



HILLCREST ASSET MANAGEMENT, LLC

## **Disclosure Brochure**

Updated 3/15/10

### **Hillcrest Asset Management, LLC.**

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For further information, please contact Deborah Trask, Chief Operating Officer at [dtrask@hillcrestasset.com](mailto:dtrask@hillcrestasset.com).

*This brochure serves as a replacement for Form ADV Part II. Form ADV gives information about the investment advisor and its business for the use of clients. The information contained here has not been approved or verified by any governmental authority.*

## 1. Advisory Services and Fees

Hillcrest Asset Management, LLC (“Hillcrest”) is engaged in the business of providing investment supervisory services.

Investment Advisory Services fees are charged as a percentage of account assets. Fees are quoted on an annual basis. Account fees are computed and billed quarterly, in advance. The initial fee shall be based on the Account’s market value at the inception of the Advisor’s management and prorated for the number of days the Account was managed during the initial quarter. Subsequent quarterly fees shall be based on the Account’s market value as of the close of business on the last business day of the quarter preceding the quarter for which the fee is due. The percentage charged typically follows the schedules outlined below.

The standard advisory fees for the Small Cap Core product are as follows:

|                                |                                 |
|--------------------------------|---------------------------------|
| 1.00% Annually on the first    | \$10 Million of Portfolio Value |
| 0.95% Annually on the next     | \$40 Million of Portfolio Value |
| 0.90% Annually on amounts over | \$50 Million of Portfolio Value |

Minimum Annual Fee of \$50,000

The standard advisory fees for the Small Cap Value product are as follows:

|                                |                                 |
|--------------------------------|---------------------------------|
| 1.00% Annually on the first    | \$10 Million of Portfolio Value |
| 0.95% Annually on the next     | \$40 Million of Portfolio Value |
| 0.90% Annually on amounts over | \$50 Million of Portfolio Value |

Minimum Annual Fee of \$50,000

The standard advisory fees for the Large Cap Core product are as follows:

|                                |                                  |
|--------------------------------|----------------------------------|
| 0.35% Annually on the first    | \$50 Million of Portfolio Value  |
| 0.20% Annually on the next     | \$50 Million of Portfolio Value  |
| 0.18% Annually on amounts over | \$100 Million of Portfolio Value |

Minimum Annual Fee of \$50,000

Our fees are generally non-negotiable; however, fees charged to any given client may be higher or lower than the stated fees or the fees charged to other clients with accounts

of comparable size and investment objectives, based on the client circumstances or investment guidelines.

All assets in any form are considered in the computation of fees. Money invested in cash balances, money market assets, client-directed assets or notes will be included. If trades are unsettled and pending, the trade date balance will be used.

In computing the market value of any investment of a client's account, each security listed on national securities exchanges shall be valued at the last quoted sales price on the valuation date of the principal exchange on which such security is traded. Any other security or asset shall be valued in a manner determined in good faith by Hillcrest to reflect its fair market value.

Either Hillcrest or the client may terminate an advisory contract at any time by giving the other party 30 days written notice. Advisory fees paid in advance will be prorated to the date of termination and any unearned portion will be refunded to the client.

## **2. Types of Clients**

Current clients consist of individuals and pension and profit sharing plans.

## **3. Types of Investments**

We offer advice on exchange-traded, over-the-counter and foreign-issued equity securities.

## **4. Methods of Analysis, Sources of Information, and Investment Strategies**

We believe a well-defined investment process starts with an overall philosophy of how stocks will outperform the market. Having an overall philosophy helps a manager make sure they are not exploiting random returns as skill.

The Hillcrest philosophy is based on the understanding that a portfolio of securities with a combination of attractive valuations and good earnings growth will consistently outperform its benchmark. The strategy's primary emphasis is the use of quantitative techniques to select individual securities in what would be considered a bottom-up approach. Our approach is inherently non-linear relying less on statistical estimations and more on investment insight. A risk control discipline limits the over- or under-exposure of the portfolio to industry/sector concentration. Security selection is the key component of our alpha generation. We utilize academic research, behavioral market theory, quantitative tools and fundamental research in our process. We invest in securities that have superior valuations relative to the market and their peers, earnings growth greater than the market and their peers and strong financials. The competitive

strength of this strategy is that it avoids introducing to the process any judgmental biases and behavioral weaknesses that often influence investment decisions.

The Efficient Market Hypothesis states that utilizing publicly available company information will lead to a fair value. It is clear that company information alone is not the only thing that affects the price of a stock. The fact that people buy and sell stocks affects the price because people have emotions and opinions about companies that are not always reflected in the data available. Due to these emotions, prices will deviate around fair value. Hillcrest utilizes behavioral finance to take advantage of this mispricing. Our expertise comes from Brian Bruce's pioneering efforts in behavioral finance. He is a founding member of the Board of Directors of the Institute of Behavioral Finance, is the Editor of the *Journal of Behavioral Finance* and has spoken about behavioral finance at over 50 professional investor conferences and universities.

What sets Hillcrest's process apart is that our research shows which factors are important and when they are important. It is important to understand, for example, that long-term price momentum cannot be positive if you plan to buy at the bottom of the valuation cycle. Positive long-term price momentum back tests very well and many managers give it a fixed weight in their model due to this fact. We understand that long-term price momentum is a good factor to use when determining to hold a stock but it can keep you from buying when valuations are most attractive. We use our experience as portfolio managers and our investment philosophy to guide our models and will use long-term price momentum only when it is accretive to the process

Hillcrest seeks attractively-priced securities with strong financials. We buy those stocks when positive information changes perception of the company. We hold those stocks as they move from under-reaction to over-reaction. We sell them when the valuation is expensive and investors are losing enthusiasm. The strategy's emphasis is securities selection. We do not engage in asset allocation, sector rotation or any top down techniques. Historical attribution shows that over 95% of returns come from stock selection.

The portfolio decision making process is quantitative and driven by (1) a proprietary model which ranks securities based on fundamental measures of value relative to growth rates and, (2) strong sentiment indicators such as earnings revisions/surprises, short interest and percentage change in short interest, (3) a risk control process that controls for residual benchmark risk while maximizing the expected return of the portfolio. Additionally, we employ a very robust fundamental (quality) component that seeks to uncover data errors and misinformation. This leads to a high degree of consistency in the practical application of our investment philosophy. In order to maintain our position at the cutting edge, refinements to the model are made as suggested by advances in our research. These refinements are generally incremental in nature and do not represent a departure from our basic philosophy.

A universe of approximately 10,000 equity securities is screened for market capitalization between \$100 million and \$2.5 billion and for liquidity which yields an investable universe of approximately 1,800 securities. These securities are ranked by our proprietary quantitative model driven by a security's fundamental measures of value, growth prospects and sentiment indicators. The top 20% of stocks by expected return rank (approximately 360 securities) are then further analyzed using fundamental techniques and the final stocks are chosen. The portfolio is then constrained by specific industry/sector and company limitations to achieve diversification. The process produces a buy list with portfolio weights ranging from 0.5% to 1%. As market action changes the weight composition of securities in the portfolio, stock positions that have appreciated to exceed 1.5% of the portfolio will be scaled back.

A stock is sold entirely if its expected return ranking falls below the top 70% of stocks in the universe.

Hillcrest intends to be fully invested in equities at all times with a maximum cash position of 2% of the portfolio.

Turnover is approximately 30-40% annually for Small Cap Strategies and 20-25% for the Enhanced Large Cap strategy.

Options and futures are not used in any Hillcrest strategy.

## **5. Education and Business Standards**

At a minimum, Hillcrest requires all portfolio managers and equity analysts to have obtained a bachelor's degree. In addition, a portfolio manager and equity analyst is expected to have an MBA, be a Chartered Financial Analyst ("CFA") charter holder or be working towards a CFA charter. Hillcrest supports and encourages employees to pursue advanced degrees and other professional designations. Hillcrest considers a candidate's business and educational background, prior investment-related experience and past positions held of primary importance.

## **6. Education and Business Background**

Biographies of key personnel are as follows:

**Brian Bruce, CEO and President.** Brian, born October 22, 1955, received his M.B.A. from the University of Chicago, M.S. in Computer Science from DePaul University, and a B.S. in Business Administration from Illinois State University. He is a member of the Illinois State University College of Business Hall of Fame and is winner of the University of

Chicago Graduate School of Business CEO Award. Brian is a professor at Southern Methodist University's Cox School of Business teaching both undergraduate and MBA classes which manage over \$6 million of the SMU endowment. Brian served as Chief Investment Officer in charge of equity management and research at PanAgora Asset Management, a \$23 billion institutional manager. Prior to joining PanAgora, he was a full time professor at Southern Methodist University and President and Chief Investment Officer of InterCoast Capital, a Dallas based subsidiary of a fortune 500 energy company. He previously worked at State Street Global Advisors, the Northern Trust Company and Stein Roe & Farnham. Brian has published numerous scholarly articles and books including *Analysts, Lies, and Statistics* which he co-authored with Harvard Business School professor Mark Bradshaw. He is also the Editor-in-Chief of Institutional Investor's Journal of Investing, Editor of the Journal of Behavioral Finance and Editor of the Journal of Trading. Brian frequently appears in the media including NBC, ABC, CNBC, Wall Street Journal, Bloomberg, Washington Post, New York Times, Associated Press, Reuters, Financial Times and Business Week. Brian also serves on many boards of directors including The Center for Investment Research, the CM Family of Mutual Funds and the Institute of Behavioral Finance.

**Ty Sanders, Managing Director, Sales and Marketing.** Ty joined Hillcrest Asset Management in 2009. Prior to joining Hillcrest, he was the Director of Sales and Marketing of the Private Client Group at Smith Group Asset Management from 2006 to 2009. From 2004 to 2006, he was Vice President and Director of Advisory Services of Envestnet Asset Management. Prior to joining Envestnet, he led the sales and marketing efforts in the Southwest region as Regional Director at Lockwood Financial Services, Inc./Bank of New York. Mr. Sanders earned his BS in National Resources from The Ohio State University and his MBA in Finance from Texas State University.

**Deborah Trask, Managing Director and Chief Operating Officer.** Deborah, born January 5, 1956, received her BA in Business from Northeastern University and her MBA from the University of Texas at Dallas. Prior to joining Hillcrest Asset Management, Deborah did operations and trading for RPF Equity Advisors. From June 1999 until she joined RPF Equity Advisors, Deborah was the Operations Manager and Office Manager for Dana Investment Advisors responsible for all of the trading and operations for its equity strategies. Previously, she was Senior Vice President in charge of operations for InterCoast Capital in Dallas, Texas. Before joining InterCoast, she was a member of the executive committee and responsible for operations of \$15 billion of domestic and international equities at State Street Global Advisors. She was a co-founder in charge of operations at India Wharf Associates. She is Managing Editor for *The Journal of Investing*, *The Journal of Trading* and *The Journal of Behavioral Finance*.

**Douglas E. Stark, Managing Director, Portfolio Management and Research.** Douglas, born December 22, 1960, received his BA from Arizona State University and his MBA in

finance and international business from Columbia University, where he graduated with honors. He is a CFA charter holder. Prior to Hillcrest, he was Partner, Senior Vice President, and Director of Research at Martingale Asset Management. Prior to joining Martingale, Douglas was a Senior Vice President and Portfolio Manager at InterCoast Capital Company where he developed a stock selection strategy and created a risk management process for an active U.S. equity portfolio active international portfolio, and emerging markets portfolio. Douglas started his career at State Street Global Advisors in 1990, where he was a Vice President and management international stock portfolios and active currency overlays.

## **7. Other Business Activities**

Hillcrest's principal business is as an investment advisor providing investment advice concerning securities to clients.

## **8. Other Financial Industry Activities or Affiliations**

Hillcrest is not registered as a securities broker-dealer, nor is it registered as a futures commissions merchant, commodity pool operator or commodity trading advisor, nor has Hillcrest made any arrangements that are material to its investment advisory business or its clients with a related person, nor does a related person act as a general partner in any partnership in which clients are solicited to invest.

## **9. Participant or Interest in Client Transactions**

Hillcrest currently maintains and adheres to a comprehensive Code of Ethics. The Code of Ethics covers many topics, including: the review and reporting of personal securities transactions, restrictions on investing in initial public offerings and private placements, prohibitions on the use of and trading on material non-public information, and the establishment of the position of Chief Compliance Officer.

All Hillcrest employees are restricted from engaging in any practices that would operate as a fraud or deceit upon Hillcrest or any of its clients. Hillcrest permits its employees to invest in securities that may also form a part of the client's portfolios. Because Hillcrest permits its employees to deal in securities that clients may also deal in, every employee is required to obtain pre-clearance on securities transactions including initial public offerings and limited offerings.

The Chief Compliance Officer periodically reviews all personal securities transactions to ensure that employee positions and trades do not present a conflict of interest with the position of Hillcrest Clients. Hillcrest employees formally report their personal securities transactions to the Chief Compliance Officer quarterly. Annually, personal holdings

statements for all access persons are also required to be given to the Chief Compliance Officer for review. Hillcrest provides regular updates and discussion regarding the firm's Code of Ethics. All employees are then required to sign an annual statement acknowledging receipt, compliance with and understanding of Hillcrest's Code of Ethics. A detailed copy of Hillcrest's Code of Ethics is available to clients or prospective clients upon request.

#### **10. Conditions for Managing Accounts**

Hillcrest does not have a minimum account size requirement.

#### **11. Review of Accounts**

Certain members of the firm act as portfolio managers for client accounts. Each client portfolio is formally reviewed on a quarterly basis. However, triggering factors (buy/sell a new security, risk control parameters, sell discipline) will compel portfolio managers to review accounts on a more frequent basis. In addition, portfolios are monitored daily on a composite basis.

Portfolio Managers meet weekly to discuss general investment policies and procedures as well as specific investment ideas. Hillcrest generates written analysis of portfolio performance based upon client needs. Hillcrest provides clients with a written annual performance analysis, including quarterly performance figures. In addition, performance figures can be requested at any time.

#### **12. Investment or Brokerage Discretion**

Hillcrest has discretionary authority to buy and sell securities in the quantities that it deems fit without first obtaining consent of the client. Hillcrest determines which securities to buy or sell, the total amount of securities to buy or sell, the broker or dealer through which the securities will be bought or sold (unless directed by the client) and the commission rates at which the transactions are executed. Any limitations or restrictions with respect to the exercise of this investment discretion will be those established by the client in writing at the commencement of the advisory relationship or thereafter. Hillcrest does not engage in principal trading or agency cross transactions.

In selecting a broker-dealer through which to purchase and sell securities, Hillcrest will review the most favorable combination of transaction cost and proceeds available under the circumstances (Hillcrest Asset Management will seek best execution). In connection therewith, Hillcrest will consider a range of factors, including price and commissions, execution ability, clearance procedures, custodial and reporting services,



and other brokerage services provided by the broker-dealer. Hillcrest does not use soft dollars and as such, research is not a factor in choosing a broker-dealer.

Subject to the above commitment to obtain best execution, Hillcrest will attempt to accommodate client requests to effect securities transactions through a particular broker-dealer.

Based upon the quality of the brokerage and/or other services provided, advisory clients may pay a brokerage commission or mark-up in excess of that which another broker-dealer might have charged for effecting the same transactions. Not all such services may be used by Hillcrest in connection with advisory clients who paid commissions to the broker-dealer providing such services. A written copy of Hillcrest's Soft Dollar Policy is available to all clients upon request.

When applicable, Hillcrest will take appropriate action and/or render advice with respect to the voting of client proxy statements. From time to time, Hillcrest may retain a proxy voting agent, who conducts in-depth research, monitoring, and provides comprehensive voting services. Hillcrest, to include any third party proxy voting agent, will vote all client proxy statements according the Proxy Voting Guidelines adopted by Hillcrest. Utilizing formal proxy voting guidelines helps to maintain objectivity and fairness, and allows for resolving any potential conflicts of interest in a prudent manner. Hillcrest therefore believes that its proxy voting process resolves all issues in the best interest of each client. A written copy of Hillcrest's Proxy Voting Guidelines is available to all clients upon request. Clients may request information on how Hillcrest voted their proxies by contacting Hillcrest in writing. Requests should be addressed to:

Compliance Officer  
Hillcrest Asset Management  
14180 N. Dallas Parkway  
Suite 650  
Dallas, TX 75254

### **13. Additional Compensation**

Currently, Hillcrest does not have any arrangements, oral or in writing, where it is paid cash by or receives some economic benefit from a non-client in connection with giving advice to clients or directly or indirectly compensate any person for client referrals.

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Hillcrest has adopted policies to protect personal information about its clients. A copy of Hillcrest's privacy policy is available upon request.