Evercore | Asset Management

Third Quarter 2009
Investment Update

More than anything else the third quarter of 2009 was marked by a feeling that the worst had passed. Industrial America might not be booming, but earnings seemed to have bottomed. The credit markets might not be free flowing, but rates fell steadily and access to the markets improved. The unemployment rate remains high, but the pace of new layoffs eased. Hardly the ingredients for euphoria, but against the base case in early 2009 of a pending economic doomsday, simply believing that the worst had passed was enough to send stocks soaring, rewarding those who took the contrarian position and remained committed to their investment processes.

As a result, thus far 2009 has been a good year for our clients. With gains in the third quarter adding to those realized earlier in the year, our Small-Cap Core and Mid-Cap Core services have risen (net of fees) 33% and 37% respectively.*

Thus far, however, the improvement has been fairly quick and forceful, largely, we believe, a function of increasing P/E ratios produced from a realization that some of the worst case scenarios seem to have been taken off the table. Going forward, we would look for a more graceful and tempered trend driven by actual earnings improvements and, in the case of financial stocks, a clear leveling off of bad loan reserve additions.

Our Firm

At Evercore Asset Management we focus first and foremost on achieving superior returns for our clients. We build concentrated portfolios of small- and mid-cap companies, one stock at a time, through extensive fundamental research. Our portfolios consist only of companies that we believe have outsized opportunity to appreciate in value. We strive to build long-lasting client relationships through consistent portfolio management and timely, straightforward communication.

Moreover, we wouldn't be surprised to see a period where performance goes sideways or at some point we experience a temporary retrenchment. After all, it's not as if the current economic underpinnings are all that solid. In particular the employment outlook remains worrisome (which should act as a deterrent against any sharp rebound in consumer spending, the source of most previous recoveries) as does the potential for companies to continue to recapitalize themselves through dilutive equity offerings as they seek to insulate themselves from a repeat of the trauma of the past two years.

As we reflect on the drama of the past 18 months, we have been considering whether any lessons can be learned from the way this cycle has played out thus far—staying mindful of the pitfalls of attempting to learn too much.

*For notes on performance please refer to the disclosures at the end of this presentation

Setting aside some of the obvious ones (e.g., beware the financial instrument that is hard to explain) and some things better left to Washington (e.g., financial services industry regulation), at least three come to mind.

First, fundamental research mattered more in this cycle than at any point we can remember in the past twenty five years. At the mid-winter nadir, many investors were envisioning near apocalypse. Entire industries (most notably banking) were declared beyond resuscitation. Seizing the investment opportunity, therefore, required a tremendous amount of courage and confidence in one's research. For those that did the research, it was the resulting confidence that allowed them to stick to their discipline and even add to their positions during the gloomiest moments. More often than not, a failure to do this leads one to suffer on the way down, capitulate at the bottom and miss the reward on the way up. It is a formula for systematic underperformance.

Second, for the inherently fundamental manager, the use of quantitative tools should be limited to initial idea generation rather than risk reduction, whether relative or absolute. For the third cycle in a row (1990-1991, 1999-2000 and the current one), such models have failed to protect investors and have even, arguably, exacerbated poor performance. In part, we suspect this is because they fail to understand newly emerging correlations, a testament to the fact that each cycle is unique. In part, we think these models have a hard time understanding leverage or, put another way, distinguishing between the market's perception of equity value and the market's perception of enterprise value. It's difficult to have much faith in buying a collection of attractively priced stocks if the book value is subject to evaporation because it is conjoined with a mountain of debt.

Third, the impact on the markets of human emotion is alive and well, perhaps even increasing in significance. We see the advent of new investment vehicles such as ETF's, as a problematic development especially when combined with the tendency of many investors to be backward looking. Theoretically these vehicles are acting to democratize the market by allowing investors a low cost way to make a diversified bet on a particular sector or segment of the market. As a practical matter, however, they seem to be adding to volatility as investors pile in from one sector to the next seeking to ride waves of market momentum. The surge in energy-related stocks in the second quarter of 2008 is perhaps the best recent example. Our bet is that the market has become permanently more volatile, in part, as a result of this tool.

Finally, investors should be careful about taking any of the lessons learned too seriously. Wall Street has a knack for never losing the same war twice. Unfortunately, the same war is never fought twice. Each cycle brings with it its own unique set of facts, twists and turns. When all is said and done, we think most investors would be best served by choosing a strategy and then sticking to it by hiring a collection of managers that are unique, committed, articulate and drift-proof. Once done, don't try to add value by over-managing the collection along the way.

Below we discuss the current positioning of our Core investment services.

Portfolio Strategy: Small- and Mid-Cap Core

As relative value investors, we have been hearing the question "are stocks still cheap?" In the latter half of 2008 and early 2009 the answer was simple—we had never seen so many companies trading at such attractive valuations. During this period we opportunistically added 18 new names and in the process upgraded and repositioned the portfolio. Our services benefited from these moves during the second and third quarters of 2009 as our early cyclical posture responded well to the market's anticipation of economic recovery. As a result, our portfolios have experienced strong net of fee returns year to date with Small- and Mid-Cap Core exceeding their benchmarks by about 10% and 5% respectively. During the third quarter we achieved positive net of fee absolute returns, with both services up about 18%, slightly behind their benchmarks.* Today, as we evaluate the question "are stocks still cheap", the answer is not as obvious. While we continue to add names with very attractive reward to risk ratios, wholesale cheapness across all sectors has come and gone.

The biggest contributors to performance in the quarter came from our investments in pro-cyclical sectors, particularly Energy and Professional Services. In prior quarters we built positions in names that were levered to the natural gas market. Natural gas prices have dropped from approximately $13 per thousand cubic feet to under $4 over the past year. As a result, companies who were in the business of drilling for natural gas saw their stock prices decline significantly. Our research led to three companies within this segment**: Carrizo Oil & Gas (CRZO), Saint Mary's Land & Exploration (SM)** and **Comstock Resources (CRK)**. There are three common themes for these investments: high quality assets, focus in the fastest growing part of the natural gas market, and natural gas prices, we believe, near or at bottom with likely increases over the next six to twelve months. During the quarter, as the market started to anticipate higher natural gas prices, both Carrizo Oil and St. Mary's experienced large upside moves. Comstock had a strong return, but underperformed its peers due to investor concerns about a potential acquisition. Comstock is a conservative company and we have confidence that if an acquisition is completed it will be executed in a shareholder friendly fashion. We continue to hold shares in all three companies and believe considerable upside potential remains.

Professional Services was another area of strong performance for the quarter. In this category, **Monster Worldwide (MWW)** and **Kelly Services (KELYA)** contributed significantly. Both companies are in the business of professional recruiting and as employers made sharp cutbacks in jobs in late 2008 and early 2009 their stocks underperformed. The stocks recovered in the third quarter as investors sensed that the economic bottom was near, and employment numbers started looking less bad. We continue to maintain these positions and believe they will benefit as a recovery in the business cycle advances.

One area of the market where we have been under represented is in Financials, and more specifically regional banks. Although not a top-down decision, we feel that many financial institutions are still in the early innings of recognizing their loan problems and potentially dilutive capital raises may continue to hurt earnings. Furthermore, with many smaller banks getting 25% or more of their earnings from excessively rapid loan growth in recent years, it's hard for us to see how they are going to fill this hole in the future. Even with this conservative

*For notes on performance please refer to the disclosures at the end of this presentation outlook, we did add one regional bank to our Small-Cap Core portfolio in the third quarter, **Eagle Bancorp (EGBN)**. Eagle's business is focused in and around Washington D.C. The real estate market in D.C. has stabilized and the economic outlook is healthy on the back of larger government and more government spending. Eagle has already raised capital and is putting it to work very profitably. The company has a 1% market share and therefore has plenty of room to grow without attracting competition. Eagle's management owns 24% of the company, which is an important element to us, and the stock is trading approximately $1 above its tangible book value. With its attractive valuation, growth prospects, and proven management team we are very excited about this investment.

As investors shifted their portfolios to have a more pro-cyclical, pro-recovery posture, sectors and holdings deemed to be more defensive generally underperformed. While on the pro-cyclical side we too were beneficiaries, we did see some offset from our defensive holdings most notably in Healthcare and Consumer Staples. Within Healthcare, **Analogic (ALOG)** was a notable detractor. The company has two core businesses: MRI and CAT scan equipment parts and airport security scanner components. There was softness in the stock this quarter due to a lack of spending on big ticket items, specifically by the TSA (a division of Homeland Security). Analogic has a new CEO, $15 million in cash to grow the business and increased TSA spending, we believe, on the horizon. We remain confident in the investment and hold it close to a full 3% weighting in the portfolio. Within the consumer space, we started buying **Smithfield Foods (SFD)** in the second quarter as we believed the supply/demand imbalance and resulting economics in the pork industry were close to their trough. Continued weakness in pork prices created selling pressure in the stock during the quarter. The company is keenly focused on cutting back supply which will continue to aid pricing in the coming quarters. We believe this uptrend in prices combined with global demand for pork will realign the positive economics of the business and Smithfield Foods will be a large beneficiary.

Portfolio Overview

	Periods Ending 9/30/2009				
Performance	MRQ	YTD	1Year	3Year	5Year
Small-Cap Core	**18.2%**	**32.8%**	**-6.0%**	**-1.5%**	**5.1%**
Russell 2000®	19.3	22.4	-9.5	-4.6	2.4
Excess Return	-1.1	10.4	3.5	3.1	2.7
Mid-Cap Core	**17.5**	**37.4**	**-1.7**	**-2.2**	**7.3**
Russell Midcap®	20.6	32.6	-3.5	-4.1	3.9
Excess Return	-3.1	4.8	1.8	1.9	3.4

Net of management fees

Periods greater than one year are annualized

For notes on performance please refer to the disclosure at the end of this document

Portfolio Characteristics	Small-Cap Core	Mid-Cap Core
P/E (ex. negative earnings)	19.1x	18.9x
P/B	1.5x	2.0x
Dividend Yield	0.9%	1.4%
Wtd. Avg. Market Cap.	$1,236 mm	$6,686 mm
Number of Holdings	36	34

Source: Evercore Asset Management and BNY Mellon Asset Servicing

Disclosures

The securities discussed above were holdings during the quarter ended September 30, 2009. The stocks we elect to highlight each quarter will not always be the highest performing stocks in the portfolio, but rather will have had some reported news or event (e.g. new contract, acquisition/divestiture, financing/refinancing, revenue or earnings, changes to management, change in relative valuation, plant strike, product recall, court ruling, etc.) of significance. They do not represent all of the securities purchased, sold or recommended by the advisor, and the reader should not assume that investments in the securities identified and discussed were or will be profitable. All information is provided for informational purposes only and should not be deemed a recommendation to buy the securities mentioned.

All investments involve risk including the loss of principal. The performance and volatility of an index may be materially different from that of a client's account. In addition, a client's holdings may differ significantly from the securities that comprise an index. The indexes have not been selected to represent an appropriate benchmark to compare the advisor's performance, but rather are disclosed to allow for comparison of the advisor's performance to that of a well-known and widely recognized index.

Core Performance Disclosures:

1. The Small-Cap Core and Mid-Cap Core Composites comprise discretionary accounts with no material investment restrictions. Net of fee performance results reflect the deduction of fees according to the applicable investment advisory fee schedule. The results include all interest, realized and accrued dividends, capital gains, capital losses and brokerage commissions. Composite results prior to February 1, 2009 are based on aggregated data at the product level. Results following that date are based on asset weighted returns. Asset weighted performance measures the average performance of all portfolios in the composite weighted by size. Performance results for individual accounts vary due to the timing of investments, additions/withdrawals, length of relationship, and size of positions, among other reasons. Past performance is no guarantee of future results.

2. Composite Inclusion: Accounts that are fully invested as of the last day of the month are added to the Small-Cap Core and Mid-Cap Core composites at the beginning of the following month. Composites include terminated accounts for all full months under management.