The AC Financial 2005
Guide to Successful 'Fund' Investment

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Whether you are looking to invest capital for income, growth, or have an existing investment portfolio that has provided disappointing performance, we believe that this document will prove invaluable.

Fact 1 - Many Investors select investments purely on recent fund performance

Fact 2 - The most popular funds can provide a disappointing return

Fact 3 - Investing in unpopular sectors often pays dividends

This document provides the evidence that following the herd, or a so called 'Star' fund manager, may not provide a satisfactory outcome.

To prove these points we tracked top fund managers and sectors over 25 years – the evidence is that the 'worst ' fund managers turned £3,437 into £1,000,000 and the 'best' fund managers turned the capital into an abysmal £1,323. The average fund manager in the best sectors provided a staggering £25 million + return. To find out how please turn to page 3.

We also show how the most popular fund sectors have historically provided a much smaller return than the least popular sectors! This is illustrated on page 4.

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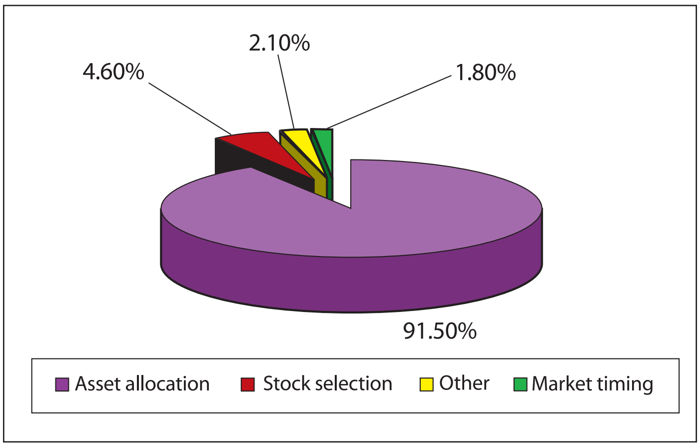
The Key to Investment Success

The research provided here relates to Unit Trusts and Open Ended Investment Companies (OEIC's) whether held individually, or within an Individual Savings Account (ISA), Personal Equity Plan (PEP) or a Pension Scheme. As will be seen, we believe that the asset allocation of any portfolio is of foremost importance and only when this is decided should consideration be given to specific funds.

Separating Fact from Fiction

There is much talk amongst certain commentators and some advisers about choosing the best fund manager as the panacea of successful investment. We believe that asset allocation is of far more importance, coupled with correctly identifying the investor's true risk profile. Once these two factors have been dealt with, fund manager selection may then be made as the third investment factor - not the first!

The key to Investment Success – Asset Allocation



Research has shown that over 90% of the difference between investment portfolios' returns is determined by asset allocation (the proportion held in shares, property, bonds and cash) of that investment portfolio. (Source: Brinson, Singer, Beebower 1991)

Whilst there are effectively four main asset classes to invest in – Equities, Property, Bonds and Cash, there are a much larger number of sub sectors within these asset classes. Indeed, the Investment Management Association currently lists 28 separate investment sectors encompassing over 2,000 (December 2005) different Unit Trusts/OEIC's within which investors may invest.

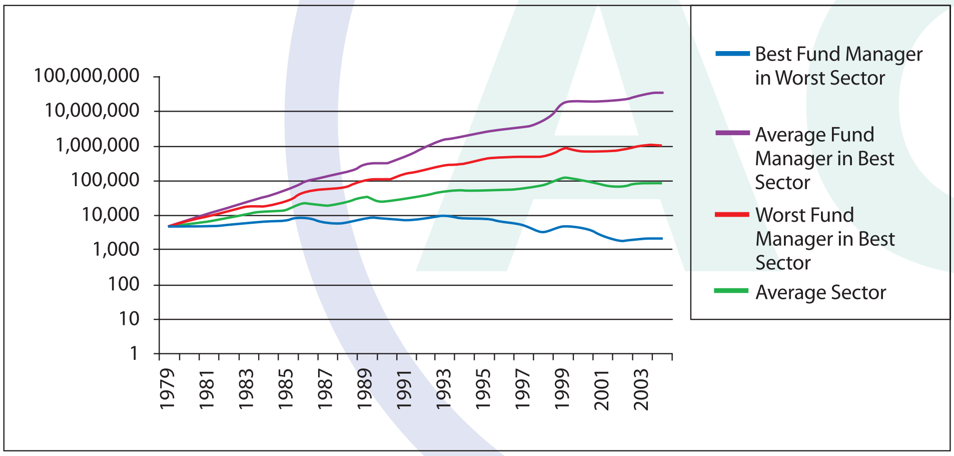
Why Choosing a Sector is more important than choosing a Fund

Our research also illustrates that choosing successful sectors is the most important factor in achieving growth. To tangibly illustrate this, we analysed Standard & Poor's (S&P's) Micropal sectors over 25 years and also looked at top funds and laggards over the same period. As will be seen, selecting the worst fund managers proved to be substantially more profitable than investing in so called 'top fund managers' funds' - providing that the sector selection was correct.

How the worst Fund Managers outperformed ‘Star’ Fund Managers

Chart showing that by selecting the worst performing fund managers in the best performing sectors each year, the investor enjoys a return of £1,000,000 compared to the best performing fund managers in the worst performing sectors that provided a derisory £1,323 - a loss of more than 61%. ***The average fund in the best sector each year provided a cumulative return of almost, a staggering £26 million!***

	Best Fund Manager in Worst Sector £	Average Fund Manager in Best Sector £	Worst Fund Manager in Best Sector £	Average Sector £
Start 1979	3,437	3,437	3,437	3,437
1980	3,933	5,758	5,758	4,510
1981	3,837	7,904	7,036	5,124
1982	4,570	11,201	9,176	6,368
1983	4,963	18,326	13,644	8,459
1984	4,838	23,785	15,283	9,734
1985	5,378	37,987	22,502	11,463
1986	5,930	67,343	36,138	15,505
1987	4,620	89,405	44,244	15,412
1988	5,028	123,522	50,660	17,926
1989	6,539	216,052	76,101	23,967
1990	5,596	238,392	81,101	19,816
1991	5,856	371,916	105,536	23,440
1992	5,920	558,878	139,012	28,076
1993	6,205	1,130,218	210,103	38,263
1994	5,481	1,326,085	224,327	36,418
1995	5,518	1,944,439	298,849	41,961
1996	4,424	2,304,549	325,864	55,542
1997	3,685	2,941,987	385,107	48,034
1998	2,843	4,131,138	358,688	53,303
1999	3,395	11,834,058	603,170	75,818
2000	2,899	13,140,538	550,996	72,604
2001	2,068	13,667,473	557,608	64,733
2002	1,356	14,595,494	576,622	53,787
2003	1,413	20,792,741	765,697	65,674
2004	**£1,323**	**£25,897,359**	**£1,000,000**	**£72,399**
% Return	**-62**	**753,426**	**28,997**	**2,007**
Annual Comp%	**-3.75**	**42.92**	**25.47**	**12.96**



Basis is £3,437 invested offer to offer with income reinvested. (Source of raw data: Standard & Poor’s Micropal) Please note that where funds were not available in the given sectors the nearest rated sector was selected.

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Choosing Sectors

In our experience most private investors select funds on the basis of recent performance without realising that most of the performance came about by the fund being in the right sector at the right time. Sectors tend to be cyclical and attract the greatest amount of new investors at the top of the cycle, just before a downturn, where the sector is overbought and due a correction. Again, to prove the point we looked at historic market history.

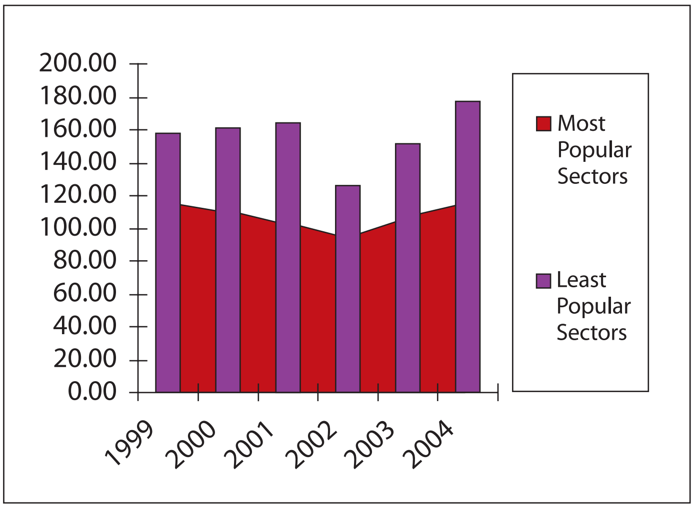
The Investment Management Association (IMA) collects data relating to sales of Unit Trusts/OEIC's, and we looked at the data for the most popular and least popular two sectors in terms of sales during the month of December for each of the six years 1998 –2003. We then followed the performance of these sectors over the following year.

Chart showing 12mth% performance 'offer to offer' all income reinvested from 1/1/1999 onwards. Performance of the two sectors in each category is averaged each year.

Year	Most Popular Sectors		Least Popular Sectors	
1999	UK Other Fixed Interest & UK Growth	14.99	International Growth & Far East Inc Japan	57.59
2000	UK All Companies & Global Specialist	-4.37	UK Money Market & North Am Specialist	2.61
2001	UK All Companies & Other Bonds	-6.24	Guaranteed/Protected Funds & UK Corp Bds	0.92
2002	UK All Companies & UK Corporate Bds	-8.51	UK Smaller Co's & Japan	-23.06
2003	UK Corporate Bonds & UK Equity Inc	12.9	Europe Excluding UK & North America	20.21
2004	UK All Companies & UK Corporate Bd	8.8	UK Smaller Co's & UK Equity & Bonds	17.18
Value of £100 on Januray 5th 2004		£115.88		176.86
Annual % Compond return		2.49%		9.97%

For investment in 2005 - The most popular two sectors in December 2004 were UK Equity Income, and Specialist **-** The least two popular sectors were Europe excluding UK, and North America

Cumulative return on £100 if reinvested using the same principle each year from 1st January 1999 – 3rd January 2005. Basis 'offer to offer' all income reinvested.



Source of raw data: Standard & Poor's Micropal

We trust that this information proves helpful and pinpoints strategies to be avoided!

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The next few pages will provide a strategy to improve long-term performance.

Balancing Sectors

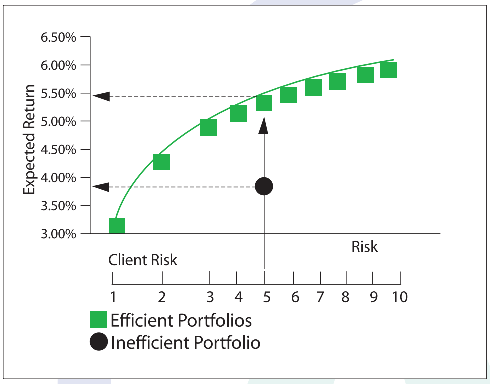
It is of course impossible to correctly identify the best single sector in advance, and therefore, it is prudent to invest in a balanced portfolio. This balance must take into account the investor's personal circumstances and risk profile. As can be seen on the previous page, even a broad balance covering all of the 28 S&P's Micropal sectors provided 12.96 % annual compound return.

An imbalance of sector selection based on personal risk profile will provide an inappropriate investment return. This could result in either too much volatility, and possible loss for a risk-averse investor, or not enough potential growth for a more adventurous portfolio.

The Right Balance for You

In 1952 Harry Markowitz, an economics post graduate, published his doctoral thesis 'Portfolio Selection'. This marked the beginning of what is now termed 'Modern Portfolio Theory' and in 1990 he won an economics Nobel Prize for his research.

This aims to efficiently balance a portfolio based on the assumed risk being taken to ensure that the maximum return is obtainable for that level of risk. For example, a low risk investor might assume that by merely investing in a deposit account with a AAA rated bank, he is making the best use of capital for the risk being taken. However, by adding slightly more risk bias, a disproportionately higher risk adjusted return may be possible. This is known as the Efficient Frontier – potentially greater return for a similar level of risk. The following chart illustrates this principle.



Risk Profile

For our advisory clients we can provide a computer generated personal risk profile based on the manner in which strategic financial questions are answered, or alternatively, investors may select their own risk profile. The risk score can vary from 1 to 10, with 1 being the least risky and 10 the most risky. A risk score of 1 will result in a suggested portfolio consisting mostly of cash, with 10 resulting in a portfolio heavily weighted in Equities. Intermediate scores will result in a broader spread of asset classes.

Sector Performance over various periods

Many investors limit their selection of sectors to a very narrow range – typically: UK Equity, Equity Income, Corporate Bonds, and maybe European and some American. However, followers of the ‘Efficient Frontier’ principle of investment would spread their investment more widely and encompass more exotic sectors and in so doing would actually reduce risk and provide greater potential for gain.

The following charts illustrate the average return in each sector over 1, 2, 4 and 6 years to 3rd January 2005. (Source of raw data: Standard & Poor’s Micropal).

UT/OEIC’s IMA Sectors	01/01/1999 03/01/2005		01/01/2001 03/01/2005		01/01/2003 03/01/2005		01/01/2004 03/01/2005		Volatility *
	% Chg	Rank	% Chg	Rank	% Chg	Rank	% Chg	Rank	
Sector	6 Yrs		4 Yrs		2 Yrs		1 Year		
S&P UT Fd Active Managed	14.14	20	-8.21	19	34.89	15	10.34	11	4.42
S&P UT Fd Balanced Managed	11.7	21	-6.48	18	28.31	20	9.12	14	3.67
S&P UT Fd Cautious Managed	17.8	16	6.27	12	22.34	21	8.55	16	2.48
S&P UT Fd Europe Excluding UK	8.31	25	-15.68	22	**43.99**	**7**	**13.61**	**7**	6.08
S&P UT Fd Europe Including UK	19.95	14	-15.91	23	36.79	13	10.15	12	5.4
S&P UT Fd European Sm Cos	**56.63**	**6**	-9.59	21	**73.85**	**1**	**24.55**	**1**	8.69
S&P UT Fd Far East Ex Jap	**57.78**	**5**	**17.69**	**5**	**46.17**	**6**	8.68	**15**	6.36
S&P UT Fd Far East Inc Jap	**48.31**	**7**	6.56	11	**40.86**	**9**	7.85	19	5.52
S&P UT Fd G’teed/Protected	9.15	24	5.07	15	12.84	24	5.99	22	1.25
S&P UT Fd Global Bond	17.25	18	**16.57**	**6**	10.88	25	3.56	25	1.69
S&P UT Fd Global Emg Mkts	**77.17**	**3**	**37.56**	**1**	**64.05**	**4**	**16.16**	**6**	7.08
S&P UT Fd Global Growth	0.33	26	-21.09	24	30.79	18	8.26	17	5.11
S&P UT Fd Japan	16.43	19	-21.55	25	31.48	16	6.06	21	5.78
S&P UT Fd Japanese Sm Cos	**100.62**	**1**	**8.9**	**10**	**63.67**	**5**	**22.72**	**2**	6.22
S&P UT Fd Money Market	20.55	13	**11.22**	**8**	4.95	28	2.62	26	0.09
S&P UT Fd North America	-13.26	27	-33.02	27	15.04	22	1.19	27	6.28
S&P UT Fd Nth American Sm Cos	18.94	15	-23.82	26	35.05	14	7.88	18	8.12
S&P UT Fd Specialist	**70.27**	**4**	5.74	14	**43.19**	**8**	**11.01**	**10**	7.51
S&P UT Fd Technology&Telecoms	-28.28	28	-60.29	28	37.29	12	0.35	28	12.14
S&P UT Fd UK All Companies	10.5	22	-9.1	20	37.64	11	**12.76**	**8**	4.52
S&P UT Fd UK Corporate Bond	**27.74**	**10**	**21.32**	**3**	9.71	26	4.84	23	1.25
S&P UT Fd UK Equity & Bd Inc	23.53	12	**10.18**	**9**	28.97	19	**11.99**	**9**	2.94
S&P UT Fd UK Equity Income	23.65	11	5.84	13	**40.77**	**10**	**16.18**	**5**	4.3
S&P UT Fd UK Gilt	17.68	17	**13.2**	**7**	5.66	27	4.71	24	1.28
S&P UT Fd UK Index Linked Gilt	**31.47**	**8**	**20.5**	**4**	**13.5**	**23**	7.75	20	1.54
S&P UT Fd UK Other Bond	**29.84**	**9**	**23.58**	**2**	31.39	17	9.33	13	1.92
S&P UT Fd UK Smaller Cos	**81.07**	**2**	-0.5	16	**69.79**	**2**	**22.36**	**3**	6.44
S&P UT Fd UK Zeros	9.54	23	-4.29	17	**68.26**	**3**	**18.11**	**4**	N/A
Mean/Count	27.82	28	-0.69	28	35.07	28	10.24	28	4.74

The top ten sectors in each category are highlighted in bold

* Volatility measures the monthly standard deviation over 3 years to 3/1/2005. A low figure is considered to be less risky than a large one. A good example is the Money Market sector, which is, in effect, a cash deposit and therefore carries no risk, being the lowest volatility at 0.09%. Conversely, the Technology and Telecoms sector – a highly risky sector shows the highest volatility at 12.14%.

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Selecting Individual Funds

Few private investors would be able to put all the pieces of this jigsaw together. A possible solution might be to select one, or more, well managed 'Fund of Funds' of the type that use other fund management funds to create a diversified portfolio. We can provide research into these funds if required, including risk assessments.

Other investors might prefer a personalised portfolio, in which case it is important to ascertain an appropriate risk level. For these investors we can provide a recommended asset allocation structure. The object will be to utilise the 'Efficient Frontier' principle of investing (see previous paragraph). Finally, following this, we will select appropriate funds within the allocation criteria, utilizing fully researched funds provided by Standard & Poor's fund rating service and/or others.

This research involves analysts interviewing fund managers of successful funds and then rating them on an A, AA, or AAA basis. Only around 20% of the 2,000 + Unit Trusts/OEIC's qualify for rating.

We are able to identify risk and allocation based on the world economic conditions by utilizing top investment house research, including sophisticated software that has been partly developed by Watson Wyatt Worldwide, global leaders in investment consulting.

Services provided for the Investor

The AC Financial Portfolio of all Sectors

This is designed for the advisory client/investor who is looking to index the average performance of all sectors. Because an index of all funds is not available we will construct a portfolio that invests an equal amount into each sector. Investors with larger portfolios might consider using such a portfolio as a core holding, with a balance made up by being overweight in favoured sectors. The portfolio will consist of an individual fund in each of the 28 sectors that has been selected using sophisticated gain/loss ratio analysis over the previous calendar year. This method of analysis is used to identify a consistent return and to attempt to avoid funds that are too volatile. Over 25 years the average of all sectors to 3/1/2005 would have provided a compound annual return of 12.96% on an 'offer to offer' basis.

The AC Financial Bespoke Service

This is designed for the investor who has specific income/growth objectives and/or requires a portfolio personally designed for them. Personal risk profiles are undertaken prior to an asset allocation model being drawn up and then populated with funds that will be selected using sophisticated research facilities. Consideration is also given to the many points raised in this document and in particular, an attempt to avoid markets that may have peaked.

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Execution Only Clients

For those investors who wish to make their own decision on funds but also wish to receive our regular mailing and periodic research on sectors, we provide an execution only service. This will involve heavy discounts on transaction costs but will exclude personal investment advice.

Our Services may be extended to the following Catergories

Pension Funds : Sipps, Ssas's, some personal pension (PP) schemes - PP schemes that do not currently qualify may be transferred into schemes that do.

Investment Bonds: Some investment bonds allow external investment into a range of Unit Trusts covering the entire sector spectrum.

Unit Trust Portfolio's: *Existing Funds*- In conjunction with a major investment institution we can transfer existing Unit Trusts/OEIC's into a personally designed balanced portfolio.

Pep's & ISA's: In conjunction with major investment institutions we can transfer existing Unit Trusts/OEIC's into a personally designed balanced portfolio. This may be of particular interest to investors who invest annually into fashionable funds, and now may have a portfolio that lacks direction.

For a 'no obligation' discussion please contact Stephen Charles on 0207 593 5620 or email stephen@ac-financial.co.uk

Risk Warnings and Disclaimers

- All statistics illustrated in this document are based on raw data obtained from Standard & Poor's Micropal and other sources considered to be reliable. As much of this data is computer based we are not responsible for information that is incorrect due to computer data malfunction. The information is provided in good faith and as such we trust that it is received in the same manner.

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- Past performance is not necessarily a guide to future performance.

- Investors should be aware that investment into Unit Trusts/OEIC's may be subject to volatility and that their investment and/or income derived from it may rise or fall in value. This means that if you need to sell, at a time that coincides with a fall in the value of your fund, you may lose money.