

## Oppenheimer Capital Global Shares Fund

31 Dec 2004

The Oppenheimer Capital Global Shares Fund is a benchmark aware international shares fund, but one which offers greater upside (and downside) through its higher tracking error approach to managing global equities. The portfolio construction process adopted by the investment manager, Oppenheimer Capital (Oppenheimer), is a high conviction, relatively concentrated approach, which should appeal to investors wanting more "bang for their buck" from an active international shares manager.

Oppenheimer is the global equity value platform of Allianz Dresdner's suite of equity managers. Oppenheimer has been managing money with an intrinsic value philosophy since its inception in 1969. This is important, as Oppenheimer has a well-established research platform and investment process to leverage off, both of which have operated across a number of different market cycles.

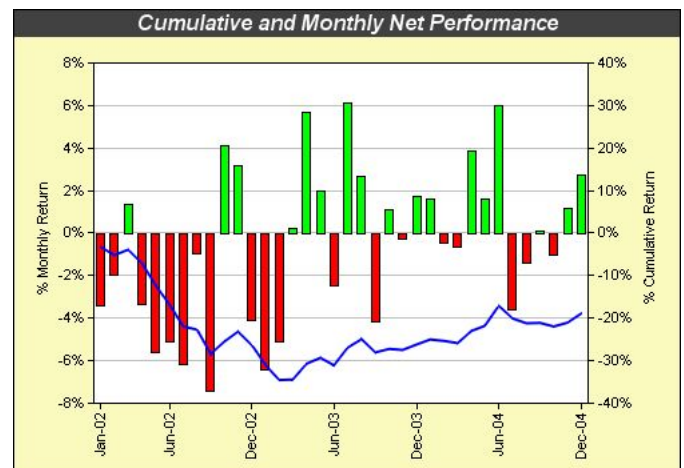
Oppenheimer's philosophy is based on the premise that consistent investment in stocks at a discount to intrinsic value is a key driver of superior long term excess returns. Intrinsic value is essentially the value of a company's long term cash flows. Oppenheimer believes it differentiates itself from more traditional value managers, in that it does not simply buy stocks based on statistical cheapness (i.e. low multiples), but in addition focuses on the quality of each stock. Zenith's style analysis of this Fund shows it displays a value (i.e. statistical cheapness) / large cap (i.e. quality) bias, which is consistent with this statement.

Ultimate responsibility of this Fund rests with Elisa Mazon as Global Portfolio Manager. Mazon is assisted by Pawel Wroblewski (Global Equities Specialist), Colin Glinsman (CIO and North American Equities Specialist and "backup" Portfolio Manager) and a moderately sized investment team of 31 individuals, which are divided into global sector teams. In many ways, Oppenheimer is structured more like a boutique in that research analysts cover multiple sectors and portfolio managers also share analytical duties. Zenith believes this facilitates internal communication between analysts and portfolio managers and ensures that there is a team based investment approach.

Based on an expected tracking error range of 5.0-8.0% p.a., the performance target for the portfolio is 2.5% - 5.0% p.a. excess return over the benchmark. This objective places the manager in the high alpha (high excess return) space of managers in this sector. Referring to performance generated over the past five years, Oppenheimer has achieved this target, outperforming its benchmark by 4.57% p.a. While performance is slightly stronger in falling markets, which is a consistent trait with value managers, the Fund also has a commendable record in rising markets.

Based on a strong and differentiated investment process and an impressive long term historical track record, Zenith believes the Fund is a sound option for investors looking for a global equities manager. Oppenheimer's boutique characteristics, its intrinsic value and higher tracking error approach should also appeal to investors unimpressed by the "plain vanilla" low tracking error approach adopted by many retail international shares managers. Accordingly, Zenith rates the Fund **APPROVED**.

Key Features	Description
Asset Class	International Shares
Sub-Asset Class	Global
Investment Style	Value
Benchmark	MSCI World ex Aust \$A
Return Objective	2.5% to 5.0% above benchmark p.a.
Tracking error (% p.a.)	5 to 8 (% p.a.)
Recommended Investment Timeframe	5 + years
Expected Portfolio Turnover	70 - 90 % p.a.
Portfolio Manager	Elisa Mazon
Investment Team Size	31
Leverage	No



## Performance Analysis

Performance Statistics	5 Yrs (% p.a.)	3 Yrs (% p.a.)	1 Yr (% p.a.)
Performance - Fund	-1.50	-6.81	9.91
Performance - Benchmark	-6.07	-7.37	10.36
Performance - Median Manager	-5.39	-6.47	9.92

### Long Term Performance

The absolute return produced by the Fund has been negative over the past three and five years. However, in assessing the absolute performance of international share funds over these periods, it is important to bear in mind that it has been an extremely poor period for global equity markets. In addition, the rise of the \$A has had the effect of further eroding returns for unhedged funds.

On a relative basis, Oppenheimer has an excellent track record over the past five years outperforming its benchmark by 4.57% p.a.

Over the past three years, performance is more in-line with that of its MSCI benchmark and median manager.

### Short Term Performance

Over the past year, the Fund has slightly underperformed its index and produced a strong absolute return of 9.91%, helped by a rebound in global equity markets.

### Current Positioning

While the Fund selects stock on a bottom up basis, the output of the Fund's stock selection has resulted in a significant underweight of US stocks and a significant overweight of European stocks.

In terms of sector positioning the Fund is most overweight the Materials and Consumer Discretionary sectors, while most underweight Utilities, Consumer Staples and Information Technology.

The Fund currently holds 70 stocks and is running a cash weighting of 2.21%.

The top ten holdings currently represent 23.68% of the total portfolio and include names which are not necessarily represented as large constituents of the MSCI Index. This is evidenced by the fact that the total of each of the names represent only 2.20% of the MSCI Index. This illustrates that Oppenheimer is not afraid to take large active bets.

Stocks currently included in the top ten holdings in descending order are: Boehler Uddeholm, Swatch Group, Wal Mart Stores, Tyco Intl, Intel Corp, Tiffany & Co, Conoco Phillips, DIRECTTV Group, SKF AB and Morgan Stanley.

## Consistency Analysis

Consistency Statistics	5 Yrs (% p.a.)	3 Yrs (% p.a.)	1 Yr (% p.a.)
History of Monthly Excess Return (%)	58.33	55.56	41.67
History of Monthly Excess Return (Rising Mkts %)	51.72	55.56	37.50
History of Monthly Excess Return (Falling Mkts %)	64.52	55.56	50.00

In terms of consistency, the Fund has performed above benchmark in over 58.33% of months over the past five years. While performance is slightly stronger in falling markets, which is consistent trait with value managers, the Fund also has a commendable record in rising markets.

Over three years, the Fund has outperformed its benchmark 55.56% of months and delivered consistently strong returns in both rising (55.56%) and falling (55.56%) markets. Zenith believes the consistency of outperformance is a strong sign that the investment process is working and repeatable.

## Risk / Return Analysis

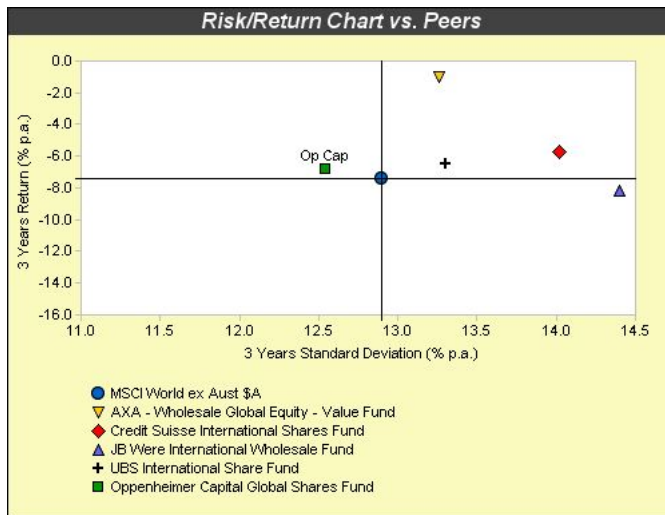
Risk / Return Statistics	5 Yrs (% p.a.)	3 Yrs (% p.a.)	1 Yr (% p.a.)
Information Ratio - Fund	0.68	0.21	-0.17
Information Ratio - Median Manager	0.16	0.04	-0.29
Sharpe Ratio - Fund	-0.57	-0.95	0.50
Sharpe Ratio - Median Manager	-0.82	-0.88	0.57
Standard Deviation (% p.a.) - Fund	12.12	12.54	8.54
Standard Deviation (% p.a.) - Median Manager	12.90	13.14	7.68
Tracking Error (% p.a.) - Fund	6.68	2.75	2.63
Tracking Error (% p.a.) - Median Manager	4.73	3.98	2.96

Over the past 5 years, the Fund has produced superior relative returns with less volatility (as measured by standard deviation) to the overall market, which is an excellent result. In terms of risk adjusted performance, the Fund has also generated a superior information ratio over the longer term relative to its competitors. While the Fund has not performed well on a Sharpe ratio measure, this is in part attributable to the poor absolute returns of global equity markets compared to the risk free (cash) rate over this period.

The Fund's 3 year risk adjusted returns are mixed, with the Fund performing slightly better based on Information ratio and slightly worse based on Sharpe ratio compared to the median manager.

Over the past year, small underperformance of the Fund versus benchmark has resulted in a disappointing information ratio while strong global equity markets have helped deliver a relatively stronger Sharpe ratio result.

The Fund's tracking error (volatility of excess returns to the benchmark) is higher than that of other international equity managers and consistent with the expected tracking error range of the Fund (5.0-8.0% p.a.) over the past 5 years. However over the past 1 and 3 years, tracking error has dropped below the Fund's usual range. Zenith believes this is a short term phenomenon based on less volatile movements in equity markets and higher correlations between sectors. Over the course of a full market cycle, Zenith would expect the tracking error of the Fund to return to its targeted range.



### Investment Personnel

Name	Title	Time with Manager
Elisa Mazen	Portfolio Manager	11 Yr(s)
Colin Glinsman	Chief Investment Officer	15 Yr(s)
David S. Phillips	Head of Research	9 Yr(s)
Pawel Wroblewski	Assistant Portfolio Manager	6 Yr(s)

Oppenheimer Capital (Oppenheimer) is the global value equity platform of Allianz Dresdner's (Allianz) suite of equity managers, which includes Cadence, RCM, NFJ Investment and Nicholas Applegate. Oppenheimer operates all investment management functions autonomously from its parent and all other Allianz owned managers, which we believe is important in maintaining Oppenheimer's culture and ongoing sustainability. However, the manager is able to leverage off Allianz's non-investment management functions of compliance, legal, human resources, technical and financial support.

Oppenheimer has been managing money with a research driven, intrinsic value philosophy since its inception in 1969. This is an important point, as Oppenheimer has a

well-established research platform and investment process to leverage off, both of which have operated across a number of different market cycles.

Assets under management (AUM) of approximately USD 36 billion are dominated by US only equity mandates. However, Oppenheimer has been running global equity portfolios since 1994, with AUM now totalling approximately USD 1.7 billion. While the management of global equities has not historically been the focus of the business, Oppenheimer appears well structured to effectively manage global equity portfolios. This is supported by the fact that incoming CEO, Bruce Koepfgen (ex-Salomon Smith Barney), is now focusing on global equities as a flagship product of the business.

Ultimate responsibility of this Fund rests with Elisa Mazen as Global Portfolio Manager. Mazen is assisted by Pawel Wroblewski (Global Equities Specialist), Colin Glinsman (CIO and North American Equities Specialist and "backup" Portfolio Manager). The three member structure provides the ability to make cross border comparisons of stocks within a sector in pursuit of the most compelling values.

Mazen and the regional specialists are assisted 31 member research team, under the direction of David Phillips (Director of Research). All senior professionals were made available to Zenith in our due diligence of Oppenheimer, which is testament to Oppenheimer's commitment to raising its profile in global equities.

The Oppenheimer research team is divided into global sector teams. Within each sector team, analysts are either focused on US stocks or Global (ex-US) stocks. Of the 31 research analysts, 20 are global (ex-US) analysts, while 11 are US analysts. Over the past few years, Oppenheimer has increased its focus on increasing its number of global analysts, which is a positive for this portfolio. Within these areas of responsibilities, analysts are not assigned specific stock responsibilities and have the freedom to target the stocks that they are most attracted to, based on their own methods of analysis. Oppenheimer believes this approach reduces the reliance on one person's perspective for individual stocks and promotes debate amongst sector team members, who may also be looking the same stocks. However, this approach may also result in Oppenheimer missing opportunities as there is an inefficient coverage of the entire universe.

In many ways, Oppenheimer is structured more like a boutique, in that:

- Research analysts tend to have responsibilities for up to two sectors and hence have overlapping roles. This approach ensures each analyst gains exposure to a broader range of issues;
- Portfolio managers also have stock research responsibilities. Zenith believes this facilitates internal communication between analysts and portfolio managers and ensures that there is a team based investment approach; and
- All of the investment team is centrally located in New York. While there are benefits for having analysts "on the ground" in key locations across the globe, there are also benefits from having the team centrally located -

the primary benefit being increased communication. Analysts are also encouraged to travel and tend to average 2 trips every month.

- Price to free cash flow;
- Price to sales; and
- Enterprise value to invested capital.

Staff turnover within the investment team is relatively low, averaging less than 10.0% over the past two years. An attractive performance based variable component of total compensation assists in retaining staff. Analyst performance is evaluated primarily by the impact of their recommendations on client portfolios. It is important not only that the analyst's stocks perform well, but that the analyst successfully engages portfolio managers to accept his or her recommendations by including those securities in client portfolios. Portfolio managers and senior research analysts are notified of a target bonus at the beginning of each calendar year, in addition to a base salary. The bonus is highly variable and represents the majority of their compensation. The actual bonus paid at the conclusion of the calendar year is adjusted to between 0% and 200% of the original target. The amount depends exclusively on the quantitative performance of individual research ideas, the impact of those ideas on client portfolios, and, in the case of portfolio managers, performance of their accounts. There are no subjective judgments affecting the percentage of the target bonus that is paid.

### Investment Process

Oppenheimer is a benchmark aware manager that seeks to outperform the MSCI World ex-Australian Index over a full market cycle through bottom-up stock analysis and active portfolio management.

More specifically, based on an expected tracking error range of 5.0-8.0% p.a., the performance target for the portfolio is 2.5% - 5.0% p.a. excess return over the benchmark. This objective places the manager in the high alpha (high excess return) space of managers in this sector.

Oppenheimer's philosophy is based on the premise that consistent investment in stocks at a discount to intrinsic value is a key driver of superior long term excess returns, with intrinsic value being the value of a company's long term cash flows. Oppenheimer believes it differentiates itself from more traditional value managers, in that it does not simply buy stocks based on statistical cheapness (i.e. low multiples), but in addition focuses on quality. Zenith's style analysis of this Fund shows it displays a value (i.e. statistical cheapness) / large cap (i.e. quality) bias, which is consistent with this statement.

The driver of Oppenheimer's process is its research capability. Oppenheimer focuses on developing differentiated insights about a company's intrinsic value. Research concentrates on identifying undervalued stocks based on temporary earnings weakness being misperceived to be permanent and/or when the sustainability of profitability is underestimated.

Cash flow analysis is the core valuation component with Oppenheimer Capital. However, the investment team tends to utilise a combination of the following valuation criteria to assess an investment's attractiveness:

- Discounted cash flow;
- Enterprise value to earnings before interest taxes depreciation and amortisation (EBITDA);

### Security Selection

The first step of the stock selection process is defining the universe. The universe that Oppenheimer looks at includes all US stocks with a minimum market capitalisation (cap) of \$5 billion and all non-US stocks with a minimum market cap of \$2.5 billion. Factors such as liquidity, free float, and trading volume of the specific security are also considered.

Step two of the research process attempts to "knock out" groups of companies that are too expensive on industry metrics, have unacceptably poor balance sheets, are in non-competitive industries or have poor business models. The end result of this stage is that the investment universe is typically reduced to around 800 stocks. This stage involves some qualitative input which is labour intensive. While Zenith believes Oppenheimer may benefit from the introduction of more formalised quantitative screens for each sector to filter the universe down to a more manageable level, Oppenheimer disagrees as they focus on those specific areas which they believe drives the mispricing in the marketplace, rather than recreating the excess information available through the sell side. Therefore this qualitative triage of the universe by Oppenheimer analysts and experienced, senior portfolio managers, while time-consuming, is ultimately a productivity advantage because it allows them to leverage their efforts, hone in on the essentials and thereby be more productive and effective than using macro-screening done by other managers.

Step three is the research prioritisation or stock assignment stage. This is primarily driven by the analysts in which stocks they wish to investigate further in their sectors. This approach provides an enormous amount of flexibility to the analysts but also a level of freedom to develop their own filtering devices and stock identification mechanisms. This approach must be properly co-ordinated so that there is adequate coverage of the entire universe and no excessive "doubling up" of research ideas. Positively, the research prioritisation stage is closely monitored by the research director David Phillips and oversight from the CIO, Global PM and Sector Managers.

Step four is the fundamental research stage, which aims to identify and value the expected fundamental changes in the nature of the business by establishing reasons for any current discount. An investment thesis is produced which includes an analyst rating and all specific risks attached to that stock. This standardisation of research output is viewed positively as it assists in portfolio construction decisions made by Eliza Mazen in that it clearly articulates the reasons for holding a stock and includes a price target based on the stock's intrinsic value. Once a stock has been researched and positively rated, an analyst must present their findings to all investment professionals and get the sector leader's approval for placing the stock on a recommended list. Each stock included on the recommended list must represent at least 30.0% upside based on the analysts' intrinsic valuation of that stock.

## Portfolio Construction

The aim of the portfolio manager, Elisa Mazen, is to generate excess returns primarily through stock selection and only residually through sector and regional weightings.

Stocks are selected from the analysts' recommended list. As the recommended list typically contains approximately 200 stocks, the portfolio manager must narrow this down to a final portfolio of around 85 stocks. As such, there is a high reliance on the skill of Elisa Mazen in selecting the final list of stocks and accordingly a degree of key person risk applies. Zenith typically prefers an approach whereby stock positions are more aligned to analysts' ratings to ensure continuity of over time and a smoother transition periods should portfolio managers depart. Despite this, Oppenheimer's process has been tried and tested over multiple market cycles and its differentiated investment process may lead to lower correlation with other managers. We also acknowledge that Oppenheimer cannot compete with the investment team sizes of the "heavyweights" in this sector (Fidelity, Wellington, UBS etc) and as such a different approach is needed.

In terms of the weightings of stock positions within the portfolio, it tends to be fairly concentrated in the top 10 highest conviction stocks, which tend to form approximately 25.0% of the portfolio. Stocks entering the portfolio tend to enter at a 1.5% to 2.0% position and then monitored before the position size to increase. Although the maximum single stock limit is 5.0% at cost, the portfolio manager may let this position run to 7.0% before trimming that position. Again, stock weightings are more the responsibility of the portfolio manager and less reliant on the analyst rating applied to each stock.

Oppenheimer entails a review process that considers stocks incrementally. That is, whether the global portfolio manager would buy the stock today if it was not already included in the portfolio. A sell review is triggered if: the stock's price appreciates to full intrinsic value; the fundamentals of the stock are predicted to change; a stock's price moves sharply in either direction; or a more attractive investment opportunity becomes available. Zenith believes Oppenheimer's sell discipline is assisted by the clear price targets provided by each analyst for all recommended stocks.

Portfolio turnover has ranged from 70-90% which is lower than most US based global equity managers, but higher than Australian equities value managers. However, this includes "trimming" and "building" positions in portfolio holdings whereas there has not been a 70-90% change in the names of the companies held in the portfolio.

## Risk Management

Portfolio Constraints	Description
Cash (%)	0% to 5%
Tracking error (% p.a.)	5% p.a. to 8% p.a.
Weight - Emerging Markets Rel. Index (%)	-10% to 10%
Weight - Holding Rel. Portfolio (%)	0.5% to 5%
Weight - Regions Rel. Index (%)	-10% to 10%

A typical global equity portfolio will contain approximately 85 stocks. Stock positions will vary from 0.5% to 5.0%. Zenith welcomes the use of a minimum stock position as it prevents the manager from holding a portfolio with a long tail of meaningless positions.

Portfolios are also managed on a fully invested basis, with a maximum of 5.0% cash position allowed.

Further hard constraints restrict investment in countries and sectors to 10.0% of the benchmark MSCI World ex-Australia Index. While the tracking of the Fund is higher than average, these constraints should ensure that the portfolio is always well diversified in both countries and sectors.

Currency hedging will be used sparingly and only on a defensive basis where Oppenheimer's bottom up strategy results in an overweight in a particular currency versus the benchmark. In that case a hedge to a maximum of 25% for that particular block may be applied.

Past and projected tracking error is controlled as well as other measurements of style, such as returns based style analysis.

Oppenheimer uses Northfield software to analyse portfolio risk exposures to a range of economic factors. Northfield is a competitor to Barra and its use is becoming more common, particularly for US based fund managers.

Overall, Zenith believes the risk management constraints and risk software Oppenheimer has in place are sound and should help to ensure that there are no unintended risks contained in the portfolio.

## Risks of the Fund

- The Fund may underperform when the equity market is not following fundamentals or not supportive of large cap value stocks.
- The Fund is not fully hedged and therefore is exposed to currency fluctuations.
- Heavy reliance on Eliza Mazen as sole global portfolio manager.

## Applications of the Fund

3 Years Excess Correlation Table	
Fund Name	Excess Correlation
AXA - Wholesale Global Equity - Value Fund	-0.09
Credit Suisse International Shares Fund	0.05
JB Were International Wholesale Fund	0.09
UBS International Share Fund	-0.34

The Oppenheimer Capital Global Shares Fund is a benchmark aware fund, but one which offers greater upside (and downside) through its high tracking error approach to managing global equities. The portfolio construction process adopted by Oppenheimer is a high conviction, relatively concentrated approach, which should appeal to investors wanting more "bang for their buck" from an active international shares manager.

Investors using this Fund as a single option should be aware that the Fund has historically displayed a value, large bias, which may result in underperformance when the market is not favoring these stocks. However, as the Fund has performed creditably in both rising and falling markets and its value bias is certainly not "deep value" (ie. like Bernstein), Zenith believes the Fund can be used a sole international equities holding or blended with a manager or managers with complementary investment styles.

An option is blending the Fund with either JB Were International Wholesale Share (Wellington) or Credit Suisse International Share Fund (Capital), which have a slight growth biases and perform strongly in rising markets, which should complement Oppenheimer. To then increase diversification and potentially improve the risk / reward profile of the portfolio, blending these funds with a satellite manager with an allocation of less than 20.0% (e.g. Platinum International Fund, PM Capital Absolute Performance Fund, Macquarie Morgan Stanley Global Franchise Fund) is also an attractive option.

As the Fund's portfolio turnover is also below average when compared to competitors in this sector, we expect the majority of the Fund's to be delivered via capital appreciation in the unit price (rather than through the realisation of capital gains in income distributions) which is ideal for those investors seeking a capital growth oriented investment.

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