

Advocate

ASSET MANAGEMENT, LLC

IF YOU'RE AN INVESTOR WHO

- Values consistency of returns and preservation of capital
- Seeks a core investment strategy to off-set more volatile, concentrated, or less transparent investments
- Takes a long-term investment outlook
- Has individual needs and risk sensitivities, that may or may not be reflected in your current portfolio
- Has been disappointed with the impersonal treatment and sales mentality of large, brand-name financial organizations

CONSIDER ADVOCATE

- We emphasize absolute returns and capital preservation consistent with your investment needs and expectations.
- We cultivate long-term capital growth. We especially strive to preserve your capital during choppy or bearish markets.
- Our strategy may add stability to your overall investment portfolio.
- Each separate portfolio is uniquely tailored and actively managed to suit your needs and risk sensitivities.
- To ensure that you receive impartial advice, we are completely independent from reciprocal financial relationships with other financial service firms and their products.
- Formed in 2001, Advocate Asset Management, LLC is registered with the Securities and Exchange Commission as a Registered Investment Adviser.

YOUR INTERESTS COME FIRST

A true advisor

Advocate approaches your investment as an advisor, not a seller or promoter of investment products. Your interests are paramount in every decision we make – advisory, trading costs, disclosure, transparency and communication, among others. We maintain the highest standards of ethical conduct. Conflicts of interest are never permitted, even in their most subtle (and barely legal) forms.

Independent service

We believe that the advisor/client relationship should be service-based, not transaction based. You are best served when your investment advisor is completely independent of transactional relationships with brokerage firms, commercial banks, investment bankers, insurance companies, mutual fund management companies, and employees of financial advisory firms.

We believe in our goals and values. So much so that we have our own money invested in the same strategies as our clients.

PRESERVING CAPITAL

Preserving your capital is our number one priority. The key to making money long-term is not to lose money.

Our goal is that your portfolio continues to grow and that your wealth compounds. Losses are not symmetrical with gains; large losses can have a devastating effect on capital, even forfeiting the ability to adequately recover from a sharp decline.

Significant gains usually result from consistent, reasonable performance over time.

One cannot live off of relative dollars.

Absolute returns, not returns relative to a benchmark, are what really count to most holders of wealth. As experienced investors, we have found that investment success is measured by achieving superior, after-tax results over a multi-year holding period.

This is in sharp contrast to others that pursue short-term performance gambits. While certain managers and areas of the capital markets may, for a time, produce notable results, our goal is to achieve long-term sustainable performance and appreciable after-fee results with your money.

Investment Professionals

David J. Kudish

David is a founder of Advocate. He is President of Advocate and chairs the Investment Strategy Committee.

Prior to Advocate, Mr. Kudish was Chairman and CEO of Stratford Advisory Group, which he founded in 1982. Previous to Stratford, he formed and was managing partner of the investment consulting practice at Hewitt Associates in 1974. With more than three decades of investment and consulting experience, Mr. Kudish is a frequent speaker at investment conferences, addressing fund sponsors on a variety of investment-related issues. He has been quoted in leading business and financial publications such as the Wall Street Journal, Business Week, and Forbes. He has authored articles in leading journals and appeared on television as an investment authority.

Mr. Kudish received a BS with honors from the University of Rochester, and an MS from the University of Minnesota. In addition, he is a graduate of the entrepreneurial Management Program at Harvard Business School.

Mike Kimbarovsky

Mike is a Principal of Advocate. Mr. Kimbarovsky is Chief Compliance Officer and Chief Operating Officer and serves on the Investment Strategy Committee.

Prior to Advocate, Mr. Kimbarovsky was a partner and managing director of Extensio LLC. Extensio is a consulting firm focused on providing strategy consulting services for a variety of multi-national clients in the financial services industry.

Prior to Extensio, Mr. Kimbarovsky served as President of Hedge Fund Research (HFR), a boutique investment advisory firm located in Chicago. While at HFR, Mr. Kimbarovsky structured and launched several innovative fund products, including broad style-based hedge fund indices. He led the team that structures various institutional-and high-net-worth-oriented multi-manager fund products for the alternative investment markets.

Mr. Kimbarovsky received a BA in Economics from Northwestern University and an MBA with honors from the University of Chicago.

JoAnn M. Seagren

JoAnn is the Director of Client Development of Advocate.

Previously, Ms. Seagren worked at Towle & Company, a boutique micro-cap investment advisory firm in St. Louis, where she was instrumental in expanding assets under management to full capacity. Before that, she worked for LaSalle Partners (now Jones Lang LaSalle) in marketing and client relations for Fortune 500 clients.

Ms. Seagren graduated Magna Cum Laude from the University of Southern California with a B.S. in business in 1986, where she was elected to Phi Kappa Phi and Beta Gamma Sigma.



INVESTMENT PHILOSOPHY

Advocate Asset Management, LLC manages all-capitalization portfolios in the domestic and international capital markets.

In making investment decisions, we incorporate factors such as macro market-valuation metrics, investor sentiment (behavioral characteristics), and non-consensus thinking. Asset allocation considerations underlie our entire investment process. Other important decision components are allocations to sectors and styles. Currently, we use low-cost exchange traded funds (ETFs) to implement our strategy.

Our strategy is divided into four main components:

- Asset Allocation
- Style Allocation
- Sector Allocation
- Investor Behavior

Asset Allocation

The asset allocation decision – what percentage of portfolio assets to allocate to equities (domestic vs. international), fixed income (domestic vs. international) and hybrid (real-return) assets – is the foundation of everything we do. Asset allocation has been proven to be the key contributor to long-term returns.

The right asset allocation for each client is the essential first step to long-term, sustainable positive performance.

In our industry, many firms devote a great deal of effort and expense analyzing which specific companies may excel in the future. However, considerable data and empirical studies support a growing consensus that most security analysts and active stock-picking managers possess little predictive ability and therefore under perform relevant indices or benchmarks. Results tend to be haphazard and penalized by high costs and fees.

There is too much noise and randomness in specific company data to make meaningful predictions about future earnings expectations. Whatever advantage could be achieved from this effort to gain an edge tends to be arbitrated away by intense competition and transaction costs.

Rather, we feel that the effort to structure the right asset allocation for each client is the essential first step to long-term, sustainable positive performance. Then we monitor the portfolio asset allocation and adjust it gradually depending on market conditions.

Style Allocation

Following asset allocation, style allocation is the key driver of portfolio performance over time. For all equities, this style decision may include style and capitalization considerations. For example, growth versus value style, or large-cap versus small-cap capitalizations.

For international equities, this style decision may include differentiating among specific geographic regions, such as developed Far East versus developed Europe, emerging South America versus emerging Asia, and a myriad of other choices.

For bonds, it includes opinions of duration, quality and issuer type (such as corporate, government, etc.) For hybrid investments, it could include evaluations such as which

real-estate sector is appealing (i.e., commercial, office, hotel, warehouse, or residential.) It could also include evaluations of commodities such as basic industrial materials, agricultural commodities, or precious metals.

Sector Allocation

Sector-related factors are widely regarded as a large determinant of a stock's price movement. Within each style class, we evaluate specific sectors, selecting those whose future prospects are more favorable. We analyze sectors from a universe that includes consumer discretionary, consumer staples, energy, financials, healthcare, industrials, information technology, materials, telecommunications, and utilities. As the economic climate evolves, it tends to favor certain sectors and disfavor other sectors. We seek to identify major reversals in long-term trends by looking for tomorrow's emergent sector leadership today. And we invest in those sectors by buying market baskets of securities, rather than speculating on the performance of a limited number of individual companies in our favored sectors.

Investor Behavior

There are many ways to evaluate human behavior in financial markets. So we use a few metrics to try to quantify the tendency for the human mind to take short-cuts to come to conclusions.

We keenly watch for factors indicating the reversal of a current multi-year trend.

One outcome of human behavior is exhibited in 'reversion to the mean' – the tendency of major multi-year cyclical trends to reverse due to extreme valuations. This is a very powerful investment force. Investors tend to overreact to new information. This overreaction is generally greater to bad news than to good news.

The shift from previously superior to currently inferior comparative performance and *vice versa* is often the manifestation of this force. We are wary of following consensus thinking after a sustained market advance or decline in a segment or sector in the capital markets. We keenly watch for factors indicating the reversal of a current multi-year trend. This is where we often find the greatest opportunities to be captured. And, it is often where we identify and strive to minimize apparent risks.

There are other facets of investor behavior that we can monitor. Reversion to the mean is just one example.



OUR APPROACH

Establish Individual Investment Policies

We establish an investment policy with you, tailored according to your individual risk profile. This policy outlines the core asset allocation mix of stocks and bonds with agreed-upon minimum and maximum boundaries. Typically, this mix remains reasonably static, or “Policy Neutral,” during most investment environments. But, when external conditions dictate, the mix is adjusted gradually to further reduce risk or to capture opportunities.

While we recognize that we cannot forecast market trends with any degree of precision – nor can anyone for that matter – we are able to identify characteristics that are usually present near or after market tops and market bottoms. We take a pre-reasoned response to adjust your effective asset allocation as major market trend changes occur. Asset allocation management underlies all other investment decisions made by Advocate’s investment team on your behalf.

Manage Risk

In our view, risk management is not about reducing risk to absolute zero; it is about targeting a level of risk compatible with your unique profile. We take this target and weight it along with external factors such as the macro economic environment and political risks that reward or penalize different economic sectors. We then structure your portfolio’s asset allocation mix accordingly. Capital preservation remains the primary goal in all of our client portfolios.

Core/Satellite Approach

We use a core/satellite approach that maintains a core component, coupled with an underweight/overweight bias toward specific industries, asset classes and global sectors. The core is defined as the Neutral Exposure Policy (NEP), which we develop along with you. The satellite component is a variance from the NEP that allows us to vary your exposure to capital markets’ opportunities and risks within pre-defined limits.

Choosing Specific Investments

Currently, we use exchange traded funds (ETFs), which are pre-assembled portfolios containing many individual securities. Each ETF represents a distinct investment style or market sector within a specific asset class. ETFs offer superior liquidity, diversification, and tax-efficiency at a significantly lower cost than most mutual funds or active investment management strategies. ETFs also offer style purity, allowing for the closest performance tracking to a specific intended asset allocation strategy.

We like to think of what we do as value-added indexing.

In just a few years, exchange traded funds have exploded to hundreds of different products. In this ever-increasing array of ETFs, each one tracking smaller and smaller slices of the market and each one varying in cost and liquidity, Advocate's experience and macro-focused strategy adds significant value to the investment selection process. The other highly important part of the work we do is to manage your asset allocation and risk exposure. We like to think of what we do as value-added indexing.

While there will always be active money managers who outperform their benchmarks – especially in less efficient areas of the markets – overwhelming empirical evidence shows that most do not and that the amount of underperformance grows as the measured time period lengthens.

The “75/25 Rule”

We adhere to what we have coined the 75/25 Rule: In an expanding economy with a rising market trend – which describes about 75% of the scenarios – we are able to take a longer-term perspective. We seek to be at a client's Policy Neutral equity exposure that is based upon that client's written Investment Policy (which we may assist in developing along side our clients.) The other 25% of the time, we are cognizant that equity markets may not be in a rising trend but, rather, in a sideways trend or a declining trend. In these instances, we seek some protection from the potential loss of capital by gradually reducing our client's equity exposure to less than the Policy Neutral level. We attempt to deviate from the Policy Neutral exposure during market conditions that are either fraught with risk or ripe with unrecognized opportunity.

Capital preservation is our most important objective for virtually all client accounts.

Tax Efficiency

Indexed investment strategies are not only superior to active strategies in performance, but are particularly advantageous in taxable accounts. For taxable clients, Advocate manages portfolios with a tax efficiency overlay. This is a result of both our investment strategy and the underlying efficiency of ETFs.

From a strategy perspective, investors cannot spend pre-tax performance, so we make sure that taxes are an integral (although usually a secondary) part of our strategy for taxable clients. We generally have very low turnover (buying and selling investments.) Historically, client portfolio turnover has averaged about 25% per year (sometimes higher, sometimes lower.) When we do sell investments, we make it a point to target tax lots that are best suited from a client's individual tax perspective. This may mean harvesting short-term capital losses or long-term capital gains.

From an ETF perspective, the key tax efficiency is in the form of low capital gains payouts. Realized capital gains distributions for ETFs are rare. Because the turnover within an ETF is generally low, very little – if any – capital is paid out in capital gains. Also, ETF managers also can use an in-kind redemption process to eliminate the stock shares with the biggest unrealized gains, thereby limiting the ETF's potential for distributing gains. Furthermore, because ETF investors trade shares among themselves rather than with the fund (as mutual funds do), ETF managers do not have to sell off individual securities to pay off redeeming shareholders.

Of course, not all ETFs are created alike. There are exceptions; there are certain ETFs that are tax inefficient, some very inefficient. It is our role to identify the best investment product that meets our strategy objectives and desired exposures for your portfolio, with tax efficiency as one consideration.

IMPLEMENTATION

Client overall risk sensitivities are expressed in a specific asset allocation matrix differentiated by exposure to three primary asset classes: equities, fixed income and hybrid.

Our clients have varying levels of exposure to equity, fixed-income and hybrid markets, so we express our investment opinion as a proportion of their Neutral Exposure Policy. For example, if at the conclusion of our research into a specific industry we believe that the domestic consumer staples industry should be 10% of domestic equity Neutral Policy, this will be implemented across most or all client portfolios. Different risk profiles may play a part in the suitability of an investment for a particular client.

As a simplified example, for a client with a 100% equity exposure (let's say 80% domestic and 20% international), a 10% allocation to domestic consumer staples would be 10% of 80%, or about 8% of portfolio assets.

For a client with 60% equity exposure (and 40% fixed-income exposure), composed of a 45% domestic and 15% international equity policy, a 10% allocation to domestic consumer staples would be 10% of 45%, or about 4.5% of portfolio assets.

On the fixed-income side, we conduct the same rigorous analysis with respect to other factors such as current yield, quality, duration, taxability and geographic scope.

For income-oriented portfolios, we focus less on capital growth and more on capital preservation while attempting to produce an acceptable yield.

Sector Choice

There is both a quantitative component to help us identify undervalued/overvalued sectors and a subjective component to help us gauge investor risk sentiment. Although this is difficult to measure, it is a critical component of market liquidity. We specifically avoid 'black-box' computer mathematical models that attempt to replace human judgment in making investment decisions.

We are constantly monitoring quantitative and risk-aversion metrics to understand the changing investment environment. These objective and subjective metrics guide us in our beliefs about where the markets are headed during our operating time frame – the next six months to three years.

Both the quantitative and qualitative components of our strategy are based on public data. We do not try to decompose specific company financial statements to glean some level of insight into their specific businesses. This is too micro-focused for our investment approach. We believe in big ideas and prefer to focus on data about global sectors, asset classes, and industrial sectors. Our internally-developed, proprietary portfolio management system is central to our data collection and evaluation.

We avoid 'black-box' computer models that attempt to replace human judgment in making investment decisions.

The core component of the quantitative portion of our strategy is to monitor statistics that are representative of the broad macro-economic market as well as specific sub-sectors (generally referred to as economic indicators by the popular press.) We collect data from a variety of sources and use a multi-factor screen to generate investment and divestment points.

The factors are constantly reviewed for their relevance and have evolved over time. Currently, we utilize 12 broad factor segments (with multiple factors per segment) as illustrated on the following page.

Factors we use to evaluate investment opportunities

On a regular basis, we re-evaluate the risk-reward characteristics of our actual investments and our virtual bench of investments, those asset classes and global and other sectors which we believe could be candidates for investment given the proper catalyst.

Sectors that have appreciated beyond our sell targets are evaluated for removal from portfolios while sectors that have depreciated are candidates for removal or additional investment.

Segment	Component
Credit	Bank-oriented factors such as loan availability, credit standards, and central bank actions
Business	Productivity data relating to inventory, equipment, and capital expenditures
Debt	Government and consumer fixed-debt and variable-debt information
Housing	Home construction productivity (sales, starts, etc)
Consumer	Consumer sentiment surveys
Inflation	Inflation characteristics, both measured through surveys and implied by capital market pricing relationships
Labor	Productivity and employment rates
Demographics	Population growth rates and long-term trends
Foreign Exchange	Relative value of currency purchasing power
Production	Domestic and global production of goods and services
Inputs	Pricing data for various key commodities used as raw material inputs in production
Momentum	Proprietary relative ranking system of various sectors



QUESTIONS

Isn't actively managing asset allocation the same as market timing?

Varying the weightings of asset classes gradually over a cycle is a legitimate form of asset management, not market timing. We believe that asset allocation should not be left static over a market cycle – that is, in a fixed percentage allocated to stocks, bonds and cash reserves. During the various phases of the market cycle, we vary the equity exposure of a portfolio in order to reduce risk or capture opportunities.

Because most investment managers do not want to or cannot manage asset allocation, and most investment consultants or brokers who advise institutional funds and individual portfolios cannot and do not want to do this, those who attempt to manage asset allocation are disparaged. In fact, if one takes a step back and considers how investment decisions are really made, there is a timing element in all investment decisions.

Overweighting, equal weighting or underweighting an asset class, investment style, market sector, bond maturity or quality level, etc. involves a timing element.

Selecting or dismissing an investment manager involves a timing element. Buying one stock (or bond) and selling another stock (or bond) involves a timing element.

Why ignore the “active style” of focusing on the fundamentals of individual companies and look at market sectors instead?

The idea that a particular company's fundamentals will somehow prevail in spite of long-term market trends and cycles may work for a short time period but is usually not borne out over very long-term periods. Companies go in and out of business, succeed or fail, with much greater frequency than do sectors and industries.

Market leadership has changed inconsistently but pervasively through the decades so that very long-term buy-and-hold approaches are usually not all that successful. Reflect on the secular growth, plateau and decline of major market sectors in the U. S. economy during the past 150 years: the railroads, utilities, extractive industries, manufacturing, clothing industry, chemicals, airlines, traditional retailers, land-based telecommunication companies. The list is rather long. As an exercise to emphasize this point, we recommend that investors examine the constituency of the Dow 30 Industrials at successive ten-year intervals. GE is the only surviving company that is still in the index and it has changed its business focus dramatically since the Dow 30 was formulated 120 years ago. Many of the leading companies that were in this index no longer exist.

The point is that investors should not ignore market cycles and phases just because long-term trends are difficult to assess and it is easier to focus upon what the majority suggest are superior companies.

Is Advocate a contrarian investor?

An outside observer may conclude erroneously that Advocate follows a contrarian investment approach. The fact is, for long periods of time when markets are within a commonplace range of somewhat undervalued, reasonably valued, or somewhat overvalued, we are not contrarian investors. During these periods, we tend to be invested at our clients' Neutral Exposure Policy levels.


When markets move into extreme overvaluation territory, we take action to preserve client capital. That is when we become contrarian, or inverse-emotion driven, as we like to think of it.

When investors are ecstatic, we are cautious; when investors are hopelessly pessimistic, we seek investment opportunities. But it is only when we assess the valuations of the market as well-above or dangerously-above fair value that we take action to reduce equity exposure. And, it is only when we assess the dynamics of the market as well-below or opportunistically-below fair value do we take action to increase equity exposure.

Do you invest both long and short?

Most of our investments have been long investments. However, when we feel strongly about weaknesses developing in a particular sector, we will purchase short exposure, typically either through inverse long investments or through direct-shorting.

This depends on the cost of each approach and to the extent short exposure is permissible by the client's investment policy.



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