

Prisma, Zurich Life's fund platform, focuses attention on the building of risk rated portfolios for your clients. Diversification across asset classes is essential in portfolio construction and the Prisma Platform gives your clients access to all investment sectors.

We asked **Richard Temperley of Zurich Life** to explain why investors should consider diversification within their portfolio and how the **Active Asset Allocation** Fund may be a solution for many.

Diversified growth, absolute return and multi-asset funds have become increasingly popular since the property and banking meltdown of 2007, even though equities have regained all of the losses experienced since that meltdown. Diversification is a key component in reducing volatility (risk) while maintaining the potential for decent long-term returns.

Diversification, however, is clearly not a new concept. Around two thousand years ago the *Talmud* told us "let every man divide his money into three parts, and invest a third in land, a third in business, and a third let him keep by him in reserve". Equities, bonds, cash and property remain the cornerstone of most investors' portfolios. Although most people like the idea of having many options to choose from, we can all become paralysed in the face of too many choices, often making poor choices or none at all. You can achieve sufficient diversification even within a single fund and so you may not need to diversify your investment choice any further.

Traditionally people achieved this diversification using managed funds, especially actively managed ones, and these remain popular in the Irish marketplace. More recently, newer forms of diversified asset funds have been introduced. These tend to have two main differentiating features; wider asset ranges and the use of alternative assets (e.g. gold), which if properly employed enable the fund manager to reduce volatility. It will be interesting to note if these funds remain in vogue if the current four-year equity bull market continues for a significant period. Given the gyrations in equity markets in recent years it is likely that they will.

However investors need to "look under the bonnet" of these newer fund types, and be aware that some funds may be employing strategies such as leverage, similar to hedge funds.

Zurich Life has three of these newer diversified funds on its platform, which between them have grown quickly in size to around €150m. They are the Active Asset Allocation Fund, the Diversified Assets Fund and the BlackRock Dynamic Diversified

Growth Fund, none of which employs leverage.

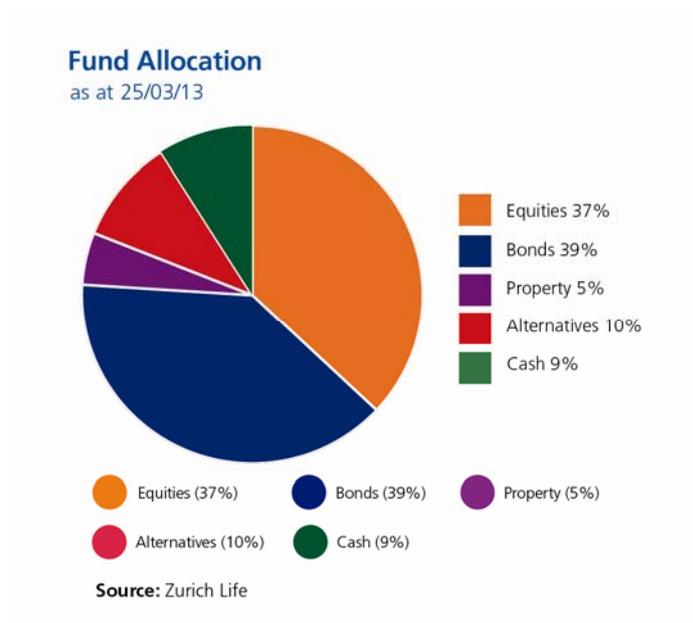
The Active Asset Allocation Fund (AAA) is a good example to look at. It is actively managed by the Zurich Life fund management team, where macro-economic driven asset allocation is an integral part of its investment process. The AAA Fund has wide asset ranges (see table below) which the fund managers use to optimize the risk/reward balance and help reduce volatility. In addition the Fund invests mainly in underlying actively managed Zurich funds.

Asset Exposures

Asset Class Exposures
as at 31/12/12

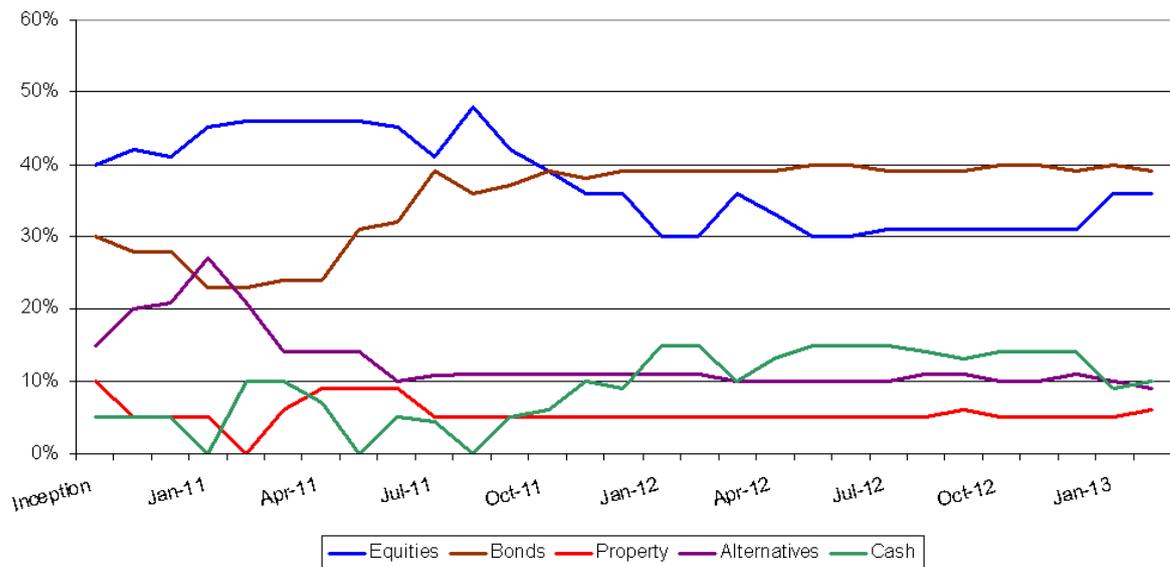
Asset Class	Typical Exposure
Equities	15% - 65%
Bonds	10% - 60%
Property	0% - 20%
Alternatives	10% - 40%
Cash	0% - 50%

Fund Allocation



The following chart shows the movement within the asset ranges during the two year life of the fund.

Asset Allocation



Source: Zurich Life, March 2013.

Alternative assets

The AAA Fund selects from a list of various alternative assets and can have between 10% and 40% of the fund invested in this asset class. The list of alternatives currently includes gold, oil, inflation-linked government bonds, soft commodities, industrial metals and corporate bonds. The Active Asset Allocation Fund is designed to perform in a variety of market conditions, so that if equities are underperforming this can be counter-balanced by the performance of other asset classes. The Zurich fund management team carefully selects alternatives that have low correlations to the movement of equity prices. Although certain assets could become more correlated in times of great stress, in general a policy of mixing assets - which have low correlations with one another - helps to diversify the fund and to reduce volatility.

Volatility

Volatility is one of the main measures of assessing the risk of a fund. It is a statistical measure of the dispersion of returns over a certain period. For example we could look at the weekly returns for a fund over a significant period of time such as five years. Commonly, the higher the volatility, the riskier the fund. A higher volatility means that a fund's returns have been spread out over a larger range of returns. For example:

	Mean Return	Volatility	Range of Potential Returns*
Fund X	8%	7%	1% to 15%
Fund Y	10%	14%	-4% to 24%

* Using a 'one standard deviation' measure of volatility. Source: Zurich Life, March 2013.

The AAA Fund has had a simulated five year volatility of just under 8%. This figure is significantly lower than many managed and equity funds. In addition it has performed strongly against similar diversified asset funds.

Popular with Investors

The AAA Fund has attracted a number of different investor types, including:

- 1) Those looking to move out of cash but unwilling to move into higher volatility equity funds;
- 2) Longer -term investors who don't want the inconvenience of periodic asset re-balancing and are happy for an active investment manager to perform that role; and
- 3) Those looking to take profits in equities but who are unwillingly be totally out of the market.

If international trends are anything to go by, diversified asset funds are likely to continue to grow in popularity. However, they are not the *Holy Grail* of the investment world; yes they can reduce volatility if that is what is required, but they cannot deliver high long term returns with no risk.

To learn more about the Active Asset Allocation Fund or any of the funds on the Prisma Platform, just speak to your local Zurich Life Broker Consultant or visit www.zurichlife.ie

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