

Portfolio Commentary –4th Quarter 2009

Small cap stocks closed out the year with another good quarter rising nearly 4% to post a return of 27% for 2009. There was not much difference in returns across the market cap spectrum during the quarter but for the year mid caps lapped the field outperforming both large caps and small caps by roughly 12%. The market rally that began last March can only be classified as stunning. Thinking back to that time there were few pundits pounding the table for equities when fear and valuations were at opposite extremes. We have always believed that market timing is a tough game to win and this episode once again reinforces that belief. Investors now seem to be wrestling with the magnitude of the economic recovery and its resulting impact on corporate earnings. We view forward looking macro economic estimates with a great deal of skepticism and prefer to focus on valuations. At this point, whether looking at 2010 or 2011 corporate earnings estimates, it does not appear that equity valuations are terribly demanding.

Small cap value stocks and growth stocks achieved similar results this quarter but for 2009 growth outperformed by 14%. As pointed out throughout the year, perhaps somewhat counter intuitively, deep value stocks enjoyed a very good year within the value universe. This phenomenon certainly benefitted the performance of your LSV portfolio for the year but had little impact in the 4th quarter. Returns across sectors for the quarter were not very disparate but several of the more defensive groups, including Health Care, Utilities and Telecom outperformed the rest. For the year, cross-sectional volatility was quite high with Consumer Discretionary, Materials and Tech all rising more than 60% while Financials and Utilities lagged, returning -12% and 7% respectively. As a result of this high cross-sectional volatility, we witnessed more change than normal in the sector weights within your portfolio. Following the rally more defensive, steady earning companies are now ranking much better in our model than they have for the past 3-4 years, largely as a result of forward-looking valuations. These types of companies therefore have an increased importance in your portfolio.

Patience with our deep value approach throughout 2007 and 2008 was well rewarded in both absolute and relative returns during 2009. Knowing that the only certainty when it comes to economies and markets is uncertainty, we maintain the belief that a disciplined data-driven investment process remains the most prudent approach to managing equity portfolios. We are aware of concerns in some circles regarding perceived homogeneity among quants and are in the midst of a 'white paper' research project on the topic that will be shared with you soon. As a firm we continue to identify new and interesting model research ideas that we hope will serve you well for many years to come.

LSV Update

- LSV's Small Cap Value Strategy is closed to new investors.
- Total assets in strategy: \$1.4 Billion. Total Value Equity Assets Under Management: \$5 Billion.
- Visit our recently enhanced website for access to LSV research papers and to find out "What's New" at LSV: <http://www.lsvasset.com>

	Market Update				
	<u>4Q09</u>	<u>1YR</u>	<u>3YRS</u>	<u>5YRS</u>	<u>10YRS</u>
S&P 500	6.0%	26.5%	-5.6%	0.4%	-1.0%
Large Cap Value Stocks (R1V)	4.2%	19.7%	-9.0%	-0.3%	2.5%
Large Cap Growth Stocks (R1G)	7.9%	37.2%	-1.9%	1.6%	-4.0%
Big Cap Value Stocks (RT200V)	3.8%	14.6%	-9.8%	-1.1%	0.4%
Big Cap Growth Stocks (RT200G)	8.4%	34.0%	-1.3%	1.4%	-4.8%
Mid Cap Value (RMCV)	5.2%	34.2%	-6.6%	2.0%	7.6%
Mid Cap Growth (RMCG)	6.7%	46.3%	-3.2%	2.4%	-0.5%
Small/Mid Cap Value (R2500V)	4.6%	27.7%	-7.0%	0.8%	8.2%
Small/Mid Cap Growth (R2500G)	5.6%	41.7%	-3.1%	2.0%	-0.2%
Small Cap Value (R2V)	3.6%	20.6%	-8.2%	0.0%	8.3%
Small Cap Growth (R2G)	4.1%	34.5%	-4.0%	0.9%	-1.4%

....Periods greater than one year are annualized. Source: Frank Russell Company & S&P