MULTI-MANAGER

The risks inherent in our funds

Collective Investment Schemes (formerly known as unit trusts or, for simplicity, funds) are inherently risky investments for different reasons. It is important for investors to understand this before investing. It is the duty of service providers, like ourselves, to explain these risks in clear and simple language that is accessible to a lay person, that is someone who is not a financial or investment expert. However, before investing we strongly encourage individual investors to understand these risks by speaking to their financial adviser, gathering more information and asking questions to get to an appropriate level of comfort.

Sources of risk

STANLIB Multi-Manager's funds are all exposed to multiple sources of risk. Risks are, by definition, uncertainties and these typically manifest in changes in price i.e. changes in the value of the funds or their underlying securities. Securities are financial instruments – shares in companies listed on an exchange, bonds; or loans to governments and companies. Each type of security has risks specific to that security. These risks can range from economic risks (such as growth and inflation), to interest rates going up or down, company specific risks and many others.

To demonstrate these risks more concretely, let us consider an investment in a company as an example.

These risks come in many different forms:

- **Market risk** – a generic term referring to price movements.
  If you buy a share in a company, the price of that share may move up and down on a daily basis – or even more frequently. This movement reflects the trading (buying/selling) of the company's shares and may be related to news/information about the company or the market more broadly – anything from economic to political news can, and does, affect markets. It may also be unrelated to news/information e.g. someone may just decide to invest or disinvest in the market. Some of the information may relate to something that has happened, but it may relate to the chance that something could happen.

  Unfortunately, all investors are exposed to these price movements. As professional investment managers, we understand this process allows for price discovery and creates liquidity, allowing investors to get into and out of markets and individual securities.
- **Credit risk** – the risk of default on a promise to repay a loan or bond.
- **Interest rate risk** – the risk that the fixed interest (coupon) paid on a loan may be different to (lower) future rates available in the market.
- **Inflation risk** – the risk that the principal and coupon paid will be eroded by inflation being higher than anticipated.

There are many other sources of risks and often asset managers typically use one or two metrics to track and report on risks. For example, equity risk (shares or stocks) are collectively represented by a metric called volatility.

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What does risk mean for the investment time horison?

The riskier a fund, the longer an investor should plan to be invested. Even if the time horizon is longer than say 10 years, there is still the chance that the investment may not deliver according to expectations or it may even make a loss. Therefore, the investment time horizon of a fund should be viewed as the very minimum holding period for an investor. It is important to understand that this is not a guarantee that the investor will not lose money if they hold on to the investment for that period of time. Rather, the chances of not losing money get progressively better the longer an investor remains invested.

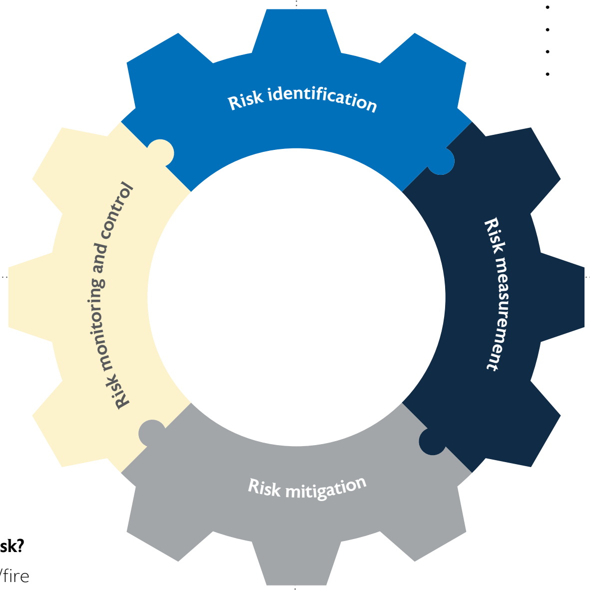
Risk Management Framework

Risk management within our funds happens holistically and at many different levels. This mitigates certain risks, but never removes them since risk is required to provide the opportunity of exceeding a cash return. To reinforce this point, we highlight that investing is a risky endeavour for which investors expect to be rewarded through returns (of capital invested and income). This expectation may translate into positive returns, but it may also lead to negative returns or losses. The greater the risks undertaken, the greater the expectation for reward.

The diagram below illustrates our Investment Risk Management Framework at a high level. It emphasises that the four main processes of risk management have a circular relationship, with continuous risk monitoring and control. This leads to further identification of risk or further clarity on risk. To better manage investment risk, the framework extends to classify the sources of risk. Since sources of risk extend across the investment process and teams, risk measurement tools and techniques are adopted across each investment function.

What is the risk?

- Manager risk
- Portfolio risk
- Market risk
- Business risk
- Liquidity risk
- Credit risk
- Regulatory risk
- Objective/goal risk



How can I measure it?

- Attribution and return analysis
- Market analysis
- Holdings analysis
- Systems

How do I monitor the risk?

- Market analysis
- Triggers/flags
- Recording/documents
- Systems and tools
- Review

What can I do to mitigate the risk?

- Underlying manager hire/fire
- Tactical tilting
- Use of derivatives
- Overlays

How we go about mitigating risks

- We employ qualified and experienced staff with the capability and experience to form well-rounded investment decisions. Further to this, we invest in the growth of investment knowledge and continuing professional development.
- A critical component of executing on client mandates is the specification of the objectives and constraints of the portfolios to be constructed. These are comprehensively described by the Portfolio Management Guidelines (PMG).
- We use high quality data sources that are trusted and as far as possible, automate the upload of the data.
- We build quality investment analytical tools that assist with analysis of the funds from both a performance and an underlying holdings perspective.
- During portfolio construction, we size the percentage allocated to an underlying manager using a framework of house factors and style. For example, a manager with a more uncertain or more variable return profile, would get a smaller allocation in the fund.

- Each fund goes through a formal portfolio review at least three times a year. During this process the fund is measured against the PMG.
- The investment process requires documentation at various stages and allows for the interrogation of ideas by numerous members of the team, as well as ensuring the investment team members share a common understanding. We produce documentation of a high standard, which is suitable for both internal and external consumption.

Risks and returns are inextricably intertwined

As a multi-manager, our funds have their risks managed by underlying managers, who are mandated to invest on behalf of our investors and ourselves through portfolio construction (portfolio design and execution through various underlying managers). Both parties have systems and processes which are focused on the risk management function. This ensures that we are only taking risks for which we expect to be rewarded, as well as ensuring that these risks are of the right type and magnitude both on an absolute basis and an overall fund level.

If you have any queries or require further information, please do not hesitate to contact us or your financial adviser. **We emphasise that investors should be comfortable that they understand the risks inherent in our funds and that these are appropriate for their investment objectives.**