

THE FRONTIER PROCESS

Our Investment Management Process

Solving the Puzzle

Portfolio managers are faced with a puzzle. On the one hand, they operate in a world full of uncertainty. What will the markets do this year, next year, five years from now? What events will change the current landscape? How will it change? When will it change? How long will the change last?



On the other hand, clients have very well-defined needs for the future. They need to fund their retirement. They need to finance their children’s education. They have charitable giving aspirations. These goals are real, unique and very personal. They must be fulfilled within a finite time period.

The portfolio manager’s job is to help clients meet these concrete goals while skillfully navigating an uncertain and ever-changing world. This requires the consistent application of a disciplined process that works no matter what the future holds.

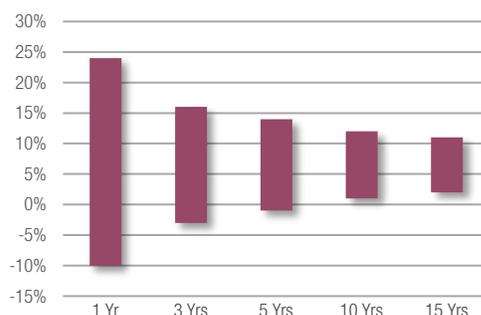
Frontier’s investment process is the product of over 25 years of research and in-the-trenches portfolio management experience. It builds on time-tested investment management principles, but includes many enhancements that have grown out of our research and experience. Our process is highly disciplined and is driven by factors we can observe and measure, not speculation about the future.

Defining Objectives

We believe that every investment strategy should have specific return and risk targets to reflect client needs. So for every strategy, we establish well-defined performance objectives that include a long-term return target and limits on downside risk. We pay close attention to these performance objectives in the management of each strategy. We set these objectives so our clients, working together with their financial advisors, can determine which Frontier strategy is most appropriate for them.

Performance Objectives – Balanced Strategy

Expected Range of Returns



The process we use to achieve our performance objectives is summarized in the following pages. Although it has produced solid results for our clients over the years, we are constantly trying to improve it, because we know that our clients rely on us to guide them through an uncertain future toward the achievement of their personal goals.

Finding Top-Quality Managers

Every investment strategy we manage consists of carefully selected mutual funds combined specifically to achieve its performance objectives. All funds are purchased on a “no-load” basis and we use many institutional funds that are not generally available to retail investors. We do not offer any proprietary mutual funds. We value the diversity of thought and the depth of talent we can access by drawing from the entire universe of mutual funds and believe that operating our own funds would represent a serious conflict of interest.

There are many reasons why we use mutual funds in our strategies. Mutual funds give us access to many of the world’s most highly skilled investment managers. They also allow us to manage risk by creating highly diversified portfolios. Mutual funds are also highly regulated and closely scrutinized by research firms like Morningstar and Lipper. In addition, they are very liquid and can be traded quickly and efficiently - important benefits in a rapidly changing investment environment.



Although mutual funds offer many benefits, as in any endeavor, some mutual fund managers are more skilled than others. Our goal is to find those managers who we believe have consistently demonstrated skill in varying market environments.

It is easy to find investment managers who have performed well in the past. It is far more difficult to identify those that are likely to perform well in the future. The key is distinguishing those who are truly talented from those who have merely been lucky.

Measuring Skill



We use a proprietary screening process to find skilled managers. Our process has both qualitative and quantitative aspects. Over the years we have discovered that both are required to identify managers who are skilled and have the intangible characteristics we seek.

The heart of our quantitative process is our use of a technique known as “returns-based style analysis.” Style analysis helps us identify managers that have truly demonstrated skill in the past and can do so again in the future.

Style analysis is widely used in the investment world. Frontier’s Founding Principal and Chief Investment Officer, Gary A. Miller, CFA, was one of its original developers and the first person to use it in managing portfolios. Our depth of experience using style analysis and our understanding of its subtleties give us a significant advantage in our search for skill.

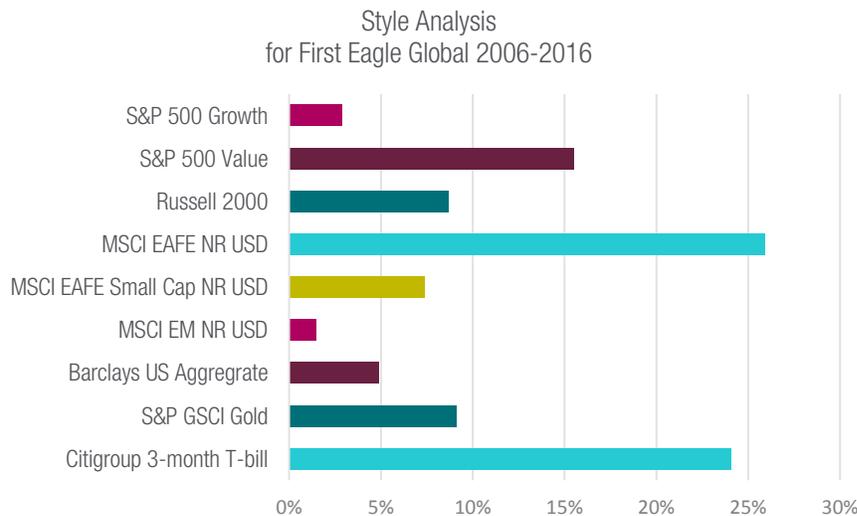


The traditional approach to manager selection attempts to assess manager ability by categorizing each manager in a “style-box” and then comparing the manager’s performance to a single index and/or a peer group of other “similar” managers. We believe this unidimensional approach leads to poor results.

Most managers don’t invest narrowly in a single asset class. They pursue opportunity wherever they find it and, in doing so, use many diverse strategies. This diminishes the usefulness of measuring manager performance against a single index benchmark and renders the creation of meaningful peer groups impossible.

A More Accurate Approach

Rather than trying to determine a manager’s skill using a single index or an arbitrarily defined peer group, we build a unique style benchmark for each manager. The benchmark consists of the combination of indexes that best explains the manager’s performance. In this way, we determine a manager’s ability using a benchmark that reflects how that manager actually invests.



Once we have built a unique style benchmark for a manager, we use it to analyze the manager’s performance. We look for managers who have consistently performed better than their style benchmark over time and have done so without major shifts in their investment approach. Consistency of both skill and approach gives us confidence the manager will continue to perform well in the future.

Understanding the Intangibles

Skill, alone, is not enough. Once we have identified managers that we believe can produce consistently solid performance going forward, we use our qualitative screens to identify those that embody the intangible characteristics we believe are important in skilled managers.

Every manager has a unique approach to investing and a unique set of characteristics that define the firm and its culture. We are looking for managers with experience, who will act in the best interest of our clients, are passionate about investing, manage assets using a unique strategy, are flexible in their approach, charge a low fee for their services and are highly motivated to generate results that will benefit our clients. Not all managers have all of these qualities, but we look for managers with as many of them as possible.



An Eclectic Combination

Once a manager successfully passes through both our quantitative and qualitative screens, we add them to our “hire” list. Our hire list usually includes between 200 and 250 mutual funds representing a wide array of asset classes and investment styles.

We believe that our hire list contains some of the most highly skilled money managers in the world. However, we do not develop emotional attachments to any of them. We review our hire list frequently and subject the managers on it to ongoing analysis.



We are not reluctant to delete managers from the list if they no longer deserve a place on it. Even those that continue to perform well are viewed by us with a sense of professional skepticism. We actually expect every manager to deliver less “alpha,” or performance above its customized benchmark, in the future than it did in the past.

The Diversification Process

We design a long-term asset allocation mix for each strategy we manage. An asset allocation mix is simply a plan for how the assets in an investment strategy will be divided among various “asset classes.”

By properly diversifying our strategies across many different asset classes we can take advantage of their varying performance characteristics. While certain asset classes may perform well in one market environment, others may lag. But when market conditions change, those that lagged may perform better than yesterday’s top performers. In this way, the right combination of asset classes can work together to improve long-term return while reducing overall portfolio risk.

In building strategies we use the following 16 asset classes. They give us broad access to the total investment universe and allow us to build highly diversified investment strategies for our clients. We may modify the list if we believe it will improve our strategy construction process. Plus our fund managers may even use different asset classes.

Our List of Asset Classes

US Equity	International Equity	Fixed Income	Alternatives	Real Assets
US Large Stocks	Int’l Large Stocks	High-Quality US Bonds	Absolute Return	REITs
US Small Stocks	Int’l Small Stocks	LT US Government Bonds	Managed Futures	Commodities
	Emerging Markets	International Bonds		TIPs
		Floating Rate Securities		
		High-Yield Bonds		
		T-Bills		

Developing the Strategy

For each investment strategy we establish an asset allocation mix that we call our “Target Long-Term Allocation.” This is the allocation we believe would produce the best performance for a given level of risk if we could not adjust the strategy over time.



Fortunately, we are able to make changes to our strategies. When we identify asset classes that have particularly favorable or particularly unfavorable risk/return characteristics we overweight or underweight them in our strategies. This adjusted asset allocation mix is our “Target Current Allocation.”

In making asset allocation adjustments we use a highly analytical process that assesses the *future* return and risk characteristics of each asset class and calculates forward-looking “correlations” among the asset classes—that is, the way they are expected to perform in relation to each other.

We believe using forward looking expectations is superior to traditional asset allocation approaches that use long-term historical averages. Long-term historical averages can mask important opportunities to improve return or limit risk.

Going the Extra Step

In developing our asset allocation mixes we overweight asset classes where managers can add more value. Asset classes like small cap US stocks and emerging markets stocks, for example, are less “efficient” than large cap US stocks. Managers have more opportunity in these areas to find bargains. We capitalize on this by emphasizing these asset classes more in our strategies.

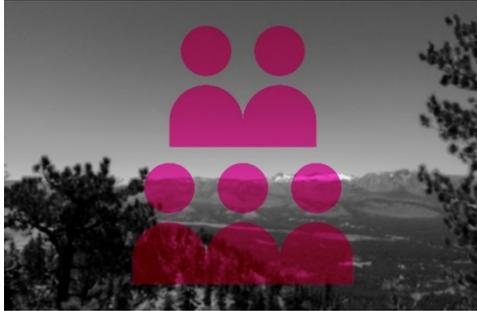
We also use our “Market Anxiety Index” to identify situations where the potential for market volatility is particularly high. When we do, we position our strategies more defensively to protect against downward market movements. Avoiding risk helps preserve our clients’ assets over the long-term.



In assessing portfolio risk we are concerned only with protecting clients against loss of portfolio value—so-called “downside risk.” Many traditional approaches to portfolio management equate volatility—upward and downward swings in value—with risk. In our view, upward swings in value benefit our clients and do not represent “risk” at all. We are focused on protecting clients against actual loss, not changes in portfolio value.

The managers of mutual funds in our investment strategies also make asset allocation adjustments. This is one of the benefits of using active managers—we get the benefit of their thinking about the markets. We are not concerned about “style drift” resulting from their adjustments or the fact that, on occasion, their views about how to adjust their portfolios differ. The collective wisdom of these skilled managers benefits our clients.

Creating the Team



We believe our approach to combining managers in a strategy is a dramatic improvement over the traditional approach. After developing their asset allocation strategies, traditional investment advisors populate their asset allocation “pies” with a series of unrelated “best-of-class” managers. Little thought is given to how these managers will perform together.

We view each strategy as a team of managers, not a disjointed collection of star performers. As legendary coach, Knute Rockne, put it: “The secret is to work less as individuals and more as a

team. As a coach, I play not my 11 best, but my best 11.”

The way we create a team of managers is unique in the investment industry. Once we establish the Target Current Allocation for one of our strategies, we map out its performance history using indexes to represent each asset class. Then we consider all the possible combinations of the mutual funds we have on our hire list. We look for the combination of funds that performs best relative to the Target Current Allocation over all one-month, rolling 3-month and rolling 12-month periods since 1998. We analyze millions of combinations to arrive at the best one.

We consider a multitude of factors when searching for the best combination of managers. We put more weight on periods that are similar to the current environment and on more recent periods. We pay close attention to down-markets so the managers we select perform well in such periods. We seek a combination that has a performance pattern similar to that of the Target Current Allocation to ensure that our strategies don’t deviate too much from this allocation target.

Staying on Course

Once we construct an investment strategy, our job has just begun. The world is always changing and our process is designed to anticipate and adjust to that change.

First, we are constantly on the lookout for new “skilled” investment managers to add to our hire list. We run quantitative analyses on every mutual fund with at least 3 years of history and perform detailed analyses on the most promising of them.

Every month we calculate our future long-term risk, return and correlation expectations for the 16 asset classes we use in our asset allocation process. We adjust our strategies based on this analysis.



Every month we look for the best possible combination of managers. If we find a better combination, we make a change. Every day we review each client portfolio. We make sure it is being managed consistent with its Statement of Investment Policy. We invest excess cash and look for ways to reduce taxes.

We maintain our model strategies on a dynamic basis so that a new client will own the same funds in the same proportion as a client who invested in that strategy a year ago. This minimizes dispersion among clients and ensures that new clients get our best investment thinking on the day they invest.

We trade each account on an individualized basis. We avoid unnecessary redemption fees, small trades that needlessly increase transaction costs and holding too much or too little of a single fund. We consider expense ratios and minimum investment requirements for each mutual fund.

Quarterly, we prepare reports for each client that summarize account activity, report performance and show progress toward the client's goals.

Reducing Taxes

We offer a tax management service designed to reduce taxes for our clients. The benefits of this service vary depending upon market conditions and each client's individual tax situation. Most clients will benefit from this service over most time periods.

Tax-sensitive portfolios are managed differently than non-taxable portfolios in the following ways:

- We analyze the tax-sensitivity of each fund and use the most tax-efficient funds.
- We shift the asset allocation to asset classes that are more tax-efficient.
- We avoid short-term gains and may delay liquidation until gains become long-term.
- We use muni-bond funds unless otherwise instructed by the client.
- We only trade if the expected value of the trade exceeds the expected tax cost.
- We actively harvest tax losses throughout the year, not just at year-end.
- We monitor mutual fund capital gains distributions and avoid large pay-outs.
- We trade taxable accounts on a "specific lot" basis to maximize tax benefits.



A Proven Process

The proof of any investment process is in the results it produces for real clients. The world is full of well-crafted product stories, back-tested track records and unproven investment theories offered up by credible-sounding individuals with impeccable credentials. They make it easy to lose sight of one basic truth. There is no substitute for the experience that comes with managing portfolios year in and year out through the rapidly changing investment environment that we have seen in recent years. We have that experience.

If you have any questions, please contact your financial advisor.