

# Schroder Municipal Bond Strategy Overview

## Summary

Schroders' Municipal Bond investment strategy seeks to maximize after-tax yield and income by investing across the spectrum of investment grade municipal debt. The strategy capitalizes on structural inefficiencies in the marketplace and focuses on fundamental, bottom-up security selection. We use a team approach in constructing investment strategy and portfolio decisions are supported by fundamental and technical research.

## Firm highlights

- Schroders manages \$328.7 billion in assets worldwide
- Wide range of fixed income strategies across all major markets - developed and emerging
- Global bond team of more than 100, including more than 30 portfolio managers and over 25 credit analysts
- Deep global research capabilities – the vast majority of research is generated in-house

## Team highlights

- \$66 billion of fixed income assets under management globally; \$1.9 billion in Municipals
- Manage dedicated municipal accounts as well as integrated municipal expertise within fully global investment platform
- Diverse team with trading and research backgrounds and over 20 years investment experience

## Key features

- Research-driven investment process that emphasizes high quality and capitalizes on market and pricing inefficiencies
- Security selection is the key driver of return
- Proven consistent process over multiple market cycles
- Proprietary database covering over 1,500 prerefunded/escrowed-to-maturity issues (advance refunded bonds generally backed by US Treasuries)
- Strategy performs well in a rising rate environment due to the high level of income generation
- Duration-neutral
- Risk management is embedded in our culture

## Investment objective

Schroders' municipal bond strategy seeks principal preservation with a high level of after-tax yield and income.

## Investment philosophy

Municipal markets are generally inefficient and lack a centralized, regulated information depository, providing investment opportunities.

We believe that an integrated team of research-driven municipal bond investors is the ideal structure to take advantage of these inefficiencies.

Using a disciplined investment process, we seek to generate consistent above benchmark returns with lower than average volatility.

All data and statistics as of June 30, 2011

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# Schroders

### Investment process

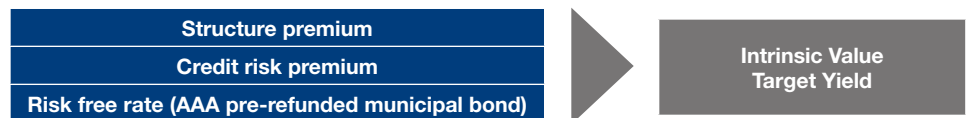
Our tax-exempt fixed income process consists of four distinct steps.

- Conduct in-depth proprietary market research (fundamental, quantitative and technical) to develop investment themes that dominate the municipal market.
- Develop and prioritize investment strategies, based on investment themes and bottom up research, which will provide the highest level of return/yield per unit of risk.
- Implement investment strategies within the portfolio, using a relative value framework to prioritize investment ideas and execute security selection.
- Continually review portfolio within rigorous risk management framework, incorporating quantitative and qualitative analytic tools.

The foundation of our investment process is our weekly US Tax-Exempt Fixed Income meeting. Here, portfolio managers combine the outputs from our economic, quantitative and credit research to establish investment themes and resulting strategies. Relative value opportunities are discussed and prioritized. Portfolio construction, including security selection, follows and is implemented by portfolio managers.

### Fundamental research

Schroder's municipal bond investment process begins with fundamental research. The goal of the process is to identify a bond's intrinsic value which may be independent of the market price. There are two components to determining a bond's intrinsic value: structure premium (i.e., liquidity, cash flow characteristics such as calls, puts, prepayments) and credit risk premium. A target yield is determined based on the bond's intrinsic value and compared to the yield of a risk free municipal bond.



Source: Schroders

A target yield is determined for every security based on its intrinsic value. This is then compared to the yield of a risk free municipal bond (AAA pre-refunded bond). Bonds trading at a significant discount to their intrinsic value are considered purchase candidates. These securities are evaluated versus other candidates across sectors and the most compelling values are purchased for the portfolio.

Credit research is an integral part of Schroders investment process and is a component of our fundamental research commitment that includes more than 25 dedicated credit analysts globally. Analysts provide credit opinions and investment recommendations on issuers held in the portfolios. The team conducts thorough research beyond the basic credit rating agency criteria to unlock value. The issuer financials, as well as project being funded, are reviewed with a specific focus on the project's objectives and merits, long-term vitality and competitive advantages. For those securities which have credit enhancement through a corporate guarantee or a letter of credit, the municipal team leverages the expertise of our global corporate credit research teams.

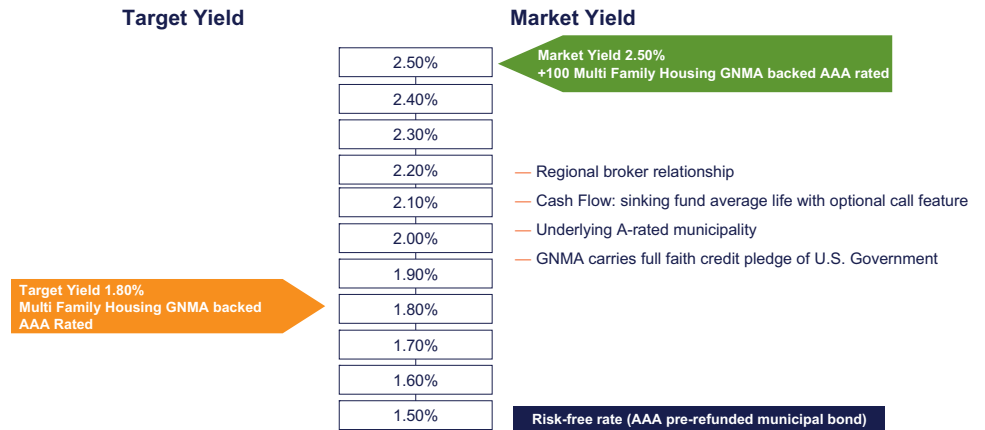
Municipal bonds are issued for many purposes. The basic infrastructure needs of state and local governmental entities, together with many other uses that provide public benefit, have led to a highly fragmented and diverse market. According to the Government Accounting Office, there are more than 50,000 issuers of debt in the US tax exempt marketplace. Each sector of the market has different factors that must be analyzed to provide an ongoing credit opinion. Key factors include financial and organization profile, including demographic characteristics, financial stability of the authority, type of loans, loan to value ratios, and cash flow sufficiency.

The structural components of each security are also thoroughly evaluated. We examine call or put features, sinking fund repayment schedules, partial principal repayments as well as other cash flow characteristics to determine a bond's intrinsic value. Understanding complex municipal bond structures and their effect on valuation is a key component of investment process.

Additionally, the team has expertise in a specific type of security, escrowed to maturity and pre-refunded bonds, that requires extensive research and review of their structural and legal documentation. Schroders has developed a proprietary database to collect and analyze issuer information of over 1000 issuers of prerefunded/escrowed bonds, allowing us to capitalize in this under-researched area of the municipal market.

## Security selection

Individual security selection is based on identifying those securities that provide the highest level of return/yield per unit of risk. Based on our fundamental research, the team sets a target yield for each bond using a rigorous, relative-value approach. The diagram below illustrates the framework used to make these decisions:



Source: Schroders

Security mentioned is for illustrative purposes only and is not a recommendation to buy or sell. The yield comparison shown is for illustrative purposes, is not intended as a comparison of any security held in a managed portfolio and should not be viewed as an investment recommendation.

The blue box shows a sample risk-free rate, which serves as a reference point for all valuations.

The orange box shows Schroders' target yield based on a thorough review of an issue (in this example, Multi Family Housing GNMA backed AAA Rated). Our analysis indicates the yield on this issue should be closer to the risk free rate. However, the market is pricing this bond at a much higher yield (green box)- indicating it is undervalued and hence a buying opportunity.

Using this relative-value methodology, Schroders' municipal bond team invests across the full spectrum of sectors and geographic regions to build diversified portfolios that offer competitive returns and high levels of credit quality.

## Risk management

Inherent within the fixed income process is a total risk management mentality. Our structured approach to risk management and monitoring utilizes a combination of formal and informal rules and guidelines, as well as proprietary quantitative models and externally supplied software tools, including, Charles River, Investor Tools Perform, and Barclays Point.

At a total portfolio level, the team seeks to reduce risk through diversification. For individual issues, position size is determined by an assessment of risk and reward across different strategies and is rigorously controlled based on the issuer's risk profile.

## Experienced team

	<b>Co-Head of US Tax – Exempt Fixed Income</b> Dan Scholl 22 yrs experience	<b>Co-Head of US Tax – Exempt Fixed Income</b> Susan Beck 25 yrs experience	
<b>Head of Municipal Credit Research</b> Eric Friedland 24 yrs experience	<b>Portfolio Manager</b> Dennis Darling 27 yrs experience	<b>Portfolio Manager</b> Ryan Haynes 11 yrs experience	<b>Client Portfolio Manager</b> Whitney Sweeney 14 yrs experience
	<b>Fixed Income Credit Analyst</b> Emily Kelly 3 yrs experience	<b>Investment Support Specialist</b> Christopher Jankowski 11 yrs experience	

As of July 31, 2011

Years experience denotes industry experience and not necessarily years employed by Schroders

## Risks

All investments involve risks including the risk of possible loss of principal. The market value of the portfolio may decline as a result of a number of factors, including volatility of the municipal bond market, interest rate risk, credit risk, liquidity risk and inflation/deflation risk. Some investors may be subject to state and/or local taxes. For more information consult your tax advisor.

## Why Schroders for Municipal Bonds

- Focus on capital preservation and income
- Unique relative value approach
- Research-intensive, bottom-up process
- Diversified portfolios of high-quality issues
- Duration-neutral strategy to minimize risk

### Important Information

#### Schroders plc

Schroders is a global asset management company with \$328.7 billion under management as of June 30, 2011. Our clients are major financial institutions including banks and insurance companies, public and private pension funds, endowments and foundations, high net worth individuals, financial intermediaries and retail investors. Our aim is to apply our specialist asset management skills in serving the needs of our clients worldwide and in delivering value to our shareholders. With one of the largest networks of offices of any dedicated asset management company and over 340 portfolio managers and analysts covering the world's investment markets, we offer our clients a comprehensive range of products and services.

Further information about Schroders can be found at [www.schroders.com/us](http://www.schroders.com/us)

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Diversification does not assure a profit or protect against loss in a declining market.

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