

Summary

The Schroder US SMID Cap Equity strategy is a bottom-up, fundamental and research-based approach. The portfolio manager and analysts seek to identify those companies that have compelling business models, a strong management team and attractive valuation levels. Sources of research include company managements, competitors, media and suppliers.

The portfolio of approximately 90 to 120 stocks is diversified by type of company, with approximately 50-70% of the portfolio invested in Mispriced growth opportunities, 20-50% in 'Steady Eddies' (i.e. companies with stable and dependable earnings and revenue characteristics), and 0-20% in Turnarounds.

Firm highlights

- Founded in 1804, with a strong family presence to this day
- Asset management is our main business
- Over 740 investment professionals worldwide
- Truly global reach: based in London, with offices in 32 countries
- Expertise in Fixed Income, Equities, Multi-Asset, Solutions, and Alternatives

Team highlights

- The strategy is managed by Robert Kaynor, CFA
- Dedicated team of 7 investment analysts with an average of 20 years investment experience

Key features

- Flexible core investment style; able to reflect changing market dynamics throughout the economic cycle
- Bottom-up fundamental research provides the basis for stock selection
- Focus on companies with strong appreciation potential selling at reasonable valuations
- Invests in a combination of three distinct and complementary types of companies; seeks to reduce volatility and tends to offer a level of protection in down markets

Investment objective

We aim to outperform the Russell 2500 Index* net of fees over a market cycle (typically 3 to 5 years).

*This index is an unmanaged portfolio of globally issued debt securities. There is no guarantee that any investor objective or outcome can be achieved.

Investment philosophy

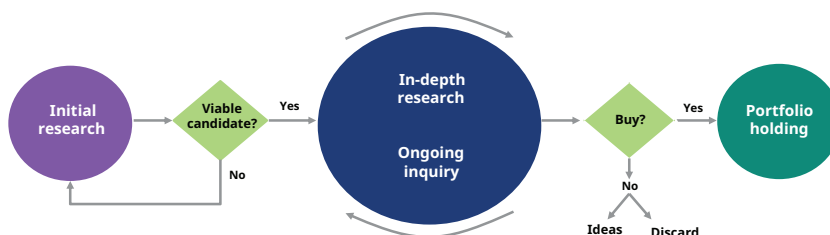
As fundamental, bottom-up investors we believe that we can add value over time through our research. In particular, we believe that operating in this less efficient segment of the market increases our opportunities to add value. Secondly, we believe that by building our portfolio with diversified alpha sources we can lower overall portfolio risk. We view our three main types of stocks (Mispriced growth,

'Steady Eddies' and Turnarounds) as representing diversified alpha sources. We believe that valuation matters, so we are careful about both entry and exit prices. In analyzing companies we focus on underlying business models and the cash flow dynamics of the model. If we find these two elements to be attractive we then analyze the valuation of the stock

Investment process

We focus on the upper end of small cap and the lower portion of mid cap companies between \$750 million to \$10 billion in market cap.* Within this universe, the analysts look to identify companies which offer strong business models, attractive margins and superior management teams. The research process

is extensive as we drill down on many of those ideas that we believe may be potential investments. We are bottom-up, fundamental, research-focused investors. The macro-economic environment will be considered in the context of the investment, but a stock must have strong attributes on its own to be purchased.



Idea generation	Deep fundamental research	Final stock selection
<p>Sources of new ideas:</p> <ul style="list-style-type: none"> Analyst generates new idea Brief write-up with supporting materials Reviewed by Fund Manager or Research Director Key question: does this stock have a reasonable chance of getting into the portfolio? If yes, proceed with full analysis 	<p>Thorough fundamental analysis of:</p> <ul style="list-style-type: none"> Business model Cash flows and financials Management track record Competitors Other relevant factors Valuation and Target price 	<p>Portfolio manager decides:</p> <ul style="list-style-type: none"> Buy, don't buy or defer Position sizing

Source: Schroders

* Represents general market cap but is subject to change

The analysts and portfolio manager look to identify investment ideas that potentially have a compelling investment thesis. As noted above, the thesis begins with a sustainable business model with attractive cash flow dynamics. We have a two- to three-year horizon when purchasing a stock.

Ideas may come from a variety of sources including company managements, competitors, suppliers or the media. Screens may also be run to ensure that we have not overlooked any companies with compelling metrics. Areas of focus include:

From the Income Statement	From the Balance Sheet	From the Cash Flow Statement
Historical revenue & sales growth	Debt levels: variable v. fixed	Historical cash flows and free cash flow generation
Gross and operating margin analysis	Fixed asset levels/depreciation	Cash flows relative to debt levels
Profitability (ROA, ROE)	Cash levels/accounts receivable/payable	
EPS growth - historical	Goodwill	
	Accounts receivable/payable	

Source: Schroders

Investment process (continued)

As noted previously, we place significant emphasis upon a review of the cash flow dynamics of the business – i.e. is the company generating free cash flow?

The focus of the analyst will vary depending on the sector. For example, in retail, margin analysis, revenue growth and same store revenue growth are key metrics. For a technology company, backlog and product cycle may be the driving forces.

If an analyst remains interested in the stock after the above analysis, the investment is considered in the context of a broader sector/industry backdrop. What has the industry growth rate been, and what is the expected growth rate going forward? How many players are there in the industry, and how does market share break down? What is the pricing and cost structure in the industry – how cyclical is it and where are we in the cycle? Finally, the valuation of the company must be attractive and the fund manager must have a high degree of conviction for the stock to be purchased in the portfolio.

Diversified Alpha Sources: A distinguishing characteristic of our approach is that we invest in three different types of growth in the portfolio. We identify these as:

- 1 Mispriced growth
- 2 'Steady Eddies'
- 3 Turnarounds

Mispriced growth are companies in which some sustainable change is occurring that we think will lead to a higher level of earnings, revenues, cash flows or margins over the ensuing two to three years.

Further, we believe that the market has not fully recognized the potential impact of this change in the stock price. Mispriced growth stocks are normally 50-70% of the portfolio, and normally our best returns are earned in this group. These stocks have tended to do best in rising markets, however, this group has not been as resilient in negative market environments as 'Steady Eddies'.

'Steady Eddies' comprise 20-50% of the portfolio and can be characterized as being stable growth companies. While their growth rates typically are not as high as the Mispriced growth stocks, they tend to have a more consistent quality to them. This can be due to a high level of recurring revenues. These stocks typically have held up well in declining markets, for the obvious reason that in that environment the market tends to be looking for companies with some predictability or stability to their earnings. These stocks provide a defensive ballast to the portfolio and have been a significant contributor to our strong downside capture ratio and lower overall standard deviation.

Turnarounds, which can be anywhere from 0%-20% of the portfolio are companies in which something has occurred to take the company from its growth path, we see a catalyst in place that we believe will fix the problem and we see some evidence that organic growth is beginning to return to the company. The performance of these stocks is less predictable (relative to overall market conditions) than the other two categories. However, historically when these stocks work they add a nice performance boost to the portfolio.

Investment process portfolio construction

The portfolio is constructed on a stock by stock basis. Portfolio weightings at the stock level are based on the portfolio manager's conviction level, with a maximum weight of 5% in any one security. Sector weights are typically a residual of our stock selection process, and while we are aware of benchmark weights, they do not play a material role in making the decision to invest in a stock.

However, we do have a guideline in place that limits our under- or overweight in any one sector to $\pm 10\%$ of the benchmark weight. The number of securities in the portfolio will be approximately 100-150. We strive to keep cash typically between 6-8% of the portfolio. The cash balance and the number of names typically reflect our ability to find attractively priced stocks.

Investment process research

Our research process is fundamental and bottom-up. The analysts and portfolio manager utilize a number of different sources to obtain their research, including companies, competitors, suppliers, sell side research analysts, the media and company financial documents. Extensive balance sheet and income statement analysis is also conducted.

Additionally, the product management team also runs quantitative screens for the analysts and portfolio manager on request. For example, if the portfolio manager discerns that a particular characteristic is currently working in the marketplace, a screen may generate a universe of companies that have a high exposure to that particular characteristic. Importantly, the portfolio manager must determine that the particular characteristic has solid investment underpinnings (e.g., high free cash flows), and that it is not a current "fad." The vast majority of our research is conducted internally.

The majority of the research that the team uses in selecting stocks for the portfolio is their own fundamental analysis on company financials and management teams. Assessing company management is a critical element of our stock selection process.

Time spent with company management will vary depending on a number of factors, including; how familiar we are with the industry, whether we have met the team before, how simple/complex the business model is, etc. The team meets with companies both on-site, in our offices and at conferences. Total meetings equal approximately 1000 per year, with about 10% of these on-site at company locations.

Approximately 20% of our research effort is from external sources. External research sources include sell side analysts, who typically work for smaller, regional firms. We also subscribe to various information and analysis services (including FactSet, Bloomberg, Thompson, ILX), financial media and industry journals.

Why Schroders for US SMID Cap Equity?

- A unique combination of stock types: Mispriced growth, 'Steady Eddies' and Turnarounds
- Designed to provide very strong downside protection, due in part to the 'Steady Eddies' held in the portfolio
- Experienced leadership; dedicated and seasoned team
- A longer term investment horizon with average holding periods in excess of 3 years

Risk disclosures

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 adverse economic and market conditions, prospects of stocks in the portfolio, changing interest rates, and real or perceived adverse competitive industry conditions. Investments in small and

medium capitalization companies generally carry a greater risk than is customarily associated with larger capitalization companies, which may include, for example, less public information, more limited financial resources and product lines, greater volatility, higher risk of failure than larger companies and less liquidity.

Important information: The views and opinions herein are those of Schroder's investment professionals, and are subject to change over time.

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