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June 13, 2008

Vanguard Adds to International Value

Vanguard decided to add some "manager value" to International Value—giving investors a fourth team for the price of three on May 16. The new team consists of Dr. Sandy Nairn and Christine Montgomery of Edinburgh Partners—Dr. Nairn is the firm's founder, having started it up in 2003, and both he and Montgomery have about 20 years each of investment experience.

It's not exactly clear why Vanguard chose to add the new team, as the fund has experienced asset outflows in the six months leading up to its addition. While performance against relevant benchmarks has been somewhat flat of late—perhaps due to the number of management teams diluting efforts in recent years, as the longest standing manager, Hansberger Global Investors, has been joined by teams from AllianceBernstein (in April 2004), and Lazard Asset Management (July 2006)—International Value's long-term rolling returns remain quite strong in comparison to International Growth and Total International Index, as you can see in the table below.

Long-Term Relative Performance Has Been Strong

Rolling 1-year

International Value	12.1%
International Growth	10.2%
Total International Index	10.8%
S&P 500 Index	5.5%

Rolling 3-year

International Value	10.0%
International Growth	7.2%
Total International Index	8.0%
S&P 500 Index	2.7%

Rolling 5-year

International Value	10.2%
International Growth	7.2%
Total International Index	8.1%
S&P 500 Index	2.9%

In This Issue

- **Vanguard Adds to International Value**
- **Fidelity Adds To Its International Line-Up**
- **Fidelity Manager Changes**

That said, the fund has been unable to separate itself and outperform either the MSCI EAFE Value Index (a subset of the overall fund's broader EAFE benchmark), nor the MSCI All Country World ex-U.S. Index, against which a majority of the fund's managers' performance is benchmarked (AllianceBernstein, Lazard and Edinburgh—Hansberger's performance is evaluated against the EAFE) in recent times. Performance against the EAFE has been slightly more favorable.

International Value has, as mentioned, put up competitive returns compared to International Growth and Total International. Over the past 10 years, the average one-year, three-year and five-year returns for International Value on a rolling basis have been quite robust. However, performance has been faltering of late. It's been almost a year and a half since the fund has beaten Total International over a 12-month period. And its three- and five-year relative returns are also beginning to suffer. This turn of events may even be putting the fund's managers in danger of losing their performance bonuses, which are paid out based upon rolling three- and five-year performance.

Until we can see some measurable, positive results, we view this manager addition as a negative for the fund, and would recommend investors seeking an international component for their portfolios consider one of Vanguard's or Fidelity's other international options over International Value. This does not mean we think current investors should sell their shares, especially if there are capital gains or back-end load consequences, but it may be worth it to wait and see before adding more to your holdings here. Once we get an idea of what kind of an effect, if any, Edinburgh Partners will have on the fund, or even how much of the fund's assets they'll be managing, we may reassess our downgraded outlook. But with performance falling off and more and more managers pulling the fund in various directions, this does not appear to be a good time to start buying shares.

Fidelity Adds To Its International Line-Up

As we mentioned in our *Adviser Fund Update* on March 6, Fidelity had plans for a new international fund, the Emerging Europe, Middle East, Africa Fund (or EMEA, for short), and those plans have since come to fruition, as the fund opened to new investors on May 20th.

The EMEA Fund will invest at least 80% of its assets in securities of emerging Europe, Middle East, and Africa issuers and other investments that are tied economically to the EMEA region (one which contains more than 80 countries, starting with Russia in the east, across Eastern Europe and the Middle East, including the entire African continent as well). Not surprisingly, the fund has been benchmarked to the MSCI Emerging Markets Europe, Middle East and Africa (MSCI EMEA) Index and is managed by London-based Adam Kutas, a 12-year Fidelity veteran who previously co-managed the Latin America fund. EMEA's expense ratio is currently capped at 1.25% and requires a \$2,500 minimum initial investment.

The fund is essentially a play on the two underlying commodities that drive the economies of the EMEA countries—crude oil and gold, both

rather volatile industries. That said, the fund does have its attractions—combined with an emerging markets fund, one could create a global emerging markets play with slightly lower volatility than simply buying a commodities fund or holding one or the other alone. This strategy may not be a comfortable choice for more conservative investors, however.

EMEA is unique in that it puts a sizeable portion of its assets in African countries, something none of the other international funds we track at Fidelity or Vanguard does, and we will be keeping an interested eye on how the fund fares.

Fidelity Manager Changes

Just like clockwork, Fidelity has shifted several more managers around this month. None of the changes should be a cause for concern for investors in the affected funds.

As of July 1st, Derek L. Young will be seeing his duties expanded due to the retirement of 40-year Fidelity veteran Richard C. Habermann, his co-manager on a number of funds. Young will take on sole responsibility for a slew of the Asset Manager funds, including Asset Manager 20%, 30%, 40%, 50%, 60%, 70% and 85% (Advisor share classes of all of the above as well), VIP Asset Manager and VIP Asset Manager: Growth. He will also take over Habermann's responsibilities at Broad Market Opportunities, and will continue to co-manage Four-in-One Index, Global Balanced, Strategic Real Return, Strategic Dividend & Income and Strategic Income. Young joined Fidelity in 1996 as director of risk management for Fidelity Management Trust Company, eventually moving on to serve as senior vice president of strategic investment services and marketing. In 2005, he began managing his first funds, and has added several per year since then. Prior to joining Fidelity, Young was a manager in the Risk Strategy Consulting Practice for KPMG. From 1991 to 1995, he worked for the Board of Governors of the Federal Reserve as a senior financial analyst and then as a supervisory financial analyst. He began his career at Empire Financial Services in 1986, where he was a vice president.

As of June 1st, Vincent Montemaggiore took over Select Banking, succeeding Ramona Persaud. Persaud has moved to a research analyst position on Fidelity's Global Research Team in London, supporting Bill Bower, who manages Diversified International. After joining Fidelity in 2004 as an equity research intern following supply chain technology companies, Montemaggiore joined Fidelity's equity research department full time in 2005, following advertising and publishing companies. In 2006, he took on additional research coverage on industrial conglomerates and managed Select Industrial Equipment from 2007 until 2008. He has most recently taken on research coverage on banks. Prior to joining Fidelity, he worked as an investment banking analyst from 2002 to 2003 at De Guardiola Advisors, Inc., and from 2000 until 2002 at Putnam Lovell Securities, Inc. following the financial services industry.

Also as of June 1st, Noriko Takahashi was appointed co-manager of International Small Cap, joining current managers Wilson Wong and

Colin Stone. Takahashi will be responsible for the fund's investments in Japan, and succeeds Tokuya Sano, who will focus on managing portfolios for overseas investors. Takahashi joined Fidelity in March 2008, but has managed Japanese small-cap equity portfolios for eight years. Prior to joining the firm, Takahashi worked at Goldman Sachs, where she was co-head of the Japanese equity small-cap team, vice president and portfolio manager. She also worked as an analyst and portfolio manager with Invesco Asset Management for the two years prior to joining Goldman Sachs. She started her career in the securities industry with UBS Securities, where she spent 13 years as an investment analyst, including five years specializing in small-cap stocks.

So what does all of this mean? When you buy an actively managed mutual fund, what you are really buying is the manager. But because managers change frequently, most published fund ratings don't consider who is behind the numbers. Our proprietary Manager Ranking System solves this problem by identifying the managers that have added the most value over time, while adjusting for differences in fund objectives and benchmarks. To find out more about our proprietary "buy the manager, not the fund" system, please call 1.800.492.6868 to speak to a representative.

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