

Institutional Small Cap Value Strategy

2Q10

Market Review

The second quarter was a tough period for stocks. The Russell 2000 Value index lost 10.60% for the quarter. The sectors that detracted the most from performance were those that lead the rally into late April: Financials, Industrials and consumer discretionary. With this decline, we saw the end of outperformance from very small lower quality companies, which have dominated performance from last year's low. Given the rich valuations and poor fundamentals for low quality stocks, we expect this trend to continue. In turn, higher quality, larger small-cap companies with solid fundamentals and attractive valuations may begin to outperform

Portfolio Highlights

During the second quarter of 2010, stock selection and interaction in the consumer discretionary and financials sectors contributed to relative performance, whereas stock selection and interaction in the industrials and materials sectors detracted from relative performance.

Relative to the Russell 2000 Value Index, at the end of the second quarter the Strategy's largest overweight positions were in the industrials and health care sectors. The Strategy's largest relative underweight positions at the end of the period were in the financials and utilities sectors.

During the quarter, we added new positions to the Strategy portfolio in Diana Shipping Inc. and Hudson Highland Group Inc. in the industrials sector, LaSalle Hotel Properties and Stifel Financial Group, both in the financials sector, Natural Gas Services Group Inc. and SM Energy Co. in the energy sector. We sold out of existing Fund positions in Kaiser Aluminum Corp. in the materials sector, Portland General Electric Co. in the utilities sector, Rush Enterprises Inc. (Class A) in the industrials sector, and St. Mary Land & Exploration Co. in the energy sector.

“We believe the resiliency of the U.S. will be on display in the next few quarters and that employment and corporate earnings trends will be positive.”

John Goode Managing Director, Senior Portfolio Manager

- 41 years of investment industry experience
- MBA from Stanford's Graduate School of Business
- BA in Economics from Stanford University

Peter Hable Managing Director, Senior Portfolio Manager

- 27 years of investment industry experience
- MBA from the Wharton School at the University of Pennsylvania

The top contributors to Strategy performance for the second quarter included National Dentex Corp in the health care sector, Meadowbrook Insurance Group Inc. in the financials sector, Lawson Software Inc. in the information technology sector, Thomas Weisel Partners Group Inc. in the financials sector and Genesee & Wyoming Inc. (Class A) in the industrials sector.

The leading detractors from performance for the second quarter included Artio Global Investors Inc. (Class A) in the financials sector, Callaway Golf Co. in the consumer discretionary sector, Tutor Perini Corp. in the industrials sector, Mueller Water Products Inc. in the industrials sector and Affiliated Managers Group Inc. in the financials sector.

PORTFOLIO MANAGER COMMENTARY



Outlook

We believe the resiliency of the U.S. will be on display in the next few quarters and that employment and corporate earnings trends will be positive. There has been a tremendous amount of stimulus, from both monetary and fiscal initiatives, in the last year. This is highly likely to have a positive impact on most of the metrics used to measure economic progress.

Our emphasis continues to be on economically sensitive sectors such as industrials, consumer discretionary, information technology, energy and materials sectors because these are likely to show above average earnings improvements over the rest of 2010. We also believe many financials will do well. Where commercial banks are concerned, we are at or just past the period where loss provisions may have peaked. Historically, this segment of the financials sector has performed well when this has occurred.

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