

Following the Numbers

Starting with the belief that the market's focus changes over time, Navellier Midcap Growth Fund has designed a dynamic model, testing a hundred criteria every quarter, to follow these changes. Despite being driven by fundamentals, this is a strict quantitative approach that eliminates all human bias from the stock-selection process.

Q: What is the investment philosophy of the fund?

A: Our investment philosophy is based on disciplined quantitative approach to investing. We believe that we can uncover inefficiently priced securities, resulting in returns that beat the benchmark index and the peer group averages through full market cycles. We employ a dynamic quantitative modeling process. Our initial universe of mid cap stocks consists of approximately 1,000 securities. These stocks have market capitalization in the range of \$1.5 billion to \$15 billion, however this can fluctuate as the market fluctuates.

Our first step incorporates a risk-adjusted momentum factor, our reward-to-risk ratio, which measures buying pressure or accumulation. Our goal is to buy the stocks that are beginning to be accumulated by other investors as those stocks will generally behave differently than the overall market. However, we don't want to buy stocks purely on momentum; we need a fundamental reason to be investing. A great example would be 1999, when many stocks went up just because their corporate name ended in "dot com". Many had no real fundamentals, no

sales growth, or earnings growth, there was next to nothing behind these companies except for the name. Thankfully, due to the rigor of our stock selection methodology we were able to avoid such stocks.

Companies are in business for one reason, to make money. They make money in two ways, increasing sales and increasing margins. This is what our process is trying to figure out - are these companies increasing their sales or their margins, which typically leads to higher than average earnings.

Q: What is your strategy in achieving these goals?

A: First, we apply a reward-to-risk analysis to our initial universe. Louis Navellier invented this analysis many years ago, while he was attempting to explain the stock market and stock performance. It is the stock's alpha divided by the stock's volatility or standard deviation. Only about 250 of the 1000 stocks make it through this first step.

Second, we use fundamental analysis on the stocks that passed the first step. It is all quantitatively driven. Our fundamental analysis screens are evaluated and updated on a quarterly basis.

Navellier Mid Cap Growth

Fund Facts

Symbol	NPMDX
Website	www.navellier.com
Address	Navellier Management Inc. One East Liberty, Third Floor, Reno, NV 89501
Tel. No.	775.785.2300
Inception	1/1/1997

Portfolio

Total Net Assets *	\$ 192.5
Avg Mkt Cap (\$ Weighted) *	\$ 6,776.6
Average Price/Earnings Ratio	31.32
Average Price/Book Ratio	6.71
Turnover Ratio	165 %

Investment Information

New Investment	Open
Min Initial Investment	\$ 2,000
Min Subsequent Investment	\$ 100
Min Initial IRA Investment	\$ 500

Risk (Against Russell Mid Cap Growth - 3 Yrs)

Alpha	-2.61
Beta	0.9132
R-Squared	86.51
Ann Std Deviation	15.67
Sharpe Ratio	0.5846

Returns vs. Russell Mid Cap Growth Index

	NPMDX	Index
1 Year (Cum.)	16.08 %	10.86 %
3 Year (Ann.)	9.67 %	14.86 %
5 Year (Ann.)	-2.56 %	-5.23 %

Returns vs. S&P 500

	NPMDX	Index
1 Year (Cum.)	16.08 %	6.32 %
3 Year (Ann.)	9.67 %	8.28 %
5 Year (Ann.)	-2.56 %	-2.37 %

Fees and Expenses

Max Sales Charge - Front	0.00 %
Max Sales Charge - Deferred	0.00 %
Max Redemption Fee	2.00 %
Total Expense Ratio	1.34 %

Portfolio Manager

Michael J. Borgen - Lead PM	May-03
Louis G. Navellier	Jan-97

* millions

Data through: 06/30/05

Source: Company Documents; Zephyr Style Advisor



We back test over 100 different fundamental criteria. This fundamental approach allows us to adapt to market changes over time. Sometimes the market is more focused on earnings momentum variables, at other points the market is more focused on profitability variables.

Once we've determined where the market is focused, we measure the alpha and the beta for each of the fundamental factors. We then optimize the factors to develop our fundamental stock selection model that typically has approximately 4 to 8 variables.

The model doesn't change dramatically from quarter to quarter, however it gradually changes over longer periods of time. For example, in 1999 it was primarily driven by sales growth, analysts' revisions, earnings surprise, momentum and growth. After the bubble burst, variables such as ROE, equity turnover and earnings growth divided by P/E, became more dominant. Lately, the model has gone back to sales growth, forecast earnings growth, historical earnings growth, and analyst revision focus, but that doesn't mean that the variables from the bear market are totally out.

Q: *How do you decide when to shift your variables from being growth oriented to being more value oriented and vice versa?*

A: We run our testing cycle about midway through the quarter, after about 80 to 90 percent of the companies have released their earnings. We do the testing for all of our different products at the same time. Essentially, every 90 days we check the market's pulse to see how it is doing and to help determine where it is going.

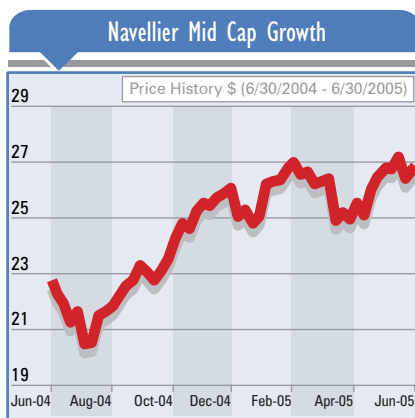
In addition, we apply our fundamental model to the stock selection process on a weekly basis and then we select the stocks that have the highest risk-adjusted performance. The stocks that made it through both of those filters, make it to step 3, portfolio optimization, which is part of our risk control.

The big difference with our optimization model is that we try to structure a portfolio that has the highest

amount of return with the lowest amount of risk without constraining the process to limit tracking error. We believe that excess market returns from our process will pay for any tracking error that we incur. Many other managers optimize their portfolios with a secondary goal of reducing tracking error to the benchmark.

Q: *So you don't apply any sector criteria or sector weight?*

A: No we don't. All of our sector weightings and allocations are a result of our stock selection process. From time to time we may be more concentrated in certain sectors, however, we do have some risk controls regarding industry



weightings. We never weigh any industry more than 20 percent in the portfolio and we never weigh any single stock more than 5 percent.

We follow the numbers where they take us. We do not personally bias our portfolios in any direction towards favoring energy, healthcare, or technology. We feel that we have developed very competitive and effective quantitative stock selection models that have proved over time to produce significant results. There is no point in trying to second-guess the quantitative model.

From an internal standpoint, the benchmark is really not in our process. We use the benchmark purely for comparison and reporting purposes. We operate within the market of the benchmark, but we do not use the sector weightings as constraints for us.

Q: *Would you highlight your risk-management process?*

A: We manage risk in several different ways. First, risk is at the forefront thinking during the entire process. Even in step one, we are using a risk-adjusted accumulation factor. Second, we are only buying stocks with higher than average fundamental characteristics and that helps to reduce risk. Third, our optimization process is trying to limit risk and to measure whether a stock becomes increasingly volatile relative to the other stocks in the portfolio.

Q: *Why do you prefer the quantitative approach to investing as opposed to individually researching the companies?*

A: In the mid-cap area of the market, most of the stocks are covered by several analysts each. It is our belief that, on average, they do a pretty good job. From our perspective it wouldn't make sense to waste our time doing what they do. Instead, we take their quality work in a quantitative format and analyze it. Our value-added comes from the disciplined process of model building that is designed to structure a portfolio that outperforms both the peer group and the benchmarks.

There are always ways to improve a model, but I really don't believe that the management would tell me anything different from their posted numbers. Company managers tend to be optimistically biased. Our process has the advantage of not having to sift through the optimistic bias that fundamental type of funds have to.

Q: *Let's say we are the first quarter of 2000 and you are running your back testing. What would your model indicate?*

A: I don't believe that there is any quantitative or fundamental model that could have predicted such a dramatic change in the market. In that first quarter of the market decline, we did trail the market. However, our stocks didn't go down as much because we still had

solid companies in the portfolio. Also, when the market changed its focus, our stock selection model for the following quarter changed its focus and we started selling a lot of technology stocks and buying other types of stocks, such as healthcare and energy.

That is how our model adjusts. It will trail the benchmark in a quarter when the market absolutely turns on a dime and goes the other way. But over longer periods of time, typically there are protracted trends. When trends that continue for several quarters, our performance relative to the peer group and the benchmark tends to be significantly better.

Q: *Could you describe your sell discipline?*

A: Many people can find stocks that can go up, but the trick is to know when to sell a stock. We came up with an effective sell discipline which is based on our buy discipline. In order for a stock to be sold, all it has to do is fail one of the three steps of our process. If it drops out of the high rankings of the risk/reward ratios, it is sold. If its fundamental characteristics start to deteriorate, it is sold. It is sold or trimmed back if it experiences extensive risk relative to the other stocks in the portfolio. Often we sell good stocks to buy better stocks.

Q: *What is the average stock holding period?*

A: It varies. Our average turnover is 160%. During periods when the market is more focused and has a discernible trend, our portfolio turnover ratio will drop. Last year it was 96% as rated by Morningstar, normally it is about 125 – 150 percent.

A lot of people have the common misconception that high turnover means poor tax efficiency. Our turnover typically comes from short-term losses, so at the end of the year, after having a positive year, it is possible to have short-term losses combined with long-term gains.

The tax-efficiency is generally a byproduct of our process. However, we

check if a stock is ranked as a sell and if we have a gain on it and the stock is a couple of weeks of becoming a long-term gain, we'll move on to capture that moment.

Q: *Could you give us an example of stock selections that worked out and such that didn't work out?*

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about

Michael Borgen

Michael J. Borgen has ten years' experience in institutional and retail investment management industry and joined Navellier in 1995 as a Quantitative Research Analyst. At Navellier, Mr. Borgen is currently a portfolio manager responsible for the management of the Mid Cap Growth, Micro-to-Small Cap Growth, and the Small Cap Growth strategy. In addition, Mr. Borgen conducts ongoing research enhancements of the firm's quantitative investment process and works on product development.

A: One of our longest-term holdings has worked really well for us. It is Coach, the maker of purses, handbags, etc, and they are branching out in other areas. Over an extended period of time, they have been able to produce high alpha with a reasonable volatility level. Coach is not the highest-ranking stock, but it has managed to stay in the portfolio for the longest time.

This is a company that continues to grow, increase its sales and manage margins. We have held the company since 2002 and their revenue growth at that time was 16.8%. Two years later it was 38.6%. Back in 2002, net margin was 11.9%, while for the 12 months ended December 2004, net margin was 21.3%. The significant increase in their sales and their margins obviously results in earnings per share growth. As of Dec 2004, their EPS growth was 16%.

This shows how a company gets into our model. If it produces the type of fundamental characteristics and the risk-adjusted market characteristics we are looking for, they can stay in our model for quite some time.

Q: *What do you do when a company like Coach falls significantly?*

A: All throughout the holding period of Coach, we have trimmed it back from a heavier weight. Despite the fact that the company has pulled back significantly over the near term, so has the market. When we measure our alpha and our quantitative factors, they are all relative to the market.

Q: *What is your viewpoint on holding cash?*

A: We want to keep as little amount of cash on hand as possible. In the long run markets go up, so any amount of cash in the portfolio would cause cash drag. We keep some cash to meet the liquidity requirements, and if there is a unique investment opportunity. We typically keep 5 percent or less in cash. ■

TICKER Staff