

## Small-Cap Values

*Small-cap investing requires a hands on approach and to do this internationally demands an investment process that is scalable. Epoch International Small Cap Fund seeks long-term capital appreciation by investing at least 80% of its assets in small-cap companies outside of the U.S. Incorporating a top-down thematic approach with fundamental bottom-up stock analysis, Daniel Geber, portfolio manager, aims to offer a differentiated investment process in small-cap investing.*

**Q: What is your investment philosophy?**

**A:** We believe in buying good businesses at the right price. Typically, we focus on management quality and use of free cash flow that a company generates. We also try to invest in industrial sectors with attractive dynamics. We emulate the valuation analysis generally conducted in private equity business.

Our investment style has a heavy bias in fundamental analysis with long term holdings of stocks. Small-cap companies are hard to understand and harder to analyze on a global basis. Our investment approach looks for growth in free cash flow and management's use of it helps us find companies that meet our criteria.

**Q: What are the main criteria that you follow to put that philosophy into practice?**

**A:** Thinking like a private equity investor is how I would characterize our investment style. First, we aim at buying businesses at the right price. That means determining the business value and comparing it to the market value. We are looking to buy a busi-

ness which is trading at a discount. We also incorporate a top-down thematic approach in our investment process to identify trends and themes to focus our research efforts.

**Q: What makes your investment approach unique?**

**A:** What distinguishes our approach is the combination of a top-down and bottom-up approach. We look for themes as a way to focus our resources, and then we conduct conventional bottom-up analysis on each stock idea. Our research team works very closely with a highly centralized decision-making process. Thus everyone on the team knows the portfolio intimately. Everybody is involved in the discussions that lead to an investment decision.

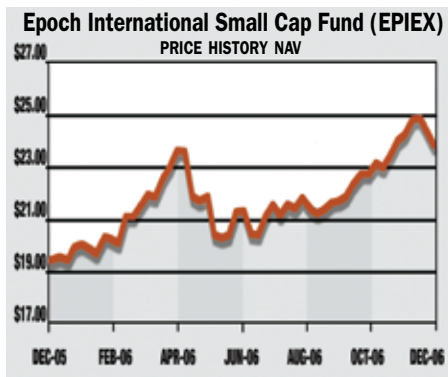
**Q: Can you explain the word 'international' in the name of the fund?**

**A:** 'International' means everything outside of the US but we have very little exposure to some of the more risky emerging markets. The big markets are defined by the benchmarks and are also defined by how we have positioned the portfolio. Western Eu-



**DANIEL GEBER** has invested and worked in international markets for most of his professional life. Before joining Epoch, he was most recently a Partner at Trident Investment Management, a macro-driven global equities long-short hedge fund. Prior to Trident, Mr. Geber was an Analyst at Omega Advisors, a New York-based hedge fund. Previously, he was an Executive Director at Goldman Sachs & Co., where he worked on private equity investments and advisory transactions including mergers, acquisitions, privatizations and equity and debt financings.

Prior to his graduate studies, Mr. Geber was an Analyst Consultant at McKinsey and Company. He holds an M.B.A. from Stanford University and a B.S. with honors in Mathematics and Computer Science from UCLA.



rope is about 2/3 of the portfolio, Asia is the next big market, and the index weightings for the rest of the world are much smaller in size and impact.

**Q: What are the benchmarks you measure yourself against?**

**A:** We look particularly closely at the S&P EMI EPAC (Extended Market Index Europe Pacific Asia Composite). That benchmark is relatively heavily weighted in Western Europe, so the biggest market as of the end of last year was the United Kingdom at about 22%, the second biggest market was Japan at around 19%, and then markets like Germany, France, Switzerland, etc. We also can and have invested in Canada. We prefer to buy in the local exchanges rather than restrict ourselves to the ADR trading in the US.

**“We are all about buying good businesses at the right price. We focus on management quality and how management is deploying the free cash flow that a company generates. We think about investments as a private equity shop.”**

**Q: What is your definition of small cap?**

**A:** We rely on S&P’s definition of small cap that is the bottom 20% of the market caps, in each one of the markets where the index is present. In certain Western European markets the bottom 20% of the market caps includes some relatively sizable stocks so that means that there are \$15 billion market caps included as part of the benchmark.

From our perspective, this presents both a challenge and an opportunity. The challenge is that we want to make sure that this stays a small cap product, so if you look at how the fund is positioned, our median market cap is slightly over \$2.5 billion.

**Q: What makes the asset class of international small caps so attractive?**

**A:** It offers a good potential for sustainable superior returns. In international small cap we find many undiscovered opportunities because a lot of the companies are too small to be covered by a large number of analysts. In my opinion, international small cap companies are under followed and under analyzed. The small cap companies in Europe tend to have higher return on investment, lower debt on balance sheet and faster growth than large and small cap companies trading in the U.S.

**Q: How many stocks do you evaluate in your international small cap fund?**

**A:** There more than 10,000 stocks and of these stocks we would consider between 2,000 and 3,000 on our investment list. We select approximately 150-200 of these names in our portfolio.

**Q: What is your selection process?**

**A:** The first step is to go from the broad investment universe to what we call investment opportunities. We use top-down themes as a screen and we also use quantitative and qualitative screens. We try to identify global trends, sometimes local trends and we try to identify themes that will provide us with an opportunity to narrow down that broad universe to a manageable size.

Our quantitative screens help us to look for companies with rising cash flows after adjusting for accounting standards. We’ll screen for free cash flow generation and recapitalization potential. We are trying to look for companies that might be attractive to private equity buyers.

We also use qualitative screens to look for transformational events: management changes, announcements of a restructuring or a spin-off. We look for changes that would offer the potential for the company moving from a less attractive opportunity to something that we like. Once we have identified the investment opportunities, we conduct fundamental bottom-up analysis on the stock. We focus on management quality, we look for their history of success, we look for the examples of their strategic vision, and of course, for their shareholder orientation.

We also go through a thorough process of evaluating the business. We look for industry drivers and the competitive position of the different players in the particular sector. We look for supply and demand characteristics and for sustainability of cash flow and earnings. We also spend time

looking at the financial strength of a company.

For each one of the investment candidates we'll develop an investment thesis. We'll try to identify the specific value of that business, and hopefully if the market is undervaluing that particular opportunity, then we'll decide to buy or sell with a determination of a price target and the downside risk.

### Q: Could you give an example to illustrate the process?

**A:** There is a Switzerland-based company in the hearing aides business that we have owned for a while. It is called Phonak. We identified the stock through a top-down thematic approach as we looked at demographic trends around the world. The baby boomer generation is aging but they have a strong desire to have a higher quality of life later in their years. That led us to look at a number of medical tech companies and we started to look at hearing aides as an investment opportunity.

People did not use hearing aides in the past because they were bulky, cosmetically unattractive, and they did not work very well. Those impediments are going away because this is a sector that is benefiting from miniaturization and from technological sophistication.


We started with a relatively small position and as we saw that the management was delivering exactly on what they were promising, we increased the position. This is not a cheap stock based on some traditional measures of say P/E or price to growth. This is a high-quality company that is generating phenomenal returns and we'd love to own it for a very long time.

### Q: How do you control risk?

**A:** We like the idea of a relatively diversified portfolio. From a risk perspective, any position above 1% is considered to be a relatively highly concentrated bet. We also like the idea of being able to express our themes through a number of names. Sometimes when we find more than one company in a sector that meets our investment criteria we spread our investment over multiple names rather than selecting one name from the sector.

There are very few names that are above 1.5% in our portfolio, so anything that is above 1% has to be a high conviction bet for us.

### Q: How would you describe your sell discipline?

**A:** The sell decision has to reflect the change to our investment thesis. It could be that the management has veered off from what they announced they were going to do before, and we do not like that. Sometimes companies could disappoint in terms of their numbers or their ability to be successful in a certain market. Sometimes the sell discipline is going to be triggered by valuation. 

## Epoch International Small Cap Fund

Symbol	<b>EPIEX</b>
Website	<a href="http://www.eipny.com">www.eipny.com</a>
Address	Epoch Investment Partners, Inc. 640 Fifth Ave, 18th Floor New York, NY 10019
Tel. No.	212-303-7200
Inception	01/25/2005

PORTFOLIO	
Total Net Assets*	\$286.7
Avg Mkt Cap (\$ Weighted)*	\$2,768
Average Price/Earnings Ratio	22.29
Average Price/Book Ratio	4.33
Turnover Ratio	64.5

INVESTMENT INFORMATION	
New Investment	Open
Min Initial Investment	\$100,000
Min Subsequent Investment	\$10,000
Min Initial IRA Investment	N/A

RISK (AGAINST S&P/CITIGROUP EMI EPAC - 3-YR)	
Alpha	N/A
Beta	N/A
R-Squared	N/A
Ann. Std Deviation	N/A
Sharpe Ratio	N/A

RETURNS VS. S&P/CITIGROUP EMI EPAC INDEX		
	EPIEX	Index
1 Year (Cum.)	38.26%	27.58%
3 Year (Ann.)	N/A	N/A
5 Year (Ann.)	N/A	N/A

RETURNS ON ASSETS	
EPIEX	S&P/Citigroup EMI EPAC
8.80%	7.04%

RETURNS ON EQUITY	
EPIEX	S&P/Citigroup EMI EPAC
19.75%	15.69%

FEES AND EXPENSES	
Max Sales Charge - Front	0.00%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee**	2.00%
Total Expense Ratio	1.55%

PORTFOLIO MANAGER	
Daniel Geber	01/25/2005

\*millions \*\*6 months after purchase

Data through: 12/31/06

Source: Company Documents; Lipper

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