The Better IR Newsletter

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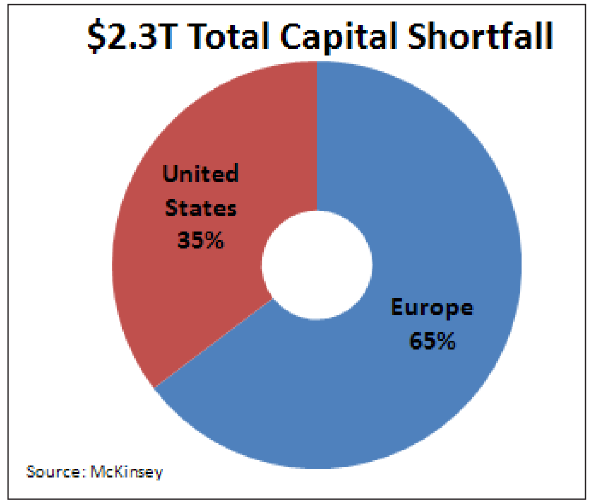
The Basel (III) Effect

Basel Framework

As of September 2010, the Basel Committee endorsed new recommendations regarding capital and liquidity adequacy requirements for the broad global banking system to be implemented as early as 2013, in some instances. The new accords come in the wake of a global banking crisis and seek to minimize banks dependence on short-term funding from other lenders that froze during the crisis. The treaty, more commonly referred to as Basel III, will require a sharp increase to the minimum core Tier 1 capital ratio from its original recommendations, as well as include a safety buffer to further pad a bank's capital position. Moreover, for the most interconnected of banks, the committee went a step further, requiring an extra capital charge on top of the aforementioned requirements.

As a result of the new requirements, the total capital shortfall across the European and North American banking systems will equate to approximately $2.3T, according to a recent McKinsey & Co. report. Inherently, European domiciled-banks will require a larger share of the total fresh capital needed as a result of its size relative to its North American counterparts and its recent sovereign debt woes, which is constraining the availability of fresh capital. Though the accords are not a formal treaty and at times discounted by participating members, as in the case with the United States largely disregarding Basel III's predecessor, the requirements will be used as a framework for many domestic policies. Accordingly, we anticipate a rush of Basel-induced capital raising as implementation periods approach in the ensuing years. In addition, the events of August and September 2011 weigh on the minds of many European banks; regardless of whether governments intervene or not banks will seek to shore up capital positions.



Capital Raising So Far and the Pipeline

Since the Basel Committee for Banking Supervision specified its specific details for capital requirements in September 2010, more than 110 issuers in the Financials sector worldwide have tapped the primary markets for close to $164B, with the stated use of proceeds ranging from general corporate purposes, to as detailed as using the raised capital to boost core capital ratios ahead of regulatory changes. Looking closer at these 110 deals, European banks have recorded some of the largest offerings in the group, headlined by Commerzbank AG's $7.8B rights issue in June 2011, Standard Chartered's $5.3B placement in November 2010, and Bank of Ireland Group's $2.8B offering in July 2011, according to Ipreo research. Looking to the future, it seems probable that the push for banks to raise capital to bolster their balance sheets will intensify as euro zone financial health problems push on and pressure mounts on European banks to adhere to regulatory requirements. Currently, the global pipeline for filed or expected deals in the Financials sector reveals 54 issuers looking to raise over $37B in proceeds as of 9/13/11, accounting for nearly 26% of the 326 deals ($147B) in the global pipeline spanning every sector, according to Ipreo research. Breaking out the filings in the Financials sector on a country by country basis, European banks account for around 16% of the total filed proceeds, while Chinese issuers dominate the current six-month backlog with about 60% of the total filed proceeds, headlined by seven billion-dollar plus filings. With many European banks yet to disclose their exact capital needs, as well as the typically short file-to-offer process for secondary offerings, the "rumored backlog" of European banks believed to be considering equity offerings in the near future but have yet to file could amass as issuers wait for an opening in the market.

Institutional Activity

Full compliance of Basel III's Tier 1 capital requirements will take full effect in January 2015, with the conversion buffer fully implemented by 2019. However, details stipulate that readiness to report and planned processes will be required for regulators as early as 2013. As a result, we anticipate a rush of capital cushion-induced equity offerings in the ensuing years prior to full implementation. Moreover, the 110 banks raising nearly $164B have already been proactive in their efforts to meet requirements, trying to capitalize on a finite amount of capital before the ensuing wave reacts. Furthermore, and perhaps more importantly in the short-term, many banks have indicated a desire to increase their capital position as a reassurance to markets and rating agencies in an effort to increase flexibility in the face of impending regulation and in a time of heavy volatility. For instance, U.S.'s largest bank, Bank of America, recently sought a $5B capital injection from legendary investor, Warren Buffett, to signal a sign of confidence in the bank's capital position. Consequently, tapping the equity markets early may be the key to a smooth transition into the new era of global banking regulation as well as instill confidence throughout the investing community.

Since the agreement was reached late last summer, Ipreo has tracked the institutional activity revolving around the plethora of banks that have already tapped the equity markets in an effort to anticipate Basel III requirements prior to formal implementation. Leveraging the results, Ipreo was able to identify investors that have the best ability to participate in such offerings and those that may shy away. In addition, a complementary analysis was conducted taking a look at an investor's allocation to Financials relative to the broader market, and its current weight relative to its historic averages in the space to adequately address those investors with a propensity to increase allocations to capital raising banks.

Top Cumulative Buyers of Capital Raising Banks (Trailing 4 Quarters)

Investor Name	Equity Assets ($M)	Style	# of Sec. Held	Value Change ($M)	Region	Wght. of Fincl's vs. S&P 500	Curr. Wght. vs. Hist. Avg.
Fidelity Management & Research Company	607,178.4	Growth	50	3,770.3	North America	Neutral	Underweight
Temasek Holdings Pte., LTD	91,810.5	Value	7	3,580.3	Asia	Overweight	Overweight
Norges Bank Investment Management (Norway)	323,593.3	Value	62	2,745.3	Europe	Overweight	Underweight
Wellington Management Company, LLP	306,381.7	Value	64	2,208.2	North America	Neutral	Underweight
Capital Research Global Investors (U.S.)	437,578.3	GARP	17	1,954.5	North America	Underweight	Underweight
Capital World Investors (U.S.)	414,542.8	Value	25	1,508.1	North America	Neutral	Underweight
J.P. Morgan Investment Management, Inc.	124,151.8	Value	63	1,027.8	North America	Overweight	Underweight
Janus Capital Management, LLC	83,676.9	Agg. Growth	7	852.8	North America	Overweight	Overweight
TIAA-CREF Investment Management	188,309.4	Index	80	803.4	North America	Overweight	Neutral
Carmignac Gestion	36,752.2	Growth	5	789.7	Europe	Overweight	Neutral

Source: Ipreo

Of the most active institutions over the past four quarters, Boston-based Fidelity Management & Research was the most prevalent, active in nearly half of the overall offerings amounting to $3.7B invested in banks. The $607B firm's Financials allocation is currently neutral-weight relative to the broader market, though underweight relative to its historic average in the space, signaling the ability to increase its exposure further. However, a large portion of the firm's allocation over the study periods came within North American issuing banks. Similarly, Boston-based Wellington, and Norway's sovereign wealth fund, Norges Bank Investment Management, exhibited a propensity to invest in capital raising banks, each playing a part in over half of all the deals over the past four quarters.

As previously alluded to, European banks will see the largest short-fall of capital due to its sheer size relative to the North American banking system. In addition, recent fiscal disruptions will exacerbate any constraints regarding the ease of raising capital from the investing community as overall pessimism dominates the environment. Consequently, European-domiciled institutions should capitalize on any opportunity presented prior to the impending rush on available capital granted European firms have thus far been slow to respond to the new requirements. Of the European deals since Basel III's inception, German-based Allianz Global Investors Kapitalanlagegesellschaft was most active in terms of dollar value invested and is currently notably underweight Financials relative to its historic weight in the space. Similarly, another German investor, Deka Investment, exhibited its interest in European capital raising banks, active in nearly half of European deals. Though the firm is currently moderately overweight relative to its benchmark, it is moderately underweight compared to its historic allocation to the Financials industry.

Top Cumulative Buyers of European Capital Raising Banks (Trailing 4 Quarters)

Investor Name	Equity Assets ($M)	Style	# of Sec. Held	Value Change ($M)	Region	Wght. of Fincl's vs. S&P 500	Curr. Wght. vs. Hist. Avg.
Allianz Global Investors Kapitalanlagegesellschaft mbH	35,919.9	Growth	13	665.5	Europe	Overweight	Underweight
Norges Bank Investment Management (Norway)	325,846.4	Value	18	512.4	Europe	Overweight	Underweight
Fidelity Management & Research Company	591,133.1	Growth	9	421.7	North America	Neutral	Underweight
Capital Research Global Investors (U.S.)	426,729.4	GARP	2	387.3	North America	Underweight	Underweight
Deka Investment GmbH	27,515.7	Value	13	365.4	Europe	Overweight	Underweight
BlackRock Advisors, LLC	265,164.5	Value	15	346.2	North America	Overweight	Neutral
BlackRock Investment Management (U.K.), LTD	291,456.9	Growth	16	331.4	Europe	Overweight	Neutral
Amundi Asset Management	65,948.0	Value	15	314.8	Europe	Overweight	Underweight
J.P. Morgan Asset Management (U.K.), LTD	90,217.6	Growth	17	215.7	Europe	Overweight	Underweight
DWS Investment GmbH	63,867.2	Value	14	209.5	Europe	Overweight	Neutral

Source: Ipreo

In Summary…

Christine Lagarde, Head of the International Monetary Fund, has drawn further attention to the issue recently and has explicitly come out and called for banks to be forced to raise more capital as the world economy enters a "dangerous new phase." In light of the crisis affecting the European economy, IROs of European banks should begin to remain keenly aware of the markets as they consider the timing of equity placements. Looking back to a similar circumstance in 2009, U.S. banks were starved for capital and were being forced to comply with new capital requirements in an attempt to shed U.S. government support. A stabilizing market in the spring of 2009 provided an opening for banks to raise north of $37B in accelerated secondary offerings in a matter of just four weeks between mid-May and the start of June. Should an opening emerge in the European markets, any rush to raise capital may subsequently dry up investors' appetite for shares in the Banking space and increase the competition for Banks looking to attract the remaining investor dollars.

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Examining the Hinges of the IPO Window: Learning from Recent Market Disruptions

In August, the slowest IPO market since May 2009 fueled talk that the "IPO window" is closed, as well as speculation as to when it will re-open. While it is impossible to predict exactly when the IPO market will pick up again, looking back at some recent periods when the window appeared closed may shed some light on the situation.

Methodology

We began by looking at the number of priced IPO deals by month, going back to 1990 using two data sets. Data from 2001-2011 is from Ipreo's Equity Deals Database, while 1990-2000 information comes from the Field-Ritter dataset of company founding dates, compiled by Jay Ritter, Cordell Professor of Finance at the University of Florida. Next, we calculated an average number of IPOs for each month of the year for each dataset. We then overlaid that information with the performance of the broader equity markets, looking for periods where the S&P 500 declined by 10% or more over a rolling 20 day period, which we defined as "disruptions." These disruptions aligned closely with the beginning of periods of below-average IPO volume. We defined a "closed window" as a period following an S&P disruption in which IPO deal count fell and remained below its calculated monthly average. The length of the closure period was measured from the first month after the start of the decline (In most cases the same month in which the decline took place) to the month in which deal volume again reached average levels. This left us with eight window closures and a few aftershock periods. We then examined these periods for patterns and lessons that could be applied to the current economic situation.

Lessons From Past Closures

The length of closed periods varied widely, from three months in several instances, to more than two years surrounding the global financial crisis of 2008. The average closure since 1998, excluding the 2008 crisis (a statistical outlier), was just under five months and 2/3 of closures lasted for six months or less. Upon closer inspection, a few more patterns emerged:

Sell-Offs Correlate With Window Closures

There's a reason we picked S&P 500 declines of 10% or more as our criteria for a window-closing disruption: with only one exception in the past twenty years, such a decline in equity markets has always been followed immediately by a closed IPO window. A steady rise in the S&P 500 and broader equity markets is also associated with the window re-opening. In that sense, equity market performance can be considered the "hinges" that move as the window opens or closes. The lone exception to this trend is a weak one at that: in March 2000, the Tech Bubble burst and the markets began to decline sharply. Two more months of above average, but declining, IPO volume followed before a four month stretch below average. Furthermore, in only one instance did a window re-open before a selling period ended: In October 2002, the selling that began in July continued, though the IPO market saw the first of back-to-back slightly above average months. Following that brief opening, deal volume dropped below average again for eight straight months. Even with these two slight exceptions, it remains the strongest pattern we found: the IPO market will typically close when equity markets fall dramatically.

Macro Disruptions Contribute

Events that lead to disruption in the macro-economic environment are good indicators of coming window closures. If equity markets are the IPO window's hinges, then macro events are like the oil that can allow the window to open and close more quickly. Every major IPO downturn in the past twenty years has come amid shaky economic conditions or just after events that fuel uncertainty about future economic trends. The table at right and the graphs below show some of these disruptions and the window closures that resulted. Today, continuing debt problems in Europe, a divided and conflicted Congress and S&P's downgrade of U.S. debt have contributed to tumultuous markets that may have once again signaled the closing of the IPO window.

IPO Window Closures, Jan 1990 - Aug 2011

Start of Disruption	Window Closure (Months)	Macro Event
Jan 1990	15	Oil Price Shock & Gulf War
July 1998	8	Russian Financial Crisis and collapse of Long Term Capital Management
Mar 2000	3	Tech Bubble bursts
Mar 2001	3	Recession following Tech Bubble
Sept 2001	6	9/11 Attacks
July 2002	3	Latin American Financial Crisis
Jan 2003	6	Latin American Crisis aftershocks, run-up to Iraq War
Jan 2008	26	Global Financial Crisis
May 2010	3	Greek credit downgraded after bailout, beginning of European Debt Crisis
Aug 2011	??	US debt ceiling debate, S&P US credit downgrade, European Debt Crisis continues

Every Sector Shares the Same Fate

Over the past decade, no particular sector seems to typically suffer more in a downturn than others. Likewise, no one sector appears to spring back any more quickly than others on average. The hit each industry takes and how it recovers varies. For example, following the September 11 attacks, Financial offerings dominated the IPO market and it was the only sector to produce any IPOs for two months, however, Financials have been affected similarly to other industries during most slowdowns. Trends and conditions within a given sector provide a better gauge of when and how strongly that sector will bounce back than do patterns from previous window closures.

Equity Markets Usually Bounce Back First

In every case we examined, equity markets began to climb back from their post-decline lows before the IPO window reopened. In most cases, the S&P 500 was at least back to the level at which the window closed, though typically higher. A notable exception to this pattern is the 2008 crisis. The S&P peaked above 1,500 just before the major slowdown that signaled the start of the crisis and has not returned to that level since. A few periods, such as the closures following July 2002 and May 2010, saw IPO volume return to normal before markets bounced back fully, however, IPO volume well above monthly average levels was not seen again until markets climbed above their pre-closure levels. In addition, since 1990, monthly IPO volume has not climbed above average following a window closure in a month where the S&P finished down.

No Sudden Recoveries

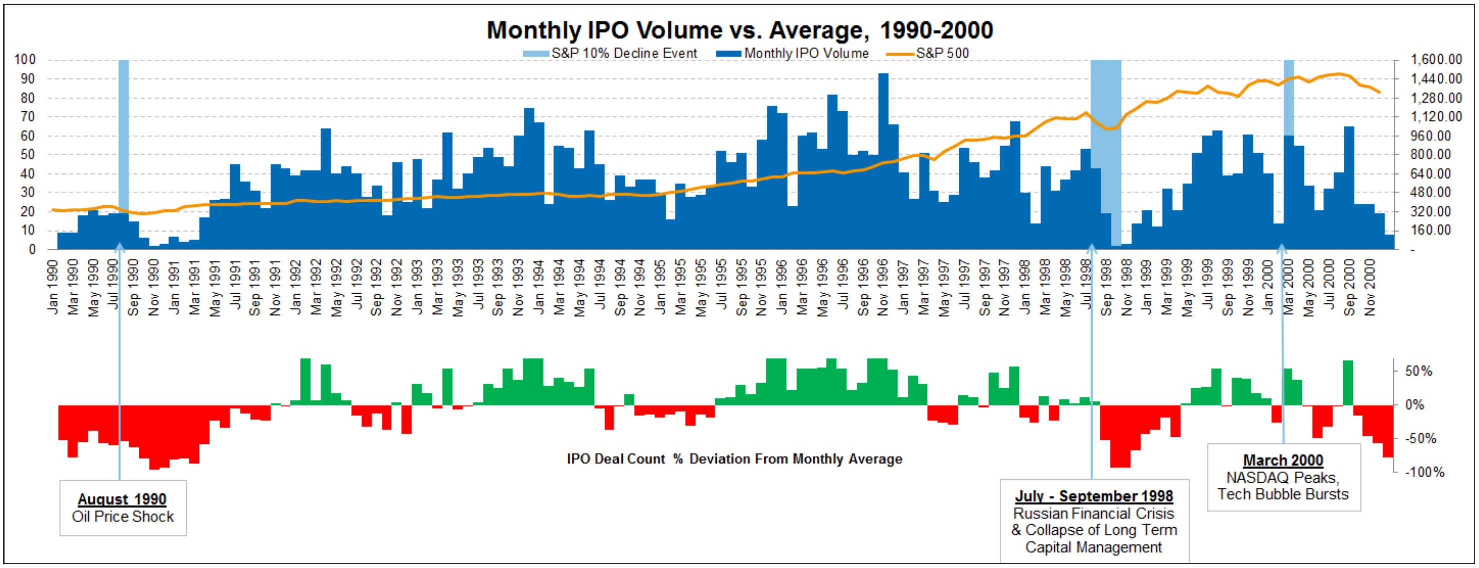
In no case did we see IPO volume suddenly jump from a major low to a major peak. Every rebound was a process of moving back towards normal over a period of a few months. The growth wasn't always constant, but every closure showed a general trend of slowly pushing upwards towards average. Furthermore, the first post-closure month in every case represented a slight increase over average, rather than a sudden IPO bonanza.

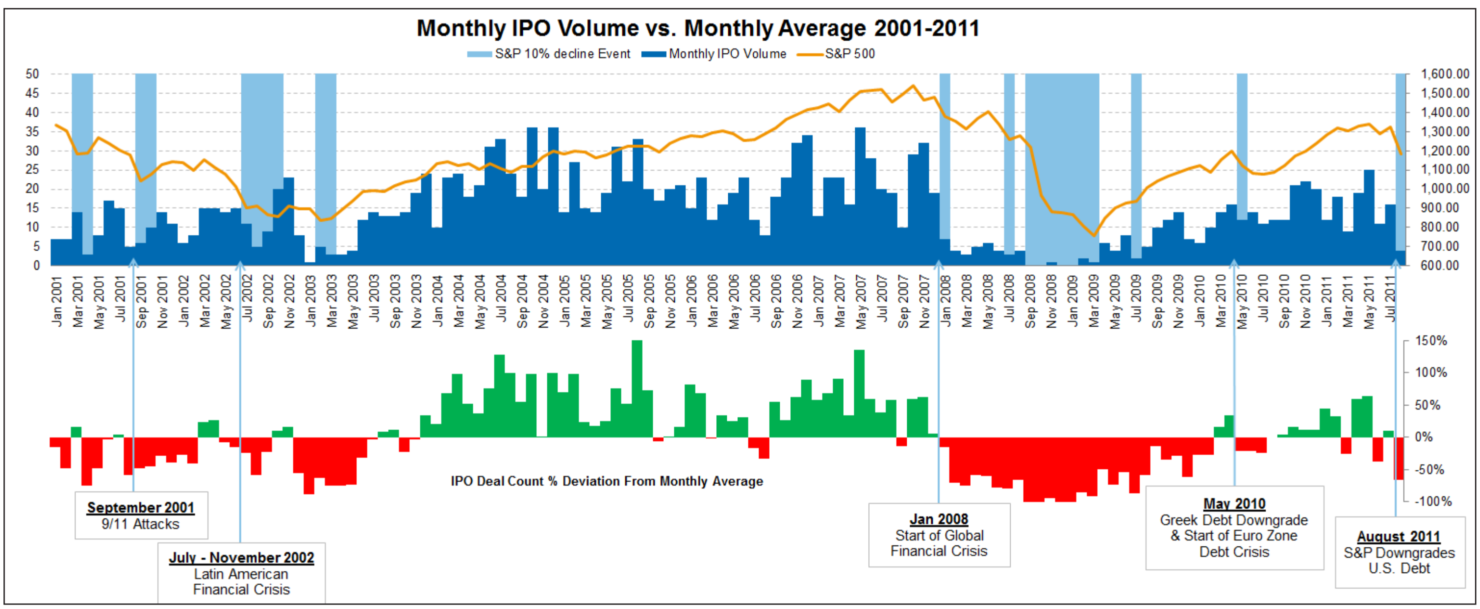
What Does this Mean For Today?

Every situation is different and past trends are no guarantee of future events, but we can make some broad predictions about what is likely to happen generally in the IPO market in the coming months:

1. We appear to be in a closed window period. IPO volume in August fell well below its monthly average and the signs that usually accompany the start of an IPO slowdown, a major macro event that fuels uncertainty (S&P's U.S. credit rating downgrade, European debt crisis or the U.S. debt ceiling debate) and a decline in equity markets, also appeared.
2. Prior slowdowns have typically lasted for a period of a few months. If today's trends follow the established pattern, we would likely see a similar window closure, though a strong current IPO backlog could potentially push the window back open sooner than expected.

3. It is possible for one or two industries to bounce back quickly, but we cannot forecast which ones based on past trends. The individual characteristics and conditions of each industry will be better predictors of recovery.
4. Equity markets have come off their mid-August lows a bit, but the IPO window is unlikely to reopen until the markets find their legs again and begin a steady climb again. Once that happens, however, the IPO market could follow quickly behind.
5. Investors and issuers hoping for the IPO window to blow back open soon may be disappointed. Past precedent would suggest that a recovery will take the form of a gradual increase in IPO volume back towards normal levels over a period of a few months.





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High Frequency Trading, Volatility, and Settlement Capture Rate (SCR)

What Do We Know So Far…?

As we've seen from prior work, we know the share of overall trading volume taken up by traditional institutional investors has fallen fairly drastically over the last five years, with a broad range of shorter-term and high-frequency traders making up what some believe is a majority of all volume across the US exchanges. The Institutional Capture Rate (ICR), last visited in BetterIR in March 2011, has given us a good view as to the impact of shorter-term traders relative to those of institutions in terms of accounting for overall volume over time. We know through the analysis of ICR that large caps are seeing a much higher percentage of total volume sourced from HFT and other short-term traders than small caps, and that in these cases "liquidity begets liquidity."

But what does this mean for day-to-day trading? How does the IRO answer the CEO's phone call with any useful response that doesn't involve just last quarter's data? These answers may be easier to come by after talking to your market surveillance firm, and can give you a much better picture of what's actually happening in the market.

Trade Settlement and HFT

Market intelligence firms that track trading in specific securities typically start off each week with the roadmap of the previous week's settled trade information (T+3), as reported in by the Depository Trust Company (DTC). The surveillance analyst will generally have, each Monday, a picture of the impact of all settled trades in the prior five trading sessions (everything up through the prior Tuesday's trades will have settled into their final homes, either broker or custody bank, after completed trades) and which banks/brokers these shares have settled into.

Generally the first exercise to conduct is a view of which banks/brokers have shown the largest increases and decreases in ownership over the prior week, giving a good starting point for identifying the institutions behind the actual buying and selling. After excluding the effects of stock loan activity, the analyst will review the total amount of share movements that settle intercustodially, moving from one bank/broker to another. However, this excludes any share movements that take place in which either:

a) the buyer and seller both hold shares at the same broker/custodian, or

b) the buyer or seller reverses its position intraday, and closes it before the end of the day, leaving zero impact to the broker/custodian's position.

As you might guess, most HFT shops fall into category B, and rarely expect to make it past a closing bell with an open position.

Settlement Capture Rate

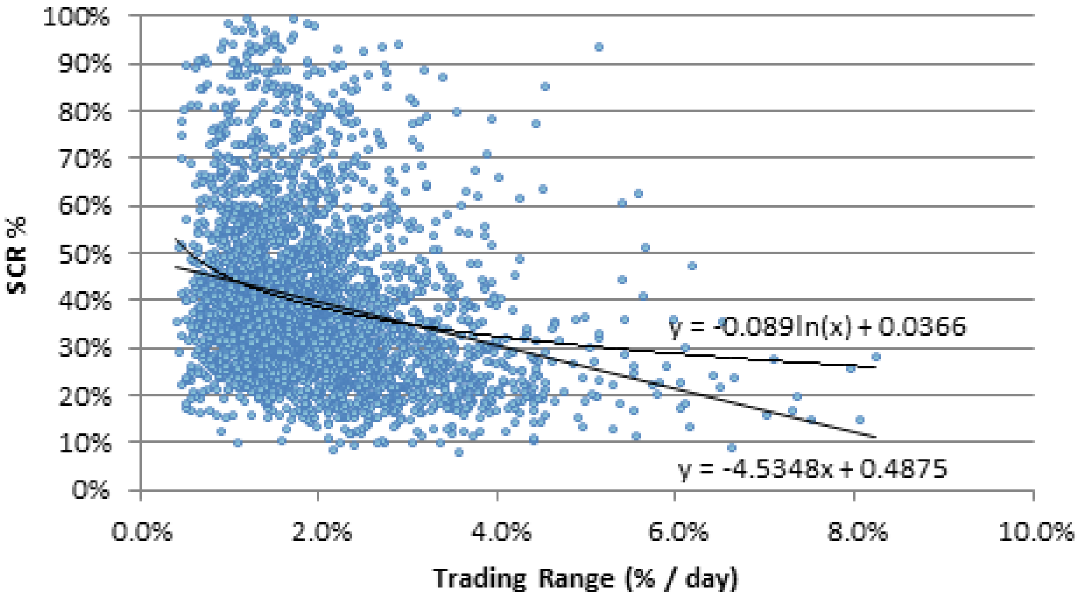
The impact of this group B, above, appears when comparing the percentage of trading that settles intercustodially with the volume traded on higher-volatility trading sessions versus lower-volatility sessions. The calculation is a cousin to Ipreo's Institutional Capture Rate calculation, but can be viewed on a daily basis. If you express the total amount of trading that can be seen through increases or decreases in DTC positions as a percentage of volume, a similar calculation can be created:

SCR for Date x = (AVG (Increases in DTC Positions, Decreases in DTC Positions)) / Volume for Date x

An interesting phenomenon appears when you compare the SCR with the volatility seen across a number of trading sessions. Ipreo uses a simple trading range calculation, [(High Price minus Low Price) / Close Price] as a useful proxy for volatility for the day's trading. Using a sample of all of Ipreo's issuer clients across the second quarter of 2011's trading, we see a consistent inverse relationship between higher volatility and lower SCR. Conversely, on dates with narrower trading ranges, we see higher overall Settlement Capture Rates. As with the ICR calculation, the lower the SCR, the higher a percentage of trading we'd expect HFT to represent. Therefore, the data shows a consistent relationship between high volatility and heavier HFT participation.

As we've seen before, HFT is generally more prevalent in large-cap stocks than in small caps – and the SCR analysis supports this theory quite well. Large cap stocks show the biggest declines in SCR on higher-volatility sessions – with a slope of 4.5 across the best-fit regression line suggesting that on average, each additional percentage point of volatility during a trading session results in 4.5% fewer percentage points of volume that will settle intercustodially (and potentially a similar-sized increase in HFT).

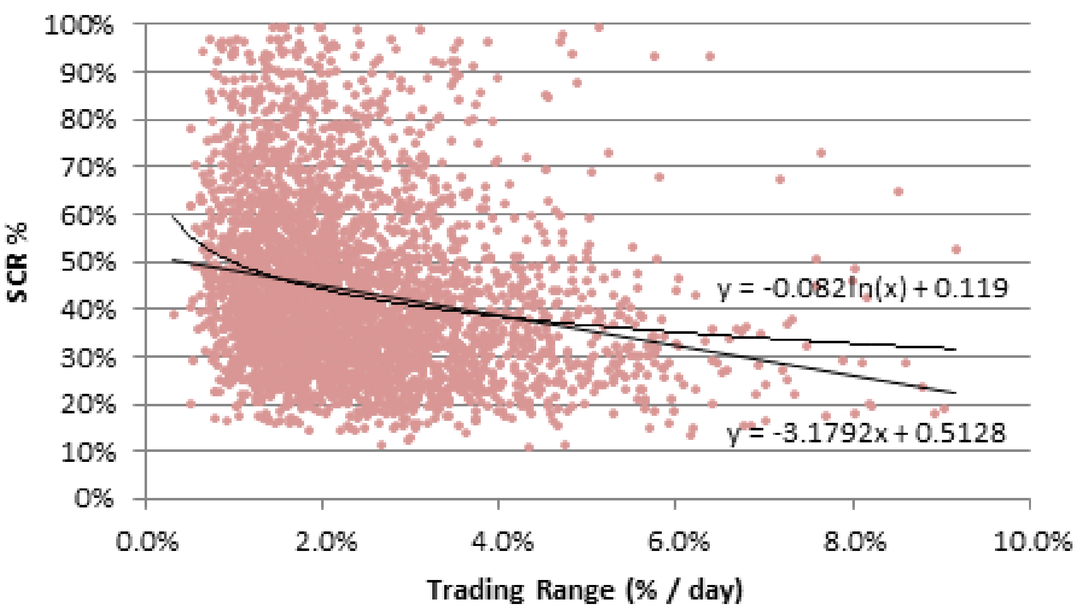
Figure 1 – Large Cap Issuers SCR vs. Trading Range, 2Q11



Source: Ipreo Research

As seen in Figure 2, below, mid caps also show this relationship, with a slope of 3.2 suggesting a slightly lower impact of volatility leading to additional HFT. For mid caps, 1 % of additional volatility equals 3.2% decrease in SCR (and likely a similar increase in HFT participation).

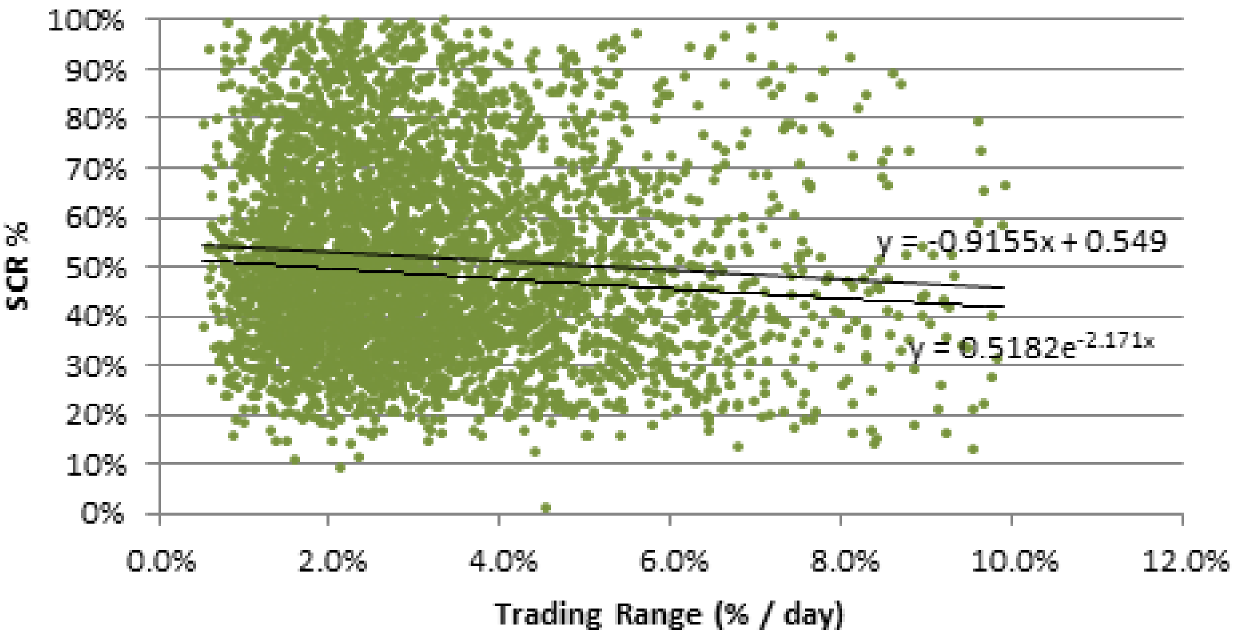
Figure 2 – Mid Cap Issuers SCR vs. Trading Range, 2Q11



Source: Ipreo Research

Small caps, as we might suspect from our prior analysis around ICR, show a much weaker relationship – just 0.9, with much more dispersion in results. Of course, "illiquidity begets illiquidity" to the same extent that "liquidity begets liquidity," and small-cap stocks tend not to offer many profit opportunities for high frequency traders, overall leaving a higher percentage of trading sourced back to traditional institutional and retail investors.

Figure 3 - Small Cap Issuers SCR vs. Trading Range, 2Q11



Source: Ipreo Research

All in all, the thesis supported across all three groups is – higher volatility equals a higher percentage of trading volume sourced to HFT.

What does this mean for the IRO trying to understand the daily impact of HFT? First, it's worth looking at both a longer-term benchmark and the short-term basis; calling up your surveillance firm can give you an idea what the typical SCR is on a highly-volatile trading session versus a less-volatile session, and give you an idea of what percentage of volume may be sourced back to large institutions. Second, be sure management is aware that while HFT has a broad impact on volume, its long-term impact on the stock price is limited – HFT's are, of course, price takers, not price makers, and institutions are more likely to be moving the stock price, while other traders attempt to make a few pennies here and there off the fact that the institution is moving its position.

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BetterIR - Firm Snapshot

Targeted Firm: Sands Capital Management ($16,996.37mm EAUM)

Targeting Profile:
Sands Capital Management was founded in 1992 by Frank Sands Sr. in Arlington, Virginia. Sands Sr. is now the chairman of Sands Capital, while his son, Frank Sands Jr., oversees investment decisions as CIO. The firm sub advises several of the Touchstone family of funds, including the Touchstone Sands Capital Institutional Growth Fund, ($1,473.18M) and the Touchstone Sands Capital Select Growth Fund, ($1,185.1M) as well as separately managed accounts and institutional assets. Furthermore, the firm manages a portion of the U.S. assets of Ikano Fund Management S.A. The firm's underlying strategy is growth-oriented, as it typically seeks companies with solid long-term earnings growth potential and innovative product offerings. Research is handled on a sector specific basis, with each sector assigned a dedicated research team. Sector specificity is important, as Sands finds broad industry trends to be an important investment catalyst.

Sands Capital arrives at investment decisions based on six key criteria: sustainable above-average earnings growth, leadership position within the industry, significant competitive advantage, a clear mission, financial strength, and rational valuation relative to the market. Companies lacking these characteristics will likely be disregarded from consideration. Moreover, the firm frequently reassesses its holdings and will swiftly exit a position if any of these qualities are no longer satisfied; as it did last quarter selling over 5M shares of Cree, representing nearly 5% of shares outstanding. For the most part, the firm exhibits a long term investment horizon, as evident from the average equity holding period of over three years. Sands Capital also tends to hold a concentrated portfolio, with an average of only 25-30 positions comprising each of its funds. Sands top 5 positions, which include Salesforce.com, ($1,291M) Amazon.com, ($1,272M) Visa, ($1,108M) Qualcomm, ($1,073M) and Apple, ($1,023M), make up nearly 35% of the total portfolio.

How to Approach:
Sands Capital Management's portfolio average 5 year growth rate of 20.6% significantly contrasts the S&P 500's 12%, thus signifying the partiality towards growth-oriented securities. The firm is willing to pay a premium for this potential growth, as evidenced by a portfolio average forward P/E ratio of 25.6X, well above the S&P 500's average of 12.4X. The firm's portfolio is biased toward the Technology and Consumer Services sectors, which make up 50% of portfolio holdings. Furthermore, Business Support Services (+$175M) and Travel & Tourism (+$109M) have seen the greatest investment inflows from the firm as of late. Sands Capital also runs the Life Sciences Innovators Portfolio, which invests strictly in Healthcare and Biotechnology firms that fit Sands growth investment profile. Firms in the Healthcare, Technology, and Consumer Services sectors with strong growth potential and innovative product offerings will likely find a receptive audience in Sands Capital. The firm also tends to invest in stocks that have already seen significant price appreciation and look primed to carry on this positive momentum.

How not to Approach:
Sands Capital is typically not interested in mature companies that pay a high dividend. The average dividend yield of Sands Capital's holdings is only 0.5%, compared with the S&P 500's 2.3%. The firm avoids small-cap investments, as these make up less than 1.5% of their total portfolio. Sands Capital also shies away from investments within the consumer goods (3.1%) and basic materials (2%) sectors, of which they only hold 7 positions combined. Moreover, Sands Capital invests almost exclusively in United States domiciled equities, which make up 97% of total holdings.

Largest Funds Managed:
- Touchstone Sands Capital institutional Growth Fund ($1,473 mm); Frank Sands; Frank Sands Jr.
- Touchstone Sands Capital Select Growth Fund ($1,185 mm); Frank Sands Jr.

Portfolio Fundamentals:
- Forward Price/Earnings: 25.6x
- 5 Yr Projected Growth Rate: 20.6%
- Dividend Yield: 0.5%
- Price/Book: 6.1x

Average Equity Holding Period: 3.5 Years

BetterIR - Fund Snapshot

Targeted Fund: JPMorgan Intrepid America Fund

Portfolio Managers:
- Christopher Blum
- Jason Alonzo

Targeting Profile:
The largest of the Intrepid funds, The $1.7B JPMorgan Intrepid Fund is primarily managed by Christopher Blum, who is the CIO of the firm's behavioral-finance group, and manages approximately $8B within the Intrepid Fund platform. By nature of the behavioral finance ideology, the fund tends to take a contrarian view of the markets, seeking undervalued securities that are out-of-favor within the investor community, often diverging from the "herd mentality". Inherently, the fund attempts to recognize how human behavior interferes with rational investing, and seeks to capitalize on the repeated systematic and predictable mistakes that investors make as a result.

Likewise, the fund also looks to identify momentum plays, as it tries to undergo the positive impetus of a given security. In light of this strategy, the fund does not demonstrate long term investment horizons, and is likely to sell out of a security when it believes it is of fair market price. In addition, market capitalization plays a quintessential role in the investment strategy, as the fund favors securities with market capitalizations over $1B. Characteristically, the fund selects stocks encompassed in the Russell 1000 index, which has a median market capitalization of $5B. In regards to industry allocation, the firm diversifies itself broadly across the spectrum of sectors, and does not display an obvious bias towards any specific industry.

How to Approach:
Garnering significant interest from Christopher Blum and his team calls for a few minimum requirements. The fund apportions 97% of its assets to US domiciled securities and 99% of its assets to companies with a market cap of $1B or greater. With this being said any company falling outside of these criteria will likely be disregarded. In addition, the fund seeks companies included in the Russell 1000 index, another important factor to consider. Although the firm diversifies itself across all industries, the Financial Services (+$23M) and Health Services (+$9M) industries have observed optimistic buying as of late. Important to note, the firm is inclined to invest in undervalued securities trading at low price to earnings ratios. Furthermore, the average Forward P/E of the JPMorgan America Intrepid Fund is just 10.2x, signifying the funds bias towards the Russell 1000's "cheaper" securities, which has an average forward P/E of 12.9x.

How not to Approach:
As mentioned above, the fund selects larger capitalization companies included in the Russell 1000 index. Thus companies falling outside of this criterion or companies with higher P/E ratios are likely to be excluded from consideration. Furthermore, although the Technology sector encompasses the largest portion of the portfolio, the industry saw a net sell of $2M. Much of this selling however, can be attributed to sells present in the Technology Hardware & Equipment and Telecommunications industries. Moreover, the fund does not typically invest outside of the US, as non-US securities comprise only 3% of the portfolio.

Portfolio Fundamentals:
- Forward Price/Earnings: 10.2x
- 5 Yr Projected Revenue Growth: 11.5%
- Dividend Yield: 2.1%
- Price/Sales: 1.7x

Average Equity Holding Period: 8 Months

Metro Area Targeting Focus - Atlanta, Georgia

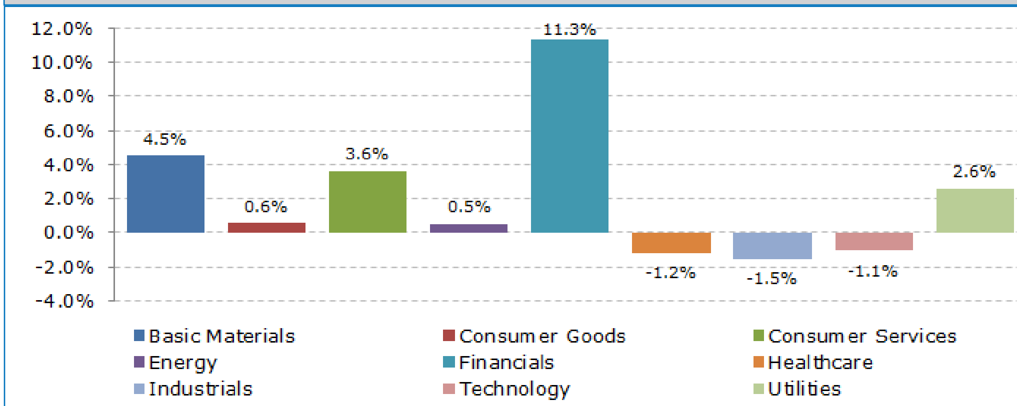
Money Center Statistics

Reported Equity Assets ($B):	$219.9
Number of Institutions:	41
World Rank:	18/174
Top Sector Weighting:	Financials
Financials Weighting:	22.0%
Top Region Weighting:	N. America
N. America Weighting:	85.7%
Total Net Buying ($B):	$26.8
Total Net Selling ($B):	-$21.1
Total Net Activity ($B):	$5.8

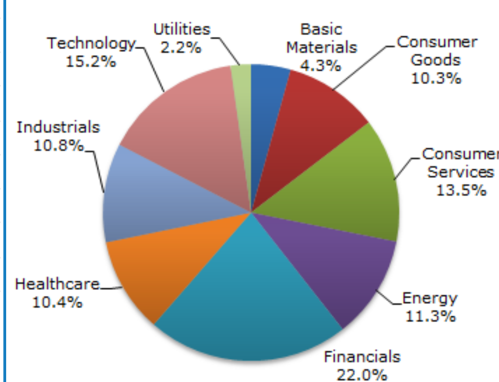
Summary Notes:

With $219.9B under management, Atlanta ranks as the 18th largest investment center in the world and the 7th largest in the United States. Atlanta investors are heavily invested in the Financial (22%) and Technology (15.2%) sectors. Financials in particular have been a favorite of Atlanta-based investors, as the second quarter of 2011 saw an 11.3% net increase in the space. Purchases in the Financial sector were led by **Invesco Advisers** (+$4.6B) and **SunTrust Bank** (+$253M). Invesco Advisers, Atlanta's largest firm, manages $141.8B; however, it is important to note that a large portion of the firm's assets are managed by Invesco's Houston office, which is home to the legacy Van Kampen Investments team. Many of Invesco's investment personnel based in the Atlanta office are part of the Global Equity Team, which focuses on global, global ex-US, and emerging market mandates, as well as fixed-income and indexed investments. **Artisan Partners**, headquartered in Milwaukee, maintains an Atlanta office that is home to their U.S. Value Team, which invests in undervalued domestic securities in solid financial condition. In the second quarter, Atlanta investors proved bearish in the Industrials sector, which saw a 1.5% net decrease in investments, due largely to selling by Invesco Advisors (-$609M) and **EARNEST Partners** (-$61.4M). Not surprisingly, Atlanta investors allocate the vast majority of their portfolio holdings to North American domiciled securities (83.1%), but this past quarter did see a 22.5% increase in Japanese domiciled investments, led by EARNEST Partner's large buys of Denso Corporation (+$7.7M) and Secom Company (+$7.1M). Middle Eastern and African domiciled securities also saw a large increase (+9.9%) in Atlanta-based ownership. **Cornerstone Investment Partners** was responsible for a portion of this influx as they purchased $22.9M worth of Israeli healthcare firm Teva Pharmaceutical Industries.

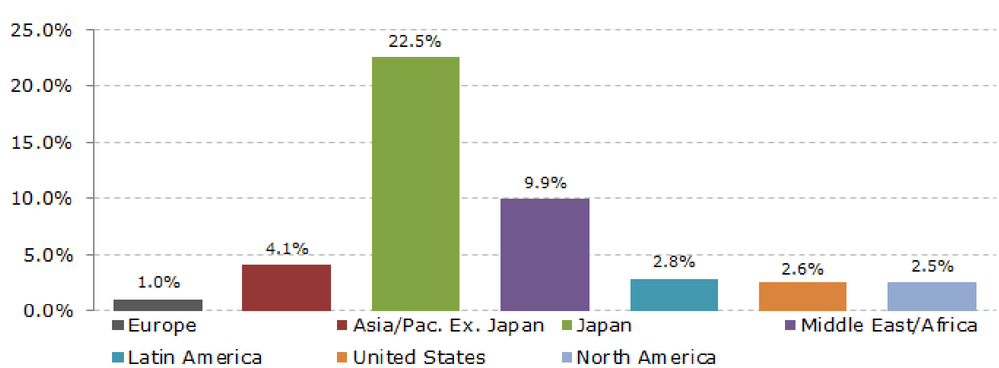
Most Recent Sector Net Activity (% Change)



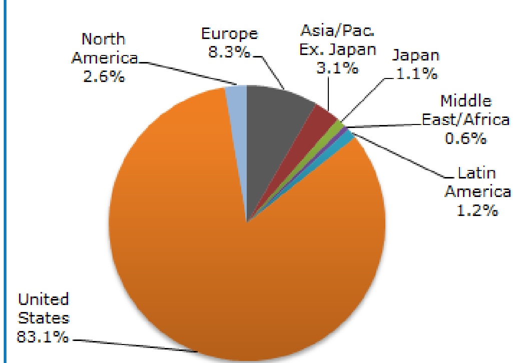
Sector Allocation



Most Recent Regional Net Activity (% Change)



Geographic Allocation



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