

# MUTUAL FUND PROCESS

## INVESTMENT PHILOSOPHY

LPL Research is an opportunistic, all-market, all-weather due diligence provider and portfolio manager. Through our investment and portfolio recommendations, we aim to avoid downside and capture upside. To this end, we are conservative when markets are tough and aggressive when they are rising. Though a very broad investment mandate, we believe this is the only way to effectively provide recommendations for our advisors and their clients.

The LPL Research Traditional Diligence team is responsible for intimate knowledge of the broader mutual fund universe, and each analyst is accountable for specific asset classes. The team follows a well-defined due diligence process when evaluating and recommending mutual funds.

The team seeks to find mutual funds that exhibit the following characteristics:

- Sound and intuitive investment thesis
- Rigorous, repeatable investment process
- Risk-adjusted performance that justifies an active management fee
- Performance through varied market environments that is consistent with expectations and the investment thesis
- Strong peer rankings over multiple periods
- Experienced portfolio management team
- Well-established back-office, compliance, trading, and client service functions
- Poised to perform well going forward, given the market environment our market team anticipates

The due diligence process consists of both quantitative and qualitative analysis. When recommending a mutual fund, the analyst must present data and research to the implementation committee regarding the management team, investment strategy, and performance profile.

- Firm and Management Team
  - Depth, knowledge, and experience of the investment team
  - Compensation structure
  - Organizational structure

There is no guarantee that a diversified portfolio will enhance overall returns or outperform a nondiversified portfolio. Diversification does not ensure against market risk.

- Investment Philosophy and Process
  - Investment strategy
  - Idea generation and analysis
  - Portfolio construction
  - Risk parameters and constraints
  - Sell discipline
- Performance Profile
  - Confirmation of our expectations
  - Ability and biases of the investment team

The Traditional Diligence team aims to recommend a diversified set of mutual funds with attractive risk and return characteristics. The group begins by screening the board universe using a proprietary peer group scoring system. This initial quantitative screen intends to reduce the list of potential funds by using several attributes, such as performance consistency, up- and down-capture participation (which measure the percentage of the benchmark's return captured by the portfolio in up and down periods), mean reversion tendencies (which refer to the likelihood of a fund's performance to move back toward its average, following periods of large underperformance or outperformance), and performance in volatile markets. The scoring system is not the deciding factor, but just one of the tools the analysts use to better understand potential mutual funds in their respective asset classes.

After conducting the screening and analysis, the analysts will coordinate several calls and meetings with the management teams of the mutual funds. In this part of the process, the analysts hope to question the management teams and learn more about the firm, their roles, investment strategies, and track records.

If a mutual fund progresses to the final stages of becoming a recommendation, the sponsoring analyst must make a presentation to the implementation committee. During this presentation, the analyst must lay out both the buy and sell discipline. No mutual fund can be recommended without a solid, actionable sell discipline. Each member of the Implementation Committee reviews the presentation, attempts to deconstruct the thesis, and asks further questions of the analyst. If those questions cannot be answered, the analyst must follow up with further analysis of the mutual fund before re-presenting. If the Implementation Committee has a consensus “yes” vote, the mutual fund will be recommended.

Once a mutual fund has been recommended, the sponsoring analyst has the responsibility to consistently monitor the mutual fund on an ongoing basis. Any issues regarding performance, people, process, or better options within the space must be discussed in a broad setting. This is primarily accomplished through the use of dashboards designed by the Traditional Diligence and Quant & Analytics teams.

Should an issue arise, the process is similar for a sell. The analyst will bring the mutual fund and potential issue to the Implementation Committee, where the committee will vet the sell presentation, ask the appropriate and necessary questions, and vote on the sell. If it is a consensus “yes” vote on the sell, the mutual fund will be removed as a recommendation. ■

#### IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide or be construed as providing specific investment advice or recommendations for any individual security.

Investing in mutual funds involves risk, including possible loss of principal. Investments in specialized industry sectors have additional risks, which are outlined in the prospectus.

Asset allocation does not ensure a profit or protect against a loss.

This information is not intended to be a substitute for specific individualized tax, legal, or investment planning advice. We suggest that you discuss your specific tax issues with a qualified tax advisor.

There is no assurance that the techniques and strategies discussed are suitable for all investors or will yield positive outcomes. The purchase of certain securities may be required to effect some of the strategies. Investing involves risks including possible loss of principal.

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