

Small- and Mid-Cap Core

Fourth Quarter 2008 Investment Update

In hindsight, the government's decision last September to allow Lehman Brothers to fail was a watershed event. Shock waves were felt throughout the global financial system with economic repercussions in all corners of the world. Investors had assumed that the U.S. government, with the help of other central banks, would do whatever it took to support financial markets and economies. The failure of Lehman Brothers caused already tight credit markets to freeze as no lender could be confident it knew a borrower's exposure to counterparty transactions. Without capital markets functioning well, corporations and consumers immediately cut back on spending. A difficult, but relatively stable, labor market quickly turned ugly and layoffs surged. 4Q GDP growth is expected to be one of the worst quarters on record and corporate earnings and future guidance are coming in well below consensus expectations. Markets around the world plunged by record amounts.

Small Cap Core: 2008 was the worst year ever for the Russell 2000 which was down 33.8%, and the worst year for small cap stocks since 1973 which were down collectively by 34.4%. Your portfolio declined roughly 29% putting us between 450 and 500 basis points ahead of our benchmark despite trailing by about 250 basis points in the fourth quarter. There is little to feel good about in a year like 2008 but we are proud to have delivered significantly better performance than our benchmark. We are all invested in our products along side of our clients so we take little solace from this result.

Summarizing the year, the Russell 2000's decline of 33.8% was better than both the S&P 500 which was down 38.5% and the Russell Mid Cap Index which declined 41.5%. Despite a U.S. recession, a global slowdown and a bear market, small cap stocks were the best performing U.S. equity asset class. The value index was down 28.9% compared to a 38.5% decline for the growth index.

Summarizing the fourth quarter, small cap stocks declined by 26.1% and continued to outperform the Russell Midcap Index which declined 27.3%, but lagged behind the S&P 500 which declined 22.6%. The Russell 2000 Value Index outperformed the Russell 2000 Growth Index by 250 basis points in the quarter (down 24.9% versus down 27.5%). No Russell 2000 sector showed a positive return for the quarter with only consumer staples (down 14.5%) and utilities (down 12.0%) down less than 15%. Financial services declined 16.8% with all other sectors down at least 20%. The worst performing sector in the quarter was energy which declined 50.7%. Producer durables (down 33.4%), REITs (down 32.2%) and consumer discretionary (down 30.5%) all declined more than 30%.

Our stock picks in materials and processing and financial services contributed positively to our performance relative to the index. Our stocks in consumer discretionary, autos and transportation as well as technology were our biggest detractors relative to the benchmark.

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Mid Cap Core: The 41.5% decline in the Russell Mid Cap Index in 2008 was the worst year in its 29 year history. Your portfolio declined roughly 43.9% putting us about 200 basis points behind our benchmark. This result followed a fourth quarter in which we trailed by between 100-150 basis points. There is little to feel good about in a year like 2008. We are all invested in our products along side of our clients so we appreciate how disappointing these results are.

Summarizing the year, the Russell Mid Cap Index was the worst performing size sector. Its decline of 41.5% trailed the Russell 2000's decline of 33.8% and the S&P 500's negative 38.5% return. Despite a U.S. recession, a global slowdown and a bear market, small cap stocks were surprisingly the best performing U.S. equity asset class. Given their out-performance, it is also surprising that mid cap fared so poorly relative to large cap stocks. In terms of style, the value index was down 38.4% compared to a 44.3% decline for the growth index.

Summarizing the fourth quarter, The Russell Midcap Index declined 27.3% and lagged behind both the Russell 2000 which declined by 26.1% and the S&P 500 which declined 22.6%. The Russell Mid Cap Value Index and the Russell Mid Cap Growth Index performed virtually the same, down 27.2% and 27.4% respectively. No Russell Mid Cap sector showed a positive return for the quarter with only consumer staples (down 17.2%) and utilities (down 14.3%) down less than 25%. The worst performing sector in the quarter was energy which declined 40.1%. REITs (down 38.1%) and consumer discretionary (down 30.2%) were the two sectors down more than 30%.

Our stock picks in financial services, materials and processing, consumer staples and producer durables relative to the index contributed positively to our performance. Our stock picks in consumer discretionary, energy and technology relative to the Russell Mid Cap Index led to most of our underperformance.

There is no doubt that the global economic environment remains extremely difficult as we start the year. Government policy decisions yet to be made will be a major determinate in whether the economy begins to recover in 2009 or whether the malaise drags into 2010. That said, there are many stocks in this market that are attractively valued and would now appear to be discounting worst case scenarios. This is a stock pickers' market and as stock pickers we are excited about the new investment ideas we are seeing each day. As always, our job is to find the most attractively valued stocks with intermediate catalysts and a management team that can execute on their plan in this type of environment.

As the year came to a close we let you know that the Boston investment team will be moving to Evercore Asset Management as of February 1, 2009. We are excited about this opportunity and believe Evercore presents a good cultural fit for us. Evercore understands and appreciates the team approach to portfolio management. They are fundamental, bottom up stocks pickers in the deep value segment of the small and mid cap space and we

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believe the way they manage money will be a nice complement to our relative value approach and provide a supportive environment. From an investment standpoint, nothing will change. We will continue to manage your portfolio with the same people, style and discipline. We will continue to use valuation, catalyst, and management as the core of our investment evaluation process which we have used throughout our history. We appreciate your support through this transition and look forward to reporting back to you at the end of the first quarter from our new home.