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**Quarter Ended 9/30/11 Performance Meetings  
 & Annual Manager Reviews**  
 November 30, 2011  
 Retirement Fund Conference Room

**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  
 Antolina S. Leon Guerrero, Member  
 George A. Santos, Member

**Staff Present:**

Paula M. Blas, Director

**Other Present:**

Maggie Ralbovsky, Wilshire  
 Doris Flores-Brooks, Office of the Public Auditor

**DB Plan**

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**10:00am-11:45am DB Plan**

**Economic & Capital Market Environment**

Maggie Ralbovsky: I'm going to start with market review. While the 3<sup>rd</sup> quarter was a very brutal quarter for our risky assets, anything that carried any risk premiums, the more risky investment, the more they sold off mainly because of your... I think your last quarter meeting we



had discussed Europe and that has gotten worse. In the previous quarter the word people were afraid of was the D word, the default for Greece, now people basically took that as something that's definitely going to happen. Now a word people are afraid of is the C word, the contagion because the Greece problem is no longer a Greece problem, it has spread to many other Southern European countries and now most recently has spread to the core countries, France for example had seen their debt interest rates spike. So the core countries people are thinking of are Germany, France and the Netherlands. The most recent debt auction for France was miserable, they had to pay the highest rate ever since the European Union was set up and the most recent Germany... Doris Flores Brooks: What rate was that? Maggie Ralbovsky: I think it was somewhere in the 5.6 range and if you put that into context in the U.S. Treasuries, 1.9% for 10 years, that is a very huge premium and if you also put in context GDP growth, so if a country is paying interest rate higher than the GDP growth, that means the debt will just grow because the GDP growth cannot keep pace. Joe T. San Agustin: What do you mean, the debt structure went up beyond the GDP? Maggie Ralbovsky: Yes. So the rule of thumb is that if you wanted countries debt to shrink the interest rate cannot be more than the GDP growth. The case in Europe is that the GDP growth is negative pretty much except for Germany, their debt has been ballooning and we know... Doris Flores-Brooks: GDP growth is negative in all of Europe or just certain countries? Maggie Ralbovsky: In all of Europe is negative except for in Germany and the reason is Germany has been showing a slow down so the main issue right now is that the European Union still hasn't had a plan to solve the past debt problem and the new debt problem is being accumulated, therefore it gives you a very gloomy view of the future because they don't even know how to solve the past yet.

So mainly the contagion fear of European debt crisis really dragged down the entire world capital markets, the only bright spot was treasuries, treasuries was the only thing that went up. Joe T. San Agustin: Despite the fact that the U.S. was downgraded? Maggie Ralbovsky: Yes. Doris Flores-Brooks: And despite the fact that we didn't reach an agreement on the deficit. It's a relative game, U.S. is still the safest place even though it's less safe than before it's still the safest place in the world. So there are many issues, small issues in the world, by themselves are not small per se and put them together the problems in the world are really gigantic.

I'm going to move on and discuss more of those separate points in this presentation. On page 4 you can see this is the U.S. data and I circled 2 big bubbles on the top of the left hand corner table. The top bubble shows us that the CPI is deflating which is bad and the reason it is bad is because if you think this country has a debt problem when the most painless way to get out of the debt problem is to inflate out of it, to have your future money worth less and less, therefore you can pay your past debt with less and less worthwhile money. The CPI deflating is in the context of the Federal Reserve keeping interest rates at zero, not only at zero, but also keep buying longer dated treasuries basically effectively making interest rates to be negative on the short end. Given all that unprecedented effort trying to make the inflation to go up a little bit, still it's deflating and that's the part that is really scary.

Joe T. San Agustin: Can you go back to that treasury, you said... to moderate the market? Maggie Ralbovsky: To keep inflation higher. Joe T. San Agustin: To keep inflation higher by having treasuries? Maggie Ralbovsky: The Federal Reserve historically the way to make money easy and make inflation a little higher is to lower interest rates and they have already lowered interest rates to zero, so what do you do now? They actually used something called quantitative easing, mainly that basically means not only to keep interest rates at zero in the

short end, they actually started to buy treasuries on the long end. Joe T. San Agustin: Long term treasuries become a long term investment. Maggie Ralbovsky: To make treasuries... the entire curve went down, yes, that's right. Joe T. San Agustin: The rate of treasuries will still be high. Paula Blas: What's the rate on the 10 year treasury? Maggie Ralbovsky: 1.92% right now, it's below the 1946 level. Joe T. San Agustin: Isn't there hope that rate will go up? Gerard Cruz: There's no inflationary pressure now, there's actually deflationary so they need to fan the fire so to speak. Maggie Ralbovsky: That's right. With all that unprecedented effort inflation is still going down which is the scary thing if you think about the only past precedence of this was the 1930's, the Great Depression and also Japan is another example. So the bottom line, even with the unprecedented effort by the Federal Reserve to make money easy the economy is not restarting, basically we are into a phenomenon where the monetary policy becomes useless, becomes very ineffective.

I'm going to move to page 5. Page 5 is another sticking point for the U.S. and that is the employment. The top chart is telling us that the wage and salary growth has been very anemic. The bottom chart is showing a very troublesome statistic and that is when somebody is unemployed the average length of this unemployment has doubled which in the past people called this structural unemployment, so you tend to become less and less unemployable which is also the scenario in Europe. In many countries in Europe people basically become chronically unemployed. Doris Flores-Brooks: This goes back to October 1961, more than 40 years, 50 years? Maggie Ralbovsky: That's right. In the U.S. the labor market had historically been flexible meaning people had been, the economy has been able to adjust, but the recent statistics have been showing this structural change in the labor market.

The next page shows us the equity market performance. I circled, actually I should circled the other 2 parts as well, the small cap, you see the small cap growth and value index is down more than 20% and the total market was down 15% and 15% was very bad but negative 22% for the small cap was even worse. This is the most volatile sell off since the Lehman failure.

Another chart I want to show you because it's relevant for our later discussion is the bottom right hand chart which is growth versus value. When the bars are above the line that's the quarter when growth out performs value. When the blue bar is below the line that's when value out performs growth and you can see really it's pretty random, there's no telling as to when growth will out perform value or when value will out perform growth and this observation for the past 10 years is consistent with 50 years of observation which draws a conclusion from our firm we believe people should not take a persistent either growth or value bias because growth or value structural bias does not pay off in the long run it only is additional risk you're taking is not rewarded, that's called uncompensated structural risk. When we do structural analysis we try to do balance to be mutual to the style balance. Just hold that thought, I want to discuss that later.

On page 7 is the fixed income market and here you want to see that big number, 27% year to date return and 25% quarter return and that is treasuries. Long term treasuries was up almost 25% for this quarter alone and that is the operational twist we discussed before which is when the Federal Reserve started to buy long term treasury and long term treasury supplies are very limited, 30 year treasury for like a 5 to 10 year period, this country stopped issuing 30 year treasuries because we had surplus once upon a time, so the supply of 30 year treasuries is actually quite limited and when the Fed decided to buy 30 year treasuries

it made a huge move into the market. Joe T. San Agustin: That's why I said the price is going to go up. Maggie Ralbovsky: The price went up tremendously, it went up 25%. You can also see I circled the high yield index, it sold off 6% and was one of the worst sell off quarters for high yield as an asset class.

I'm going to move to page 9, page 9 is the international markets. You can see that the international markets sell offs was worse than the U.S. with the entire non-U.S. equities sold off close to 20% for this quarter and emerging markets sold off more than 22% which is a similar kind of sell off as small cap in this country, so more beta sector sold off more.

Next page is the European debt issues, you can see Greece is the top blue bar. This chart is saying that in the private market Greece debt is trading at 25% interest rate higher than Germany's debt, 25% which is basically pricing into a virtual default. So what happened after the ending of the September quarter, the whole market already knew Greece was going to default, what happened in October, we had a huge rally in October partly because the European Union reached a conclusion that we have to make Greece default. The way they did it was to ask all the banks to take a 50% haircut, so if you hold Greek debt you voluntarily take a 50% cut which does not qualify as technical default, therefore all the credit default swaps did not work which is another reason why Italy, Italian debt, Spain debt, France debt sold off because the market realized I tried to hedge my position by buying credit default swaps but they are telling me it's not a default, it's a voluntary haircut. Gerard Cruz: But it was temporary, it was not a permanent impairment. Maggie Ralbovsky: It is. Gerard Cruz: I thought it was just a provision. Doris Flores-Brooks: I was going to say from an accounting perspective at whatever date they're going to record their investment it has to be at market. Maggie Ralbovsky: It depends on the country. Doris Flores-Brooks: In the U.S. you are required. Gerard Cruz: You mark it against your capital, but it's not an OTTI impairment is it, because if it's other than temporary impairment like Lehman then you're right you do have to extinguish it and at that point the credit default swaps do kick in. Maggie Ralbovsky: Okay so this is not qualified. Gerard Cruz: It's a voluntary, it's almost like setting up a provision but you still hold it as an available for sale so that if for some whatever reason the value does start to kick up if there's no default and you hold it to maturity then you get the coupon.

Maggie Ralbovsky: I cannot answer your question about that because mainly the holders of this debt are European banks and one of them already marked down the whole thing, others are taking a more gradual move and they're not marking it down, but technically speaking this does not trigger credit default swaps which has spooked the market because the market all of a sudden realized it's going to happen to all the other debt which is part of the reason MF Global went under because MF Global has hedged positions of European debt and Jon Corzine went on the record saying we're hedged, yes we have a lot of European debt but we're hedged, but the hedge did not work and that's part of the reason they went bankrupt.

Let me start with reviewing the macro conditions on page 11. The current condition is a very abnormal recession, this is not a normal recession. A normal recession in the past 40 years and if you study them they are inventory adjustment so basically some part of the economy becomes over heating and the Fed will raise interest rates and kill that cycle and then the new cycle starts when they lower interest rates the inventory gets sold off the economy adjusts... Gerard Cruz: It is inventory adjustment they did they just haven't adjusted the housing inventory. Maggie Ralbovsky: In this cycle however, it is a big debt bubble burst, therefore they do not have the capacity to do it because everybody has to de-lever, everybody

has too much... when I say everybody, obviously I don't mean everybody. The private sector as well as the public sector has too much debt and therefore the Fed lower interest rate has asked people to borrow but people can't borrow because they're still in the process of delivering their previous debt. Mortgages are one example and there are all these other debts that people are trying to write down.

So in order to compensate this lack of demand for credit creation even with unprecedented Fed movement, the Government has to borrow, the Government basically around the world are borrowing to the tune of 90% of all the borrowing. That's on my second bullet point, across the world, 90% of the borrowing in the world right now is Government borrowing. In the past 2 years that was 98% of the total borrowing in the world, 98%. Doris Flores-Brooks: Compared to even the private sector? Maggie Ralbovsky: The private sector borrowing was only 2% of the total borrowing in the world. Doris Flores-Brooks: That's unprecedented. Maggie Ralbovsky: The only precedent was in the 1930's when Government borrowing for the world was 100%. Doris Flores-Brooks: But that was in the 1930's, that was the Great Depression. Maggie Ralbovsky: That's right. Doris Flores-Brooks: So is this really a depression and we don't want to say the "D" word? Maggie Ralbovsky: Let's talk about it. Another statistic I want to show you is from 1960-2007, that is the current money managers or the investment manager's history, conclusions everyone drew were based on this period and the Government borrowing was between 2% and 39% of the world borrowing. In the worst case recession before 2007 the Government borrowing was 39% of world borrowing and in the past 2 years it was 98%. What does that tell us? It tells us that the private sector is in a classical de-leveraging and de-leveraging takes a long time to be adjusted because once an economy is in a de-leveraging mode, the Federal Reserve's policy will become useless.

So, this really makes you wonder whether we are going to enter into a great depression kind of a scenario. I actually had dinner with Alan Greenspan a few weeks ago together with some clients. Doris Flores-Brooks: So what did he have to say because a lot of people felt he was responsible for all of this when he... I don't want to talk about that, let's talk about the future, that is subject to debate when we have time, I do think he contributed to that, but I don't think it was purposeful. His mandate is to keep inflation low, to keep employment high, he did both of that. The side effect is really for generations to study what happened, so let's say, the point I want to point out is his assessment, he says that this current environment in the world is like nothing else but the 1930's and he believes we're going to enter into a depression kind of scenario in the next 10 years. Gerard Cruz: Depression for 10 years? Maggie Ralbovsky: Yes, that's what he said. He said if he were a pension fund he would buy long term treasuries and he would buy some gold. The reason he wants to buy some gold is because he thinks the entire world's currency are going to race to the bottom, basically the way to solve everyone's problem is to devalue the currency, race to the bottom therefore gold becomes a --- currency, even though nobody has a gold standard right now. That's the number one reason, the number 2 reason is he thinks China is a wild card and he says the only reason he is not calling 100% certainty that we're going to enter into a 1930's depression is because now there is China. China is a country that can generate any GDP growth they want, it's a country with 50% savings rate with unlimited supply of labor, their GDP calculation depends on the input, not the output, therefore they could just decide to buy a whole bunch of commodities, it's irrelevant what they use the commodities for because GDP calculation is the input. If you say they have a housing bubble, fine, just stop putting stuff in housing and put it into office space, road, it doesn't matter what they use the money for. So it's a country that can really create commodity inflation in the world without

generating growth in the world which enters into the 1970's scenario. So he's not certain if it's going to be 1970's or 1930's, but either case it's pretty bad for equities.

Let me show you some bear market perspectives on the next pages. I put in a circle there, this is the period everybody was referring to, the 1930's period where the bear market did not end until 1946. If you look at the chart it's not straight line down, this chart you can see from the bottom, the first icicle bottom to the... there's a huge rally here, more than 100% rally so even though these last 10 years doesn't mean for the 10 years there's no rally. The people who were living during this 10 year period didn't really know when it was done which is to say that it depends on your planning horizon. Even if we know we're going to enter into a 10 year depression you cannot sell all your equities. You see this kind of pattern it's not a straight line down or up, it just makes us more conscious if we should be more balanced on risk allocation. That leads to my next page.

My next page is a discussion I think we had before, but this is more structured of the thoughts, the thoughts are more structured here which is to say that what kind of paradigm investment period can you fall into. There are basically 4 kinds of paradigms because the underlying factor eventually drives the performance of the investment assets are either economic growth or inflation. If you combine these 2 factors you get 4 combinations of these 2 factors, rising growth rising inflation, rising growth falling inflation, falling growth falling inflation, falling growth rising inflation. These are the 4 paradigms that we could experience. Let's look at the goldilocks growth period, the goldilocks growth period was the period we immediately went over, it basically started from the 1980's all the way until the first bubble burst in 2000 and that's the period where equities have really done well, emerging market debt does well, corporate spreads does well which was also the period where the slogan was created that equities for the long run which based on a whole generation of money managers, people who go to business school were trained in that kind of a culture because that's the immediate history, people could observe, which is not to say that it's wrong, just saying this is one paradigm that we went through where growth was strong, inflation was falling and Government interest rate was falling and it was just a very, very favorable environment.

In hindsight as we look back we knew that growth was based on a few historical factors which cannot be repeated. Number one historical factor was the leveraging, if you look at historical leveraging of this economy, historically the U.S. economy total debt versus GDP was about 50-60% for the longest time, ever since the 1930's all the way to 1982, until somebody thought of a way to create mortgage backed securities, all these different financial engineering instruments were created which can make leveraging very, very effective and make the economy, basically banks don't have to carry the debt they issue anymore, they can sell to the investor and clean the books and move on. So, the leveraging all of a sudden from 50% of GDP shot to 170% GDP, this is total percent debt, not just Government debt. In 2007 before the mortgage debt bubble burst, the economy was at 172% GDP in terms of debt, total debt to the U.S., so that was a 20 year run of de-leveraging, so that made capital really cheap, that's number one major reason that contributed to this 20 year growth. Number 2 reason was the emerging market privatization, so you have the unlimited supply of cheap labor from China, from India, from Brazil, Argentina, the labor cost was so low therefore there's no contribution to...the growth does not contribute to inflation.

Now both of these factors are not going to be forever there and we know that the leveraging is gone, the leveraging factor is gone. Wilfred Leon Guerrero: I don't understand when you use the word leveraging. Maggie Ralbovsky: Leveraging is credit creation, so basically people can

borrow money easily therefore they can invest for the future and the reason they can borrow money easily is there's plenty of ways for banks to unload the debt they have issued. Wilfred Leon Guerrero: How much does corporate greed come up...? Maggie Ralbovsky: I don't want to talk about those factors. I'm not an expert in that matter. Okay, let me tell you my view. Corporations are in existence to make profit, that is by definition so you cannot say they're greedy right, that is how they should function. Now we also mention (Al) Greenspan made money too easy, well why easy money could work then but not now, because then there's unlimited demand for higher rate mortgage securities, there's no demand now. There's many, many counterbalancing factors that contributed to the problems, it's not just one factor, so corporate greed, what is corporate greed? Wilfred Leon Guerrero: You talk about leveraging and what have you and I'm looking at it in terms of what they're doing is they're going for cheap labor. Maggie Ralbovsky: If you ask people in China they felt it was a huge revolution for them to improve their quality of life, so there's demand there for that. Wilfred Leon Guerrero: But what is that doing to this country? Doris Flores-Brooks: We lost all the jobs. Maggie Ralbovsky: At some point it's going to come back because at some point the cost of shipping goods from China will be so expensive that it's better off to produce in the U.S. My husband works for Toyota and they're moving all the Camry production to North America. Doris Flores-Brooks: Because our labor is cheap. Maggie Ralbovsky: And the shipping, there's no more shipping and the infrastructure is there. Everything has 2 sides, there's a demand side, you can't just focus on supply side, the supply side is greedy, the supply side is too easy, but there's a demand side there.

So the social issues aside, that is not our topic today. I want to make a point to say this goldilocks in our portfolio cannot last forever and we might be at the end of that. Very few people are expecting this scenario to be the future scenario. Many people say we're going to be in this quadrant for the next 20 years. So which quadrant are we going to be in? We could be in this quadrant, this quadrant is high growth, high inflation quadrant which was the 1970's. For 10 years the only thing that beat the cost of living adjustment was commodities, so commodities ruined this kind of scenario, so could that be the case? It's the growth side that's the question, so this is high growth, high inflation. You can make a case for high inflation, but is growth going to be there. If we ended up to be high inflation when we observe that oil prices are high, food prices are high, we will end up in this stagflation scenario. In stagflation we'll need gold to survive and TIPs survive, inflation linked bonds survive, these are the 2 categories that will survive in this scenario.

While the worst scenario is this left hand bubble corner which is the great depression scenario which is where (Al) Greenspan is putting his money on, in this scenario Government bonds is the only thing that survives. If it is not very severe you also see high grade corporate bonds survive, because if you think about de-leveraging, what is de-leveraging? De-leveraging is the private sector trying to pay off their debt. So if you bought a corporate bond, that corporation is trying to pay off that debt that makes you get very, very secure because the corporation is using money to invest for the future but rather it's using the money to pay off the debt to make the debt holder better off. Equity holders are really going to be destroyed because equity holders are the residual holders after all the other creditors have paid off whatever is left over for the equity holder, so equities are going to do terribly in this quadrant.

Now what does that mean to us? I want to point out to the fact we talked before and that is the current portfolio, the current GGRF portfolio really has a lot of concentrated allocation into this top left quadrant. It is hard for us to predict whether we decidedly will be any one of



these quadrants, but our point is that we need to consider the risk of being in these other quadrants and therefore being more balanced, you can't really just put all the faith in one quadrant because that quadrant has very, very high probability that it's not going to repeat. Gerard Cruz: So like what, in terms of our existing allocation, what mandates would you say is... Maggie Ralbovsky: Okay, so this is my 3<sup>rd</sup> time meeting with the Committee, meeting with the Board and I understand we have a lot of constraints currently with regard to the law and all that and I also understand baby steps are preferred so I'm hoping to make a baby step proposal tomorrow with regard to changing some of the constraints in the law. Currently the trend in the institutional investing world is something people call "bonds are the new equity." People are getting out of equity but they do not buy just high grade Government bonds, people are buying something called "diversified credit baskets" and those baskets have lots of high yield in it, emerging market debt, CMBS, floating rate loans. Wilfred Leon Guerrero: You really should get in the mode to protect what we have. Maggie Ralbovsky: Because as I said earlier, if you think of a company's balance sheet it starts with bank loans, that's the lowest risk allocation, they borrow from the banks first, the banks give those loans out and those are secured loans so that's the first tranche of security, the next are unsecured tranche which are the debt they issue to the general public, those are the bonds and after that is something called preferred convertibles and then equities. If you think of the pecking order, when a company has money how do they distribute to different stake holders, they start from bank loans first all the way down to equities. Now the law currently allows you to go the bottom, not the top, is that logical? It allows you to buy a high yield company's stock but not the high yield debt, is that logical? Your law. Gerard Cruz: It's true, but if a company defaults who is the first to go... Maggie Ralbovsky: The equities wiped out. The bank loans get 60% of recovery rate historically, high yield gets 40%. Equity holders get wiped out.

I think another role for me is to bring to the Committee what is the new trend in the institutional investment world, people are getting out of equities, they're buying what they call "diversified credit," which is equity substitute. Gerard Cruz: So what if we owned European debt today or let's say we bought it last year, where would we be today versus our current position in equities? Maggie Ralbovsky: You're talking about sovereign debt and that's different from what I'm talking about. What I'm talking about are corporate. If you look at corporate versus corporate equity, European debt, sovereign debt is obviously out of the control of the corporations. Joe T. San Agustin: All you do is try to balance within equities and bonds, what is the best balance and now we're going to try to reverse it so we have more bonds than equity. Maggie Ralbovsky: The balance is irrelevant right now because we can't even go there. Joe T. San Agustin: Traditionally it's 60/40. Now you're going to have to go through what you said, a structural debt. Maggie Ralbovsky: Now you're going to use a more smart way to take that equity risk. Basically you take an equity risk that has a downside protection which is called high yield. Joe T. San Agustin: What about preferred bond, preferred stock? Maggie Ralbovsky: Preferred stock you're still not allowed if it's high yield ranked, high rated so it's that rating I want to talk about.

So my point here is really we want to assess the possibility that our future paradigm will show up to be very different from the past and whether our portfolio is prepared to deal with that. On page 16 here is a summary of what we have done for the 3<sup>rd</sup> quarter. On the bottom chart you can see the total fund had a negative 12.91% return. So 3<sup>rd</sup> quarter was down by 12.91% and that underperformed benchmark by -1.97% and you can see that every composite underperformed and the main reason later on I can show you is that there's a very strong growth bias in the U.S. equity composite and growth underperformed in this quarter.

number 2 is a very strong small cap bias in the total portfolio and we have seen earlier small cap underperformed large cap significantly. Number 3 is that active management underperformed and number 4 was fixed income managers were underweight in U.S. Treasuries.

(End of discussion on economic & capital market environment)

## **DB Plan Performance**

Maggie Ralbovsky: Let's move to page 17, page 17 is the quarter. The blue bars are your performance and the black bars are the benchmark performance and I do not want to observe how big those numbers are, the thing I want to observe here is how many composites are below the zero. This tells us even though we saw we were diversified, all these diversification were very much correlated with each other which goes back to our previous discuss that if you just break down all the things that correlates with growth, 94% of your portfolio correlates with growth, even though bonds went up it was so inconsequential. Gerard Cruz: But in this scenario no matter where we were, where we would have otherwise been, our options regardless, this says that there was no place to run. Maggie Ralbovsky: In the choices you can make. Gerard Cruz: This is all equity though, where else can you go besides international and domestic? Maggie Ralbovsky: I'm saying you have too much in those, you need to consider the different sectors of fixed income. Doris Flores-Brooks: We need to expand fixed income. Maggie Ralbovsky: You need to expand fixed income but not in the current format, the current format is not efficient enough to take... But you need to reduce all these allocations and move to some other sectors and also diversify. Paula Blas: It's Triple B, they're high grade type bonds. So that's what she's saying, you're concentrating just in high investment grade type bonds. Maggie Ralbovsky: Which by itself is not bad, all the other sectors you're ignoring, you're just assuming they're not there and the world has moved on, those sectors are there, in the 1950's they were not there, now they're there which we recognize them.

Page 19 is the most painful thing to look at for this quarter. In the public fund universe you rank 100, 100 percentile for this quarter. Paula Blas: Is this one year, the fiscal year? Maggie Ralbovsky: This is one year, the fiscal year, you are down 2% for the fiscal year and that ranked 94th percentile. Gerard Cruz: That's a 94th percentile? So the index was in the 93rd percentile? Maggie Ralbovsky: That's right, that's your asset allocation. So you can observe that, your asset allocation is pretty much... the fault is not entirely active management, it's the asset allocation because your asset allocation ranked 93rd percentile. Doris Flores-Brooks: 93rd, that means we're at the bottom as opposed to... because last time we were in the 8th percentile. From one quarter to the next we went from the top to the bottom, in one quarter. Maggie Ralbovsky: What does that tell you? That tells you that it is highly driven by the market. But we did go with the market, the benchmark we're not too far from the benchmark, so we're not... Maggie Ralbovsky: I'm talking about the benchmark, I'm talking about whether the benchmark is the right allocation. Joe T. San Agustin: That's your end point, because we have been using the benchmark all the way through as our measurement, the benchmark has always been our measurement. Maggie Ralbovsky: Your measurement against the benchmark is only measuring active management. As a Committee, as a Board, your main decision is asset allocation. Joe T. San Agustin: That's true, but you evaluate the investment market on the basis of how far they are from the benchmark right. Maggie Ralbovsky: That's right and we do that too, but I want to just express my view that I do believe asset allocation...

Doris Flores-Brooks: It's down to 1.1, 1.2. Maggie Ralbovsky: 1.2 or 1.17. Paula Blas: This is as of 9/30/11. Maggie Ralbovsky: We have 1.26 billion at the end of October (2011). November (2011) was a bad month, November equity market was down at least 5% for the U.S. and more internationally. So it's highly driven by the equity market performance and it is very volatile. My point is we need to be more balanced and basically do not ride that kind of volatility month to month.

Okay, so page 21, asset allocation, the message here is that asset allocation is relatively close to the policy, there's no mandatory re-balancing, I know you re-balance when the time comes for you to pay... Joe T. San Agustin: Really we're not too far away from anywhere in the market, we're right there in the market. Maggie Ralbovsky: Yes, if you use that measure, if you use the measure of your current benchmark, the current target policy and I would like to discuss the current policy, not the relative performance. Joe T. San Agustin: I know but I'm just using that one angle at the same time looking for the growth and at the same time looking at the investment angle, but at the same time you have to have a measurement against your investment managers. Maggie Ralbovsky: Okay, let's talk about that.

On page 29 here is the U.S. equity. On the allocation we're pretty much on target, that's on the first column, the first panel and then the middle panel I noted the performance and the green shaded our out performance managers and the red shaded are underperforming managers and the neutral ones are the neutral ones. There was one manager who outperformed and that was MetWest and all the other managers underperformed, some more than others. The third message here was on the column that says "Notes on Manager Prior Status," versus the current status so I highlighted the change of our manager research group's opinions. Paula Blas: Why does it have Wilshire upgrade to focus list for Robeco? Maggie Ralbovsky: Robeco was upgraded to focus list. At Wilshire we have different rankings for managers, the neutral ones are average, an average manager ranked neutral, ranked average, then half the managers ranked below average and usually those managers we do not hire, then half the managers ranked above average. In above average there's above average and there's good and the top ranked managers are focus list managers. Joe T. San Agustin: You have that category listing, in other words you separate the categories? Maggie Ralbovsky: Yes. Focus list managers are the best ranked managers and the analysts actually, their bonus is dependent on the focus list managers. So the performance of 3 year trailing are measured every quarter, so our analysts are at the end of the year, their bonus is dependent on that, so they actually change those focus lists once in a while because it's related to their own bonus. So sometimes they take a manager off a focus list not because they changed the fundamental opinion of the manager, just because they found a better manager to put on the focus list and because it has something to do with their own bonus they can do that once in a quarter. Paula Blas: I guess Maggie because you have Wilshire down twice, one up here at the top where it says "Wilshire Downgrade to Below Average" and then you have them upgraded to focus list. Maggie Ralbovsky: That's a different manager. Robeco was upgraded to focus list and Atalanta Sosnoff was actually downgraded to below average. Explain some of your terminology here, what do you mean by focus, is focus good? Gerard Cruz: Focus is great. Joe T. San Agustin: So that is the highest grade.

Maggie Ralbovsky: I have a few recommendations here today and the first one is to replace Atalanta Sosnoff with an index fund. Last time we talked about index funds and we also talked about the fact that Atalanta Sosnoff is currently used as a core manager and it is not a core manager, I have a section below to show you later on this manager is decidedly a growthy manager. Wilfred Leon Guerrero: But you're just recommending that as a

temporary thing to put in an ETF? Maggie Ralbovsky: No. I'm recommending initiating an index fund allocation and use that as your core manager instead of Atalanta Sosnoff. That's the number one recommendation.

The next recommendation is to remove MetWest off the watch list. It has been a year and I think we talked about giving them a year on watch and it has been a year since their CIO left, so I am recommending removing them from the watch list and return the ETF money back to them. Joe T. San Agustin: MetWest has always been traditionally one of our best managers. They were on a temporary watch, but before that they have always been good. We've been making a lot of money, they're our source of funds.

The next recommendation is, we still remember Arup Datta, he left, he was here last quarter. Paula Blas: He was the one that was pretty much in charge of the strategy because they were quantitative. Maggie Ralbovsky: So he actually left and the main reason was, we actually talked to him the day he announced his departure, we actually went to his office to meet with him and he basically alluded to the fact that the new CEO and him don't get along. They had a new CEO name Mike Even and he has a vision to build up Numeric for 20-30 different strategies and Arup (Datta) has a vision of more focused, do a few things and do it really well, so that's the philosophical clash between these 2 people and Arup (Datta) made it very clear that he is not in agreement with the strategic direction of the company. So Mark at the time decided to elect somebody else as the CIO which escalated this situation and he decided to move on. Joe T. San Agustin: So you only put them on watch because of new management? Maggie Ralbovsky: That's right so we recommend putting the strategy on watch, the reason we don't recommend immediate termination is because this is a quant strategy. If you think of quant strategy it has consistency, it doesn't depend upon a particular person, however the troubling factor is the company's strategic direction of a proliferation of products, that could take the focus off research, so we want to observe, watch him to see if the strategy can be executed successfully, it's not to say people who have a lot of strategies will fail by definition. So we are watching them, we will watch them and I propose a 1 year watch period, we could always decide less than 1 year but this is the default watch period. We also recommend to keep Eaton Vance on watch, I believe they will come on Friday, tomorrow actually.

The recommendation for Atalanta Sosnoff was not only because we downgraded it, I want to show you page 30 which is a continuation of the previous discussion. Let me explain that chart, the graph on the top right hand corner, that is a holding base style drift map, this is a graph of the holdings of the managers, the characteristics of holdings, history to current. You see there's many, many squares on that chart and the smaller squares are more distant past and the bigger squares are the more current, so when the squares get bigger, that's more current and this manager definitely decidedly drifts towards to the growth side. Many, many years ago they were a core manager, you could call them a core manager. The red dot is the benchmark, that's the core benchmark Russell 1000 Index and the index was pretty much in that same spot and Atalanta Sosnoff drifted towards the right hand corner, the right hand side and actually never was off to the left hand side, so it is a growth manager.

So this is the style chart and I want to show you the performance, the up and down market is on the next page in the upper right hand corner. If you look at 10 year history these do better 71% of the time when market is down they do better, but you can see that statistics has eroded recently, you can see how bad recently they underperformed. The anchor of the

portfolio does not fulfill the anchor so that is my main reason to recommend replacing them with an index fund.

Core and satellite is a standard design of portfolio, meaning you have a core that is very low active risk, basically track the index and you have satellite managers that does different things, growth, value, small cap and all that, but you need a core and the current portfolio doesn't have a core, it has the core that's suppose to be Atalanta Sosnoff but this manager really highly correlates with growth right now and really it's not very consistent at all. Atalanta Sosnoff underperformed by 8% in the past year. Joe T. San Agustin: They changed their strategy since we hired them. Paula Blas: They were actually core and then they kept on ...all the way up to current... to growth. Wilfred Leon Guerrero: In bad times they were doing well. Maggie Ralbovsky: In bad times doing well is a good strategy, but not for a core manager. Core managers should do well and it doesn't matter in good times or bad times, it should just track, that's to anchor your portfolio and I do believe using an index fund as an anchor. What is an index fund? An index fund is a passively managed portfolio that basically buys all the stocks in the Russell 1000, therefore it doesn't matter... Gerard Cruz: It's going to beat the Russell 1000. Maggie Ralbovsky: It's going to beat the Russell 1000 because we expect BlackRock's index fund to beat the Russell 1000 because they do securities lending and that more than offsets their fees. Historically it has beat the Russell 1000 after fees by 5-10 basis points because of securities lending. So that is basically viewed as an anchor for a portfolio and I did some scenarios for you if we did that what is the portfolio going to look like.

Okay, before I move to the page with 2 graphs I want to talk about the top page which says, "Unintended Structural Risk," this is not just your Atalanta Sosnoff but also all your other managers. Pretty much all the managers drift towards growth, in the past it was a growth cycle so they mostly drift. The most consistent one on the value side is the Russell 1000 Value Index which was your ETF, then you can see MetWest drifted to the core. Robeco actually drifted more back to value, so these 2 even though they drift, they're not consistently in one direction, they drift both ways. Atalanta Sosnoff is the one that is supposed to be in core, but it's not in the core and you can also see Winslow was a decidedly very high growth manager which by itself is okay because we hired them for growth, the problem with the portfolio is you don't have a strong balance on the value side which makes the entire composite to be growth.

So that's your drift chart here. Then I did some scenario analysis, what if we use the Russell 1000 Index Fund in lieu of Atlanta Sosnoff. Let me explain that table on the bottom page on the right hand side. There's 4 scenarios, number one scenario composite 1 is your current portfolio which has 15% in Atalanta Sosnoff and pretty much equally weights to the other 4 managers in large cap and the other 2 managers in small cap, I assumed you put the Russell 1000 Index Fund back to MetWest as you can see in this scenario number one which is your current portfolio and you can see the estimated fee right now is 51 basis points for your total management.

Now I did scenario 2, 3 and 4. For scenario 2 I moved Atalanta Sosnoff to the Russell 1000 Index Fund and that's going to lower your fees to 46 basis points because the Russell 1000 Index Fund we got a quote of 3 basis points. On composite 3 not only did we move the 15% into the index fund but also we moved some to the Russell 2000 Index Fund just to see because Eaton Vance is underperforming, what if we move half, that's just the scenario, in that case we can lower our fees to 40 basis points. Composite 4 is try to also correct your

small cap bias, remember you not only have a growth bias, but also a small cap bias. So what if I move some small cap to the Russell 1000 Index Fund, basically rebalance more to large cap and that's scenario 4 and that's going to lower your fees to 39 basis points.

Now structurally that's the top graph, the top left hand graph. The current composite is the blue square and composite 2 which is the one we just replaced Atalanta Sosnoff is the red dot, composite 3 we not only replaced the Russell 1000 but also the Russell 2000, you can see that does not correct your small cap bias by much, actually it becomes more small cap. Scenario 4 is the one that we move more from small cap to large cap which corrects your small cap bias to some extent and also corrects some of your growth bias. Gerard Cruz: You keep saying that we have a small cap bias, how do you define that? Maggie Ralbovsky: You see that gold football, that's the Wilshire 5000 composite, that is the market so if you're neutral, neutral plot there and in that market there's 84% large cap, 16% small cap so the Russell 1000 is 86% of Wilshire 5000 and your current allocation is 25% in small cap, so instead of 16 in small cap you have 25 so in scenario 4, composite 4 I moved that to 16 so what if you do not have that small cap bias, that is the question to ask.

The reason it didn't do as much is because all your managers are very, very growthy right now, so we're hoping the value managers move to value more, they have historically moved back and forth, that is the trade off for active management is because you want people to take this kind of stance, but you don't want all of them to move at the same time, you really want some value managers to stick to value and currently both of your value managers are very core, that's why we couldn't correct very much. Gerard Cruz: But value managers aren't, maybe significant isn't the right word, but they're right in the middle there. Maggie Ralbovsky: Where? Gerard Cruz: Right on the top. Paula Blas: Robeco is now back to value. Gerard Cruz: Robeco and MetWest. Maggie Ralbovsky: MetWest is very core. MetWest is right on top of the middle line, that's core, so it does not balance the Winslow. Gerard Cruz: I'm just wondering if your definition of value and theirs is different. I mean what they would consider value because value companies would be different. Maggie Ralbovsky: They're probably different but who is to say they should call the shot, when we design a portfolio we want to be balanced. Let me cancel what I said right now, it wasn't the correct expression of what I was trying to say.

If you recall earlier I showed you a chart that shows that every quarter growth style versus value style is random, so taking a growth bias or a value bias does not pay off in the long run. When we design a portfolio we should try to not purposefully take a bias, now we ended up with a bias for multiple reasons. Major reason is because we don't have a core manager that holds the core. The secondary reason is our value managers... Gerard Cruz: Are looking growthy. Maggie Ralbovsky: That's right. In the historical context the reason currently many, many value managers are not value is because they stay away from banks. Banks are a huge sector in the value, to the tune of 25% and if a manager tries to stay away from banks they will plot core or close to core which we shouldn't say that's wrong because that's what you pay them to do. Gerard Cruz: So you're saying you should not withstanding the fact that they may not see any investable reason to be in financials, you're saying by virtue of their definition they should? Maggie Ralbovsky: No, that's why I said I cancel what I said, that was not my point. My point is that we cannot correct your portfolio all the way to core because we pay people to make these decisions which is okay and I have no problem with that, therefore I'm okay with any of these scenarios even though they haven't been correcting all the way to the core, because we understand the context of why these things happen and we also understand the fact that your value managers are not decidedly forever

systematically in the core quadrant. So I'm okay with a value manager not being value, but I'm not okay with Atalanta Sosnoff being growth. Gerard Cruz: I don't dispute that, I'm just trying to rationalize, except for the fact that it gets cheaper as you go further right, how would we be considered over weight in small cap equity and therefore reduce that allocation, because we made a conscious effort to stay in small cap, to stay at 25 and I'm wondering if it's a function of time that we appear to be small cap heavy and maybe as the cycle changes then those that are in what's defined today as small cap will auto correct itself and then we'd be looking sometime in the future of moving more money back into small cap. Maggie Ralbovsky: That will not happen because by definition 86% is large cap, forever 86% is large cap, forever 16% is small cap, but if you say, I purposefully want to over weight small cap and that is okay if it's a conscious decision to over weight, actually unlike the growth and value bias that does not pay off in the long run. Small cap bias has historically had mixed results, they are years where small cap works, so if you say I purposefully want to take that risk, that is fine, I want to make sure we understand that is the risk we are purposefully taking, so I'm just making it as one scenario, I'm not saying that's the scenario. Gerard Cruz: I understand.

Maggie Ralbovsky: So what if we did one of these scenarios, the performance. So I plotted the performance on the bottom graph. Paula Blas: So now you have your risk and return? Maggie Ralbovsky: Now you have your risk and return and you can see the current football is the current square, that's the current portfolio, it has higher risk. The blue square is the current portfolio and your goal is to move to the north west quadrant not the south east quadrant. Right now you're in the south east quadrant. You can see all the other 3 improved towards the north west. Doris Flores-Brooks: And composite 4 goes way over... Maggie Ralbovsky: Composite 4 goes way over to the right hand side, the bias as Gerry (Cruz) pointed out earlier, this is the time period where small cap underperformed. There are periods in the past where small cap outperformed, so if it is a conscious decision you make to over weight small cap and this is the period you have to basically say we decided on that and we knew that period was going to have this kind of suffering and we're just going to suffer, that is okay, however if you want to observe the red dot versus the blue triangle which both do not correct the small cap bias, the red dot is actually better, there's nothing you can say about the triangle because the dot is right on top of the triangle, it's the same amount of risk.

I want to present these to the Committee so we can decide on where to go and my conclusion is that if indeed we want to keep a small cap bias we should go to composite 2 which is basically replacing Atalanta Sosnoff with an index fund. So the recommendation is to move Atalanta Sosnoff to an index fund. The 3 choices are the what if analysis and composite 2 is the default. Wilshire's tradition is to go to 4, Wilshire's tradition is not to bet on either small or large, but we do recognize our clients will do that so we do have clients who have small cap bias and we will tell them that we do not believe small cap has a consistent premium, historically even though the belief is not as strong as the growth and value. Gerard Cruz: So what has a consistent premium historically? Maggie Ralbovsky: Small cap doesn't, nobody, nothing. So structural risk is not a risk you get paid for, so we usually want the portfolio to be very neutral in terms of growth or value or size. You add value not by taking structural risk, you can take active risk, but not structurally active, structurally in any bias. Gerard Cruz: So we gain value by taking... how, how would we...? Maggie Ralbovsky: Stock selection. People do stock selection. Active manager does drift a little bit, we tolerate a drift, but in terms of portfolio design we do not have a systematic bet because those don't pay off. Wilfred Leon Guerrero: Is this the only recommendation that you have? Maggie Ralbovsky:



This is one of the recommendations. Wilfred Leon Guerrero: What is the other one? Maggie Ralbovsky: Tomorrow. Wilfred Leon Guerrero: You're talking about the bonds or the equities... Maggie Ralbovsky: Tomorrow, that's not on today's agenda. This is heavy lifting for this presentation, this part, this is done. So I believe it will be up to the Committee to decide whether to take this recommendation, but here's the recommendation and I'm going to move on.

I have a few summaries for the other managers, let me just be brief. Numeric was put on watch because the key person has left. MetWest take off watch, INTECH is still on our focus list, we like that manager, I know they had very difficult time during the crisis, but this manager has a very unique portfolio construction. Gerard Cruz: How old is that guy who created that or is he even still there? Maggie Ralbovsky: Yes. I don't think we have an issue with that. Winslow has a concentrated portfolio, Winslow is an okay manager, we ranked them pretty well. They can be volatile because they're very strong out to growth and focused style but it's a good satellite manager because they're not a core manager, we don't really hold them to be the core kind of thing so we're okay with them. Robeco we just put them on the focus list so we really like this manager and Eaton Vance is the manager we have concerns of. Eaton Vance you're going to see them tomorrow and this is a manager that recently had some turnover in their analysts ranks, actually the analysts ranks turnover has been continuous, although they'll tell you their team is self-contained, they don't really use much of the analysts pools input which is probably not entirely true, it's true to some extent but it is the case. Nancy (Tooke) she is a very strong figure in the team. This strategy has really underperformed recently, but it's not like the analyst turnover is so bad we have to fire them immediately but their performance has been so troublesome. Eaton Vance has underperformed since inception by 5% a year. Gerard Cruz: Are we firing them? Maggie Ralbovsky: No, I'm not recommending firing them but I want to put them on watch. We hired them in September of 2010, we usually give them at least 3 years. So that's the scenario here.

I'm going to move on to the next composite on page 38. We want to see the fiscal year and that is the one year and you can see that Atalanta Sosnoff for the one year period underperformed by 8%, INTECH outperforming, Winslow was underperforming somewhat, Eaton Vance was underperformed by 4% since inception and if you look at October numbers, Eaton Vance was underperformed by 5% since inception annualized, so the underperformance is for every year for Eaton Vance.

So that is U.S. equity and I'm going to move onto non-U.S. equity on page 41. On page 41 we have 2 manager research opinion changes, for Fisher we downgraded them to above average from good. The main reason was because of the non-dedicated research approach, they have analysts that does U.S., they have all strategies, they have U.S., emerging market, global, it's all done by the same managers, sometimes the same analysts, sometimes we think a more dedicated approach would be stronger, would have stronger insights, so that is the reason for the downgrade. You can see Earnest was actually upgraded to the focus list. We like the fact that this manager has analysts who all have practical experience in the field of recovering, so if somebody covers the medical companies they actually work in that industry so all analysts have practical experience in the industry.

Wilfred Leon Guerrero: How come you're upgrading Earnest when they underperformed? Maggie Ralbovsky: The upgrading/downgrading is not entirely performance driven, it is mostly a forecast for the future, so they see very strong traits that makes them believe the



manager has a unique source, therefore they could have a sustained competitive advantage to generate good performance in the future and they will upgrade them, so it's not past driven. Just look at what's happened in the past, sometimes you don't get a good indication of the future.

The bottom line is there's no recommendation for any change at this point, so here is the summary. We do have a strong small cap bias and that is the main reason we underperformed as well for this composite. I'm going to show you the strong small cap bias on page 43. The gold football is our composite and the benchmark if you look at the pink square is the benchmark including all companies in the world is the pink square. We do have a small cap bias, however I'm not recommending any changes at this point for this partly because of the definition of small cap and large cap in the world is very... it's not like in the U.S. where people have a consensus to what is small cap, what is large cap. For all the other countries some entire countries are small cap, some entire countries are large cap, so the definition is not very agreed upon.

So no change recommended for international composite and I want to have a couple of things to say about fixed income. Wilfred Leon Guerrero: Can you straighten us out? Focus is the best one... Maggie Ralbovsky: Then above average and then average and then below average and below average is basically managers we do not hire. Doris Flores-Brooks: So focus is your best? Maggie Ralbovsky: Yes, focus are our best managers. There is no manager status change for this quarter for fixed income managers but we do have 2 managers we have concerns with. The first one is Franklin Templeton that purchased MF Global and MF Global is the company that went bankrupt and it's not that they purchased them, they purchased them in August, that's the thing that puzzles me. Paula Blas: It's the timing of when they bought them. Maggie Ralbovsky: They bought this bond at par and sold it for 30 cents on the dollar. The size isn't very large but they lost \$400,000 and they actually wrote a note to say why they bought it and the main reason which I can't figure out is it's John Corzine's company so it's going to be okay. John Corzine was the CEO of Goldman Sachs and he was the Governor of New Jersey, so that was like the main things they mentioned why they bought it which wasn't... Gerard Cruz: Good enough? Maggie Ralbovsky: It wasn't good enough for me. So that is one concern that we have although it wasn't to the point that it was we downgraded them, we sort of don't know if we should downgrade them, we want to watch them. I do believe the main reason was because this manager became so big and when they become so big you pretty much pick up anything that's in the market. To fulfill it. Gerard Cruz: Who is the other one? Maggie Ralbovsky: The other manager we had concern with is Garcia Hamilton. Gerard Cruz: They had a tough quarter. Maggie Ralbovsky: They had a really tough quarter and they had a very concentrated portfolio which is not very risk controlled, the manager seems to have a very high tracking error. There are no recommendations on these managers, I just want to point out these 2 concerns. Gerard Cruz: You're right about those 2 managers, especially Garcia Hamilton. (end of tape 1)  
(End of DB Plan performance discussion)

### **1:00pm-1:45pm Winslow**

(start of tape 2)

Clark Winslow: Thank you for inviting me, it's good to be back after about 3 and half years ago when I was last here. What I would like to do is just briefly give you a comment about performance just for a moment and do a little refresher, what is Winslow Capital's

philosophy, what are we trying to do for you, for the portfolio, what are the key things that we follow in our disciplines in making decisions in the portfolio, bringing you a little up to date about the firm overall and we can talk about the portfolio what's going on in the world, what do we make of it, what do we see and are doing in the portfolio for you and essentially the bottom line there is that our belief is that this is not the 4<sup>th</sup> quarter of 2008, this is not a collapse in the financial markets and I'll explain why that is our view and what we're doing.

The bottom line at the moment after all the volatility going on all over the world, the portfolio is down about 2% year to date as of yesterday which is about one percentage point ahead of the benchmark. With all the volatility going on last week was the worst Thanksgiving week since 1935 or something like that and then Monday the portfolio was up nearly 4%.

Basically since we started working for you at the very end of 2008 the portfolio has gained about 70% and we've been running a little over 100 basis points per year ahead of the benchmark, the Russell 1000 Growth and the total portfolio as of a few days ago was a little over \$80 million dollars.

Let me refresh again what is the essence of Winslow Capital and I'll go over our philosophy and strategy for you. Basically our overall objective is to achieve a consistent out performance over time for our clients and so we know managing money well is a tough business, you've seen that looking at managers over the years and we think we're different from nearly all the managers right out of the box in that we believe in having a hyper focus at least gives you the opportunity to out perform and so from that point of view our hyper focus is we only do one thing, we only do large cap growth and not only that but all of our accounts are managed exactly the same way within a few percentage points with a different position like we manage money for Deere & Company, we count on Deere stock, we manage money for JP Morgan, we count on their stock, but otherwise essentially the same. So we're managing around \$30 billion dollars now for about 75 clients and one of the things you might be interested in is basically we're doing what is called the soft close, we're not taking more clients, we remain open in the mutual funds that we manage, but otherwise we're not taking new separate accounts because we want to make sure we keep the flexibility to be able to sell when we want to protect your interest in the portfolio because we believe selling is a very important part of controlling risk. On the front part of our book or motto is "seek opportunity, control risk," as we're trying to do the best that we can on the upside carefully but we also want to make sure we try to keep as much as we can of what we're making so controlling risk is very important.

In looking at our objective of consistent out performance over time along with that we've got the same portfolio management team now for nearly 13 years and we've been following the same philosophy and process in that time and so what we believe is the best way to achieve good long term performance is to own good businesses, we're not buying turn arounds, good businesses with good balance sheets producing above average earnings growth. When we're buying the stock for your portfolio, pay attention to valuation if it's a sensible valuation for the kind of growth that we see and then build the portfolio with different parameters in mind in terms of earnings growth rates from say, 10-12% in a normal economy up to 50-100%, so on balance the portfolio will be producing an earnings growth rate of 15-20% area again in a normal economy. We'll have a range of price earnings ratios 8-10 times to 25-30 times, we'll have a range of market capitalizations 5 billion up to 3-400 billion and as I said a range of earnings growth rates. What we're trying to do is build this quality portfolio above average earnings growth but one that also protects you on the downside. When we look at our record

over the last 13 years we have average about 400 basis points per year ahead of the benchmark. Now the last few years of course have been quite challenging because we had the bear market and then we had 2010 and 2011 all the worry about a double dip and all the Euro questions and so when we look at your portfolio we're very pleased the companies are doing well, they're having great earnings and the valuation is attractive and when the market focuses a little bit more on the U.S. and the businesses, the portfolio goes up and strong out performance but when everybody worries about Europe and what's going to happen to the financial system and is the economy going to move into a recession, then it goes down.

So what I said in the very beginning is that our belief is that this is not a repeat of the 4<sup>th</sup> quarter of 2008 and we wrote a letter in early August about that after the fiasco of the debt increase for the U.S. that basically when you look at the key ingredients in the U.S. economy, businesses are very strong with good cash flow, they have the most cash they've ever had on the balance sheets as a percentage of their total assets, probably something near \$2 trillion dollars of cash which they can use for increasing their dividends or stock buy backs increasing capital expenditures or acquisitions. When you look at the consumer back in the 4<sup>th</sup> quarter of 2008 the consumer savings rate was zero or probably -1% and today the U.S. savings rate is up to around 4%, it had gotten up to 5% I think it will probably come back to 5% again and if you look at it in terms of the burden of the debt services a percent of income has come down almost from where it was 10 years ago. Yes we have to work through the pressure and the housing market but that seems to be bottoming out and when you look at the banks in the United States their capital ratios are much better than they were, their loans and deposits are a much better number and so when you look at the key ingredients in the economy they're much stronger than they were back in 4<sup>th</sup> quarter of 2008 except unfortunately for the Federal Government. The Federal Government has been having a sharp rise in the debt as a percentage of GDP and the deficit that we all know about. Now this is a longer term problem over the next 5-10 years but the sooner we can address it the fewer changes need to take place that affect everybody to solve their problem. The good news it is out there to be solved.

You turn to Europe and the question there really is about the economies of Italy and Spain and so forth. We've all been reading about Greece but we have new Governments in Greece and Spain and Italy and people who are very highly experienced in terms of economics and understanding financial problems. So even though they can get the programs together to do the right thing of course you have to have the people go along with it. I think the most important thing of where we stand in terms of Europe and looking at these different things we're working on whether it's the stabilization fund or what the European Central Bank can do or the IMF and so forth and so forth, is the big leaders in Europe primarily of course Angela Merkel in Germany and (Nicolas) Sarkozy in France, they understand now that there is a big problem and they have to deal with it in a very significant way. So I think that the worst tail risk of a financial melt down has happened in the 4<sup>th</sup> quarter of 2008. Of that happening in Europe and spreading over the U.S. I think will most likely not happen.

So that means your portfolio is selling at, the overall market is selling at about 12 times earnings, historically a very low price earnings ratio and your portfolio is about 16 times with 20% earnings growth. The position we've taken overall in the portfolio is one of being moderately pro-cyclical, that is being both in the economy and to emphasize again the balance in the portfolio on the different sectors. So unless you had any overall questions I'll be glad to get into a little bit more details on that for you. Wilfred Leon Guerrero: Do you have a listing of... Clark Winslow: Your whole portfolio, I do. In fact let me just pass these

out right here, this is the portfolio as of the end of October. So that gives you the portfolio and you'll see at the end of October the portfolio in the lower right there was just a touch under \$82 million.

So basically one of the key things about how we operate and I'm looking now at the book here on page 2 is our investment team. Clearly when you're a large cap growth manager, making earnings estimates is important right out of the box to have the most experienced team to make the best estimates that you can to drive that growth and performance in the portfolio. The team continues to be headed by Justin Kelly and Bart Wear, they are the 2 co-portfolio managers and I'm in the position of Chief Investment Officer, but Bart (Wear) and Justin (Kelly) make the final decisions in the portfolio and then we've added over the last 2 years more people to the team and as you see they're looking at their years of experience probably averaging around 20 years of experience of each of the members. We have every part of the economy covered with again highly experienced people so I'm very pleased about the team and I don't really see any major additions on the horizon looking ahead. The team is driven not by the amount of assets our clients have but where do we see changes in investment opportunity. So with the tightness of the oil supply in the world we see a longer term secular upward price pressure on oil which also creates somewhat of an umbrella for alternatives when you're looking at coal or gas or solar or wind or so forth over the years so we recently added an energy analyst, Michael Hoover, 36 years of experience, they have already been covered by Justin Kelly and of course Justin (Kelly) still works on it with Michael (Hoover) reporting to Justin (Kelly) who covered that area for about 20 years. So a very strong investment team.

The next page is our support team, our administrative team and our portfolio administrators are 10-12 years experienced CPA's with 7-9 years of experience, so again throughout the whole team one with people who have succeeded somewhere else before being hired at Winslow Capital. By the way, almost everyone we hire on the team is someone who is well known to a person in Winslow Capital which means we basically have had zero turnover at the firm because of the strong selection process.

Now as I mentioned, we're nearly \$30 billion in assets so we announced a process of closing down to new accounts and we're still open in the mutual fund we manage for New York Life and we're still open in 2 other mutual funds that we have. Of course we're doing that in order to preserve the ability for you to and for clients if they want to add to the accounts they still have the right to do that so when we say close, it's what's called a soft close so the current clients can still add to accounts if they wish, but not taking new ones.

Wilfred Leon Guerrero: You don't have the November figure? Clark Winslow: Well since November is not over yet I do have the October figure. Wilfred Leon Guerrero: So October is the latest that you have? Clark Winslow: The latest is -2% and that's as of yesterday, year to date, down 2%. Wilfred Leon Guerrero: I'm trying to remind myself, what kind of manager are you? Clark Winslow: Large cap growth. Wilfred Leon Guerrero: How do you do your selection, how do you pick your stocks? Clark Winslow: Okay, let's look at page 4, entitled "Generating Alpha." The way we pick our stocks is we start off doing a quantitative screen of about 700 companies in the Russell Index, that is companies that are above 5 billion market capitalization and in doing that we're looking at various factors in respect to revenues that income growth of balance sheet factors, cash flow and so forth. That initial quantitative screen reduces that pool of 700 down to about 300. In the second step we're doing a preliminary qualitative analysis of trying to understand what is the market growing --- that

has been ---, what's happening to it's market share, how strong of a competitive advantage do they have, what do we think of management, what about the balance sheet, where are their return invested capital and free cash flow and what do we think of the industry do they have head winds or tailwinds, so if the price of oil is going up that's a tail wind for energy companies, but it's a head wind for retail companies because the consumer has less money to spend on their retail purchases. When we do that we then reduce that list of 300 to approximately 100 companies and from those 100 that's when we're doing are detailed research talking to management, talking to Wall Street analysts, doing intensive analysis of what do we see in this business or the industry where there are various changes going on so we can possibly see earnings growth be than as generally looked for, better than Wall Street consensus estimates. Once we say this is a business of Winslow Capital quality business we want to invest in then the question is, what about the valuation of stock because even on our higher earnings estimates we might think that the valuation is already full so we want to make sure that it's fair of the qualitative factors.

And then when it comes to building the portfolio as we see here in portfolio construction in the middle of the page we're looking at where this company would fit in to impact their earnings growth rate in the portfolio, the market valuation size, liquidity, the valuation, the price earnings ratio, the growth rates and so forth. We have a self imposed discipline of plus or minus 10 percentage points maximum variation in ways to control risk. So let's say healthcare is 20% of the benchmark, we can be in your portfolio 30% or 10%, but we're not going to be 40% or zero, we just think that's too extreme to get way out because when the market shifts and you're so far away you could be considerable behind the benchmark very quickly.

Now the way that this process is implemented is that the analysts bring their recommendation, their ideas for discussion with Bart (Wear) and Justin (Kelly) particularly and then questions get asked about the business and why you think their ideas are going to be so strong and so forth, then the analyst goes back to do more work on those questions and then when the analyst has answered the questions and feels the valuations are attractive, brings it back for a final review and that's when Bart (Wear) and Justin (Kelly) decide if it's going in the portfolio by the time we go through the process most of the time the stock will go but the question is what percentage of weight to go in the portfolio and they make that decision.

Wilfred Leon Guerrero: The sectors, do you have a ratio for those? Clark Winslow: Plus or minus 10 percentage points. So if we look at the portfolio today (let's see here) on page 10, you will see on the left bars there is the sector weight in the portfolio that you have consumer discretionary 15% of the portfolio there or in technology down near the bottom 31%. If you look over at the right column it will tell you how much you're over or under weight versus the benchmark. So at 15% consumer discretionary you're 1% over the benchmark weight or for consumer staples which are much more slowly growing, we're considerably under weight minus almost 9%.

So as I said the portfolio is essentially moderately pro-cyclical weight, that is we're a little bit over weighted in technology, slightly over weighted in industrials, financials not really lenders other than JP Morgan but asset managers like Franklin Resources and under weighted in consumer staples. Wilfred Leon Guerrero: Consumer spending determines a lot and influences the portfolio right? So like the last couple of days, the Black Friday event, that should help... Clark Winslow: Well that's part of the reason that the portfolio was up nearly

4% on that Monday, partly the market sold down too much on Thanksgiving week when nobody was around and very little trading could affect the prices but yes, it was a good, a surprisingly good shopping period and also this morning the consumer competence index came out and surprisingly better than expected but of course that was mirrored by what happened in fact in retail spending. What we're dealing with and why we're very careful of course in building your portfolio is we are dealing with a secular de-leveraging, I mean the consumer has to continue to de-lever some more, the U.S. Government has got a major secular de-leveraging that it has got to address and get through and if they did the right thing, which means having some revenue raisers controlling the entitlement costs, making little changes slowly over many years out you can get these things under control and then the valuation instead of being 12 times earnings it could be 15 times especially if you're basically against control of the problem so the worst results won't happen which we think would be the case, there would continue to be problems and a long work out.

The thing is that you have to keep in mind when you read all the stuff going on in the newspaper in the world and so forth and so on, you know we're not buying the economy, we're not buying the stock market, we're trying to find around 60 businesses out of the initial 700 that I mentioned that we look at, 60 businesses that are out performing the economy and 60 businesses that have a reasonably sensibly attractive stock price relative to their fundamentals and growth rate and so that's what we're trying to do in the portfolio.

Now if we're wrong and Europe is a much worse situation and it drags the economy to a recession here, the portfolio is not positioned for that, but we come to work every day and we're analyzing what's going on in the world every day to make adjustments as we see it. As I said, the bottom line is we think moderate growth in the U.S. economy, moderate recession in Europe, looking at Asia and China a soft landing there which means 6-7% growth in GDP in China, not 9 and 11 but not 3 or 4, so therefore as I said when the market focuses on the businesses and the fundamentals and the strong performance, the portfolio goes up and strongly out performs, when the market gets nervous about the worst outcome of what can happen and so forth, it goes down. Because we're a growth portfolio, if you think the world is going to be in a recession, generally people don't want to pay that much for growth, but the point is your companies have very strong cash flow and even if earnings were all disappointing, the valuation is not all that high and they have good return on invested capital in your portfolio.

By the way, you might be interested in how does your portfolio rank among peers and this is just something you can pull up every single day just going to marketwatch.com, this is the mutual fund that we manage for New York Life Insurance Company. Wilfred Leon Guerrero: Is 28% good or bad? Clark Winslow: That's high. Number 1 is the best, so the 28<sup>th</sup> percentile means you're in the top 3<sup>rd</sup> almost top quartile, year to date, one year 3 years and of course we haven't managed for you for 5 years but we're at the 4<sup>th</sup> percentile 5 years and 10 years. Wilfred Leon Guerrero: Say that again. Clark Winslow: If you look at year to date the 28<sup>th</sup> percentile, for the last 12 months 26<sup>th</sup> percentile, the last 3 years which is basically your portfolio, 27<sup>th</sup> percentile. Now for our clients that we have had longer term they're in the top decile, 5 years and 10 years 4<sup>th</sup> percentile. Wilfred Leon Guerrero: I'm not seeing how you're getting the percentage. Clark Winslow: That means that we are, if you take 28<sup>th</sup> that means we're better than 72% of all the other large cap growth managers year to date and so essentially we're around the top quartile performance year to date, one year, 3 years and top decile performance over the longer term. Another way that we look at it is we also look at our 61 managers of large cap growth... Wilfred Leon Guerrero: These are your clients?

Clark Winslow: Yes, that's right and it's the same as your account because we manage all the accounts the same way. Wilfred Leon Guerrero: This is not necessarily public pension funds? Clark Winslow: Well we manage all the accounts the same way so you would end up with approximately the same numbers in the universe. Or are you saying for among all pension funds? Wilfred Leon Guerrero: Yes. Clark Winslow: No, I don't have the data for that, but you can go to the internet every day and get this data. I'm sure Wilshire has all kinds of data to look at too.

Any questions at all about the portfolio? Wilfred Leon Guerrero: Just the standard questions. Are there any issues with regulatory agencies? Clark Winslow: No, nothing. We are plain vanilla, you can't get any more plain vanilla. We do one thing, we do the same thing for all clients. Wilfred Leon Guerrero: And no personnel changes? Clark Winslow: No, just additions to the team, we're now up to 28 employees. It's a very efficient firm because of the fact that we just do the one thing and all the accounts are managed the same way and we have highly experienced people, so you don't need that many people because when we buy a stock or sell it, we just say how many shares for each one of the client account because we do the same thing every where. Wilfred Leon Guerrero: You founded this company right? Clark Winslow: That's correct. Wilfred Leon Guerrero: How come you're not the President? Clark Winslow: Well, I'm the Chief Executive Officer, so the President reports to me. Wilfred Leon Guerrero: Okay and you don't call yourself Chairman? Clark Winslow: I don't call myself Chairman, actually there's a technical reason for that because 3 years ago we combined with Nuveen Investments and therefore we no longer as Winslow Capital have a Board of Directors, but we do have a Board of Directors through Nuveen and there's just a few Nuveen people as a formality so that's why I'm not Chairman now, I'm the Chief Executive Officer. If you have any problems requesting you know where the buck stops, right here and when I came out here 3 and a half years ago to present to you I said I wanted you to know that the people who make the final decisions when it comes to it, I'm not managing the portfolio or anything but the final, final decisions I'm involved in. The good thing with the firm is that Bart (Wear) and Justin (Kelly) are the portfolio managers, they're managing the portfolio and we manage Winslow Capital on a team basis, so Mike Palmer the President and Bart (Wear) and Justin (Kelly) and also Jean Baillon who is our Chief Financial Officer and Chief Administrative Officer have been with us since the beginning of the firm nearly 20 years ago. Even when I was the majority shareholder of the firm we managed it as a team, as a true partnership so I'm very pleased that if that question of if something happens to me, we have a very experienced people running the portfolio and managing the business. Maggie Ralbovsky: Was the transaction to Nuveen part of your exit plan? Clark Winslow: Not really because I don't have an exit plan, but I'll tell you what it was, what attracted us to Nuveen was as we were getting around \$5 billion dollars we found more time was being taken out by HR, by IT, by legal and compliance and all of this stuff and what we like to do is find good businesses and build portfolios and talk with clients. I mean, I got the application for Harvard Law School but I said, I don't want to be a lawyer I went to Harvard Business School and Nuveen said, look we can take over a lot of these non-investment functions for you so you can keep focusing on doing investments and we looked at their model and their business is 100% investment management, they have 6 other boutique affiliates and each one of those kept their own identity, kept their own culture, did well for clients and they said, you guys keep running the business and so they do all of our HR, basically we're on their global enterprise IT system, about half of the legal compliance, if you notice on page 3 we have our Chief Compliance Officer, Laura Hawkins, MBA, 28 years of experience, because we have a very high compliance culture at Winslow Capital and so I wanted to maintain that. So that's



why we did it and we signed 5 year agreements and we're in the process of negotiating for 2014 to 2018.

I did have one little operational portfolio question. I know we're hired because we're a U.S. large cap growth manager, there is a very small part of the index that because of that technical definition we're not able to own for you. In other words, there are U.S. companies which are incorporated outside of the United States but they are U.S. companies and they're in the Russell 1000 Growth benchmark, the benchmark where we're measured on and what I would like to have you consider is to allow us to own those U.S. companies which are in the benchmark even though they're incorporated strictly for tax reasons outside the United States. Now they are relatively a few companies like that, like Carnival Cruise Ship Lines, a U.S. company the Arison family runs it and they're headquarters are in Miami, but they're incorporated in Panama because they have the best laws for shipping. There are just a very few companies but there are some that we own for our clients and I think that it makes sense at least for you to review that to see whether you want to allow us to own those companies that are U.S. businesses but they're incorporated outside the United States. Gerard Cruz: But they fit all screens and our tests in every other... Clark Winslow: Exactly and they're in the benchmark. They are called BDI's which means benefit driven incorporations, so they incorporate in Bermuda and they incorporate in the Caymans and they in Panama or something, but they are U.S. companies, it's not like we're buying a foreign company in Thailand or China or something like that, these are U.S businesses. When you hire us to be a large cap U.S. manager, if we are buying some of those which we do own for other clients and not in your portfolio, we would like to be able to do that so there's more commonality.

Wilfred Leon Guerrero: Is that negatively impacting us right now? Clark Winslow: It is actually, it's a moderately probably 30-40 basis points over the last few years, a difference in our portfolio. Maggie Ralbovsky: Why wouldn't that fit the 15% foreign limit? Clark Winslow: Because we don't have that. Maggie Ralbovsky: Page 5 is 15% foreign. Clark Winslow: This is our normal standard guidelines, this is not Guam (fund). In that it says no more than 1.5% because that happens to be a stock that we had when you came to that conclusion. Gerard Cruz: I don't think there's a law that restricts us. I think it is allowed, if I'm not mistaken, it is possible. Clark Winslow: It says no ADRs. Gerard Cruz: I think you're right, I don't think there's a legal restriction, we'll check, I think it was a policy decision because we have international managers. Clark Winslow: And I totally understand that because like I said, you hired us to be a U.S. large cap growth manager, but these are U.S. large cap growth companies, they just happened to be incorporated outside of the United States, but they are in the benchmark we are measured against, they are U.S. businesses and so I'd like to just ask if it was alright to very simply to just say any company that is in the benchmark, U.S. company, even if it's foreign domicile it would be okay to own.

Gerard Cruz: How's the benchmark, about how many percentage... Clark Winslow: Well I asked... there are a number of smaller companies but some of the bigger ones are Schlumberger, Marvel Technology, Mcdermott, Invesco Financial, Freescale Semiconductor, Carnival Corp. Gerard Cruz: About 10%? Clark Winslow: I'd say 8% of the benchmark, 8% maybe in these types of companies. Now we never own that much at one time but it can be 5% of the portfolio and so we don't 2, 3, or 4% that we do for other people, for other clients, but they're U.S. companies so we're within your desire to be having us buy U.S. companies and your international managers buying international companies because this is a U.S. company but technically it's incorporated outside. Russell addressed that about 4 years ago and they said we got it so these companies will be in the benchmark. That's all I ask is that



we be allowed to buy if they're in the benchmark. Wilfred Leon Guerrero: I suggest that you go ahead and write a letter to us and clarify it. Clark Winslow: Okay. Gerard Cruz: Approximately how much of it is in the benchmark, around 8-10%? Clark Winslow: I would guess around 8. Looking at these companies I don't even know because they're a lot smaller companies. Gerard Cruz: The reason why I'm asking is because there is a limitation on the amount of concentration in international equity and so we want to make sure that we don't push up against that limitation. Clark Winslow: It includes whatever I'm sure, because we're only talking about a few percent here in the portfolio, at the most maybe 5%. Paula Blas: And I think right now it's kind of like they're half foreign and half U.S. I mean that's kind of, where do you want to define them.

Gerard Cruz: So a letter and then we'll do some analysis. Clark Winslow: I mean, I know what your objective is and we will be operating from that point of view. Now we do own Bidu and that clearly is a Chinese company so that would be outside of what your desire is. Gerard Cruz: Is that a direct investment or is it through an ADR? Clark Winslow: It's through an ADR, because we only buy ADRs, a company that is actively traded in the U.S. and only where we know about them because we're doing all the research on the U.S. company. I mean, if you're following Google, how can you not know about Bidu, but we understand, we are a U.S. large cap growth manager.

Joe T. San Agustin: By having this extension, do you think there's a compensating benefit? Clark Winslow: Well it just means a few more companies that we'd like. Joe T. San Agustin: What would be the net value in your overall, what would be contributing to the overall? Clark Winslow: Well when we looked at the past the question asked was there a bit of a difference in performance and the answer is yes, so when you look at our composite... Joe T. San Agustin: What impact is that going to be, additionally or negatively? Clark Winslow: We would expect it would be a slight positive addition to the performance because the reason we own them is we think that they're strong stocks. It's not going to change the dynamics because all it's going to do is bring you in line with our other portfolios more. Joe T. San Agustin: So there is no additional risk? Clark Winslow: No, there's no additional overall risk.

Wilfred Leon Guerrero: Thank you very much. Clark Winslow: Thank you. Anything else? (No). (end of tape 2)  
(End of presentation by Winslow)

### **2:00pm-2:45pm Intech**

(start of tape 3)

Ellen Lee: Some changes internationally, our CEO is Dick Weil and he came on board February of this year, so when I saw you last year he talked in discussion with Janus. He's from Pimco, he was the Chief Operating Officer for Pimco, so he came to Janus and he really improved operational and put international business very closely tied up with the head office. Internationally we had Augie Cheh he joined this year too in May and he's from Allianz Bernstein, he was the Asia's CEO for Allianz Bernstein and at Allianz Bernstein he increased the AUM dramatically from 40 billion to 70 billion during the time that he was moved from New York to Asia. So we want to have that kind of growth in Asia and especially in Janus. Gerard Cruz: So he runs Asia? Ellen Lee: He runs international, so anything non-U.S. he runs it, so with him we have a lot of resources support from U.S. We expanded the team dramatically in Europe and in Asia we increased the client service team, the sales team, so

the idea is to grow the business in Asia. This year we had 3 big new mandates into international in Asia. We do pretty well in China, Korea and Thailand. Business wise we try to improve ourselves putting more people, work better, more systematic, we have more resourced from the U.S., more support.

Maggie Ralbovsky: Are you talking about Janus or INTECH? Ellen Lee: Janus Group, not INTECH specifically. Maggie Ralbovsky: And you're from Janus? Ellen Lee: I'm from Janus and Janus has a distribution team to distribute INTECH products, Perkins products and Janus products and each subsidiary has a very unique range of products and INTECH being one of them. Joe T. San Agustin: So you use to be with INTECH? Ellen Lee: I'm always with Janus so in terms of distribution, in terms of servicing, it's always Janus and INTECH is manufacturing of the product. Gerard Cruz: The product we bought was INTECH. Ellen Lee: Right. So anything business oriented, servicing oriented, marketing is Janus. So Christian (McCormick) is going to tell you about the product itself.

Christian McCormick: Does anyone else need an extra presentation book? As Ellen (Lee) was mentioning, I'm a managing director, part of the portfolio group at INTECH. So just to address those 2 topics off the bat if you want to start on pages 2 and 3, there are no regulatory issues going on currently at INTECH, we're not under investigation for anything, so that's good news. Organizationally we haven't really had any changes as to date, but I mentioned this last year, we have a succession taking place at the end of this year, so on page 3 if you look at the top of the page the 4 individuals there, the 2 in the middle, Bob Garvy our Co-CEO and Dr. Fernholz who is our CIO, they are really the founding members of INTECH. Dr. Fernholz founded the process back in 1987, he really incepted the firm and although Bob Garvy joined in 1991, he's really responsible for INTECH as an organization, so it was 4 years after our founding, but we consider them both to be founders.

Since 2008 we've had a succession plan in place for both of them to step down, so at the end of 2008 we promoted Jennifer Young who was our President to the Co-CEO position and she's been with us since 1999 and on the other side we promoted Dr. Adrian Banner to be our Co-CIO also at the end of 2008 and he has been with us since 2002. So December 31<sup>st</sup> of this year Bob Garvy and Bob Fernholz will officially step down, but they will still maintain some employment at INTECH. Bob Garvy his official title will be Consultant, he will be exclusive to INTECH, he will be visiting clients and helping on the distribution side, but he will have no more managerial responsibilities or operational responsibilities, everyone at INTECH will report to Jennifer (Young) as the sole CEO. Dr. Fernholz, the great news there is that it certainly in terms of names a big shift for us because he was the original founder, but because we use this unique process, this mathematical model, the model is not automated so to speak, but really it's the model that determines how portfolios are constructed and what Dr. Fernholz does is his role has been really for the last 5 years to do additional kind of broad market research into ways that we can improve that process. So really all that's happening is he's losing that CIO title and all of his supervisor responsibilities for our research group, but he's going to continue to be one of our researchers and do the same thing he's been doing it's just now he doesn't have to manage anybody in the process. Dr. Adrian Banner will manage our Princeton research and all those individuals in green there are part of our research group, they're based in Princeton, New Jersey. Everyone you see in yellow except for myself and a few other folks on the road are based in our headquarters which is in West Palm Beach, Florida. On January 1<sup>st</sup> we expect to look the same as December 31<sup>st</sup>, there's really no change, just those 2 folks will have different titles and will have moved down in the organizational chart.

The only other hire to mention below Jennifer (Young) on the far left, Dr. Danny Meidan, we hired him in December of last year right after I met with you. We brought him over from BGI, Barclays Group in San Francisco and although he's one of our PH.D's, he is really a liaison between individuals on the client service side such as myself and our mathematician group that's based in Princeton. He tries to put in English in layman's terms all the mathematics that they do, so he's more instrumental in some of the research we do for clients and putting together these presentation books and so on, but he heads up that internal group there in Florida. Aside from that there are no other major changes.

Turn to page 4 and 5 and actually let's jump to page 5 and review the quarter as a whole, although I'm sure Maggie (Ralbovsky) has already gone over that, the 3<sup>rd</sup> quarter and you can see there was really no where to hide both U.S. large caps and small caps and of course internationally got hit a lot worse with everything going on with the financial crisis in Greece and the corresponding effect on Europe and the worries that created on the effect that it's going to have on what is a nascent U.S. economic recovery. We are not as you know fundamental managers, we use that mathematical model and I'll touch on that in a little so we're not trying to predict or forecast when markets are going to go up or down but a market like we saw in the 3<sup>rd</sup> quarter does affect us in that markets have been relatively stable before that coming off the financial crisis and the quick turnaround in 2009 the markets have been up but it was a relatively stable environment up until the 3<sup>rd</sup> quarter when all of a sudden stocks really turned on a dime and dove downward and it was an abrupt shift that really no active manager saw coming but that kind of quick shift is what can cause trouble for our model and I'll go into some more specifics there.

I want to turn ahead to page 9, it's always helpful and it's certainly helpful for me to just do a quick review of when I say our model, what it is we're doing exactly and how it is that we're different and the best contrast is to think of us as a more specific asset allocation model. So the same thing you're doing and you're doing now with Wilshire your new consultant is determining what combination or mix of asset classes is best for your retirement fund. Stocks, bonds, real estate, maybe private equity in some other asset classes, you hold these asset classes in different combinations because each one has its own characteristics, its own risk and return characteristics. The idea is for the overall fund you're trying to meet a certain actuarial target rate of return but you'd like to minimize the amount of risk that you take to get that return. Because these asset classes don't move up and down in tandem with each other, they have different correlations and because they have different characteristics, that determines the combination you're going to hold. Well, that's really all that we're doing on the individual stock level, so our entire premise is that a cap weighted benchmark such as the Russell 1000 Growth, the S&P 500 in which the only consideration for how that benchmark is put together is size, the biggest company is the biggest stock and so on, they're ranked order by size. We think that's an inefficient way to put a portfolio together so we're just seeking to re-weight the benchmark to what we think is a more efficient combination of weights based on the individual characteristics of stock and stock price movement. So what we care about is, how does a stock move, how volatile was it and just like in the asset allocation model, what is it's correlation to other stocks. Ideally we want a stock that goes up and try to match it with a stock that goes down, so we're looking for that more efficient combination to slowly generate an excess return over time, but minimize the amount of risk that we take to get there, the same as an asset allocation model except we're just using individual stocks to do that and that's what the model is targeting.

Gerard Cruz: So what kind of market environment do you best perform in given the model?  
Christian McCormick: There are 2. One is more of a stable environment where there aren't a lot of quick changes going on. That affects us more on, I think we're a little bit more honest than other managers about that is we may outperform in a market that's jumping all over the place, but we just may be lucky, we may be over weight in the stocks that happen to have jumped the right way, because the model is structured to over a very long term build up to that return and if we happen to get a great boost in a quarter I'll be the first to come in and say we just happen to own the right stocks, we got a little bit lucky. So it tends to show up in the more magnitude of out performance or under performance.

The second piece of an environment that helps us is what the model is looking for, I mentioned that we're looking for stocks that have lower or negative correlation to other securities, the fuel for the excess return, how is it that we beat the benchmark over time is we're looking for stocks we expect to be more volatile than the benchmark itself. So the benchmark is moving up and down and over time we want stocks that are going to move up and down by a greater margin and then we do some re-balancing there and as you can imagine, those tend to be the smaller stocks within a benchmark. So a stock like Exxon, Microsoft, the bigger a stock is the more it tends to behave like the benchmark itself, it drives the benchmark. In order to get that differentiation we tend to over weight the much smaller names within the benchmark, so they're not small caps per se, just smaller large caps within the benchmark and an environment that helps us is obviously when those small cap stocks do better than the large cap stocks which did not happen in the 3<sup>rd</sup> quarter.

On page 10 we have performance through September (30, 2011). Since inception on a gross basis that unfortunately dragged that since inception number down to 60 basis points ahead of the benchmark. On an absolute basis returns are still very strong, even on a net basis we're about 17.37%. On page 12 we'll give you the update through October (31, 2011).

So September and October were very difficult months in particular for this strategy. The good news in November so far we're about 40 basis points ahead for the month of November and now that things are calming down our performance has responded but you can see even given the 3<sup>rd</sup> quarter in October, the longer term returns one year and 2 year are still strong, we're still kind of trending in the right direction after what was a bad 2009.

Gerard Cruz: So you guys do this rebalancing, the model rebalances how often?  
Christian McCormick: Every 6 business days.  
Gerard Cruz: So you're in and out of positions every 6 business days?  
Christian McCormick: There are 2 factors. The one thing that we're very aware of and I actually remember this came up last year and I brought one of our trade book list that details our trading costs. It's a balance between rebalancing enough to capture the volatility we need, but also realizing that trading costs are a big part of it. I mean the trading costs are this insidious piece of asset management that no one talks about, it's hidden but it eats away at returns. So it's a balance that we've always had to strike, so in order for your portfolio to be rebalanced, it's a GGRF portfolio, you would rebalance on Monday one week and then Tuesday the next week and Wednesday, so it has to be your day to rebalance. On top of that around each individual position, let's say General Electric, let's say we own 3% of the portfolio in General Electric, we have trading bands around that, so if the model says I want to own 3% of GE, so that's where we put your portfolio in, it has to move up or down by a certain margin, it has to break those bands before it triggers a rebalancing otherwise trading costs would just eat into any benefit that we have, but turnover is still high.  
Gerard Cruz: Does this work internationally, do you do this for international markets as well?

Christian McCormick: We do, a global portfolio manages an international portfolio. Gerard Cruz: And you're able to bring down your trading costs in the global markets as well? Christian McCormick: We are. The same with the U.S., we're really just a large cap manager, we need to have those larger liquid stocks, so although we have a global portfolio, we can't trade emerging markets because most of them are too small and the trading cost would go up too high, it would just eat into it too much. So both U.S. and internationally it's only large cap equities that we can do.

And quickly, just a snapshot on page 13, it gives you some comparison versus the Russell 1000 Growth Index. That portfolio characteristics box demonstrates that we're really not too different from the benchmark. We own 275 securities, that's quite a bit less than the benchmark itself but the names that we don't own are the very, very smallest names of the benchmark. Our beta is actually a little bit less than one, but dividend yield, price to book, we tend to be very similar to the benchmark. Where the big difference is and this is what I mentioned about over weighting those smaller names is you see our weighted average market cap in that top left hand box, we're at about \$51 billion versus the benchmark of \$88 billion and we break that down further so you can see in the portfolio table right below where we've broken it down by market cap range. You can see the Russell 1000 28% of the benchmark is in stocks that \$100 billion or more in market cap and we have about a 50% under weight to that and so where does that money go from that under weight? You can see we have tremendous over weight to the stocks that are \$2 billion - \$15 billion in range so it's not really systematic, it's not that we just like larger cap securities it's just that we don't really get the volatility characteristics that we need and over the long term that tends to be a wash, it hurts us as much as it helps us and the 3<sup>rd</sup> quarter in particular it was awful.

We'll skip the volatility environment and let me go right to diversity, let's start on page 19. Diversity just means size, when I call it market diversity, how diverse the market is, when I say diversity I just mean size. So within a benchmark the larger mega cap securities versus the smaller names. What we show you on page 19 is a graph that goes back to 1966, we actually have gone back to before the great depression and you get the same picture, but any period of time when this graph is trending downwards, that's a period of time where capital is becoming more concentrated in the larger mega cap names in the benchmark, they're out performing or they're leading the benchmark out and as you suspect, that would be a headwind to our performance. Any period of time where they're trending upward the smaller or mid-size names are doing better and that tends to be a tailwind to our performance.

Going back to 1966 you can see this is a very choppy measure, it's not smooth but it tends to be mean reverting over time, it starts and ends at zero, so that really adds some evidence to what I mentioned, over the long term it will help us as much as it hurts us. You can see recently a good snapshot was the trend downward at the global financial crisis or even the tech bubble is diversity tends to be a tremendous headwind to us when there's a big flight to quality, when there's a big market event to the negative. In 2008 you see the financial crisis and it's small just because it was a quarter but you can see it trend downwards at the very far right hand side of 2011 and that's what we saw in the 3<sup>rd</sup> quarter was all of a sudden the market turned around, stopped on a dime and had a tremendous negative quarter, but not only did it have a negative quarter but if you turn to page 21, the disparity with how different size stocks were doing was tremendous and this is something that we've actually rarely seen.

So a couple of things on page 21 we've broken down that same table I showed you earlier on market cap sizes, we've shown you how each different market cap segment of the Russell

1000 Growth performed over the 3<sup>rd</sup> quarter. You can see that the stocks that are the mega caps, greater than \$100 billion in that far left hand shaded box, they were only down about 4% in the 3<sup>rd</sup> quarter and you compare that to the other market cap segments especially the \$2 billion - \$15 billion where I mentioned we have that heavy over weight and that was down almost 20% so within the Russell 1000 it was an awful quarter for the benchmark, but you'll see those larger high quality names actually didn't do that poorly, they were only down about 4%, whereas the smaller names where we're over weight were down almost 5 times as much. To have that disparity is unusual and the other thing that made it unusual is this for some reason was more distinctive to growth equities, in core you saw it a little bit, in value you didn't see it at all so it's rare to see core growth and value diverge that much, but the evidence is really here. We had a strong under weight to the stocks that were only down a little bit and we had a huge over weight to these stocks that were down quite a bit and that corrected itself a little bit in October and unfortunately that market rebound we saw, the high quality names did just as well as these other names, but that relationship has evened out a little bit more starting in November and we've seen performance respond.

Hopefully the takeaway is we don't try to manage this on a quarterly basis, we don't do any predicting or forecasting on what the market is going to do from quarter to quarter, we think that just gets you in trouble. The idea that we have and this goes back to minimizing risk, is we have very strong risk controls because for a market like the 3<sup>rd</sup> quarter we're just trying to navigate it as best we can, we don't want to be 10% behind the benchmark or 15%. Like this is awful, it's a huge move against us if we can maybe just be 2 or 3% behind the benchmark at worst that helps us preserve the portfolio return over the long term.

Just to put it into perspective on slide 20, these numbers aren't performance numbers they are diversity measure, but what we saw in the 3<sup>rd</sup> quarter was if you think about it as a headwind or a tailwind as I mentioned, so if it's a negative number it's a headwind, if it's a positive number it's a tailwind. So going all the way back to 1966, looking at every single rolling 3 month period for over a 40 year period what we saw in the 3<sup>rd</sup> quarter was in the 3<sup>rd</sup> percentile move against us, that's how bad it was, there was only 2% of all the other movements over 40 years that were actually worse than what we saw in the 3<sup>rd</sup> quarter which goes back to what I mentioned and I showed you with the benchmark of how unusual and distinctive it was. So to have such a tremendous move of stocks against us and to only be about 1.3% behind the benchmark, you know we're never happy when we under perform but to navigate it that well we're very satisfied and we see that things are rebounding in November so far.

The other good piece that I'll end with and hope to give you some confidence is on page 22. Looking back at that same 4 year period what we did, this was just out of curiosity, this was research born out of the size of the move that we saw against us in the 3<sup>rd</sup> quarter, we said okay, if you take the top 5%, the worst 5% of declines in diversity so headwinds against us, what did the market look like afterwards? And you can see that following that quarter the worst 5% a quarter forward it was about flat as the market kind of took time to find its bearings, but one year forward and 3 years forward diversity reversed itself dramatically, so it turned into what would be a tremendous tailwind for us. So this gives us some confidence that after such an awful move, we'll see a bit of a boost in performance and we saw that after the tech bubble, we saw that after the financial crisis in 2008 as it turned around dramatically and it was a nice boost for our performance.

And that ends my formal comments, I want to leave plenty of time for questions and discussion. Maggie Ralbovsky: I thought when we met I thought we talked a little bit about transaction costs and monitoring and volunteering the use of an outside vendor to assess your efficiency in trading, would you just explain to the committee why that matters and how you use that information. Christian McCormick: Sure. As I mentioned, for INTECH in particular hopefully you really have a same level of scrutiny for your other investment managers, it's transaction costs are really this hidden piece. You have management fees, that's very obvious and out there in front, but transaction costs eat directly into the return of the portfolio and we have always felt strongly about having an independent group monitor just how we do in absolute terms but also if there's a best practices that another manager is using that we can somehow employ. The good news is we have found that we're the best practice model, many other managers can't duplicate the way we trade.

An overview is this mathematical model that we use assumes that trading costs will be 40 basis points of value of the portfolio. So that's the commission that we pay our brokers and that's the market impact, how much we move a stock by buying or selling it ourselves and as long as we're below 40 basis points, we can meet our excess return target. So the 2 go hand in hand. Once we get above 40 we start eating into our excess return target, we just try to minimize them.

On page 6 and 7 in that section you can see on a basis point perspective have our trading costs have oscillated over the years both in terms of annually and then we break it down over the last 4 years quarterly on page 7 and you can see a tremendous spike up from the 4<sup>th</sup> quarter of 2008. That actually wasn't due to commissions, that was due to how bizarre the market was and how volatile it was. As we put in an order to buy a stock at price X, 5 minutes later it was 5% different, it had changed dramatically so we still had to buy or sell but the price was just a lot different and that was why the trading costs spiked so dramatically. You see they came down and for all of 2010 and in the second half of 2009 we've really been in our historical averages, but our trading costs are well below that 40 basis points ceiling and we pay a fixed commission of no more than 5 basis points to the brokers that we trade with so anything above that is really due to market impact.

If you turn ahead to page 8, that breaks down that market impact commission combination. So you'll see the 5 basis points there that is the red bar and then the market impact which is that tan bar. Again market impact simply is if the model wants to buy X number of shares of GE and GE is trading at 30, because INTECH is large and we put in a big buy order for GE, we're going to move it away from 30. So market impact measures how far away from 30 we get it and the good news is we tend to be very close, we don't move it that much and that's a benefit of owning hundreds of different stocks is although we trade quite a bit we're trading small amounts in each stock so we tend not to have a lot of market impact.

We use an independent group called ITG, they use to be called Plexus and they do an external monitoring of our trading costs and then they compare us to other managers and the comparison is on page 13 and we do this annually and it's through December 31<sup>st</sup>, 2010, they compare us to 58 other large cap managers. So contrary to say a return graph that looks like this, here you want to be close to the bottom. That red diamond is where we've ranked quarterly going back to the 2<sup>nd</sup> quarter of 2008. A good comparison is in 2008 Q4 you can see that our trading cost did spike up but if you look at the size of the graph, just everybody's trading cost spiked up, we still remained in the bottom quartile so we want to be well below median but we expect to be around the bottom quartile of total trading costs

versus our peers and we are. Even though we rebalance often we're doing an effective job at keeping our costs relatively low and to make sure those don't eat into returns.

Maggie Ralbovsky: The reason I wanted to discuss trading costs partly was because the current IPS has a section director at brokerage. I know in practice it wasn't really strictly enforced, (can I use that word) but I want to bring to the attention of the Committee that maybe certain things in that policy we set historically, you may have lost relevance. The fact that most of the trading cost is not commission cost makes it important to look at in light of this kind of analysis and we know that Plexus is actually the firm that does this kind of analysis and maybe I'll put this back to you to tell us how you control the trading cost, like in practice how do you do that? Christian McCormick: In practice the way we do it is the biggest piece is we don't trade in any soft dollars, that's probably the biggest one and we don't really need it because we're a mathematical model. Soft dollars is maybe where you pay a little bit higher commission to a certain brokerage firm and in addition to trading with them, they give you research or they give you some other resource. For example, a firm may trade with Goldman Sachs and that may be more expensive but Goldman Sachs provides them with research on different sectors that they can use. We don't like it, we think it creates a conflict of interest and with the director brokerage the irony is usually what you're getting back is the soft dollars that you traded in. We compared our trading with other managers and even after their net trading cost from their director brokerage programs, we still came in lower than them just because you're just getting a piece of your soft dollars back. Maggie Ralbovsky: You're getting a piece of your commission back. Christian McCormick: Right. Maggie Ralbovsky: So the market impact cost could be higher so it's invisible to you and you thought you got the better deal because you got some money back but your execution is actually worse.

Christian McCormick: Right and the way we keep the execution in line is we use a group of 12 brokers and this is on page 9. This is the purest thing of free market capitalism that we have is we set those 12 brokers against each other and it's a very simple mandate, we're going to pay you the same commission, all of you the same hard commission, we're not going to pay you any soft dollars, we're purely going to evaluate you on how effective you execute our trades, so how low that market impact is. It's simple, we trade often enough, we trade frequently enough that we generate a lot of revenue just in our hard commission for these brokers and we say to them, if you're one of our top brokers, if you do our best execution, you will get most of our trading business in a month. So you can see on page 9 the top 3 brokers get about 37% of our trading business, the next 3 get about 30% and the remaining 6 only get 30% and although we don't provide names, we send each of these brokers monthly a name and where they appear on that list, so they know if they're number 10 or 11, if they don't work to get back up to number one or number 2, they're going to consistently see less business from us. The nice thing is it's an easy way for them to measure themselves and for us to measure them and all we care about is market impact to get that as low as possible, the lower you get it, the more money you're going to get, the more trades I should say.

Wilfred Leon Guerrero: That's very interesting, I thought brokers just buy stocks and sell stocks. Maggie Ralbovsky: It's not that simple. Christian McCormick: You've heard, it's just been in headlines, high frequency trading and dark pools, all of these fancy things going on, it would make it difficult for us to do it and we actually rely on the brokers to say, trade the best way you know how, but you're only going to get X amount of commission and we're not going to pay you any more or less we pay our other brokers, it's just volume. Wilfred Leon Guerrero: No, there's something missing here because you're evaluating their



performance and it just seems like their job is to buy stocks and sell stocks but you're saying... Christian McCormick: There are good ways and bad ways to buy and sell stocks. Wilfred Leon Guerrero: Okay, what are the good ways and what are the bad ways? Christian McCormick: Well, the good or bad ways could be where they're getting the stocks from, so if market impact isn't a big deal maybe just going back and again this is just hypothetical, as many examples you can use, maybe there is not a good broker, so maybe they make one phone call and say, I need to buy 1,000 shares in GE and the person on the other end says, okay I'll sell it to you for \$33 dollars and he says, okay I'll take it but in reality if he just called someone else, they would say, I would have sold it to you for \$32.90 and he could have saved 10 cents. Or, if it's a big brokerage house say like Merrill Lynch or Goldman Sachs, they may have stocks in their own inventories, stocks that they own and they're going to want to off load it at the most beneficial price to them, probably not to you, so the broker may just trade from their own inventory of stocks as opposed to going out and finding the best price for you as a client. So, without holding their feet to the fire, I don't want to use the term lazy, but they may not be using all the tools available to them to find the best possible price for you. It's just a question of that, who has the best price, is it for you as an INTECH client or is it for them as a broker.

And also it's not just like by desire, some of the trading costs are related to the efficiency of the technology. For example, you mentioned the higher frequency trading, there are people who have computers that can actually see your order before you trade the order, therefore they trade ahead of you, so those are the high frequency traders, they actually have a computer that captures, so Goldman Sachs, you're going to buy tens of hundreds of thousands of GE before you execute that trade, they already saw the order and they trade... (end of tape 3)

(start of tape 4)

Maggie Ralbovsky: ITG their job is to basically benchmark the whole thing, they get all the data so they can tell you which broker did better than other brokers. It is a service that many, many quant managers, quant managers tend to use this more because it's more important and easier to factor into their model. There are many invisible costs. Christian McCormick: Right. What brought trading down was decimalization, so I don't know if you remember, we use to trade at fractions and when you trade in fractions, even 16ths which is where they're trading at, you had a nickel kind of between the spread, they buy and sell spread that was quoted. When you moved to decimalization, that dropped down to a penny. It's funny, when the spread is a nickel so it's a difference between say \$30 dollars and 1/16 dollars and \$30 dollars and 2/16's and if you're right that's costing you a nickel per share when it dropped down the decimalization now it could just be a penny. So, if I want to buy GE at 30, exactly what Maggie (Ralbovsky) mentioned, will see that I want to buy GE at 30, they will jump in quickly and buy it themselves at \$30 dollars and a penny, that doesn't sound like too much of a big deal but if they do that repeatedly, just gain a penny on anything that they do, it makes it more expensive for me and they profit and so that's a way what we're evaluating our brokers on is hide our, how well do you hide our trades, not just buy or sell, but how well do you hide from the market what it is that we're trying to do by buying and selling. Joe T. San Agustin: You're basically monitoring yourself. Paula Blas: And you would measure that through marketing. Christian McCormick: Right and you would see the effect and we added a variety of things in addition, it's not just brokers, but when I mention the trading bands around each stock to determine rebalancing, those use to be fixed numbers plus or minus 10% so if GE was 5% of the portfolio and it went above 5.5 we would sell, if it went down to 4.5, 10% above or below we would buy or sell, but what we

found out is that we didn't see evidence of this, but Dr. Fernholz has always been paranoid about trading costs is that he's like, well if someone sees a buy order for GE on Monday and they somehow understand that it's INTECH, that probably means that we're going to be buying it on Tuesday and on Wednesday and on Thursday and on Friday as well. So that was kind of a tail that we had. So we mixed up the bands and added some things to kind of throw a monkey in so we're not rebalancing in any sort of pattern as a way to do it. He'll be the first to admit there are a lot of very smart people out there with advance --- that can pick this up and just because he can't see them doesn't mean they're not there, so we'd rather play it safe and hide it as best we can.

So it's good and I'm glad certainly that Maggie (Ralbovsky) has her eye on this, it's just this piece doesn't get a lot of publicity but it can really eat away into your returns if you don't watch it.

Wilfred Leon Guerrero: Does anyone else have anything? Ellen Lee: Do you want to touch on the market diversity because in the U.S. market, the small cap, large cap, the movement seems to be quite visible, but in terms of global, you mentioned the global equity, the global portfolio that exists too perhaps less obvious because it's more diversified but same principle applies to the global portfolio. Do you want to touch on that and talk about the difference? Christian McCormick: Yes and just that diversity graph, the one I showed you on page 19 if you look at international markets it looks exactly the same. Ellen (Lee) is right, the highs and lows tend to be more tempered, but it's funny, there are so many cyclical things in the markets, growth versus value, international versus U.S., where these groups just switch off, which ones are out performing the other. Size it's the same thing, within a benchmark you have periods of time where the larger mega cap securities are doing well and periods of time where the smaller mid-sized caps names do well and the same holds true internationally, again the highs and lows are a little bit tempered but it switches back and forth and you get that same phenomenon and that affected our portfolios in the 3<sup>rd</sup> quarter, our global and international portfolio really in the same way as well.

Wilfred Leon Guerrero: Okay, any others? (No). Thank you very much. (end of tape 4)

### **3:00pm-3:45pm Atalanta Sosnoff**

(start of tape 5)

Kamani Kuala'au: Thank you very much for having us and it's good to see you every year. As you know already we have our President out here, Craig Steinberg and I'm sure you want to hear from him and I'll let him jump into the presentation. Craig Steinberg: Well this is my 4<sup>th</sup> visit here and it's good to see some familiar faces. For the people who aren't familiar with me my name is Craig Steinberg and I am President and one of the 4 portfolio managers at our firm Atalanta Sosnoff. I realize we only visit you once a year so just to reintroduce you to the firm, I put together what I feel are the important points which is on the first page of the presentation that we sent to you.

We manage about \$8.5 billion dollars of assets and I think what's important to understand about Atalanta Sosnoff relative to our size is that we're single focused in essence a single product firm. We don't have a small cap fund, a mid cap fund or an international fund, we try to do one thing, large cap equities to the best of our abilities. I think another important thing about Atalanta Sosnoff is that we've been doing this for a very long period of time. The 4 senior money managers at Atalanta Sosnoff as a team have been together for over 10 years

now and if you look in the middle column of these performance numbers this is what those 4 people produced over that time period. The founder of the firm Martin Sosnoff and myself have been working together for over 25 years and our equity composite returns that we've accomplished are on the right. So it's a firm that focuses on a single thing, large cap equities and we've been doing it for a very long period of time.

The other thing about the firm that's probably important to tell you is that all of our company sponsored retirement assets are invested identically to our clients, so all of our retirement plans are invested identically to your retirement plan.

A couple of other things in terms of the investment style, if you look on page 2 what I think in terms of style is what makes us unique is we focus on something called earnings acceleration. Not only do we want to own individual companies where there are strong business prospects and a good outlook for growth, we try and take that concept one step further which is that not only do we want to have a strong outlook for growth, we want to buy those individual companies where we see events like a change in management or a new product introduction which could make the growth rates accelerate, make them higher going forward and when investors see earnings acceleration they tend to reward that step up in growth with higher valuation. So that's our specific style it's earnings acceleration in large capitalization growth companies.

The way we implement that in terms of portfolio management is on page 3 and in our opinion there are a lot of different approaches to portfolio management. In essence we're competing against an index, the S&P 500 and many managers you will see have a large number of stocks that look very similar in terms of the weighting compared to the index and it tends to be called closet indexing. We have a very different approach, we believe that to add value above the index over time, one has to be willing to make the composition of their portfolio different than the index. So what you see with us and we've always done this is the way we implement our style of earnings acceleration at the portfolio level is typically 40-45 stocks and we will invest in industries and sectors on a thematic basis. So I think it's important to understand is not only are we an active manager, we're one that has the courage of our conviction and we're willing and over time have added value by having our portfolio be significantly different in this composition than the index.

If you look on page 4 this shows you as we were directed to show you, this is our performance for the fiscal year ended September 30, 2011 and what you can see is that we were down and we under performed the S&P 500. To give you an October update, we rebounded with the market and slightly under performed in the market and then in the November update I will tell you that November has been a very volatile month but we were doing better than the S&P 500 half way through October.

So, since the market's bottom early in 2009 we have had a major head wind in terms of our performance but it's one of the factors that has caused us our under performance in the last 2 years.

If you look on page 5 what you can see is this is a history of the stock market, the S&P 500 over the last 4 years and I think very hard to predict, but looking back over the last 4 years what you really see is a big V, we have just got back to where we've come to, but the composition of the market in these different environments has had a dramatic impact on our relevant performance and in this up portion of the market cycle what you've seen is that

lower capitalization, lower quality stocks have actually out performed and this has happened at market bottoms in the past. The reason for this is that one, these stocks are most beaten up in the down portion of the market so they're spring loaded to out perform when the market recovers. So this up portion of the market which has been the portion where we've under performed, we've significantly out performed in the prior portion, we've had a disadvantage if you will, in terms of having always operated in large capitalization high quality stocks.

To give you a sense of quantifying that impact, if you look on page 6, when I mention that we own and always have owned large capitalization stocks, to define that the weighted average market cap of a portfolio today is over \$100 billion dollars and historically we've always felt it's been our mandate to operate in the \$80-100 billion plus area. When you look at how these stocks have done over the last couple of years, what we did was we looked within the S&P 500, the index that we're competing at and what you can see is a very clear pattern of how stocks have done has largely been determined by how big their market cap has been. We're operating in the far left here and if I can draw a line down the middle of this chart I would say even to the far left of that and what you can see is that since the market's bottom in early 2009 these stocks are only up about 59%. If you go to the next tranche it's up 78% and if you go all the way to the extreme it's 172%.

One of the factors and I don't want to say it's the only factor, but one of the factors in our under performance is that the type of stock we invest in large cap high quality hasn't done well in this portion if you remember this portion of the cycle. We always operated in big cap stocks and we're not going to change our stripes because they under performed for a year or 2. What you see is that historically we've done very well on a relative basis in down markets and one of the factors is that big cap stocks tend to have the liquidity to hold up better than others in the down market. Maggie Ralbovsky: How does that explain the 3<sup>rd</sup> quarter of this year, small cap significantly under performed and high quality significantly out performed so why did you under perform? Craig Steinberg: I think that the biggest issue for the 3<sup>rd</sup> quarter this year is really on the next page, page 7 which is that the other factor particularly as of late, is that on account of your basis we entered the year with a much too optimistic point of view in terms of economic growth. In other words, if you go back to January and February the U.S. economy was producing over 200,000 jobs per month, interest rates at that point in time were rising and we felt we were in a self sustaining economic recovery. If you track the relative performance of our portfolio what you saw is that we first started to under perform when there was a spike up in oil prices and that was largely due to the unrest in the Middle East. In addition to that there was that there was the earthquake in Japan which disrupted supply chains. In other words there were a variety of... we had a portfolio that was positioned for a much higher economic growth setting than what actually transpired and there was a variety of events which I think depressed economic growth.

So the problem for the better portion of this year and including the 3<sup>rd</sup> quarter, was that we had too optimistically positioned portfolio and when you analyze the relative performance what you can see is that the under performance came from 2 factors. One, because defensive sectors like healthcare, consumer staples, because none of them exhibit our criteria of our acceleration we're very under weighted in those sectors and as economy slowed down and the market toughened, investors sort of moved into defensive sectors. We were under weight in those sectors and that accounted for about half of our under performance. The other half is as I said, we had a portfolio tilted towards economic growth and that was too optimistic so some of our investments were more economically sensitive sectors like the

autos here for example also under performed. So I think that primarily this year a significant factor in our under performance is that we were too optimistic in terms of what happened to the economy.

We realize that was wrong and if you look on page 8, we've made adjustments to the portfolio and very logically since we were too optimistic what you've seen is we reduced our exposure to the more economically segments of the economy. So we've reduced our energy exposure, we've reduced our exposure in industrials and in materials, these are probably the most economically sensitive segments within the S&P 500.

When you look at the portfolio today on page 9, on a sector basis we're over weighted in the technologies sector which is in essence really a function of individual stocks which helps take you through, also the consumer discretionary individual stocks. The actual portfolio industry by industry and sector by sector is on page 10, but I think what might be more useful for the Board is if you look on page 11. As I said, we were too optimistic in terms of economic growth that was wrong and we've repositioned the portfolio. When you look at the portfolio today it's clearly positioned for a much slower economic growth, it's not positioned for a recession, but it is positioned for slower economic growth and I think that there are 3 thematics in the portfolio today that we think will enable it to out perform going forward. The first one is in the upper left and with a lack luster economic setting, what we've tried to do is to concentrate on individual companies where whether it be because of market share gains or product introductions, they can grow through this slow economic growth and deliver high double digit type earnings. You have to go name by name, but those stocks are on the upper left.

The next thematic within this portfolio is differentiation at the sector level. If you look at the various sectors within the S&P 500 what you can see is that there is some significant concentration in our portfolio in the aerospace industry, the pharmacy benefits, the managers, the HMO's and oil services and agricultural companies, all sort of thematics within the sector.

The last pillar of this portfolio transcends a variety of sectors and what we've done is focus in on individual companies that have the income strength and balance strength to create their own earnings growth largely by share buy back. In other words, I think everyone has seen countless articles about how cash rich corporations are. What we have tried to do is take that one step further and identify the individual companies where the management has this vision and is taking it forward by buying back significant amounts of stock. As an example, Direct TV, the satellite provider, if our analysis is right we believe that in the next few years they have the capacity to shrink the shares outstanding by over a third which will directly translate into higher earnings per share.

So I think that the 3 pillars of this portfolio is first the high sector growth companies, second, thematics within the sectors and last this overall thematics of finding companies that can manufacture their own earnings growth in a very challenging overall economic setting.

If you jump to page 13, as I mentioned before we're not closet indexers and we thematically invest and we're willing to be different than the index. I think for a long period of time and I can show you the numbers, we've added significant value to that, however, we're not always right so what this shows you is our performance over a variety of periods of time and what you can see is just like we've under performed in 2010 and 2011, the fiscal years there have

been other periods of time in the past where we under performed, however in the ensuing time periods we've come back and out performed the market. So, it's not uncommon for us and I think you'll find this with other active managers or focused or concentrated managers, there are periods of time where you significantly out perform, but you don't always get it right and there are periods of time where you under perform. When you put it all together, if you look on page 14 what you can see here is this is our track record for your account inclusive of the tough period of performance, relative performance we've had for the last 2 fiscal years. What you can see is there are periods of time when we have gotten it right, there have been periods of time when we've gotten it wrong, but when you put it all together and net the 2, what you can see is that over 5, 10, 15 and 20 years we've out performed our index. It hasn't always been a straight line, but over longer periods of time we've significantly out performed the index and it's been a very long term relationship.

If you go to page 15... Maggie Ralbovsky: What's BCIGC? Craig Steinberg: That's the Barclays Intermediate Government Index. At one point in time this account was a balanced account, that goes back over a long period of time, but this is the performance on an inception to date basis.

So just to try and summarize, I think after very outstanding track record relative to the index, we've under performed over the last 2 years. I think part of it has been being a large cap manager has been a head wind, I think that's changing and large cap stocks are now starting to out perform and secondly earlier this year we got our top down call wrong which is created under performance, but as I said we've repositioned the portfolio. When we look at the repositioning of the portfolio I think there are 3 critical points, one are those high secular growth stocks, 2 is differentiation at the sector level and 3 the thematic of companies creating their own earnings growth by buying back stock and taking other action.

When I look at the longer term track record that we have, I have a lot of confidence. There have been other periods of time like this where we've under performed and you've always seen us come back and then some in the past, so even inclusive of these last couple of years which has not been good, we have been able to add value. It's not unexpected that we go through some tough periods of time because as I said, we're not a closet indexer and we tend to focus and you don't always get it right.

So with all that said let me open it up to questions. Maggie Ralbovsky: Did you have any outflows recently? Craig Steinberg: Yes, we have had about a billion dollars worth of outflows this year. Very typical, we've seen this in the past, it's very typically if you're familiar with accounting it's last in, first out, the most recent clients tend to leave you first. Also happens to be heavily retail investors.

Maggie Ralbovsky: Do you have an update for the 2<sup>nd</sup> half of this month, I know you updated us to the first half of this month. Craig Steinberg: I do not have specific numbers. What I can tell you is that I've never seen a more volatile environment. On Monday the market was up 3% and the week before I think it was down about 3% and relative performance is almost a day to day type of thing in that type of environment.

Wilfred Leon Guerrero: Any SEC issues, regulatory agencies? Craig Steinberg: No. Gerard Cruz: Management changes? Craig Steinberg: No. This investment team has been together over 10 years. This has been a very long term relationship one that we value very much and

we thank you for your support and for your patience, it goes back to 1986 and I go back to 1985 with the firm. Wilfred Leon Guerrero: Thank you. (end of tape 5)  
(End of presentation by Atalanta Sosnoff)


**Respectfully submitted,**

**Affirmed:**



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**Stephanie A. Herrera**  
**Recording Secretary**



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**Wilfred P. Leon Guerrero**  
**Chairman**

