



GOVERNMENT OF GUAM  
**RETIREMENT FUND**  
STABILITY · SECURITY · REWARDS

Felix P. Camacho  
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Michael W. Cruz, M.D.  
Lieutenant Governor

Paula M. Blas  
Director

**Quarter Ended 12/31/09  
Performance Meetings  
& Annual Manager Reviews**  
March 25, 2010  
Retirement Fund Conference Room

**Thursday, March 25, 2010**

**Board of Trustees Present:**

Joe T. San Agustin, Chairman, Board of Trustees  
Wilfred P. Leon Guerrero, Ed.D, Chairman, Investment Committee  
Gerard A. Cruz, Member  
Wilfred Aflague, Member  
Antolina S. Leon Guerrero, Member  
Katherine T.E. Taitano, Member

**Staff Present:**

Paula M. Blas, Director  
Diana Bernardo, Controller  
Rosalia Bordallo, General Accounting Supervisor

**Other Present:**

Terry Dennison, Mercer Investment Consulting

**Defined Benefit Plan:** Pages 1 to 35

**Capital International (Emerging Markets)**

Dr. Leon Guerrero: You can say anything you want in this discussion. For our part we are looking for is how you did last year, what you expect next year, whether there are any changes in personnel and whether any regulatory agencies have issues with you. For the record the people present are the Board of Trustees, our Chairman of the Board, Mr. Joe T. San Agustin, Paula Blas our Director, Terry Dennison from Mercer Investment Consulting, our Trustee Wilfred Aflague, Trustee George Santos, Controller Diana Bernardo, Rosalie Bordallo and myself, Wilfred Leon Guerrero.

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**Joe T. San Agustin**  
Chairman

**Wilfred P. Leon Guerrero, Ed.D.**  
Vice-Chairman  
Investment Committee, Chairman

**Antolina S. Leon Guerrero**  
Secretary

**Gerard A. Cruz**  
Treasurer  
Audit & Operations Committee,  
Chairman

**George A. Santos**  
Members' & Benefits Committee,  
Chairman

**Katherine T.E. Taitano**  
Trustee

**Wilfred G. Aflague**  
Trustee



Philip Hsin: I'd like to do an introduction of who we are, we're both based in Singapore. My name is Philip and I'm responsible for the relationship management and the overall person responsible for this account is Andy Budden. Andy has been with us for about 7 years and his role is primarily an investment specialist which means he basically represents the portfolio management team, so he's part of the investment team and he's very closely tied in to the different managers that are managing this portfolio for your account. Andy's background is he was with Watson Wyatt (Investment Consulting) for about 12 years as a consultant in Asia as well as in the U.K.

We were provided with a list of items to discuss and the first thing we were asked to discuss was performance since the date of inception. Let me start by looking to page 1 and looking at just the inception numbers, there are 2 inception numbers to the end of September and inception to the end of February. For both periods coincidentally the market returned a positive 8.6% and our contribution on top of that benchmark return would have been 3.6% per annum for the period ending September 2009 and 2.8% per annum for the period ending February 2010. The markets during this period was actually quite interesting if you go back to when the portfolio started which was August 2006, 2006 for that period and 2007 were both positive years, with a year of a pretty large drop in the market place, over 54% in 2008 and of course as you are aware, the markets rebalanced strongly in 2009 and the last couple of months the market has actually come down a bit by about 5.2%. So that's really a quick review of what's happened to the benchmark as well as the portfolio.

The one year September 2009, the market was up 21% and this is despite a 27% drop in the quarter 2008 and that was actually the largest quarterly drop for the whole year of 2008 and we still end up with a positive number so that's great for your portfolio. I think the sentiment during this period was that it turned to a very bleak environment. As you know we started in the beginning of 2008 and a lot of bad news came out and it ended with a lot of credit tightening as well as a slide in commodity prices but then it turned at the beginning of 2009 with signs of economic recovery, we're starting to see IPO's especially towards the 3<sup>rd</sup> quarter of 2009, IPO's activity picking up again and we also saw improving earnings for corporates out here in emerging markets. So that was a snapshot of what happened in the market place.

In regards to our portfolio in that period, the 12 month period, we added 190 basis points or 1.9% over the benchmark. The key contributors to adding the value over this period was primarily our overweight to China and our stock selection and sector positioning in energy and information technology.

Dr. Leon Guerrero: We have a right up from Mercer and this quarter that you're talking about is ending September 30, 2009, ours is December 31<sup>st</sup>, the periods don't match. Philip Hsin: We have a request here to look at performance since inception, performance to September 2009 and then for the 5 month for October 2009 to February 2010. We were asked to provide for you fiscal year. Diana Bernardo: We've always sent it and asked them to do it that way, we do an annual review for the fiscal year ended so the only reason why the information doesn't tie to Terry is because had we seen them also in December, then we would have been comparing the information

to Terry's report in December, we just don't see all the managers at one time. Philip Hsin: For next year we can do both and if you like we can send the information when we get back. The quarter ending 2009, the 4<sup>th</sup> quarter, the market was up about 9%. We outperformed during that period as well, I just don't have the specific numbers with me.

Andy Budden: We can start by talking a little bit about your fiscal year and we can bring you more up to date. On page 4 of the materials, just to remind you briefly of the approach that we use to manage your portfolio. There are actually 3 things that are useful to how we look after your money. The first thing is we are bottom up stock pickers so we do try to understand macro issues but our real skill is looking at individual companies and understanding their business prospects and then deciding which stocks we want to hold, it's all about the stocks for us. The second one is the research, the way we think about the individual companies based upon research that's conducted by our own team of analysts so we don't really rely on publicly available resources conducted by the broker community, it's our team of analysts. The final thing is that when we receive your money, we use an approach called the multiple portfolio manager system for managing your portfolio. Essentially we receive your money and we divide it up into 6 or 7 different portions each one of which is managed by a different portfolio manager who has their own very distinctive style and also a very good long term track record of delivering good results so when we combine these 6 portfolio managers, hopefully we create something that's going to help grow the assets of your pension fund over time. Joe T. San Agustin: You divide it into 6 or 7, each one of them has an allocation of what we gave you, do you have the breakdown of that, what each one gets, you do have that allocation breakdown? Andy Budden: We don't generally disclose that number. Joe T. San Agustin: We give you millions of dollars and you don't want to tell us how you divide that money, I don't understand that, at least give me an idea. Andy Budden: We don't disclose a precise number because it changes over time. Joe T. San Agustin: You do have an allocation strategy and I just want to know what your strategy is. Andy Budden: The breakdown is approximately 25% of \$60 million to the research portfolio. Within that research portfolio, each of the research analysts would basically pick their and it gets built up until it reaches 25%, the remaining 75% is divided amongst the 6 managers, so each one would have approximately 12-13%. Joe T. San Agustin: Within those portfolios you have returns, you can't share that with us? Philip Hsin: We do not share the returns of individual portfolio managers, what we kind of live and die by are the results of the overall fund, which over time have clearly been good. Joe T. San Agustin: We're the one taking the risks and you don't want to share that with us? Philip Hsin: We're hopefully sharing the results of the portfolio with you and those are built by individual portfolio managers. Joe T. San Agustin: I don't feel comfortable with the fact that you allocate within yourself and you don't want to share how you allocate that with us and what are the individual portfolio returns, what kind of risk you are taking within the diversification. Philip Hsin: The rationale behind that policy of not disclosing individual manager results is really that we as an organization, would like to focus on the long term and what we find in some instances, when these numbers do come out and we do get client requests to focus on a certain manager or not wanting a certain manager and often what happens in the portfolio is that it might do badly in one time period and we don't want to have any biases towards moving

money away from any particular manager, so it's part of our policy not to disclose that. Joe T. San Agustin: Just keep in mind that I'm very uncomfortable with that, but go ahead.

Let's talk about the results of your portfolio and why over the last fiscal year and why your portfolio outperformed and Philip has already described how the fiscal year was divided into 2 very distinct periods. The first half was a huge market crash and the second market period was one of recovery. In summary I think that your portfolio was positioned extremely well through the down turn and the beginning of the recovery but then it just kind of kept pace with the market during the recovery and it didn't outperform that much during the recovery.

I can talk about some of the individual stocks that helped and hurt the portfolio. One area of the portfolio that was particularly successful during the fiscal year were the investments we made in China and there was quite a range of companies that performed well. One company that you might have heard of is a company called BYD which is actually a manufacturer of rechargeable batteries. One of the things that we find very exciting about BYD is that they also have an auto company and in particular they're auto company is basically using hybrid cars, making hybrid cars and the auto company is already about half of their business and half of that profitability is growing very quickly. The stock has been successful and has actually gone up about 5 times during the review period. Another very different company is a company called China Shenhua Energy and that's actually one of the biggest coal miners in China and the mine coal that's used to generate power and they are growing their rate of production very quickly. In short, they're part one of the big solutions to China's power needs over the next 20-30 years and they're a very strong stock. Something very different is a company called Nine Dragons which is the largest manufacturer of paper in China and in particular, they focus, not so much on this paper, but on container board and packaging. As you might expect in the economic downturn, when the market crashed, the stock was absolutely killed. We're very fortunate that we were able to buy it at \$2 after it had peaked at \$25, so we were able to buy it at a very low and enjoy a very strong recovery in that stock so that's something that really worked well for the portfolio. Other parts of the portfolio that worked well were we had investments in the IT sector, in particular, Samsung, that was a very strong stock for the portfolio and there are some more consumer related stocks in Latin America were also quite strong.

The things that didn't work so well, I'll highlight a couple of areas in particular. The first one is we do have a large focus on telecom stocks in your portfolio and telecom is a sector that has underperformed quite significantly over the fiscal year, so clearly being over weight, telecom was not the right thing to do with your money. We're actually sticking to our guns there, we still see lots of value and potential for attractive returns there for many of the telecom companies. We see them around the emerging market world and that would include companies like America Movil which is the largest provider of mobile phone services in Latin America. Other companies like Bharti in India and also the Polish telecom company as well which is facing lots of challenges so we think it's still going to be able to grow it's profits as we move forward. The other parts of the portfolio that didn't work out too well was actually the investments we had in India and a company that didn't work out in particular is a

company called Suzlon Energy. They have a very specialized business, they make the blades that go into turbines? And clearly the demand for turbines as we've gone through the economic down turn has dropped right down and Suzlon's business really did fall onto its knees and so that was a mistake in terms of our investments as well. Over this period the good news is the positives outweighed the negatives and so overall we were able to deliver our performance on top of what was a reasonable market return over the overall period.

Philip Hsin: (Terry provided us with the one year and three numbers as of December 31<sup>st</sup>) On the one year basis, the market went up about 78.5%, we on a relative basis were down by about .7%, so we delivered a return of 77.8%. On a three year basis, we had a positive return of 2.8% over the benchmark of 5.1%. Andy Budden: I'm going to repeat a comment I made at the very beginning when I say that during the down turn we outperformed with your portfolio quite successfully and during the very strong market recovery, we actually underperformed. I think that's consistent with the fact that during the calendar year of 2009, we underperformed overall. Please do not interpret this as an excuse, it's more a characteristic of capital, we focus very much on the actual underlying businesses of companies that we try to invest in, we tend to have a long term focus, we're looking for companies that can generate growing profit over a reasonable time period. What we find is that unfortunately this approach does not generally outperform during very strong market rallies. During very strong market rallies the companies that tend to do best are the companies that people thought were about to go under and so the stocks have gone very low and when the market recovers people think actually they're going to survive, so the stock takes off like a rocket and we don't tend to hold companies like that because they don't really fit with our long term quality approach, so unfortunately in very strong market rallies, we do under perform. What we're hoping is as the market becomes more rational and that is exactly what's happened over the last 4 or 5 months, we hoping our focus on long term profitability is actually going to start to become much more rewarding again and that's certainly the experience we've had in previous cycles and we've been managing emerging markets for over 20 years now so hopefully that behavior of characteristic is going to continue in the future.

Philip Hsin: The second section, again it is for a 5 month period ending February 2010, would you like to focus on the 2 months in 2010? Dr. Leon Guerrero: What Mercer has given us for December 31<sup>st</sup>, there was an increase in the value of the portfolio by \$4.6 million, that was as of December 31<sup>st</sup>. Can you give us some of the companies that you mentioned because I think there's been a turn around in what you just mentioned happened in September to now. Andy Budden: I think that's absolutely right, so the results in more recent months have been slightly different and in particular, some of the stocks we hold in your portfolio in China, we have not performed that well recently, there's been a lot of concern of what's going to happen to the Chinese economy. It clearly ran through the crisis very well because in part, the Chinese authorities used every gun they had in their armory to make sure the economy didn't slow down. Now the challenge that they have is now that the economy is racing off again, how do they start to put some of those guns back in the armory without the economy slowing down much more than they intend. The stock market investors are very worried that the Chinese Government is going to mess this up and

in fact the economy is going to basically crash or slow down much more than the Government thinks it will. Our view is that the Chinese Government is going to be able to handle this quite well, we think they've managed the last cycle, the economic crisis, the recovery very well. We also know that since it's a very much controlled economy that actually the Chinese Government has more tools, they have a very direct impact that it can use. We might not all agree with this politically, but in terms of how you control an economy, they have a lot of control and so we think that the Chinese economy is going to stabilize, it's going to slow down a bit and then it's going to stabilize and a lot of the companies that we're holding in the portfolio will hopefully start to perform well again.

With that said, we have actually reduced the exposure of your portfolio to China and we have found that investments in other parts of the emerging market world, where we think there's also good growth prospects and so we have rebalanced the portfolio a little bit.

On page 14 of the materials you will see some comments, basically a summary of what helps the results over the last 5 months, in fact, these comments would refer to the last couple of months as well. I can start by focusing on the negatives, there's a materials company here, Vale is the world's largest producer of iron. It's a Brazilian company but you can say in many ways it's just a Chinese investment because much of the iron that gets produced is sold to China. So when people are worried about the outlook for China, Vale will go down and hence, that is the stock that hurt the portfolio.

At the bottom you can see stock selection in India has again been an issue for the portfolio. Bharti is a large telecom company in India that is facing increased competition. So again, telecoms have been an area that's hurt the portfolio and that's something where we really have to stick to our guns and decide whether or not we want to keep that in your portfolio. In terms of the things that have worked well, we are pleased to see there have been a bunch of companies coming through performing as we hoped they would. United Spirits is a company that has fantastic prospects. It's an Indian company and it's on it's way to becoming the largest producer of spirits in the world and they're growing their volumes, 15-20% so its business is growing very quickly. They're also benefiting because one of their key input costs is the price of sugar based ethanol and that price is coming down so volumes are going up, costs are coming down, so profitability is soaring and that's something that we think is pretty exciting in the investments for today and in the future.

One of the things in China that did perform very well for the portfolio is a company called Weichai Power. Weichai Power makes diesel engines primarily for trucks and virtually entirely sold into China and as the Chinese economy has clearly stabilized, Weichai Power has performed very well. In fact, we think one of the big surprises not just for trucks, but probably for cars as well, over the next 4 or 5 years will be the rate at which Chinese auto manufacturer's break out of China and start becoming a key player around the world and so Weichai Power we think plays right into that, it's a company that we hope to hold in your portfolio for sometime to come.

We're going to pause to see if there are any other particular questions that you have on historical results in the portfolio before we talk about the future. Dr. Leon Guerrero: China Shenhua is doing well? Philip Hsin: That is the coal company that has very large --- in China and is part of China's electricity generation problem for the future, so the company has wonderful profitability prospects.

Would it be helpful if we spoke briefly about what we expect in the coming year moving forward? Turn to page 21, here we summarized some of our views of how we think about the world and the first comment we made was it looks to us that emerging markets economies has stabilized and are racing ahead and also looks like global developed economies, they aren't exactly racing ahead but it does look like they've managed to escape the latest economic crisis. So stabilization has happened and we think that gives a nice positive foundation for emerging markets to start moving forward again.

The next comment that we'd like to make would be that we actually think the valuations for emerging markets are fair, not cheap but fair. When we think about equity markets, we always think about the 3 components of return. We think first about profit growth, then we think about how much investors are prepared to pay for that profit growth, so that's basically the valuation of the market and then there's dividend. In the emerging market world, dividend isn't very important so it's ultimately all about valuation and earnings growth. Last year the reason emerging markets was so strong was valuations went from historic lows back up to historic averages. So as of today, we don't think valuation is going to drive your portfolios results so it's all about earnings and the good thing is we think that the prospects for earnings or profit growth in emerging markets as of today is pretty strong and in fact, market expectations are the profits in emerging markets this year will grow at something like 25-30%. So all other things being equal, that would mean hopefully we're going to see another double digit type return in emerging markets over the next couple of years, so I think that's a backdrop.

What we are particularly excited about is China certainly and increasingly India. In the past we've found things interest, but whenever we go to India, frankly we always think it's a bit of a mess. Literally it's a mess, infrastructure is poor, systems are very inefficient, Government is kind of wonderful, but scary in its inefficiency, but what we're now starting to see is some signs that things are starting to change for the better. In particular, infrastructure in India is going up very quickly and that would be a great starting point for India, so we think that India could be an important part of the portfolio moving forward. Dr. Leon Guerrero: What kind of impact does Google have in China? Philip Hsin: The impact on China will be negligible, the impact on Google in the long term could actually be quite positive. China is a very small part of Google's business today so the fact that they are pulling out of China doesn't really matter. It could be a big part of their future business so maybe they've actually just cut off an important part of their future. The impression that our analysts have from the work they're doing in China at the moment is that the average person in the street in China, they're impression of Google has actually gone up quite significantly as a result of what they're doing, so if Google was ever to re-enter the market, it's likely that they would get a much bigger market share because people think of Google as a



place they can go to get unbiased information from the internet. This in short term, neutral to slightly negative, in the long term, potentially very positive and certainly is creating a lot of debate in China, but I don't think we should expect to see China change its rules on information availability anytime soon, the Chinese Government has very strong views on how the country needs to be run. Dr. Leon Guerrero: Is there a competitor? Philip Hsin: There's one search engine in China which is run by a company called Ali Baba which is pretty big already and it's likely to get bigger now. They basically run a portfolio of internet based businesses including a big search engine which is essentially Google's business. Ali Baba is a very small position in your portfolio and it's probably going to stay small because the stock is very expensive so we think the future prospects are be good, but if you're paying 50 times earnings when the market average is more like 15 times earnings, that's not the kind of stock that we feel comfortable buying.

I'd like to make a comment on the outlook, if we think about the emerging markets over the last 18 months, I think we would say it's been very macro market, so what's really driven the market is fears about an economic slowdown and then euphoria about an economic recovery. So it's very emotional, people have just been buying stocks because they think it's going to go out of business and then buying stock because they think it's not going to go out of business anymore. What we think is going to happen from this point forward is macro issues will still be important, but actually it's going to become much more about what can individual businesses do, are they going to grow very quickly or are they going to grow more slowly and in investment terms, we would call that a stock pickers environment. We are quietly hopeful that we're entering an environment where an approach that's used by a company like Capital will hopefully start to be quite rewarding, so the market on average we think is going to go forward. We think if you can pick the right companies then the portfolio could actually move forward more quickly and so that's how we're thinking about the current environment. There are of course risks, at the very least emerging markets are always volatile, they always find things to worry about and get excited about so it will definitely go up and down a lot. In addition, if the global economy does start to slow down a bit, that's going to be a problem. If the financial sector starts to see more signs of poor health then that would also be a problem for emerging markets. In addition, one thing that we're thinking about very carefully now is trade protectionism. If different countries around the world are struggling with their economy start to put down the barriers to protect their own domestic industries, that could really hurt emerging markets as well. So those are the things that we really worry about that our central view would be from here, the portfolio continues to go up in value.

Is there anything that we can try to clarify on any of this? Wilfred Aflague: Earlier you said that our portfolio, that you were slowing down or decreasing our portfolios involvement in China, here it says it's a key source, did you mean that you're just concentrating on certain stocks and companies in our portfolio? Philip Hsin: Yes, in short term. I know that sounds very inconsistent. In the short term we have certainly reduced the size of some of the positions we have in China where we felt the stocks were going to have a head wind because of the people's concerns about what the Chinese Government is doing. So the idea that China could just be a weaker market

for the next 6 months maybe, so we've kept positions, but we've reduced the size of them. In the long term, there are many reasons why we think we should continue to focus very strongly on China and it has to do with demographics, fiscal ---, currency reserves, export, lots of tailwinds which are right behind China. In addition, I think it's also important to know there's many different ways to invest in Chinese and Indian growth and one way is to invest in companies in China. Another way is to invest in companies outside China, the benefit from the growth. One company that we mentioned earlier in the meeting and it's Vale, it used to be known as CVRD and it's the big iron --- in Brazil, so it's a Brazilian company, but it's very much about China. There are other companies around the world where we see that exposure to Chinese growth and we choose to hold that non-Chinese company rather than the Chinese equivalent.

Andy Budden: Just further clarification here, this statement here doesn't talk to our view of whether or not China is attractive or not as an investment environment, but rather talks to China being a key source of the growth we are going to see in the global economy. So if China is not very careful of how it deals with the withdrawals and does it wrong, it could have a huge impact on the global economies and I think that's what this point here is pointing to that.

Joe T. San Agustin: In your returns, what is the Chinese policy on withdrawals for investments for returns, the policy of taking money out of China? Andy Budden: I think that's a great question and this is one area where the rules are very black and white and we feel very comfortable that your assets are secure. When we invest in China, we're not actually invested in the Chinese Stock Exchange. The Chinese Stock Exchange is very hard for foreigners to invest in. The companies we've mentioned today like BYD and China Shenhua and other companies, Ali Baba, the way we invest in them is through stock that they have listed on the Hong Kong Stock Exchange. Obviously the conclusion I'm drawing is if your money is invested in Hong Kong, it's fine. It's a stock in Hong Kong of a Chinese company and the way that's being structured and the way the market interprets it is that actually it gives you a share in a Chinese company and you can buy and sell it quite freely and take your money out of the stock exchange and out of the Hong Kong dollar just like that. We are not allowed to invest in Chinese listed companies; it's not possible for us to buy them in the first place. Joe T. San Agustin: The real estate investment trust is still working in China, is that going up? Andy Budden: Well real estate in general is going up very strongly in China at the moment and this is something that we're worried about and it's something that the Chinese Government is worried about as well. One of the risks in the world right now that we didn't mention, is the concept of liquidity, basically there's lots of cash floating around the world right now because Governments have spent lots of money and also because interest rates are very low so it's very easy for companies and countries to actually get a hold of lots of cash. Once people have cash, that cash generally tried to find a home and one of the places where cash from all around the world has been finding a home recently has been in Hong Kong and Chinese real estate and the prices have gone up to the highest levels. The Chinese Government is all over this, they absolutely want to control this bubble because when the bubble bursts, bursting bubbles cause pain and so the Chinese Government is

trying to put in all these policies to slowly bring it back down. That is a big issue right now but it's not something that we're invested in your portfolio.

Dr. Leon Guerrero: Do any regulatory agencies have issues with you? Philip Hsin: No we don't have any problems with regulatory agencies. Dr. Leon Guerrero: Any personnel changes? Andy Budden: There have been personnel changes over the last year. One of the changes is we created a global executive office. Prior to the formation of this office and this happened about 2 years ago, we at Capital have a history of running things on a community base and what we found 2 years ago were things were not reacting very quickly in terms of making decisions, so we actually created this executive office where there are only 2 members, the 2 most senior members of the organization, both of which are investment professionals, they're now responsible for the business, both investments and non-investments and that's helped a lot in terms of streamlining decision making in our organization. It's been cut down from a large community to 2 people in respect to how we manage our company. They of course still get input from different committees and different participants because Capital has always been very much a community organization. The other change is that we created an equity investment committee as well which is comprised of 2 very senior individuals as well on the investment team and those 2 individuals have been delegated the role of overseeing the equity investment process. I think the emerging markets in general, the team hasn't changed, there have been no changes to your portfolio management, it's been more administrative changes.  
(End of presentation by Capital International)

### **Fisher Investments (Non US Equity Developed Markets)**

Dr. Leon Guerrero: We want to make sure we're looking at the same time frame. What period is your handout? Chris Davis: It's through the end of February and the one I have is updated to March 12. Dr. Leon Guerrero: You can lead us in a discussion of what you've done last year, what you expect from this year, you can tell us about your organization, are there any changes in personnel, whether any of the regulatory agencies have issues with you. Chris Davis: Fisher investments, we're one of your international managers benchmarked versus the MSCI EFEA. Page 1 is a highlight of our organization. We had a very successful year as a firm last year and part of that success stems from the stability of our organization, as you can imagine, throughout our industry and within this financial crisis, there was a lot of disruptions within individual companies. At Fisher Investments, we're 100% employee owned, we have zero debt, all we do is asset management so we don't have any subsidiaries, mutual funds or anything that would sort of conflict with our mission. This in terms of the people that are managing the portfolio, they're the same people that are at the firm when you hired us, there hasn't been any turnover in the senior decision makers and actually throughout this financial crisis we've actually expanded our research group that supports the senior investment professionals. So it's actually been an opportunity as a result of the stability of our firm to really expand our resources when in fact I'm sure our peers have been cutting back.

Page 2 and 3 is just a partial client list of what you see yourself as well as your neighbors down in Saipan. Lots of these clients have been around for many years and we have very long stable client list of institutions.

Very quickly on page 4, I just wanted to give a quick overview of our process, how we go about constructing the portfolio, so maybe it will make a little bit more sense when we start talking about our views on the market and how we currently have your portfolio postured to take advantage of it. We're a top down manager and I believe it's very different from your other managers that are really focused on it from a bottom up perspective. With that being said, I'm sure throughout the presentations even from your fixed income managers and I understand your equity managers, I'm sure you have heard about how these macro events have really impacted their ability and all managers ability to outperform throughout this period of time and these macro events are certainly a matter and people are starting to focus a bit more of their attention on it. We've always been top down and believe that by making country and sector decisions or sort of fishing in the categories of stocks that are most likely going to do well. With that being said, we were founded back in 1979 on a bottom up fundamental process, so this top down element sits on a security selection process that goes back all the way to the late 70's.

The next few pages are really a snapshot of how the portfolio looks and from a country allocation perspective, I'd just like to thank the Board as well as Terry for allowing us the flexibility to opportunistically invest in the emerging markets, I know that was flexibility that you gave us and it certainly paid off within your portfolio and I'll be able to talk a little bit more about your performance. This is a category of the world that we're very excited about right now and think that a lot of the fears that you hear about in the press and a lot of the risks that are at the forefront of most investment conversations these days are tied to the U.S. consumer and the slow down in the U.S. consumer, but we're most excited about the emerging market consumer and that for so many years, 10, 20 years ago, the U.S. catches a cold and the rest of the world gets pneumonia, well I'm prepared to talk a little about how that has changed and why the contribution of the U.S. consumer isn't what it used to be.

On page 6, this will give you a sense of the success that we had in the portfolio particularly last year. If I could just take a step back and if you can recall those dark times, where people, lots of market practioners where sitting here and saying, we're heading into a great depression like scenario, things look really bad, things felt really bad. We were in the camp that we didn't anticipate a great depression like scenario, there was an extreme amount of risk aversion and so another way of thinking about that is there's a big flight to safety, that if things got really nasty, people got scared, sold off what they perceived to be the highest areas of risk and did things that made them feel more comfortable in areas that made them feel safer. An example of that would be selling out of the emerging markets and let's say owning big blue chip U.S. companies. Within a sector, that would be selling things like consumer discretionaries and information technologies and buying consumer staples or healthcare or things that are a little bit uncertain economic times.

We very deliberately changed the portfolio during that period of time to take advantage of what we believe to be the early phases of the next bull market and we did that in the first quarter of last year. Actually, with the idea of, we can't time the bottom perfectly and we never said we could, but we knew we were somewhere at the bottom of the bare market and we're posturing the portfolio really to take advantage of what we foresaw the next 12 to 18 months. So that decision is, we increased your weights within the portfolio to things like information technology and consumer discretion. Areas of the market that were just drastically sold off and people, not to over simplify, but really freaked out and sold valuations and the opportunities were just really too good to pass up. While we were saying this is probably the biggest and worse bare market we'll ever see in our lifetime, the opportunities that we saw were the biggest and greatest that we'll probably ever see in our lifetime again.

So the portfolio looks different today than it did last time we had this conversation and part of that was tied to really taking advantage of this V shaped recovery which we were really very early on in righting about.

Another note worthy item here is we continue to be fairly pessimistic on financials, that this was a category that fits that bill that really got beat up because of the global financial crisis and we knew financials were going to rebound, but the underlying fundamentals were so poor and the regulatory environment was so uncertain to us that we felt, we have enough exposure when the market turns around that the underlying fundamentals for financials globally was enough for us to continue our underweight to financials and have maintained that underweight throughout this entire period of time.

Page 7 is quick sense of our sell disciplines, we're a very low turn over manager, so we tend to be more like a buy and hold manager, we don't really turn the portfolio quite frequently. Page 8 is a page dedicated to risk control, we think risk is very important and dedicate a lot of our resources to risk. At the bottom is more towards your organization and we believe you need to have risk controls at the portfolio level but you also need to have structure in your organization as not to be adversely impacted by poor market environment. So, we are 100% employee owned, we have no debt, so throughout difficult periods of time, we're able to from an organizational perspective, really survive a challenging environment and therefore not have to worry about things that are unrelated to the market.

Page 9 is performance, as I mentioned, I tried to update this to the most recent date as possible. So we have the year to date, we have 2009, we have 2008 and then we have since inception and then it's clearly broken out from both a gross fees perspective and a net fees perspective. As you can see for 2009 we had a very successful year for you and as I mentioned, that really stems from our decision to posture the portfolio for the assuming bull market and so we had a very successful year.

In one of the questions that Diana asked me to address in this meeting was, how did the portfolio fair during these volatile times. You think of this crisis and you think of it ending in early 2009 and really starting in 2007, but we've tended to navigate the portfolio fairly well, our returns are certainly really good last year and over the entire

time period on a peer group comparison, pretty good. We're very confident that we're in a period of time where we should continue to achieve above average returns for you.

Terry Dennison: With respect to the year to date, if we simplify things and break the portfolio returns into 3 components, developed market, emerging market and currency, approximately or just on a relative basis, what are the major components of that kind of zero-ish return? Chris Davis: For the index? Terry Dennison: For you and the index. Chris Davis: Ok. Emerging markets have lagged at developed world through March 12. Our performance is a little bit different in your case, we're actually doing from a composite standpoint where we're beating the benchmark this year as you know, there was a pretty major withdrawal you made earlier on and that caused a bit of a drag on performance. In terms of currency, I'd really have to get you the specifics on each individual country because it's been, from a developed perspective, has it been a good thing or a bad thing to own international, it's been flat, the U.S. markets have been up and the dollar has...Asian currencies have done fairly well, the dollar has suffered as of recently as there's been a little bit more stability, so I don't know the exact proportion of that return.

Terry Dennison: If we were in a period where the dollar, not necessarily because it's strong and reflecting a strong U.S. economy, but a rather weakness elsewhere, particularly the euro and the pound, how do you think about currency in your process, do you ever hedge, is it simply a component of the stock selection decision, what do you think about currency because there was such a long period was weakening, but now at least temporarily, there seems to be a bit of a trend of strengthening, particularly versus the euro? Chris Davis: I think it's a conversation we had a lot, maybe 4 or 5 years ago and certainly it makes sense to have the conversation again. Being top down and picking countries and allocating and over weighting and under weighting countries, we make a currency forecast and we have interest rate forecast, so while we don't explicitly hedge, it is incorporated in our overall decision making in terms of over weighting and under weighting in particular areas of the globe. Most of our clients, that is their preference and I would say in our long term outlook, we feel we're in the camp that over the long term that sort of nets out to be about zero and you sort of end up just paying a cost, but most of our clients if they do try to hedge, they do it through an over weight program.

Joe T. San Agustin: You made a statement that we made a withdrawal which hurt your performance, could you explain that? Chris Davis: It was about \$50 million right on the dot actually if I can recall correctly. Joe T. San Agustin: And that hurt our performance, \$50 million out of a total of \$113? Chris Davis: So what happens is, you raise money, you have cash and there's a fairly meaningful portion of the portfolio that's in cash and if the market is going up in that period of time then essentially it's holding a position that is lagging the market, it's not doing as well. Joe T. San Agustin: I'm just trying to find out because that's a judgment, an action that management called because we need the money...that effectively cut your performance? Chris Davis: It was essentially saying that, basically you had a big percentage of the portfolio that was in cash, it wasn't a result of us realizing gains or losses, it was just saying... Joe T. San Agustin: Was it a principle withdrawal? Rosalie Bordallo: It was more for us rebalancing the portfolio. Joe T. San Agustin:

And we didn't realize it was going to cost us our overall return? Terry Dennison: Mr. Chairman, it all depends on what happens in the market, why you're doing this transaction, if the market would have been going down at the time they were realizing cash, you would have benefited. Joe T. San Agustin: So it's a swap? Terry Dennison: No, it's not a swap at all. Joe T. San Agustin: We gave it to somebody else. Terry Dennison: Swap has a very technical meaning. The point is, they have to realize cash because you want to have cash, you don't want securities. If the market is going up, it hurts you because part of the portfolio is invested. If the market is going down, it helps you, but that's largely a random effect. So, you can't tell when you say, I need money or I need to deposit money, whether it will help you or hurt you, because it depends on what's going on in the market at the time, it's unknowable. Joe T. San Agustin: That impact of what we did, I can't reverse that because it's already done, but this can become kind of a lesson learned, what happened when we took money out to rebalance. Terry Dennison: It's not a lesson because there's no way to tell what's going to happen in the future. Joe T. San Agustin: Well that's what he's saying is that we lost money because of that. Terry Dennison: We lost money because the market went up at the time that they were assembling the cash. If the next time we do it the market's going down, it benefits our performance. Joe T. San Agustin: But that's not what I'm getting. By the last withdrawal, you figured it affects it, you lost money. Chris Davis: I'm sorry if I mis-communicated. Terry Dennison: This large withdrawal at exactly the time we did it because to come up with \$50 million, they have to sell things. Loss, gain, it doesn't matter, it's irrelevant, but we have to get the money to be able to give it back to Northern Trust so it can go to other managers. If the market is going up when we're doing that, it hurts us because that \$50 million is not participating in the rise. This time it hurt us, next time, it can help or it can hurt.

Dr. Leon Guerrero: I think another way of looking at this is, we have an approved allocation so what happened is, we had to rebalance it and that's what happens when you rebalance, you take from... Joe T. San Agustin: You try to minimize the risk, but this seems to be a large risk involved. Dr. Leon Guerrero: I know, but if that's what the plan calls for... Joe T. San Agustin: I hope we're able to recoup that. Dr. Leon Guerrero: So that we can stay within the guidelines, that's really what the bottom line is, we have an approved plan and you have to stay within the plan and that's just one of the things that happens when you rebalance, you take from the winner and you give it to the loser. Joe T. San Agustin: I'm just trying to minimize the risk, but when you make a statement like that, it needs to be clarified.

Chris Davis: On page 11, you asked about our perspective on the market and I'm guessing that last year when we talked, we were probably your most bullish or optimistic manager and I'm probably guessing this year, we're probably again your most bullish manager. I don't know, but I'm just guessing and that's just from my own experience. We believe that equities are very cheap, we believe that fundamentals are very strong, that global stimulus is still going to be a tailwind for the global economy, we believe there's lots of skepticism in the market, there's a tremendous amount of fear, which is a classic recipe for the market to climb the wall of worry which is very typical in the early phases of a bull market and I'll drill down into some of the specifics here. Balance sheets here are very strong, the yield curves globally are steep, that tends to be a bullish factor. This is really the first recession which

companies had the technology to monitor their inventory in real time and adjust their inventory, so it's almost when Lehman went under, it rang a bell in the market and all companies said, we're going to cut costs, we're cutting our inventories and they did it very very quickly and it exasperated the market conditions at that point in time, but also they could turn that spigot right back on pretty quickly. So we think there's a bit of an overreaction from a company perspective and just a minor uptick in growth which we've seen from virtually most recent economic data and certainly Q4 GDP in the U.S., there's going to be a tremendous amount of upside surprise for the markets.

If I could skip a page to page 14, I think this is really important. Page 14 is a chart of the U.S. economy and the light green bar there that's personal spending; lots of people don't fully appreciate how stable the consumer is. You hear this fear about the U.S. consumer, but lots of people don't really understand that the biggest components of consumption are things that we need. Rent is a huge allocation, where we live, toothpaste, consumer staples, healthcare, that the discretionary component of consumption is actually fairly small and so there's not a tremendous amount of volatility. If you look at this chart you could say, the personal spending didn't fall off a cliff you would believe, certainly if you watch the financial press, but this business spending, that dark green bar there, really fell off a cliff. I mentioned that real time inventory where companies just cut costs dramatically, that was a component overall growth particularly in the U.S. that drastically slowed down. So from our perspective we're saying, for the economy to turn the corner, you wouldn't exactly expect the U.S. consumer to drive us out of this, you would expect businesses to drive us out, because that spending limit, there's a low volatility there. As you see this increase in business expenditures, that's going to really drive growth in our opinion and not consumers.

Terry Dennison: If we go back to the pre-crash period, there was a general understanding that consumer spending was 70% of GDP and none of these lines add up to anything resembling that. The personal spending, if that's in billions, that's kind of a side show, I mean, I don't understand the scale. Chris Davis: If you could just flip the page, I think that could answer your question. This breaks it apart, so this shows you total decline in GDP was 3.8%, that light green bar, so this scales the contributions. As Terry mentioned, ok great, it's not highly volatile, it didn't fall off a cliff, but certainly a minor change has a big impact because it's such a big overall component of GDP. So, what you see here is this is the contribution to decline so that very center where you see personal consumption of -1.2%, that was the overall contribution towards that big decline in the U.S. GDP, but again if you could focus really on a business investment, that's really what made up the bulk of the slow down. That really surprises a lot of people because you hear in the press that the housing ATM machine dried up and U.S. consumers is dead and there's going to be a tremendous amount of de-leveraging, but it actually wasn't a huge impact in the slow down in our economy.

Terry Dennison: These 2 data series on page 14, one is called business fixed investments and the other is called business investment, are they in the same data series? Chris Davis: That's right. Terry Dennison: Because business inventories wouldn't be in business fixed investments. Chris Davis: That's right. Terry Dennison: So you attributed a lot of this to rundowns and pipelines and just in time



production and just enough inventory, but that's not fixed investment? Chris Davis: Yes. Certainly you had, on top of companies that were slowing down dramatically, they certainly weren't going out and buying new machinery, they weren't buying new plants and that abrupt slow down as a result of slow growth was a big contributor. Terry Dennison: And what are the low levels of capacity utilization, what's going to make that change? Chris Davis: We think the low levels of cap utilization is a good sign of another fear that's overlaid of inflation, but again going back to, and this the U.S. just because it's a major fear, going back to the growth of the emerging market consumer, in the increasing consumption from the emerging markets, that is really going to drive demand for more goods and is going to fuel really the opportunity for companies to invest. We're sitting at a period of time where corporate balance sheets, ex financials are sitting on a historically high levels of cash and rates are very low, so they're either going to buy back their own stock, which is bullish, or they're going to increase business investment or fixed investment capital goods tied to that figure.

Terry Dennison: I'm not in my mind making the connection. If we're very low levels, relatively low levels of utilization of productive assets, because they took all the high cost assets offline and banked a lot of the higher cost, why are they going to spend it on this, they don't need to. In fact, they can increase earnings dramatically by not doing it and they can also pay dividends as opposed to share buy backs or sitting on the cash which is earning them nothing. I don't see how this number reverses. Chris Davis: Right and I think your point is basically is, if your factory is operating at 10%, you're not going to build a new factory because you got a lot more room to crank out a lot more widgets because you already have the capacity to do so and that's a great point. I think what works when we look at this as a fear and we break this apart, lots of what we do is try to focus on areas that the market is really overly concerned about and dispel them and try to take that as an opportunity to implement it within the portfolio. So business investment down by 3.5%, it doesn't need to go up back by 3.5%, you don't need to see a huge shift in that to see GDP growth. For example, 4<sup>th</sup> quarter of this year, right, the revised figure was 5.9%. Joe T. San Agustin: How is this conversation related to your --- is that a contributing factor --- why we're losing investments, because there's no --- but you still have personal spending. The consumer is shifting to imports rather than local which contributes to why businesses don't have the customers anymore. Chris Davis: In the U.S. we tend to import more than we export, definitely when our dollar appreciated that gave us a little benefit of buying things more so in the past at a relatively cheaper rate. In often times, growth comes before unemployment, not the other way around, unemployment is a lagging indicator not a sort of future bell of... Joe T. San Agustin: This is a fixed investment -- - industry ---, and that's covered by that decline --- increasing import to meet the demand, if people don't have jobs, that spending should go down. Chris Davis: That's right and we look at it from your perspective and how you allocate your assets, from an international standpoint, we manage an international mandate for you and even U.S. companies drive lots of their revenue from abroad which... globalization has certainly provided a better opportunity for U.S. companies to tap consumers outside of the U.S.

Dr. Leon Guerrero: Do you have the dollar amount of these, you only have percentages? I'm having trouble with these figures. Chris Davis: I did not put the

dollar amount. This just takes your account irrespective of the dollar amount, so as Mr. Chairman mentioned before, over \$100 million and now we're about \$80 million that we're currently managing, but this just takes a look at it from our performance in both absolute and relative terms. Dr. Leon Guerrero: According to Mercer's report on December 31st 2009, the market value of your portfolio is \$138.9 million. Looking at our figure here, the market value as of March 22<sup>nd</sup> 2010, it's \$84 million and I think this might be taking into consideration the withdrawal, but if you take the \$50 million off, it still doesn't match. I think last time we had a discussion about your company getting into other ventures. Chris Davis: Terry and Mercer asked us to address that. We were in a position that we were acquiring other companies because we had a lot of cash and thought it was a good opportunity, but we have since stopped that, in the last meeting we gave you an update. We also addressed writing books which we continue to do, our most recent book was tied to emerging markets, but Ken Fisher has written books since he started the firm, his dad wrote books, he was a famous investor as well and believed that educating the public is part of our DNA. Joe T. San Agustin: You do investment books, are they in circulation? I'd like to see what you have. Chris Davis: I can send some over. Terry Dennison: Are the books all written by Ken or are the ghost written by other people? Chris Davis: Ken's most recent book he wrote "Only 3 Questions That Count" that was written by Ken with some help from our staff. The most recent books were guides, there were sector guides and county guides, we wrote a book about energy, we wrote a book about emerging markets, we wrote a book about the sector consumer staples and as you can imagine, having done lots of research in there, it's more just accumulating more research and putting it in a book format. Ken doesn't write those books, those are really ghost written. Terry Dennison: Having written 25 pages of things I know all about, I know how long it takes to do that and not just sit down over a weekend and bang it out. How much time does it take for the analyst to work on these books and is this a distraction from what they're primarily there to do? Chris Davis: Well I don't think so, we don't believe that, the analyst who helped write the energy book was our energy analyst, so the process of writing the book has actually been a great thing for our employees, they take a lot of satisfaction in it and it's nice for an analyst at the firm to put out a book with his or her name on it. Terry Dennison: So just getting back to the amount of time they spend, is it like 10% of the year, 20%? Chris Davis: I don't know the percentage, but it's pretty low. We have an entire content team outside of our research group that all they do is write, so the analysts would come up with something raw and then a content team that's completely outside of our research group, is in charge of making it readable. I'm happy to send all of them to you, we've actually gotten great feedback.

What we did for the acquisitions, we bought very small independent brokerage firms that it was sole..., we had 100 clients, \$500 million in assets, we could buy it for however much money we thought was fair and then we would put their clients within our retail platform very easy and if the client said, this isn't going to fit, we didn't take on the client. So they came either directly to our platform or they didn't.

Wilfred Aflague: I noticed on your client list under Sovereign Government, is that by design or did you go specifically for these island countries and territories of the U.S.? Chris Davis: It wasn't really by design, I think it was...we're very proud of all of our

relationships and it wasn't like we were trying to target areas, there wasn't a specific appeal and as you imagine, the familiarity of our firm, as you get relationships in certain areas...

Dr. Leon Guerrero: Do any of the regulatory agencies have issues with you: Chris Davis: No. Rosalie Bordallo: You're not in litigation or anything of that nature? Chris Davis: No. Rosalie Bordallo: Any firm changes: Chris Davis: Same people, same process.  
(End of Presentation by Fisher Investments)

### **Dimensional Fund Advisors (Non US Equity Small Cap)**

Kevin Hight: One of the areas that you asked us to talk about was the general market environments and I brought a slide I used in our last discussion a year ago and also updated with the current, with the 3 globes on it). The first one being what the market environment was like back in the end of February last year, obviously it's a decidedly different environment than it has been for the last 12 months. We were looking at a period of time, end of February where you're seeing anywhere from 30-60%, 75...small declines in the market place, basically upsetting their balance and reminding people that there really is risk in the equity markets, something that I think a lot of investors have forgotten. The following page is updated through February 28, 2010, I think it's reflective of what we've talked about many times in these past meetings and the importance of staying dedicated to the long term strategic allocations, you can see how quickly these numbers have come back as well. We're about even from where we were. A lot of these returns, particularly emerging markets, which this portfolio is not invested in, but you can see we had days in the spring of last year where we had 5 and 6% gains in a single day, I think just reflective of how quickly it is and how important it is to stay strategic in the asset allocation.

With that I'll step back to page 2 for the agenda, you asked us to share some perspectives that we had on the market context. Based on my math, the allocation that you hold in place with us is about 3% of the plan, that's just a rough approximation based on the information you put out on your website and what I know to be in the account. The following 2 pages, we described just how quickly the market changes and really reminding people that there is risk in the market place. One of the questions I recall from last year was what should we do now, should we stick to the position and what we like to remind clients after you experience that horrible down turn that we all went through is that's the payment of the risk. Right at the core of Dimensional's philosophy is very simple, risk and return are related and far too frequently people forget that and think that there isn't a risk aspect to it, but we think it's critically important.

Just to recap for those who weren't at the meeting last week and just to remind people about Dimensional, investment management is our sole business, (this is all on page 4) we're independently owned, primarily by employees and directors. We have trading offices in Austin, Santa Monica, London and Sydney and we've been doing what we do which is providing asset class returns for more than 25 years. We take a very

scientific approach, it's very much based on academic theories that we think is well tested, we're not trying to time the market or make fundamental strategic or tactical bets and we think our track record is there to support that. The firm just like the market place has had it's ups and downs over the last few years, in the last few years we've gone through that \$100 billion mark a couple of times and in early 2008 we were at about \$160 billion, we dropped all the way down to \$85 billion and then had come back to currently about \$172 billion, \$165 billion as of the year end. One of the fortunate things about our approach in our client base is throughout the down turn, we continue to see that positive cash flow with all of our clients.

At the core of Dimensional's equity philosophy is trying to capture systemic risks, factors that really drive long term returns rather than trying to forecast where we think the market's going. We try to construct our portfolio to capture size and value premium and of course the basic equity market premium as well and page 7 is a way to sort of think about that aspect. We think this is a good framework for thinking about general portfolio allocations as well. If you want to enhance your expected returns that you need to provide, seek out areas of the market that provide them, but they come with a certain level of risk. For example, in the case of this strategy, the international small company, it's a broad market, we're not taking a perspective necessarily on value versus growth stocks, but have tilted the portfolio to allow you as the client to take some of that small cap premium that we believe exists in the market place and incorporate it into your portfolio's allocation.

Page 8 is a chart that we've seen many times, we think over long periods of time that the data is available that these premiums do pay off and that exposure to small cap stocks and emerging stocks can in fact have a realized return and not just an expected return. The area most particular for this portfolio's concern is the green set of columns. These are index returns.

Page 9 is a way to look at this in the type of exposure that we're really trying to believe, a big comparison to what we do and what an index provider does. We're trying to provide you the client the exposure, in the best way we can define it, the complete asset class. The ---on the other hand have lots of great positives to them but they're also replicable and so they frequently cannot go down as small as we can. What these 2 charts show over long periods of time and these do move up and down, that there's a monotonic effect to small cap stocks, that the smaller you go, the higher the long term expected return is. The added benefit is our squares correlation are relative to each of those deciles as we step down and go smaller and smaller actually decreases to getting a diversification benefit and not just in terms of a number of names, but in terms of potential impact on the broader portfolio.

The value and size effects we talked about, they do move around. On the next 2 pages show them on an annual basis and also on a rolling basis and I think you can see in a couple of different areas how quickly they can move around. We showed you the U.S. international just to get some perspective on it, but you can see in many circumstances those bars can shift quite dramatically and these are calendar year numbers so if you were to look at it on an even shorter period of time over a rolling

period, you can see a significant impact, the size effect has really come back and gain -- since last March, the 12 months ending that was also quite negative.

Page 11 shows that on a 5 year rolling basis, I think that's informative but can also be a bit misleading, in that it looks a little bit more of a cyclical aspect than it really is. I think what we saw on the previous pages that it could move around pretty quickly even if there does appear to be a pattern in there, trying to predict from that pattern can turn around and impact is a risky proposition.

Page 12, again this is another reminder of why you want to be in an international small cap strategy. Not only does it provide hopefully a higher expected return, but also as a good diversifier when you compare it to a U.S. based perspective, a little less so if you're comparing it to other international stocks, but generally has a really low  $R^2$ .

To move on to how Dimensional operates, page 13 is just to give you a summary of the graphical view of how we look at ourselves. There really is very much of a team based environment, our investment committee has the ultimate responsibility for all portfolios at Dimensional. Supporting that effort is our portfolio management team, or trading team and of course our research. As I've said before, research at Dimensional is not about finding fundamental stock picks that we think as an organization will out perform the market, but really is reviewing an enormous volume of quantitative data looking at market movements, looking at doing academic research projects and trying to find ways to adjust what we do in the market place to enhance our process. I'll give you an example, one of the projects that we're currently working on what Dimensional called the tick data project and what we've done is we've taken every trade that Dimensional's done in the last 3 years and this is basically as much as we could get at the time and what we did was, obviously we had our own trade information, but we also asked our brokers to provide all of the information on the fills on the other side of the equation. So if we're buying 10,000 shares of a particular company, we want to know about all the underlying trades because there might be 10 1,000 trades on the other side that matched and we got the trade data from both of those and we actually went out and bought the entire tick data base for our entire universe and so there's about 13,000 in the universe and every single tick that occurred during this entire period of time, this is data that is so large that it's actually shipped out on hard drives, you can't ship them on disk because it's not big enough and we've run a whole series of experiments looking at how we traded in the market place versus what if we traded in a different way, if there were different ways of providing liquidity to the market place, could that have enhanced our trading. We're still fairly early in the project but it's very encouraging from our perspective, but that's the kind of research that we'll do, highly quantitative with large amounts of data but again, we're trying to find ways of enhancing the portfolio.

Compliance is that last blue box on the bottom, which really sits outside of the process intending to monitor it up and down and up and down and sideways and crossways, however they can.

From a functional standpoint, page 14 gets into details about who some of the individuals are. Our investment policy is our group of folks who get together on a periodic basis and think about how we can improve our portfolios and also view things like changes and country issues. For example Israel, Israel is a country that's in the process in an MSCI environment moving from an emerging market country to a developed market country. If we find that is something that we think is consistent with our client base what they would want as well it's the investment policy committee that's been in the discussion of how we would go about doing that and at what time do we want to implement such a strategy. In fact, we are going to be moving Israel into our developed market strategies and that's something that's going to be taking place later this year. The investment committee as I said, has the ultimate responsibility for all our portfolios, our portfolio management team has to report into the committee, they meet at least twice a month or more frequently if market circumstances require. The portfolio management team is a large group of folks who really work cohesively in managing our strategy. The way that we implement our strategies is more along the lines of a construction project rather a pay star, we're not looking for people to hit the ball out of the ball park, but we really take our strategies and execute them in a very refined way with consistency being so critical. We think we have enormously talented people, but it's not a star system.

In terms of actually getting into the process, page 16 is just a visual on how we go about, it's an exclusionary process rather than an inclusionary process. By that, we start with a framework of, we want to buy everything as we define in the asset class in that market place unless they're reasons not to do it. Obviously very different from a traditionally active portfolio where you may be picking 60, 80, 100 stocks that you think are the ones that are going to outperform. We'll start with that and make our definitions in terms of what we think are the asset class and then look at a whole other series of what are quantitative and qualitative factors that we think could impact and that includes things that we don't think perform like the asset class we exclude REITs for example for most of our equity strategies, not because we don't REITs are a good investment, we think they operate differently, if you want an investment in real estate or REITs, you should do that separately.

For us to look at momentum is a big factor in terms of, we're looking at it in a relative basis, basically our momentum screens are designed to slow down our trading process either from slowing up our selling securities because they have an upward momentum and continue to perform well and to slow down our buying if they on a relative basis are underperforming. We don't think you can necessarily create a true trading strategy to play up from one to the other, but we think it can help on a relative performance basis in that regard.

Page 17 gets into what particular investments could do all around. We invest in the international small company, we're trying to capture the entire non-U.S. developed market small cap asset class. The strategy is currently using a funded fund structure, that is a result of, after we launched our Japanese and our U.K. strategies back in the mid 1980s and it was rolled out to other Europeans, it just made sense to roll them all together. Dr. Leon Guerrero: The process involved in this, how do you go about investing in Japan, how does the money go from you to the company? Kevin Hight:

What we're buying are publicly listed companies. Dr. Leon Guerrero: Are these companies listed in the New York Stock Exchange? Ken Hight: We do have the ability to use ADRs and so a foreign company will be listed in London or in your case, New York, but primarily we like to invest in the local markets and we do that in a couple of different ways, we use a lot of local brokers, but increasingly we can also do a lot of the trading ourselves. Let me give you an example, if a client were to give us \$50 million and we want to invest it in this strategy, we first make the regional allocation based on which vehicles they are and then our traders will implement --- both by providing orders out into the market place to brokers and also trading it ourselves and we now do about 80% of our trading ourselves, we use relatively few outside brokers and they'll go out into the market place and look for trading opportunities and they will go out within a broad range of those names. So in the case of international small, we may have 400 securities in Japan for are eligible for purchase. Portfolio managers look at which securities in the portfolio are underweight relative to target, they will also look in terms to what's going on in those particular securities, whether or not there is a period of negative momentum and whether or not that should impact how we should invest. Other than that, there will be new screens of new companies whether or not they were in distress and other factors and then they will take that 400 names of Japanese securities and maybe 100 of them are eligible at a particular moment in time. So we're taking that \$50 million and a quarter of it's going to be in Japan and looking to place orders across potentially --- stocks, since we're not an index manager, we're not trying to get to a particular weight, those are just what are eligible for us to buy. Dr. Leon Guerrero: We're interested in the flow of money. Kevin Hight: It will simply be that we will be going out buying securities and it's delivery versus payment system, so we go out and put \$50 million to work, that money would flow from our custodian through the broker dealer whose involved, it can go through a variety of different ways, there's a lot of trading mechanisms, a lot of our trading would go through ---, it's a global broker, we will trade through their platform, there will be an exchange, there's a clearing house on the other side of the, basically between the broker, where all the brokers get pulled to ---- in the United States. Dr. Leon Guerrero: This broker in Japan, does he have any, is there any restrictions in terms of what he can and cannot do by the Japanese Government or the U.S. Government? Kevin Hight: Yes and we will review every one of the brokers that we will trade with, if we're going to trade, we're not going to do the trading ourselves, we're using a clearing broker. If we're using an actual 3<sup>rd</sup> party broker, we'll do a formal review and we review that on an annual basis, the strength of their brokerage house in terms of what their capital levels are, who else they trade with, but we look for broker diversification as well and these are all highly regulated brokers. That's also why we tend to only trade on the major exchanges. Most markets have multiple exchanges, we'll only actually trade for securities and through brokerage houses on the primary exchanges just because it's a higher level of security. All the trading that we do and this is delivery versus payment, they have to give us the stocks in exchange for cash and similarly when we want the cash, we'll deliver the stocks and they deliver the cash, it's a simultaneous transaction. The money would go from the client into the market place and back again. The client will wire money from their bank to PNC who is our custodian, we would be made of aware of what the cash balances are because most Dimensional's strategies are commingled, so we'd be pulling all together that cash, having what are available cash is, we have X amount of dollars that we can

invest, portfolio managers will buy a program and instruct the traders on how much they want put to work, the traders will implement it through a combination of various trading venues, in some cases we will give instructions to 3<sup>rd</sup> party brokers to implement on a set amount of money we want put to work, other parts we'll do ourselves basically throughout the day, working down that number until we get the targets we want. In the market place those orders are being executed same day it's delivery versus payments, the money is being wired out, exchange for the securities which are being booked at our custodian, the cash is being transferred from the custodian to the 3<sup>rd</sup> party. Dr. Leon Guerrero: That broker in Japan is being regulated by the Japanese Government? Ken Hight: Correct. Dr. Leon Guerrero: Do they have any obligation to the U.S. Government, do they have a license? Ken Hight: Frequently many of them do, all the major Japanese brokerage houses, they're going to have operations in both locations, but we also use a lot of local Japanese brokers. Dr. Leon Guerrero: The reason why I'm asking is we deal with our Legislature, when you're investing in a foreign country, how do I know the Retirement Fund is being protected? Ken Hight: At the end of the day the assets that you are invested in are held in a 3<sup>rd</sup> party custodian, so we never touch the money. The risk that you face in the market season on the other side of, not being able to extract the stocks if you needed to collectively get the money back. Dr. Leon Guerrero: Do you have an agreement with the Japanese Government and the U.S. Government about this kind of relationship? Ken Hight: What the regulatory relationship between the U.S. and the Japanese, I don't know, but I could look into it, but in general what we look to is that there is an agreement within the market place and the market itself, the exchanges in brokerage houses are operating in a developed market in a liquidity aspect, meaning that they're flowing and freely trading with the use of the --- system, that there's centralized clearing, that it all is in a regulated environment. Our confidence is high enough that we think we can get the money in effectively and that we can get money out effectively. We do this for emerging markets for example, which for our investment in this portfolio, we have a similar kind of process and we actually can trade 2 different ways and you can do this to some extent in the U.S. as well, you can trade locally or you can trade through ADRs and GDRs. The ADRs and GDRs can be a slightly higher level of comfort in terms of basic mechanics of the exchange. If there's a fundamental breakdown in the economic system in those other countries, then that's a potential risk, we think it's a very slight risk but it is in any market, you can have an environment where the U.S. just stops the trading and you wouldn't be able to get your money out until the market basically restored itself. The confidence level we have with the market is that the market will continue to function, prices may go up or down based on factors within the local market, but we don't think that there's going to be a fundamental collapse of that system and money will just stop moving across through the system.

Dr. Leon Guerrero: I think people will talk about how in India their structure is improving through these kinds of transactions, what is improving there? Ken Hight: A lot of the tax rules are improving in India, they're no longer as punitive to foreign investors as they use to be. We think that there's lots of examples of other countries that we think are improving, Russia is a country that we think has weathered the financial crisis, the markets did not cease, so that's been a country that we've been quite concerned about whether or not the market environment would operate in such



a negative period of time. They've gone through political turmoil, they've gone through the same economic turmoil the rest of the world has and the market's continued to operate. So our comfort level is moving up but we still don't invest locally in Russia, because we're still not confident that our clients and us as our proxy have the capital production that we think is important to be able to extract money. Similarly with China, we don't invest in China, we invest solely in Hong Kong. Dr. Leon Guerrero: So you basically rely on the laws of the country that you're investing in? Ken Hight: Yes. Dr. Leon Guerrero: And you feel confident that there's confidence in that system, the law, that's where they get the green light? Ken Hight: Correct. We spend a lot more time with it on emerging markets because of the level of risk that's concerned, but when you look at all of the countries that we trade in and we even continue to look at the brokerages, the exchanges that we trade on, we make sure that we meet our confidence level in the market environment. --- We do look at it on a country basis, we do look at what the capital laws are and as well as the exchanges. Our process when we want to add a new country that we're going to be trading in is to not only --- but actually to go visit the country to make sure we --- regulators and we've seen how the market operates and we have that in an efficient market.

Back on page 18, what we're trying to do, the general perspective from our clients is that they're trying to look at investing in international small stocks is to get an investment that balances off --- typical investment which is being to large cap space, either they're doing that because they don't have that investment and want to cover the asset class or they want to tilt the portfolio to those factors that we talked about. So our strategy is designed to work in that context.

Page 19 gives you an example just from one country of what we're trying to do. We'll look at all of the countries within the eligible space and we'll divide it by country level and region and what we're trying to target is the smallest 10-15% of stocks. We think that everything above that really functions much more like a large cap stock. We'll use a number of names approach, in this case Australia has a number of names, which is periodically reset and ---reduces the portfolio turn over. From that name, we're looking at about 366 in Australia's case, of eligible securities. When I mentioned earlier about the index being replicable, most indices, although there has been some micro ones that have come out, usually they stop at a --- that's quite a bit higher, I believe the MSCI is typically around 250 million, so we're looking at companies that go down significantly smaller. Going back earlier to the monotonic chart, we think that's where a lot of the bang for the buck is. We then apply a whole series of additional screens on top of that, those are quantitative screens and there are other kinds of screens, we mentioned the asset class concerns like REITs. We also take out things that we think are pricing and trading issues, we don't think that IPOs tend to perform well so we want to make sure they're seasoned and certainly any company that's been D-listed, doesn't necessarily mean we'll sell it, but we certainly won't buy anymore. Also if there's sufficient liquidity and liquidity could be measured at the exchange basis particularly more in the emerging markets, but in developed markets as well and whether or not the individual security is trading. We want to make sure there's enough liquidity that we could move money in and out, more importantly out at the right time.

On page 21, at the end of the trading day and this is just a snapshot as of 12/31/09, you end up with a portfolio very broadly diversified, 4,200 securities, more than the MSCI EAFE index. That is really a function of the fact that we go much smaller, as you would expect, if you go smaller and smaller in the market cap number of names goes up and we want to be able to own all of those in time. (I'll show you a slide in a couple of minutes that talks about why that's so important in why we trade, it gives us a lot of flexibility when it comes to trading.) And a couple of meaningful statistics, the median market cap, \$277 million versus \$610 million, again just the fact that we're going so much smaller, we're still holding a broad range of small cap stocks, but our ability to go smaller means that the median is going to drop.

Sector weights are really just in there as an FYI. We really don't target any kind of sector weight in our portfolio, we think that there's a natural sector rotation by buying small stocks. We do put limitations on how much of a sector you can own, but other than that, it's a residual.

Page 24 talks a little bit about trading, this is just reflective of a sampling of the bid/ask spreads across different size ranges of companies, so going from fairly liquid stocks to ones that are quite illiquid. You can see that the spreads can be quite wide and these are for retail spreads, so these are maybe putting 100 stocks to work not putting \$100 million to work. If you look at the total trade volume and the smaller the market, there's not a lot of trade volume, so you need to be able to have a lot of flexibility, a lot of focus on costs, otherwise, you're going to basically eat up all your potential for returns through poor trading.

Page 25 is just to give you a graphically idea of the kind of process that we go through when we're thinking about putting those dollars to work in any country. We'll look at the \$50 million that we own to put to work and we'll actually create a buy list that in terms of dollar --- that is larger, if you want to put \$20 million to work, our traders can go out and basically show offers for up to \$40 million. They're not going to take all of those, but by having lots of different flexibility, we can wait for people who are anxious to sell to cross the spread and basically give that to us. So that 3% number, if we sit patiently on the --- because any given day, we're ambivalent whether or not we buy stock A or stock B because by the end of next week, we'll own them both. We can sit there and wait for the sellers to come to us, we pick up effectively that spread, there's a reduction in the total cost and that just gives us a lot of flexibility, so we can sit patiently waiting for all those potential offers to come in. Additionally because we have such a large number of names, we can sit with a lot of, our target weight for a particular stock, maybe it's 5,000 versus 10,000 shares, we can sit patiently waiting to slowly build up that piece just by doing small orders, each of the sellers would come to us and just because it's a lot of flexibility.

We're seeing in the project I mentioned earlier, the Tick Data, we're seeing that being there being a liquidity provider, being the company, especially when it comes to small stocks, other brokers, other investment managers have to come to, really is a significant advantage to us. At worst we are trading in line with the rest of the market place and perhaps giving, in some cases the numbers --- we're adding value back --- order of 70-80 basis points.

The thing that ultimately drives everything is performance, so the next 2 pages are the time periods that you specifically requested. On page 26 is performance as of February 28, 2010 and fortunately March is looking very good for us. If you look at that one year, the number why you didn't want to get away from strategic allocation number, coming back with 66% return, that kind of number is what makes the long term numbers look more palatable. You can see across the bottom line are relative numbers held up reasonably well. We underperformed a little just because the market index provided did such a bad job, not that it was intentional, but over long periods of time, we continue to perform.

Page 27 is as of September 30<sup>th</sup> which I believe is your fiscal year. The relative number obviously we're less than enthusiastic about it, but we still think the absolute number is good. So far for March the markets are up, the small cap markets are up about 5.5% and I think we're up about 6%. That is really sort of the conclusion of my formal comments.

Dr. Leon Guerrero: Tell us about your new CEO. Kevin Hight: In January of this year, Eduardo Repeto? Who had been our Chief Investment Officer, was appointed to our Co-CEO. There are a couple of very valuable assets, it provides a more solid framework all around the long term succession plan in our organization. David Booth who founded the company back in 1981 continues to be acting as the other Co-CEO, but they sense over time that we need to make sure his role, --- built in the infrastructure that he be able to continue to manage the firm without any kind of ---. This kind of co-sharing is actually something that is not new to Dimensional, the first 25 years of Dimensional, our co-founders we Co-Chairman, so Rex ---- and David Booth ran the company jointly. When Rex retired, we continued to explore how exactly we wanted it to be structured. Eduardo is a brilliant guy, probably the smartest guy I've ever met, whose actually his roots are in aeronautic engineering, he was doing his post grad work at Cal Poly Tech when we discovered him about 10 years ago and really what we were looking to find was someone who both the interest in markets but also the quantitative --- to do some really complicated things --- on a trading --- and Eduardo has really stepped into that role and has been off like a rocket ship. He was appointed to head of our research group, I believe it was 6 years ago, he became Chief Investment Officer 3 years ago and CEO this year. We think that's a positive step in terms of our continued build up of succession plan for the organization.

Related to that in some degree was back in December of the previous year when we opened our Austin office, one of the fundamental reasons we opened the office was to make sure we had 2 full service trading floors in the United States because so much of our business is either coordinated through or run through the United States and that gives us --- full capability. We actually have the ability to pass or trade --- in London to Austin or Los Angeles to Sydney so we have 24 hour capability and we --- with the infrastructure and Austin is a big part of that.

Other than that, there have been very moderate personnel changes. Andrew --- who headed our Sydney office as the senior trading officer has moved to London and

become Chairman of our London office, but other than that it's been relatively modest. We were actually fortunate through that period of time, the down turn, that we didn't face a situation where we had to lay off employees, in fact we have gone back into growth mode, we have hired and we're about 460 worldwide and we probably added close to 20 people just this year who are involved in trading and client service functions.

Joe T. San Agustin: Can we go back to page 26. I noticed the index is net dividends, on our portfolio side, is that also net dividends? Kevin Hight: I think that sometimes causes confusion. The MSCI calculates their indices in several ways. The net dividends, you'll see it as price, gross dividends and net dividends.... Joe T. San Agustin: I'm just trying to compare the 2 columns. Kevin Hight: The impact of dividends or the withholding taxes on the portfolio is included into the... Joe T. San Agustin: Are the 2 columns both net dividends? Kevin Hight: Yes, by regulation the net dividends that are paid out in foreign markets, they require withholding rates, that's a realized number, there's nothing you can do about that, you can do some kind of tax reclaim. Joe T. San Agustin: The 2 columns should both be named net dividends so I can understand this and it's clear to me. Kevin Hight: In Dimensional, if you go back in time, none of the indices show true net numbers, so for example, the international, the EAFE Small Cap was launched well after we launched our international small cap strategy, they never went back and back filled... Joe T. San Agustin: What is our dividend statistic on this one, what is our dividend rate, what is the gross, let's put it that way? Kevin Hight: I would have to calculate that, it's not something we've been typically asked about, but I can tell you off hand that you received from distributions from the fund, about just shy of \$3 million in distributions. Joe T. San Agustin: What would that be in terms of percentage rate, rate of return? Kevin Hight: The \$3 million is what has been paid out from the fund, but that's a different dividend number than what's been appropriated... Joe T. San Agustin: I'm just trying to figure out, I gave you \$38 million, what are we making? Kevin Hight: You're making money from the performance of the --- price of the stocks. Joe T. San Agustin: I invested \$100, what am I making, 10%? In this \$38 million dollar investment, what did I make out of my investment? Kevin Hight: If you go back to page 21, if you take the weighted average dividend of all the --- securities in the portfolio, if you take the dividend rates times the weight in the portfolio of all the securities that have versus what's in the index, this is the weighted average dividend. So on average, securities in the portfolio pay out about 2.3% (2.28%) in terms of income. Additionally from that, in a realized environment, you would actually take away a portion from that number because there's a required withholding at the country level. Joe T. San Agustin: I'm making less than the index, my return is less. Kevin Hight: You're getting a lower dividend, but we think the equity price that you're going to get, that's really where the difference is. When you get down to the very small end of the market place where a lot of the stocks we're buying are, frequently those stocks do not pay dividends, that's true in all markets. Joe T. San Agustin: Yes but I get capital gains. Kevin Hight: Right, but capital gains are just what are realized in the performance numbers. Joe T. San Agustin: I know what you're talking about, I'm more interested in, if I'm investing so much money, what am I getting. Kevin Hight: That's really what the performance numbers on page 26 and 27 are trying to explain, it is a daily value portfolio so you can take money the money whenever you choose, so

you've realized a period of time when you've been up about 66%. Since inception, the last column, the numbers are negative, it's less but it's a couple of hundred basis points ahead of the index, you're better off with our strategy versus the index and I think you'll see it over a long time, it will continue to get paid off in terms of that premium being captured. Joe T. San Agustin: I don't understand. I'm here to make money, not lose money, this doesn't seem favorable to us. Kevin Hight: That's certainly our objective. The fundamental concept of the capital structure, there's a risk associated with it and there's going to be periods when it declines. Joe T. San Agustin: If I have to get rid of \$38 million, what would be my capital loss? Kevin Hight: You wouldn't have a capital loss if you were to get rid of it. You've given us about \$40 million and as of last night, the portfolio was at \$40,975,000. You started out giving us \$34 million, dividends are paid out to you.

Terry Dennison: I have a question, one thing we don't have in our asset allocation is emerging markets small cap, which you do have a fund for, but it just happens that I don't want to look at performance because it will look very attractive, what in your mind are the merits of adding that as an asset class? Kevin Hight: The base line from a Dimensional perspective is that you should try to own the entire market and that there are risk factors built into the premium associated with that. The fact that you don't have that exposure to that asset class, basically is a potential drag on you being able to capture the entire equity premium, particularly the premium for emerging market stocks. With that being said, I think that from that perspective alone, trying to capture the emerging markets small just provides a well rounded starting point to having exposure across the entire equity market place. To the extent that you had an increased appetite, you could over weight and try to capture that on premium and the numbers right now are very high, but we also came out quite low from last year. You want to make sure that if you're doing it, you're doing it from a strategic aspect and not simply chasing return numbers. If you buy off on the concept as we do that your starting point from an equity allocation might be the only market place and then try to balance your portfolios exposure based on the long term expected return and your tolerance for risk. It makes a lot of sense having an allocation to that, roughly proportional to the market weight. Terry Dennison: What would that proportion be right now? Kevin Hight: Emerging markets right now I think is about 11 or 12% and with emerging small with the way we structure the portfolio just like our other strategies is trying to capture the bottom 10%, so you're looking at about a 1-2% allocation for your equity market. Certainly one of the advantages we've seen other clients doing it in a commingled vehicles, when you talk about liquidity issues, there's no place that's more telling than emerging market small cap stocks. You want to make sure, whether it's with us or anyone else, you're in a vehicle that can meet whatever any liquidity environment that you want to be invested in. So we think that if you're broadly diversified across markets and across countries, then you could do that.

Dr. Leon Guerrero: Any regulatory issues? Kevin Hight: No regulatory issues. You usually ask me whether or not we have any conflicts with Mercer, but no we do not.

Wilfred Aflague: Roberto, your Co-CEO, what about his research duties, is he going to be covering that or are you going to find someone else? Ken Hight: He'll continue to

be actively involved, he's remaining, he still has the CIO title, he's the Co-CEO and the Chief Investment Officer. He still technically has head of research, we're in the process of trying to pass it out to another partner in the organization. That role really is to just manage his research team. Wilfred Aflague: How long is this arrangement anticipated, is he not thinking of retirement? Ken Hight: He's not currently thinking, it's in his potential to do that and I think that like all CEO's that have been running an organization for a long period of time, wants that more flexibility into his schedule and not have as much day to day responsibility, so much of that is getting passed to Eduardo, but he has made it clear that he has no current plans to retire and I would expect that he would continue his role for at least another 5 years and then from there, we'll see how things develop. I think quite honestly, he's got a really nice job, the organization is doing well, this structured approach means that it's a very reliable process, our clients in aggregate are happy, we know we're seeing that positive flow, from a business standpoint, things are very good and I think the team's been put in place to support the infrastructure, it's quite solid.

Dr. Leon Guerrero: You said as of last night the portfolio was at? Ken Hight: \$40,975,000. Dr. Leon Guerrero: You have 4,000 securities, in September there was 39, in February there was 38 and last night it was 40, it seems to me that this is very volatile. Ken Hight: That's the market, that's what's happening in international small companies. We just had a lot of , as people's risk appetite comes back to the market place, we're seeing an appetite for riskier stocks, small companies ---, so both in terms of cash flow going into those, the general market appreciation... the 4,000 securities, you're part of a much larger --- .If you go back to the emerging small, international small, it's small --- much more, we think it makes sense from a strategic standpoint, but there's a little bit of all these kinds of risk factors if you really think about it from a strategic standpoint. There's a lot of volatility in U.S. small caps. Terry Dennison: Now you have the country risk plus the currency risk, so you have a lot of sources of volatility, but the returns are a great deal higher. The object is to have a diversity of returns so everything doesn't go bad at the same time and that's not easy to do. Part of the reason for adding volatile asset classes is that they're not very correlated with the rest of the portfolio, you get to keep the return, but you don't feel the risk. Ken Hight: That's where we looked at page 12 of the presentation, the R<sup>2</sup> affected the correlations, we think that's a very sound basis for getting into these kinds of asset classes, which is both the return aspect, but even with that volatility, that lack of correlation over long periods of time, I think really does benefit the portfolio.  
(End of presentation by Dimensional)

### **AXA Rosenberg (Non US Equity Small Cap)**

Ying Du: Initially we have our Asia Pacific CIO calling in but he's having some flight problems and now he's somewhere in the air so Simon --- is head of our strategy engineer for Asia Pacific and basically Singapore and my colleague Amy Lo, also working on client services. Join a call from Hong Kong and my name is Ying Du, I'm Director of Client Services, Asia Pacific. Thank you very much for this opportunity.

Dr. Leon Guerrero: For the record, you can say anything you want, what we're looking for is your performance for this past year, we'd like to know what to expect from you next year and why, we'd like to know whether there are changes in your personnel, we'd like to know if any regulatory agencies have issues with your company, we'd also like to know about how you proceed with your process of investment. We have present our Chairman of the Board, Mr. Joe T. San Agustin, our Director, Paula Blas, Terry Dennison our financial advisor from Mercer, Trustee, Wilfred Aflague, Diana Bernardo, our controller, myself, Wilfred Leon Guerrero, Vice Chairman of the Board and Chairman of the Investment Committee, and Rosalie Bordallo, our General Accounting Supervisor. We'll turn it over to you and you're leading the discussion, but we'll be interrupting you as things come up.

Ying Du: Thank you very much for the opportunity to be here. Obviously the performance is quite disappointing for the past 18 months and we are going to highlight why we underperformed and most importantly we want our colleague Simon to give you some input on how we're taking this opportunity to improve our investment process from stock selection point of view and also from a risk control perspective. Also of course we will address the other issues that you mentioned.

I will start with page 3, just a quick recap of your investments, currently you have one investment in our Laudus Rosenberg International Small Cap Fund and this fund is invested in the ex-US Extended Market Index (EMI) and AXA Rosenberg is a sub advisor for this particular fund.

Going into more details about the performance, on page 5, this is the highlight for each period that you requested. As you can see on the first part of the page, the majority of the underperformance actually came from 2009. You can see at a certain point 21% underperformance, this basically was the driver for the past 2-3 years. If you look more detail into this 2009 period, the down months were really March, April and May, so for each of these particular months in 2009, the negative alpha was 2%, but putting this into a longer perspective, on the lower part of the presentation on page 5, you see that from 1999-2006 this fund outperformed consistently of the benchmark, almost every single year. We need to understand why we underperformed in such a huge magnitude in 2009.

If we go to page 11, this gives you more perspective about how the market was behaving during that period of time. The graph on the right side, the top chart, is actually a long term confirmation of our fundamental belief which is the forward earning and the price change has a very clear relationship which means if a company has higher forward earnings, if a company's forward earnings are attractive, then that will reflect on the return, so you see that the chart is a very positive slot. What happened in the first half of 2009, I just mentioned we delivered a negative 2% alpha for the 3 consecutive months, what we can see on the chart on the left side is a rally, from February to June, we see that the company with very attractive earnings, for example, you see that we can take telecommunications as an example. Actually from return perspective, the return is actually not that high compared to the materials for example, which means the market was not rewarding, the earnings, that company was building up. So this really highlights what driven the market was, during that 4 to 5

months period, the market was really chasing the beaten down stock, the high beater stock, regardless of a company from the fundamentals, because our true belief really is when you invest in the fundamentals, you invest in the earnings. So that's why you see we outperformed significantly during that period of time. Another factor which can also explain the significant under performance is on page 13, the left side chart, we try to analyze the stock which out performed during the rally. You see the book to price, the first factor was not rewarded because the market as I said was chasing down the beaten down stock and not really the good fundamental companies. The most significant factor which really hurt us was the 3<sup>rd</sup> bar, the relative strength. We call this a prior price of momentum, so this is really the momentum factor and we only have a slight over weight to this factor but it's because the market was behind in a very extreme manner to penalize in this factor, so only --- will become a very huge detractor to the portfolio performance. These 2 are really the highlights of why during that period of time we underperformed but in a nutshell, the market wasn't really rewarding, the good companies with good fundamentals. So for the past 18 months the market was really driven by the macro economy it seems, because you know that in 2008 the market was really down during the financial crisis and in 2009 all the Government support from various countries especially starting from March, the market has 17 year in history, the biggest rally in the history. So all these factors actually not really based on the individual companies fundamentals.

So that's the main reason for us to under perform and I think the most important that we are asking ourselves is, we can't as active managers just blame the market, we can't just say that the market in rewarding earnings. We ask ourselves what we can do to improve ourselves from stock selection point of view and also from risk control point of view. Of course our research is always ongoing, for the past 25 years of history, we have a research center to do this ongoing research. This recent market environment really gives us a very rich side of data to do further analysis. We identified some areas on our 2 stock selection models, valuation models, earnings models and forecast models and also on the risk control point of view, how we can protect the portfolio going forward. That's why we invited Simon, my colleague because we want to give you an update on how we are improving ourselves and how we can protect better in the extreme market environment, which is not favorable to our investment process. I will pass it to Simon if you have no questions on my part. Simon will provide a little bit more update on research side. Dr. Leon Guerrero: That's fine, but I think you want Simon to explain what the changes are in the process.

Simon: Ok, thank you. Shall we go to page 24, update on research. On page 25, this is a snapshot of the research and investment process team. I don't think I need to go too much into detail, in this case I just want to highlight, the bottom, recent research initiatives, on 3 frontiers. The first is the accounting framework for example, goodwill, the second is additional quality measures to better estimate mean reversion for the companies at the extremes of the ROE which is the return on equities and the third, risk model enhancements.

On page 26 is the evolution of the foundation of AXA Rosenberg's stock selection process. So, you're probably aware that in 1985, that is a valuation model which is used exploit mis-pricings and in 1992 is the earnings change and investor sentiment



models, in 1998, the earnings forecast model. I will highlight on these 2 frontiers which is the enhancement to earnings forecast model and enhancement to the valuation model. After that I will walk you through the enhancement of risk model and then last is to touch a little bit on the next step of what we are currently engaged in the research focus on this company life modeling.

So let me start by backing up a little bit to, other than the disconnect between the earnings and the price recently experienced in the market, has produced a difficult environment for our alpha, mostly for our investment models; however our past experience has given us confidence that the market should reverse to normal patterns, therefore creating an increased opportunity for above average aspect of alpha. We remain confident in that --- and remain the prominent driver of market returns. In particular, market investors, they reward, market investors have rewarded 2 key dimensions of earnings. The first is the long term cumulative earnings yield and second is when your earnings change.

So our research in the past and has been ongoing, our objective is to preserve and enhance our long term cumulative earnings yield while at the same time capturing the near term earnings growth. The point I'm trying to drive here is, the ongoing research has not eluded away from our current belief of the capturing of the long term cumulative earnings yield as well as the near term earnings growth. I would just like to make that clear before we go into the discussion of the enhancement.

Let me start of by talking a little bit about the enhancement in these earnings forecast models. We believe our propriety for --- of earnings has changed or have been more accurate than ever and I believe you have seen evidence from the chart in the past on how we compare our earnings forecast --- versus ---. The recent environment has provided us with a rich set of economic data and enhanced the modeling of earnings. Improvement in the forecast accuracy has been achieved by using quality measures, the better model the --- reversion to mean in the ROE, the return of equity. If you remember, within our earnings forecast model, there are 2 components, the first uses the fundamental indicators and the second uses the market participant indicators which - the investor sentiment ---.

So what I'm going to go through now is focusing on the fundamental indicators --- earnings forecast models. Underneath these fundamental indicators, what we have is what we call a --- measures, as in measuring the trend in earnings, measuring the trend in ROE. The improvement that we have made in here is to use quality measures to better model the mean reversion --- extreme in the ROE. These quality measures we're talking about is a composite of AXA Rosenberg's --- measures which includes the measures of stable earnings growth and the persistent profitability of companies. --- highlights --- stable earnings growth and the persistent profitability of companies. So making use of these measures, we're able to better improve the forecast of this earnings new change or what we call the revised forecast of earnings new change. This revised forecast of earnings --- change are highly correlated with the realized earnings new change and therefore we're able to provide a more even distribution and exposure to the highest quality companies and also a more selective exposure to the lowest quality companies, that is the objective. I talked about what we are looking

into and which components and our objective is to improve the forecast and because this improved the forecast, basically because we found out the true historic --- that this forecast change has high correlation in the realized earnings new change and what are ways to improve this forecast, therefore we will be able to capture that realized earnings new change in the portfolio construction.

Ying Du: I'll just jump into to highlight this in a nutshell for this earnings forecast improvement that we are making is really to introduce this quality major to the mean reversion for ROE. So the idea is really a good company because normally there is a rate mean reversion, idea is a good company because there's peer pressure, so a bad company will slowly revert to the mean --- and a good company will come down. So this is the mean reversion that we're talking about, but now we're introducing this quality major, which means the good company and the bad company on both segments, they don't revert to the mean in the same rate. For example there are 2 good companies, one may stay ---- for longer period of time than others so we have to be able to differentiate these different companies, so introducing this quality major is really helping us forecast the earning better, more accurate. So this is really the idea on the earnings forecast model improvement.

Dr. Leon Guerrero: That sounds good, but it looks like you're developing a new process. Ying Du: It's actually not a new process, it's just that we're making improvements to one element of our model. As you can see from the chart in our 25 years of history, we are constantly making improvements. In the beginning, 25 years ago when our founder --- first started the company in California, there was only one model, valuation model and secondly, he added this earnings forecast model. We don't change our core belief, we still believe that we should be focusing on earnings and once we build a portfolio with this earning advantage, it will be rewarded in the longer term, it will be translating to our performance. So we didn't change our fundamental belief, but we did do in the past, do the enhancement, so this is really part of the enhancement, it didn't change our model.

Simon: If you go to page 26 under 1992, earnings change and investor sentiment models, you will realize that the revision to mean in ROE is part of the earnings forecast model which is --- to the fundamental indicators of the earnings forecast model. The enhancement we're talking about here is really to refine the modeling of -- - reversion by using extended quality measures --- to have more precision in modeling --- and inception items.

Terry Dennison: With respect to the way you're using the model, it's our understanding that you instituted a manual over ride to the model in September 2009 reducing the weight of the relative strength factor by 50% and it's our sense that while you've over ridden the model at the stock level in the past, the manual model over ride of the model weights is very rare and it seems that you question your confidence in your own model. Could you comment please? Simon: I think that with regards to the dangers in enhancement, in this case what we call the relative strength which is part of the earnings forecast model, maybe I am able to walk you through... (end of recording)

Simon: --- to look at each of these individual items, especially the increasing amount of good view --- percentage of total assets over time especially if you look at since 2006, 2007, the overall percentage of --- over total assets has increased quite substantially during the last 2-3 years. By looking at this --- good view the discretion of company management will help us to form a more consistent --- in our valuation model. So these are 2 enhancements to the valuation model and our earnings forecast model as we have discussed and I think the 3<sup>rd</sup> thing that's highlighted is the risk model. The enhancement in the risk model here try to capture emerging risk and how to --- which is the start of the discussion of risk management. --- the enhancement in the risk model --- help us capture emerging risk --- what we're trying to do here is to look at recent history of emerging --- so as to quickly adjust to the changing conditions. So it provides a more accurate prediction of the equity market risk which of course would help out in periods of heightened mobility and what it is trying to do here is to reduce the over exposure to --- what we call trans--- risk, they're not really captured by our original risk model which is more of a traditional defined attribute --- the defined attribute risk model here is something very similar to --- risk model. So what this enhancement is to introduce this component where it is able to recognize and to identify emerging risk in the market. Where is this information coming from, it's from ---movement among the stocks. What we are trying to do here is capture risk which is evident in the price movement fund but not yet defined. While capturing this unfolding risk, we also recognize that this risk has a high correlation of the economy indicators --- each of these themes over time. So to be able to capture these emerging themes, these emerging risks, we're able to --- an overall risk or over tracking error of the portfolio --- to the increasing volatility in the market. So this is the --- part of this risk model by introducing the second component called the stage --- where there is recognizing the various stages of the market volatility.

Ying Du: This risk model is complimentary risk model, it doesn't replace our existing risk model, it's just to further help our existing risk model to protect the portfolio going forward.

Simon I think you can briefly touch on the company life modeling. Simon: Ok, with the evolution of these enhancement changes, the company is engaged in extensive research by looking at the company's evolution. As we recognize the evolution of the company goes through various stages, from the first stage, the company IPO to the next stage of the growth stage, --- of a --- stage and a --- stage. What this company life modeling is trying to do is to systematically analyze companies through the economic transition over time and over evolution of company life and by doing this, we're able to improve the accuracy through the combination of valuation and earnings forecast model to identify the phases the company is going through meeting with the various competitions in the market --- the company in the growing stage how they're able to compete, how they're able to combine competition to the stage where companies --- stage in facing up to the competition in the industry and a company is in a declining stage, how the company can continue to survive and how the company can compete in the competitive environment industry. This is really trying to create responsiveness --- change in the business condition influence are caused by the --- point of evolution as I illustrated here through the --- stages of the company life span.

Ying Du: Actually this life cycle modeling is actually a very ambitious project. It is still ongoing, it's completely new and it helps us to stay competitive I guess compared to our peers, especially managers with --- investment process. We don't have a lot of detail to review this is just our way to be transparent to our client, this isn't research we are doing, we are not implementing anything on this part yet, on this life model. Just to answer because you asked 2 more questions that we haven't addressed yet, on is on the regulatory issue, for the past year, we don't have any regulatory issues with any authorities that we invest in, that we carry our business in. You also mentioned about personnel change, in terms of senior management, Terry knows as well, we have a very stable work force in terms of senior management as well. Last year effective beginning of this year, our Asia Pacific CEO was actually Australian, he decided to, for personal reasons, to join an Australian firm, which allowed him to bring back his kids to Australia, because our company doesn't have this opportunity to provide to him. His replacement has already been in place the first of January of this year, it's someone from our AXA Investment Managers headquarters Paris, so the transition has been very smooth on this side. In terms of other personnel change, I think I can update you all is the fund and the management, the size, currently we are having \$60 billion US dollars and since the financial crisis, we always manage our cost very carefully, but it's no client related cost and no staff related cost, it's --- opening cost like internal ---, those kinds of cost. This year we have made a decision to cut 10% of our staff and mostly including the contractors, so to really help us and stay competitive and to be profitable. We're still a profitable company and we still have stable employees, most of our staff in Hong Kong, particularly in the U.S. have worked more than 10 years, myself and Amy, we've all stayed more than 10 years with the firm. From that side we're a lot different from other managers in being stable given this type of market.

(End of presentation by AXA Rosenberg)

**Respectfully submitted,**



**STEPHANIE A. HERRERA**  
**Recording Secretary**

**Affirmed:**

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**Gerald A. Cruz,**  
**Acting Investment Committee Chairman**