



# Qualitative Fund Research

Legg Mason Brandywine Global Opportunistic Fixed  
Income Fund

January 2019

## About the Manager

Legg Mason is one of the world's largest funds management groups, with a history that dates to 1899 with the head office in Baltimore, USA and over AUD\$1 trillion funds under management. The firm is listed on the New York Stock Exchange and employs approximately 3,300 employees in 39 offices worldwide. Legg Mason's operates as a global multi-affiliate model. Legg Mason provides a global platform and centralised business and distribution support for its nine affiliated fund managers that include: Brandywine Global, Clarion Partners, ClearBridge, EntrustPermal, Martin Currie, RARE Infrastructure, Royce & Associates, QS Investors and Western Asset. Each affiliate operates independently under its own brand and investment process.

Brandywine Global Investment Management, LLC (Brandywine or the "Manager") focuses on classic value investing, which includes the management of global fixed income portfolios. Information as it relates to New Zealand investors can be viewed [here](#).

Legg Mason advocates for strong [governance](#), and actively promotes a culture of compassion

spanning across , philanthropy, community and volunteerism, and environmental responsibility, available [here](#). FundSource Ltd views corporate citizenship and governance frameworks as extremely important foundations from which a manager starts to engage with the clients' experiences.

Legg Mason Brandywine Global Opportunistic Fixed Income Fund is the only Legg Mason Portfolio Investment Entity (PIE) fund offered in New Zealand. The Australian Unit Trust (AUT) has been available to New Zealand investors since its inception on 2011. Legg Mason has other funds across its suite of managers whose funds are available to New Zealand investors under an AUT structure and a Dublin domiciled UCITS range.

The [Brandywine Global Fixed Income](#) team led by a team of four, managing an investment team of 19 portfolio managers and analysts. The investment team is located in Philadelphia, Singapore and London. Legg Mason's distribution team is based in Australia.

## Using this Fund

**This is General Advice only and should be read in conjunction with the Disclaimers, Disclosures and Warnings at the end of this document.**

The Legg Mason Brandywine Global Opportunistic Fixed Income Fund ("the Fund") is a high conviction and alpha seeking fund that is based around value investing. The Fund is benchmark agnostic and will invest in a mix of global bonds and other global debt securities offering higher real yields. Currency is actively managed, with the purpose of hedging and enhancing returns. As such the Fund will generally sit within the defensive component of a balanced portfolio, more specifically the global fixed interest sector.

The Fund is subject to market risk and movements (both positive and negative), from investment grade

fixed interest securities. The Fund may enter into derivative contracts to manage market risks, such as FX forwards, interest rate derivatives, and credit default swaps. The Fund is suitable for investors with a minimum investment horizon of three years.

The Fund is a Portfolio Investment Entity (PIE) which currently invests in an underlying offshore fund, also called the Legg Mason Brandywine Global Opportunistic Fixed Income Fund. The PIE structure provides greater certainty for New Zealand investors. The fully hedged NZD PIE Fund commenced on March 2018 and has a very limited track record.

Question	What the Manager says	What FundSource think
<p>What are the Manager's assets under management - in total and in this Fund?</p>	<p>Brandywine Global, as an independent affiliate of Legg Mason, offers the advantages of an investment boutique backed by the resources and infrastructure of one of the world's leading asset managers. As at June 2018, Brandywine Global manages USD \$75 billion across a range of differentiated fixed income, equity, and alternative solutions. Over 20 years, the Global Opportunistic Fixed Income Strategy has grown to over USD \$28 billion.</p>	<p>Legg Mason has a long track record in operating its global multi-affiliate model. The Legg Mason Brandywine Global Opportunistic Fixed Income Fund is Legg Mason's first foray in to the New Zealand market with a Portfolio Investment Entity (PIE) fund. FundSource notes Legg Mason has a several of its multi-affiliate managers and funds available in the New Zealand market, via its Australia registered Australian Unit Trust (AUT).</p> <p>The PIE Fund structure commenced in March 2018 and has been established with Implemented Investment Solutions (IIS) a Wellington based company that specialises in PIE structures for offshore fund managers.</p> <p>Despite the PIE Funds short timeframe, the Fund has received relatively strong support in the New Zealand market, with current funds under management (FUM) of NZ\$226.8 million, as at September 2018.</p> <p>Brandywine has a suite of seven fixed income solutions, with this Fund viewed as the flagship fixed income solution. New Zealand investors have already entrusted more than NZ\$800 million invested in this Brandywine Global strategy.</p>
<p>Who is accountable for managing the Fund, and how long has the investment team worked together?</p>	<p>The Fund is co-managed by a team of four: Steve Smith, David Hoffman, CFA, Jack McIntyre, CFA, and Anujeet Sareen CFA. David, Jack and Steven have been working together for over 20 years, while Anujeet has been a recent addition, joining the firm as a Portfolio Manager in 2016.</p>	<p>Responsibility for this Fund lies with the Portfolio Management team of Smith, Hoffman, McIntyre, and Sareen. As stated most of the team have worked with each other for over 20 years. Sareen had 22 years with Wellington Management, where he was managing director of global fixed income and a global macro strategist, as well as chair of the Currency Strategy Group. FundSource believes this is a very experienced fixed interest team that is prepared to add new senior resources as required. FundSource considers Hoffman and Smith to be key people. If either were to depart FundSource believes this would be a significant loss.</p> <p>Francis Scotland, Director of Global Macroeconomic Research, is considered to be a key person, due to the Fund's process being heavily influenced by the top down macro views, rather than fundamental bottom up security level research. Scotland is responsible for developing and maintaining Brandywine's proprietary macro economic research facility which contains financial information for over 50 countries for which this Fund can invest.</p> <p>The broader fixed income team totals 27 personnel, four fixed income portfolio managers, three global credit portfolio managers, six traders, and 14 analysts. FundSource notes the trading and credit teams are separate to the team responsible for this Fund. Two traders primary role revolves around this Fund, while the credit team are called upon as required, including regular weekly and monthly meetings.</p>

		<p>FundSource notes there have been some team departures over the past 24 months. One departure from the high yield team and two departures from the analyst team. The later analyst departures relate to this Fund but is not considered to be material.</p>
<p>What objective is the Manager trying to achieve?</p>	<p>The Fund seeks global bond investments offering the best combination, in our view, of high real yield and attractive fundamentals given our macroeconomic outlook. This value-based strategy maintains a primary focus on sovereign debt with a goal of unlocking the potential performance benefits of mean-reversion tendencies in interest rates and currency valuations. To avoid the inefficiencies of global bond benchmarks, the team takes a benchmark-agnostic approach and limits investment to only the 10-20 countries and currencies we consider attractive investments. For over two decades, the Global Fixed Income team has achieved its risk-adjusted returns by implementing a process of country rotation through the broad global fixed income universe. The strategy allows the investment team wide latitude and flexibility to opportunistically own non-investment-grade credit and sovereign debt.</p> <p>The Fund aims to earn a return before fees and taxes in excess of the FTSE World Government Bond Index hedged into NZD over rolling five-year periods.</p>	<p>Brandywine management style emphasises the search for fixed income securities with the highest real yields, this is achieved by employing a process that is primarily macro driven and internally produced.</p> <p>The process seeks to manage risk by purchasing undervalued securities and managing currency to protect and increase returns. Factors that are important to the investment process are issue selection, duration management, country rotation and active currency management.</p> <p>The Fund is benchmark agnostic but does reference its performance against the FTSE World Government Bond Index (hedged into NZD). The Manager has not provided specific guidance around the outperformance of the performance reporting benchmark.</p> <p>The preservation of capital is central to the Manager. The Manager ultimately views risk as the probability of permanent capital loss.</p> <p>The PIE Fund's updates and factsheets are available <a href="#">here</a>. Longer dated performance is available for Australian Unit Trust is available <a href="#">here</a>. Further performance information is available on the <a href="#">Disclose website</a>, and <a href="#">FundSource</a>.</p>
<p>What does the Manager invest your money into?</p>	<p>The Fund is an actively managed portfolio of sovereign bonds, investment grade corporate bonds, mortgage securities, currencies and other similar securities. The Fund can also invest in emerging market and high yield debt.</p>	<p>The Fund primarily invests via government issuance. With security selection generally being the residual of the Manager's country and currency selection. When the economic environment is conducive and the market, according to price differentials or spreads, signals value, the Fund can invest in corporate and mortgage-backed securities.</p> <p>The Fund is expected to primarily invest by holding physical securities, rather than using derivatives. However, derivatives can be used to obtain or reduce security, market exposure, and currency exposures. The Fund is expected to hold a portfolio that invests in approximately 8 to 16 developed countries and 0 to 5 emerging markets. The Manager believes the exposure to a market offers the greatest value and the highest return potential. Real rates are combined with currency analysis to derive value.</p> <p>The PIE Fund is structured to ensure it complies with relevant laws, and subsequently will not invest in securities issued by companies involved in the</p>

		production or distribution of cluster munitions.
<p>What are the inherent risks imbedded in the Fund?</p>	<p>We view risk as the probability of the permanent loss of capital. Our process seeks to minimize this risk by avoiding assets with the following characteristics: those that trade at a significant premium relative to their intrinsic value, especially where the information supporting asset prices is well known and completely discounted, or where early signs appear of economic/policy processes that could trigger a renormalization of lower prices. We also seek to control absolute risk by following mutually agreed upon investment guidelines.</p> <p>Rather than retain or eliminate various forms of risk, we strive to control the relevant risks. All Global Opportunistic Fixed Income portfolios are managed by our portfolio managers; holdings and weightings are identical, subject to restrictions placed by individual clients. We follow our mutually agreed upon investment guidelines seeking to control absolute and relative risk.</p> <p>There are four primary risks associated with the Global Opportunistic Fixed Income strategy: country risk, interest-rate risk, currency risk, and credit risk. Details can be viewed in the <a href="#">Product Disclosure Statement (PDS)</a>.</p> <p>We believe our mandate is to intelligently evaluate and assume risk on behalf of our clients in order to meet and exceed their objectives. We focus on the absolute value of the securities and markets we buy. We believe "real" risk (the risk of losing money) is based upon the relationship between price risk and information risk. Prices are higher when there is little information risk and investors, perceiving no risk, are confident. Conversely prices are lower when information risk is high. Our job as value investors in bonds and currencies is to arbitrage price risk versus information risk. We take very little price risk by purchasing undervalued securities and we believe it is our skilled assessment of information risk that has produced what we believe to be superior returns over time.</p>	<p>The Manager has a long track record in employing its primarily top down macro focused investment strategy. This leads to a portfolio that has a differentiated country and currency exposure to most fixed interest sector funds. However, this does not change the underlying risks compared to peer funds. Fixed interest investing generally carries similar core risks based around country, credit, interest rates, and currency risks. The Manager will employ tools such as yield, duration management, and credit quality to assist in managing portfolio risks.</p> <p>Brandywine fully hedges the currency risk to NZD for the PIE fund. Similarly, Brandywine take this approach for all local currency fund structures. The Manager can increase the level of currency exposure above fully hedged 100% position. This allows the Fund to manage currency risk to coupon payments, while having the ability to express the Manager's positive view on that country.</p> <p>Brandywine Global believes that volatility and tracking error are measures of price change not risk of capital loss and therefore are less valuable as guides for constructing a portfolio. The Manager believes successful investing in global bonds relies as much on avoiding losses as pursuing gain. The Fund works to reduce absolute risk while accepting benchmark risk. Avoiding overvalued parts of the market has tended to dampen its downside volatility.</p>
<p>Why does the Manager believe the future prices of the Fund's investments will vary?</p>	<p>Brandywine Global believes that global, economic and asset price imbalances are corrected over the medium to long term by adjustments in interest rates and currencies. High real yields not only boost income returns through time, but having exposure to these markets, positions investors to take advantage of the mean-reversion properties of interest rates. Interest rates mean-revert because they are such powerful economic regulators.</p> <p>Elevated real interest rates restrict consumption and discourage capital investment, which can ultimately slow economic growth and bring down inflation, thus allowing bond yields to decline. At</p>	<p>The Manager has a capital loss framework. Therefore, the Manager looks to preserve capital. FundSource notes this implies there is a bias to downside protection, rather than outperformance.</p> <p>Mean reversion sits at the core of the Manager's process. The process starts by ranking global bond and currency markets. Valuation metrics drive the ranking process with real interest rates (nominal interest rates less rate of inflation) central to the ranking of global bonds and a variety of valuation methods informing the ranking of currencies.</p>

	<p>their extremes, currency valuations also act as economic regulators, slowly forcing changes in corporate and individual economic behaviour. Currency markets offer similar mean-reversion characteristics and active currency management plays an integral role in the Brandywine investment process, whether searching for undervalued opportunities in the currency space or managing risk by hedging overvalued currencies.</p> <p>Brandywine Global's investment approach combines a top-down analysis of macroeconomic conditions with a bottom-up fundamental analysis to identify the most attractive valuations during a business cycle.</p>	<p>Fundamental factors such as the economic cycle, inflation, external imbalances, capital and trade flows, and policy considerations are included. The purpose is to determine if pricing anomalies can or have led to policy conditions which provoke mean reversion.</p> <p>When governments determine policy adjustments are required, interest rates are likely to change, which will have positive or negative impact on fixed interest securities, government or corporate, and currencies. This will cause variance in security valuations.</p> <p>Over and undershooting in bond and currency markets, relative to their long-term values, provides opportunities for the Manager to enact its thesis. While investment decisions are strategic with long-term profits in mind, the Fund can take advantage of tactical opportunities.</p>
<p>Why does the Manager believe you should give them your money rather than to someone else or to an inexpensive index fund?</p>	<p>The Fund benefits from the following competitive advantages:</p> <ul style="list-style-type: none"> <li>• A total return investment approach that benefits from a macro-driven process with a focus on the high real yields.</li> <li>• High conviction strategy where concentrated positions in the Fund are based on the portfolio managers' conviction levels and not index weightings.</li> <li>• Unique diversification fund – Historic returns are not highly correlated to competitor funds.</li> <li>• Risk control that provides a defensive strategy without sacrificing upside</li> <li>• Diversified Sources of Alpha             <ul style="list-style-type: none"> <li>o Country Selection – a focus on countries with the highest real yields</li> <li>o Active Currency management aiming to protect capital and increase returns</li> <li>o Active Duration management</li> <li>o Credit.</li> </ul> </li> </ul>	<p>There is insufficient history for the PIE Fund to draw any conclusions. FundSource notes the Brandywine AUT fund has a six year track record, and sits in the FE Analytics NZMI Fixed Interest Global sector. The Manager launched the underlying strategy in 1998. While the PIE structure is new, the investment strategy has a long 20+ year history. This FE Analytics AMI Fixed Interest Global Bond sector consists of 101 funds and covers a large number of strategies, performance of the AUT has been higher than the FE Analytics sector average.</p> <p>FundSource highlights the Manager's approach to investing is to have relatively small investment teams run each portfolio. All research team members are generalists, including portfolio managers, rather than sector specialists. Investment ideas are multi-lateral and are based on the team's research. The final decisions are made by consensus among the portfolio managers. Positions sizing in the Fund is based on the manager's conviction levels, there is no correlation to index weightings.</p> <p>The PIE Fund performance is available via the fact sheets on the <a href="#">Implemented Investment Solutions website</a>. Further performance data is available via the <a href="#">Disclose website</a> and <a href="#">FundSource website</a>.</p>
<p>How does the Manager decide to buy or sell investments?</p>	<p>Once team members endorse an investment recommendation, the aggregate level of conviction among team members guides position size across the suite of Global Fixed Income strategies. When the portfolio managers are in agreement, larger position sizes will typically reflect that conviction level. When a smaller majority is in agreement, the team may take action, albeit at a smaller position size. Position sizes are based on a combination of conviction level in an investment idea, the expected return from that investment, and finally the size of a</p>	<p>The Manager's research effort is based on the analysis of macro-economic conditions in order to determine where the most attractive valuations exist from a reward/risk perspective. The Fund will focus on the highest real-yielding (nominal interest rates less rate of inflation) countries in the world with supportive currencies.</p> <p>Secular trends, political and monetary conditions, and business cycle risks are also considered in determining the likelihood of capturing the value seen in</p>

	<p>bond or currency market and prevailing liquidity conditions. Limits are generally set based upon liquidity considerations so that the ability to enter and exit positions quickly is maintained and with limited market disruption.</p> <p>Brandywine applies a top-down, value-driven process when structuring global fixed income portfolios. Real yield is the primary measure of value for bonds, and the investment team prefers to focus on undervalued currencies that have started on an appreciating trend, otherwise it will hedge and even short select currency exposures if it is felt that a currency is overvalued. Other factors that are considered include inflation rates, political risks, monetary policies, business cycle stages, and liquidity conditions. In terms of relative importance, the investment process would rank the country and currency decision first, followed by duration and then security selection.</p>	<p>real interest rates and contribute to country weighting decisions.</p> <p>Any deterioration or improvement in political and economic factors can lead the Manager deciding to exit a position or reweighting the portfolio. These factors will also determine the degree of attractiveness of the currency, and Fund's positioning around a specific currency. The depth and breadth of liquidity is an input in to position sizing, as well as the combined Portfolio Manager's conviction.</p> <p>The Fund can invest via sovereign bonds or corporate bonds, with sovereign debt securities being the base case. The Fund will only invest in credit that represents significant value relative to their own history or their peer group, on an industry and quality basis. The Global Fixed Income team collaborates with the Global Credit team to identify specific securities for inclusion in the portfolios, as appropriate.</p> <p>The portfolio positioning will vary as fundamentals and valuations change. Securities are sold when a bond or currency no longer meets the Manager's high real interest rates and an undervalued exchange rate definition of value.</p> <p>The Manager reviews the portfolio asset allocation of the Fund on a daily basis to take account of market movements, and inflows and outflows. Rebalancing occurs when meaningful change to the desired levels has occurred. This assist in managing transaction costs for the Fund.</p>
<p>Has the CIO/ Portfolio Manager personally invested in the Fund? If so, paying the same fees as other investors?</p>	<p>While Brandywine Global does not have a co-investment policy, the Firm's principals and key members of the Investment Team may invest a portion of their assets in strategies where the Firm either sub-advises a mutual fund or manages a privately-offered commingled investment vehicle. While their investments are considered confidential, the total investment of current employees in the Firm's investment products significant.</p> <p>Brandywine Global's Code of Ethics (the "Code") prohibits employees from engaging in any securities transaction without obtaining the appropriate pre-clearance (unless the transaction is subject to an exemption from pre-clearance). The Firm's Code of Ethics, prohibits Access Persons from engaging in personal trading activities involving (1) inside information, (2) knowledge that the Firm has a pending order for, or is considering the purchase or sale of, the Security, or (3) transactions within the seven calendar days prior to or following a purchase or sale of the same Security in a client account. There are additional restrictions on securities of the Firm's parent company, Legg Mason Inc. In addition, Firm employees are prohibited from engaging in any securities transaction that requires pre-clearance within the seven calendar days prior to or following a purchase or sale of the same security in a</p>	<p>FundSource believes that the interests of investment personnel are better aligned to those of the investors, when investment personnel are significantly invested, and at the same fees. While neither Legg Mason or Brandywine requires investment personnel to invest in this Fund, the Manager indicates the investment team have materially invested.</p> <p>The Manager has detailed the rules imposed around trading of securities by investment personnel. FundSource notes this is in line with global practice, where investment personnel can invest directly in securities.</p> <p>FundSource believes stronger alignment is achieved when investment personnel must invest in the funds, they are responsible for. FundSource confirms the co-investment in the strategy is significant. Accordingly, FundSource believes there is a strong alignment with investors, and the appropriate compliance frameworks in place to prevent investment personnel from gaining an advantage over investors.</p>

	<p>client account. Lastly, the Firm imposes holding periods and limitations on short-term trading. Brandywine Global utilizes a web browser based automated personal trading compliance platform, FIS (formerly SunGard) Protegent PTA, which allows for automation of certain functions, including preclearance of securities transactions and numerous surveillance capabilities.</p>	
<p>How much latitude does the Manager have to deviate from the weightings of the Benchmark portfolio?</p>	<p>Portfolios may deviate from the Benchmark portfolio for a number of reasons, mainly customisation of client mandates, base currency differentials. However, in executing on the individual accounts, the aim is for these to be managed in line with the Benchmark portfolio without discretion.</p> <p>Tracking Error: n/a  Duration: 1 to 10 years  Targeted Volatility: n/a  Sovereign &amp; Treasuries 0 to 100%  Investment Grade: 85 to 100%  Non-Agency Mortgages 0 to 20%  High Yield 0-15%</p>	<p>Potential investors should be aware that this Fund is not benchmark aware, and therefore has very few hard or soft limits that it must adhere to. The Fund does not aim to replicate any aspect of the benchmark.</p> <p>The Fund is an actively managed portfolio of sovereign bonds, investment grade corporate bonds, mortgage securities, currencies and other similar securities. The Fund can also invest in emerging market debt, high yield debt, and below investment grade non-sovereign and corporate debt. FundSource notes that while the Fund's mandate is broad, the Manager is reasonably conservative, viewing risk as the permanent loss of capital.</p> <p>The Fund will have a minimum average portfolio credit quality of A-. This assists in managing portfolio risk, which is driven by the Manager's macro focused process. Which is likely to produce a portfolio that is different to most peer funds, providing diversification benefits to an investor's portfolio.</p>
<p>On what basis does the Manager believe the fees they charge are justified?</p>	<p>Brandywine Global is an active, benchmark agnostic manager with a long track record of delivering on client objectives. Fees for the fund has been set taking into consideration to the peer group and to reflect the level of active management within the investment process.</p>	<p>The PDS indicates the fee for investing is 0.82%. Compared to the FE Analytics NZMI Fixed Interest Global sector, the fee for this Fund is well below sector peers. FundSource notes the FE Analytics sector has 52 peer options.</p>
<p>How would you describe the quality of your organisational and investment governance processes?</p>	<p>As a client focused investment manager, Brandywine Global's focus on investment governance reflects that of our investors. Investment governance of is of the utmost importance given our clients include superannuation and retirement schemes, sovereign wealth funds and retail investors. An Enterprise Risk Management team works with the portfolio management teams on an ongoing basis to manage Operational Risk by working to implement independent controls, segregating responsibilities, and implementing appropriate policies and procedures. The Director of Enterprise Risk Management serves on the Investment Committee in overseeing investment practices, market risk and the Valuation Committee.</p> <p>Brandywine also has policies and procedures in place to monitor and mitigate OTC counterparty risks with its trading partners. We seek to mitigate credit risks with counterparties by trading with parties with strong credit ratings, trading operation and internal control policies, realising</p>	<p>The Investment Manager has embedded compliance and risk management systems in to the investment process. The Manager uses the Bloomberg Asset and Investment Manager (AIM) System for fixed income trading. FundSource notes this includes pre-trade, and post-trade compliance. Wherever practicable, prior to execution, all trades are run through its compliance module to help ensure adherence to guidelines. All trading activities are run through post trade compliance systems. FundSource believe pre and post trade compliance are global industry best practice.</p> <p>The Manager conducts regular due diligence on it brokers and dealers, and only uses those that whom Brandywine believes provide quality service and execution. Brandywine seeks to achieve best execution with every trade.</p> <p>The functions driven by the Enterprise Risk Management team are viewed positively. The use of a team compliance and risks management team external to the</p>



	<p>profit/loss frequently and diversifying trading with multiple counterparties.</p> <p>The Enterprise Risk Management team interacts with the investment and trading functions on a frequent and often daily basis in supporting the efforts around market and credit risk. Enterprise Risk Management produces position, currency and counterparty reports and information utilised by the investment team in an effort to monitor exposures relative to limitations in the investment mandate or on a firm-wide basis.</p>	<p>investment management function, is in line with global peers.</p> <p>FundSource notes the investment team meet regularly intra weekly and formally and informally. The investment team have a series of regular monthly and quarterly formal meetings to ensure policies, procedures and guidelines are adhered to. Feedback from external risk management teams are also discussed broadly across the investment team.</p> <p>FundSource notes that the Manager employs Environment, Social, and Governance (ESG) proprietary factors have been fully integrated in to its top down and fundamental research processes. The Manager can use third party rating and research to enhance their understanding of ESG issues. From a New Zealand perspective, the onus on compliance with New Zealand laws lies with IIS, as the responsible manager for the PIE Fund structure.</p>
<p>Is there alignment of interests through; ownership of the Manager, and remuneration of the investment team?</p>	<p>Brandywine Global operates as a wholly owned but independent subsidiary of Legg Mason, Inc. ("Legg Mason"), retaining complete investment autonomy and control over management, investment, and employment decisions. While Brandywine Global employees do not have a direct ownership interest in Brandywine Global, the Firm does have control over all earnings after payment of a fixed-percent revenue share to Legg Mason.</p> <p>The members of the Fixed Income Investment team earn a base salary and bonus tied to investment performance. The performance bonus is awarded based on peer group outperformance on periodic performance and is weighted to place more emphasis on longer-term outperformance, and less emphasis on the short-term. Investment professionals may also receive bonuses based on the profitability of their product group. The portion that is not retained is shared with the other investment teams in an effort to smooth income and to promote cross-team fertilization and cooperation. We have found that this form of compensation aligns the interests of investment professionals and clients and leads to accountability and low-turnover among Brandywine Global's staff. In essence, the portfolio management teams own all of the residual profits of the Firm, which we believe leads to responsibility, accountability, and low turnover of people.</p>	<p>The ownership and operational relationship between Legg Mason and Brandywine is not uncommon, in terms of global funds management. This is less the case in New Zealand. The number of fund managers in the New Zealand market is very small compared to global funds management.</p> <p>The remuneration structure of the Brandywine investment team is in line with global practices, consisting of a base salary and performance based bonus. Linking the variable bonus to longer term performance improves the alignment to an investors experience.</p> <p>The structuring of the variable performance based bonus is what would be typically seen in boutique fund managers, in that there is a direct correlation to the businesses profit and loss statement. This is despite the investment team having no direct equity ownership of the business.</p> <p>The sharing and smoothing of profits across all investment teams is not commonly seen. This can bring synergy across all Brandywine investment personnel. It is unclear how this aligns to investor experiences as they relate to the full Brandywine product suite. Particularly if there are periods of significant underperformance, in absolute terms.</p>

## Conclusion and Rating

Overall, FundSource believes the Manager is filling a gap in the New Zealand market place, from an asset allocation perspective. Macro based global fixed interest funds are not common in the New Zealand market place.

The Manager is well resourced and has partnered with appropriate service providers to assist in managing the PIE fund structure. Implemented Investment Solutions, who is responsible for the PIE Fund, outsource some service functions to highly regarded service providers in the New Zealand market.

The Brandywine investment team has strong industry experience and manager tenure, this extends to its relationship with Legg Mason, as a part of its multi-affiliate structure. The investment team is well resourced and has been structured along core responsibilities. FundSource views Legg Mason and Brandywine as having strong alignment with investors due to the investment team for this Fund being having significant personal investment in the strategy.

The Fund has performed strongly against the peer sector funds, when looking at the investment strategy this Fund invest via, and the Australian Unit Trust. The PIE Fund has a very short track record. However, FundSource believes there should be little difference in outcomes, other than adjustments for fees versus the parent strategy and Australian Unit Trust.

It is important to understand that the Fund's investment strategy can appear to be simple. However, FundSource highlights that macro based investing can be extremely complex and requires considerable attention to be paid to country, region, political, and currency changes. All of which have proven to be volatile, despite a long running bull market backdrop. FundSource notes macro based investing can produce very different asset allocation outcomes to fundamental bottom up security selection. There may be periods where the Fund's asset allocation and performance be very different to other peer global fixed interest funds.

The Funds' basic fee is well below the average FE Analytics NZMI Fixed Interest Global sector and FE Analytics AMI Fixed interest Global Bonds sector fees. The Manager, Legg Mason Brandywine, and the Implemented Investment Solutions have worked together to achieve a very compelling fee structure, for New Zealand investors.

FundSource recommends that investors carefully consider that the Manager's approach to macro based investing in the fixed interest sector meets their needs and objectives. The Fund can be classified as either a Fixed Interest Fund or an Alternative Fund. Alternative funds, as an asset class, typically comprises  $\leq 10\%$  of the overall asset allocation.

### FundSource Rating: **AAA**

Fund ratings are current as at the date of publication of this report. FundSource reserve the right to review and update fund ratings from time to time.

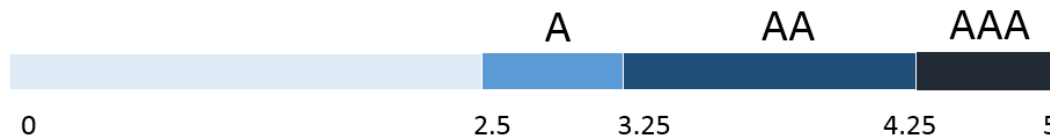
## Research Factor Weighting

Research Process Category	Model Factor Weight	Analyst Average Score
Corporate & Investment Governance	15%	4.25 / 5
Investment Philosophy & Process	20%	4.40 / 5
People	25%	4.67 / 5
Portfolio Construction & Implementation	15%	4.17 / 5
Risk Management	15%	4.40 / 5
Investment Fees	10%	4.43 / 5

Overall Average Score: **4.41 / 5**

## FundSource Rating Guide

The qualitative rating of a fund is a function of the FundSource Research Factor Weighting process, which is built around the six core qualitative research process categories. The weighted scores result in an overall score, out of five, which is then matched to the following rating:



### AAA: Highly Recommended

Funds that have superior average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, significantly experienced and stable senior personnel, a sound track record over a full market cycle, a clearly defined investment philosophy and process, and a portfolio consistent with that philosophy and process. The management company will also have established effective controls to maintain that philosophy.

### AA: Recommended

Funds that have strong average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, experienced and stable personnel, a sound track record over a full market cycle, a clearly defined investment philosophy and process, and a portfolio consistent with that philosophy and process. The management philosophy must be coherent and consistent with existing portfolios and processes.

### A: Investment Grade

Funds that have good average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, experienced personnel, a sound track record a defined investment philosophy and process, and a portfolio consistent with that philosophy and process.

### FW: Fund Watch

There has been a material change with either the manager, this may include, but is not limited to, departures, new hires, process changes, changes to the investment philosophy. This is considered to be an interim measure, to enable further investigation, re-evaluation and an appropriate course of action to be determined.

### S: Sell

This category covers previously recommended funds that are no longer recommended because of some material change. Removal from recommended status might be for a variety of reasons such as a fundamental change in the fund management company or in the manager's investment strategy, or because a fund did not meet its original expectations. The implications for ongoing service are that the fund should be reviewed on an individual client basis to ensure it still matches their original investment objective.

### NR: Not Rated – Screened/ Not Rated

Funds in the Not Rated – Screened category have provided information and/or FundSource has conducted an initial analysis of the fund, but has chosen not to provide a recommendation at this stage. FOR Not Rated funds the manager may have provided information, but no review meeting has been conducted

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Client focused outcomes are underpinned by the belief that the role of business model innovation and accelerating technological change opens up new possibilities, to put client interests at the centre of the financial services industry focus. This is based on John Hagel's work on the possibilities for "Disruption by Trusted Advisors" and John Kay's "Other People's Money: Masters of the Universe or Servants of the People".



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