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# Chartwell Consulting

## Sample Client Performance Report

**Fourth Quarter 2002**

*Performance Summary & Asset Allocation Review*

*Presented by:*

*Chartwell Consulting* 

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## Market Update

### ECONOMY

Three very significant events occurred during the latter half of the 4<sup>th</sup> quarter, although their effects will not be evident for some time –

- (a) The Federal Reserve cut its target for Fed Funds, to 1.25%. The European Central Bank also cut its target for overnight funds;
- (b) The Fed signaled a major policy shift, confirming they were willing to take various unprecedented steps to combat deflation;
- (c) The Bush Administration began laying out its ideas for a significant tax cut, including the elimination of taxes on dividends;

December's report from Commerce indicated real GDP grew at an annualized rate of 4% during the third quarter, making the cumulative one-year advance 3.25%. That is very close to the long-term average for annual GDP growth. However, the prospect of a slowdown in consumer spending, the primary component of GDP growth, has investors worried.

For the third quarter in a row, corporate inventory accumulation added to GDP growth. Even so, the broad Inventory/Sales ratio declined to 1.36x in November (lowest figure in eight years). This represents a very favorable pre-condition for increasing production in 2003. Corporate investment on equipment rose for the second straight quarter (+6.7%). Industrial production was up only 2.1% in 2002, and capacity utilization edged up to 75.4%. Corporate fixed investment will not add much to GDP growth until the capacity utilization figure approaches 78%.

Our negative trade balance currently detracts 5.0% from annual GDP. It has placed a 0.6% annual drag on our GDP growth since 1998. Only personal consumption has had more impact on GDP. Through the first eleven months of 2002, our trade deficit increased 18% versus 2001. A weaker Dollar *should eventually* cause the volume of imported goods to drop and exports to rise (thereby adding to GDP growth).

Current estimates are for 4<sup>th</sup> quarter corporate profits of the S&P 500 companies to rise 24% versus 4Q01. This would be the fourth straight quarter of moderate year-over-year profit growth, leading to a 19% increase for the full year 2002.

### FIXED INCOME

A 50 basis point Fed Funds rate cut in November helped push short-term rates down by 20-35 basis points. Conversely, investors were net sellers of long term T-bonds during the quarter, and their yields rose 20bps. All "low risk" bond market sectors produced negative returns in October and November, because coupon income was not high enough to offset the price declines caused by modestly rising interest rates. A sharp rally ensued in December, as interest rates again retreated. Overall, investors favored the higher coupons offered by bonds rated "A" or lower, and credit spreads narrowed. The end result was a strong quarter for higher risk securities, but low returns otherwise.

The high-grade bond markets have been strong for investors over the past three years, but rising prices have left this area with very low yields entering 2003. Money market funds will return less than 1% this year. Intermediate term government securities (26% investment grade bonds) yield an average of only 2.3% per annum. Mortgage-backed bonds (35% of the universe) only yield 4.6% to investors. The low investment grade (“BBB”) sector enjoys an average yield of 6%, but “AA” or better corporate bonds yield less than 4%. At this stage, only non-investment grade bonds offer high yields, with “top quality” junk bonds paying 10-11%.

### **U.S. EQUITY**

The S&P hit its current cyclical low of 776.76 on 10/9, and then began an eight-week, 20%, rally through November. Despite a weak December, an 8+% quarterly return was the overall result. The quarter’s advance was decidedly led by technology, telecom, and other business cyclical stocks, and not by consumer-related firms. Market strategists typified the 4<sup>th</sup> quarter’s advance as a positive vote on the prospects for a business-led economic recovery.

The quarter’s rally was broad-based from a market cap perspective. Stocks over \$1bn in market cap performed similarly well, and stocks under \$500mm posted double-digit returns. Stocks in between, comprising just 4% of the total market but a majority of the small-cap index, underperformed. Style leadership rotated at the top, as large value again outpaced large growth.

The full year 2002 stock market will be remembered as the most volatile in recent history. There were more high volatility days (market up or down at least 1%) and extreme volatility days (market up or down at least 2%) than in any year since the Great Depression. A primary contributor to this was the breadth of equity investment pain in 2002. Over 75% of S&P stocks declined in price last year, even though earnings were rising. For the first time since it has been tracked (1981), each S&P sector declined.

### **FOREIGN EQUITY**

After a weak third quarter, developed and emerging international equity markets generally rallied along with our domestic one. The pattern of return was also the same, with a weak December following strong returns in October and November. The big exception was the Japanese market, which declined 8% in Yen terms, after having been the strongest developed market during the first three quarters of 2002. European markets led developed markets in the 4<sup>th</sup> quarter, advancing almost 6% in local currency terms and 11% in US\$ terms. The Euro rose over 6% versus the Dollar in the quarter and nearly 18% for the year. Asian markets outside Japan rose during the quarter. Emerging Markets were led to top tier returns by Latin American countries. Telecom and information tech shares led the rally, followed by financial services and energy.

2002 was a very disappointing one for European investors. The region’s combined markets dropped 29% in local currency. The EU’s economic stability and growth pact has so far hurt the latter. Real interest rates, especially in Germany, remain high despite modest inflation.

## General Outlook/Recommendations

**Rebuild Overall Equity positions** – To summarize, 2002 was a very trying period. Investors panicked. Stocks plummeted and volatility eroded confidence in the market. Nonetheless, we believe the worst is behind us. We believe the economy has bottomed and is recovering, and that stock prices now reflect lowered expectations for near-term economic growth. Following December and January's market weakness, equity values again appear extremely attractive compared to high-grade bonds. Equity fundamentals have continued to improve throughout 2002, whether measured by profits, cashflow or balance sheet strength, yet stocks are still selling for low multiples of "bottom of cycle" earnings. Gradually, today's highly risk-adverse investors will regain their interest in equities. Nonetheless, the re-valuation process will be volatile, particularly given the highly unfavorable geopolitical environment. Thus, we still recommend no more than a re-building of under weighted equity positions back up to "strategic neutral" at this time;

**Overweight Foreign Equity** – We continue to recommend this tactical overweight, which proved successful in 2002. Looking forward, its fair to say European markets may have over-reacted. Earnings there have not gone through the "profits depression" we did in the States. Yet, Price/Earnings or Price/Book based valuations have dropped back to early 1990's levels. The European central bankers also have considerable scope and reason to lower interest rates further. The Dollar's overvaluation was narrowed substantially in 2002, but not eliminated. Further, there is ongoing pressure in the form of a \$1.1 billion per day negative currency effect due to our large current account deficit.

**Underweight Interest Rate Risk** – We continue with our tactical recommendation to emphasize shorter-term, higher coupon, credit bonds. Poor returns in the 4<sup>th</sup> quarter from high quality bonds, on a very modest interest rate rise, should give investors pause. We are very concerned about a reprise of 1994 or 1999, when previously top-performing long Treasury bonds posted double-digit losses. The biggest (best?) fixed income managers are reducing portfolio durations and increasing allocations to higher risk corporate and international bond sectors.

**Comparative Asset Allocation (\$ in thousands)**

| <b>MANAGER<br/>or FUND</b>      | <b>STYLE</b>        | <b>\$ Balance<br/>12-31-2002</b> | <b>Allocation %<br/>12-31-2002</b> | <b>TARGET<br/>ASSET MIX</b> | <b>\$ Balance<br/>9-30-2002</b> | <b>Allocation %<br/>9-30-2002</b> |
|---------------------------------|---------------------|----------------------------------|------------------------------------|-----------------------------|---------------------------------|-----------------------------------|
| Large Cap Value                 | Large Value         | \$31,809                         | 16.9%                              | 21.4%                       | \$29,723                        | 17.9%                             |
| Large Cap Growth                | Large Growth        | 25,463                           | 13.5%                              | 19.0%                       | 24,405                          | 14.7%                             |
| Small Cap Core                  | Small Value         | 12,126                           | 6.4%                               | 7.1%                        | 11,026                          | 6.6%                              |
| <b><i>U.S. EQUITY</i></b>       | <b>blended</b>      | <b>\$69,398</b>                  | <b>36.8%</b>                       | <b>47.5%</b>                | <b>\$65,153</b>                 | <b>39.2%</b>                      |
| International Equity            | International       | 9,899                            | 5.2%                               | 7.5%                        | 9,494                           | 5.7%                              |
| <b><i>TOTAL EQUITY</i></b>      | <b>blended</b>      | <b>\$79,297</b>                  | <b>42.0%</b>                       | <b>55.0%</b>                | <b>\$74,648</b>                 | <b>44.9%</b>                      |
| US Fixed Income                 | U.S. Total Return   | 52,209                           | 27.7%                              | 24.8%                       | 51,314                          | 30.8%                             |
| Global Fixed Income             | Global (hedged)     | 41,150                           | 21.8%                              | 20.2%                       | 40,376                          | 24.3%                             |
| <b><i>FIXED INCOME</i></b>      | <b>Global fixed</b> | <b>\$93,360</b>                  | <b>49.5%</b>                       | <b>45.0%</b>                | <b>\$91,690</b>                 | <b>55.1%</b>                      |
| <b><i>CASH ACCOUNTS (4)</i></b> | <b>money market</b> | <b>15,950</b>                    | <b>8.5%</b>                        | <b>0%</b>                   |                                 |                                   |
| <b><i>TOTAL PLAN</i></b>        | <b>balanced</b>     | <b><u>\$188,607</u></b>          | <b>100.0%</b>                      | <b>100.0%</b>               | <b><u>\$166,338</u></b>         | <b>100.0%</b>                     |

### Asset Allocation Observations and Recommendations

- The Plan's Total Equity allocation ended the 4<sup>th</sup> quarter at only 42% of total assets, which was 13% below its target. The combined cash account held 8.5% of total assets, compared to a 0% target. Fixed Income portfolios totalled 49.5% of assets, or 4.5% above target. The Plan's rebalancing policy indicates rebalancing should take place when exposure to a primary asset class (equity, fixed income, or cash equivalents) falls  $\pm 5\%$  outside its neutral target. Accordingly, a rebalancing of the Plan's asset mix back to neutral targets is indicated. We suggest using January 31, 2003 asset values to calculate the required funding shifts.
- Funds would be beneficially placed into the most undervalued and underweight equity areas first – international equity, US large-cap growth, and US large-cap value. The Plan's small cap equity allocation is also below its target. Based on the conservative assumption that total Plan assets fell 2% in January, to \$185 million, the following asset shifts would be needed to move to neutral weights -

| <u>Asset sub-class</u> | <u>Action</u> | <u>\$</u>   | <u>Current Manager</u> | <u>Funding Source</u>  |
|------------------------|---------------|-------------|------------------------|------------------------|
| International Equity   | ADD           | \$3,975,000 | International Equity   | Combined Cash Accounts |
| US Large-cap Growth    | ADD           | \$9,690,000 | Large Cap Growth       | Cash + USFI            |
| US Large-cap Value     | ADD           | \$7,780,000 | Large Cap Value        | USFI + GFI             |
| US Small-cap Core      | ADD           | \$1,000,000 | Small Cap Core         | USFI + GFI             |

- Re-balancing could occur all at once, or in some staged fashion. If you are concerned about making substantial additions to equity accounts at this time, then we recommend breaking each of the above values into 3 or 4 equal-sized tranches, to be executed at regular intervals over the next 3-6 months. When re-allocation is complete, we suggest maintaining a 2% (target) combined cash balance, as part of your overall fixed income target (currently 45%).
- It has been some time since the Plan has reviewed its overall strategic asset allocation policy. The current strategic asset mix served the Plan well during the three year bear market, but may not be the the most appropriate strategy as we *look forward*. Chartwell recommends that the Plan conduct an asset allocation study to review potential asset mixes in light of the low level of interest rates, the Plan's demographics, the Plan's funding requirements and the outlook for prospective returns from various asset classes. A proposal for an asset allocation study is being provided under separate cover with this performance report for your consideration.

- The Plan's overall return for the 4<sup>th</sup> quarter was positive, at 3.9%. This lagged the blended index benchmark by 1.2% and ranked very low (80<sup>th</sup> %-tile) in its peer group.. The principal reasons for this result were: (a) very conservative asset allocation, which accounted for 0.7% of the underperformance, and; (b) weak performance by certain managers, particularly Large Cap Value Manager and Large Cap Growth.
- For the latest full year, the Plan's total return was (6.0)%, which exceeded its blended index benchmark by 1.7% and ranked in the top third of a similarly balanced universe. Good *relative* performance during a period of very negative absolute returns. The Plan's conservative asset allocation contributed 100% of the positive relative return, as net manager performance only matched the target indices.
- Over the last three years, the Plan has achieved a (1.0)% annualized return, bettering its benchmark by 2.4% annually and ranking a superior 10<sup>th</sup> %-tile among peers. Excellent *relative* performance during a bear market for stocks. Value-added by your active manager team contributed 75% of the excess returns achieved over the past 3 years, with your asset allocation decisions adding the remainder.
- The Plan's fixed income managers (US Fixed Income Manager and Global Fixed Income Manager) have done a good job of providing some relief during this tenacious bear market. Both exceeded their index benchmarks for the quarter and the year. Universe rankings the past quarter for GFI were weak, as the global fixed income universe includes *unhedged* global managers, and these managers performed very well as the US\$ weakened. GFI instead maintained its generally hedged posture.

Sample

### 4<sup>th</sup> Quarter 2002 Performance Summary

|   | % of Plan Assets | 4Q 2002          | Year to Date     | 1-Year           | 3-Years          |
|---|------------------|------------------|------------------|------------------|------------------|
| <b>Total Fund Composite</b>                             |                  | <b>3.9</b>       | <b>-6.0</b>      | <b>-6.0</b>      | <b>-1.0</b>      |
| <i>Rank in Blended Universe (%-tile)<sup>1</sup></i>    |                  | 80 <sup>th</sup> | 29 <sup>th</sup> | 29 <sup>th</sup> | 10 <sup>th</sup> |
| Target Policy Index Benchmark <sup>2</sup>              |                  | 5.1              | -7.7             | -7.7             | -3.4             |
| <b>Domestic Equity Composite</b>                        | <b>36.8%</b>     | <b>6.5</b>       | <b>-20.0</b>     | <b>-20.0</b>     | <b>-8.0</b>      |
| <i>Rank in Blended Universe (%-tile)</i>                |                  | 47 <sup>th</sup> | 37 <sup>th</sup> | 37 <sup>th</sup> | 20 <sup>th</sup> |
| Target Policy Index Benchmark                           |                  | 8                | -21.5            | -21.5            | -13.7            |
| <b>Large Cap Value Mgr.</b>                             | <b>16.9%</b>     | <b>7.0</b>       | <b>-20.1</b>     | <b>-20.1</b>     | <b>-5.0</b>      |
| <i>Rank in Broad Large Cap Value Universe (%-tile)</i>  |                  | 61 <sup>st</sup> | 58 <sup>th</sup> | 58 <sup>th</sup> | 37 <sup>th</sup> |
| Russell 1000 Value Index                                |                  | 9.2              | -15.5            | -15.5            | -5.1             |
| <b>Large Cap Growth Mgr.</b>                            | <b>13.5%</b>     | <b>4.3</b>       | <b>-23.1</b>     | <b>-23.1</b>     | <b>-14.8</b>     |
| <i>Rank in Broad Large Cap Growth Universe (%-tile)</i> |                  | 68 <sup>th</sup> | 30 <sup>th</sup> | 30 <sup>th</sup> | 16 <sup>th</sup> |
| Russell 1000 Growth Index                               |                  | 7.2              | -27.9            | -27.9            | -23.6            |
| <b>Small Cap Value Manager</b>                          | <b>6.4%</b>      | <b>10.0</b>      | <b>-11.8</b>     | <b>-11.8</b>     | <b>7.0</b>       |
| <i>Rank In Pure Small Cap Value Universe</i>            |                  | 9 <sup>th</sup>  | 22 <sup>nd</sup> | 22 <sup>nd</sup> | 18 <sup>th</sup> |
| Russell 2000 Index                                      |                  | 6.2              | -16.2            | -16.2            | 5.5              |
| <b>International Equity Manager</b>                     | <b>5.2%</b>      | <b>4.4</b>       | <b>-20.5</b>     | <b>-20.5</b>     | <b>-</b>         |
| <i>Rank in International Equity Universe</i>            |                  | 70 <sup>th</sup> | 89 <sup>th</sup> | 89 <sup>th</sup> | -                |
| MSCI World ex-U.S. Index                                |                  | 6.6              | -15.5            | -15.5            | -                |
| <b>Fixed Income Composite</b>                           | <b>49.5%</b>     | <b>2.0</b>       | <b>10.5</b>      | <b>10.5</b>      | <b>9.5</b>       |
| <i>Rank in Blended Universe (%-tile)</i>                |                  | 81 <sup>st</sup> | 27 <sup>th</sup> | 27 <sup>th</sup> | 11 <sup>th</sup> |
| Target Policy Index Benchmark                           |                  | 1.6              | 10.3             | 10.3             | 10.1             |
| <b>US Fixed Income Manager</b>                          | <b>27.7%</b>     | <b>2.0</b>       | <b>10.7</b>      | <b>10.7</b>      | <b>10.7</b>      |
| <i>Rank in Broad Fixed Income Universe (%-tile)</i>     |                  | 29 <sup>th</sup> | 10 <sup>th</sup> | 10 <sup>th</sup> | 5 <sup>th</sup>  |
| Lehman Gov't/Credit Intermediate Bond Index             |                  | 1.6              | 10.3             | 10.3             | 10.1             |
| <b>Global Fixed Income Manager</b>                      | <b>21.8%</b>     | <b>2.0</b>       | <b>10.4</b>      | <b>10.4</b>      | <b>8.2</b>       |
| <i>Rank in Global Fixed Income Universe (%-tile)</i>    |                  | 88 <sup>th</sup> | 47 <sup>th</sup> | 47 <sup>th</sup> | 32 <sup>nd</sup> |
| Salomon World Gov't Bond (Hedged) Index                 |                  | 1.4              | 8.1              | 8.1              | 8.3              |

1. Total Fund Blended Universe: 21.4% Large Value / 19.0% Large Growth / 24.8% Brd Fixed / 20.2% Global Fixed / 7.1% Small Cap / 7.5% Int'l EQ

2. Total Fund Policy Index Benchmark: 40.4% R1000 / 24.8% Leh. Aggregate / 20.2% SB World Gov't Bond (H) / 7.1% R2000 / 7.5% World, ex-US

## Manager Performance Commentary

- + **US Fixed Income Manager (USFI)** was once again the Plan's best performing fixed income manager during the 4<sup>th</sup> quarter (and the year). They were moderately overweight corporate bonds during the quarter, and emphasized lower-quality investment grade bonds to take advantage of historically wide credit spreads. As spreads tightened during the quarter, corporate bonds performed very well. Their moderate overweight to mortgage sector bonds also helped performance. Conversely, USFI's longer portfolio duration (i.e., more interest rate risk due to longer maturities) detracted from performance during the quarter as interest rates rose. However, this definitely helped during the rest of 2002.

At +10.7% per annum over the last 3 years, USFI's medium-term performance for Chartwell Client has been superior.

- + **Global Fixed Income Manager (GFI)** turned in an acceptable quarter of performance, particularly given their assignment to manage a generally hedged global bond portfolio. They also exceeded their target index for the year. GFI's performance in the quarter was driven by a number of factors: (1) country selection (underweight US and Japanese bonds, overweight Denmark and Sweden); (2) currency hedging (had some exposure to Euro, Swedish Krona, Danish Krone and British Pound); (3) longer portfolio duration, and; (4) security selection. The latter was the largest contributor to performance in the quarter, as GFI's 20% exposure to corporate bonds and 9% to emerging market debt added value. GFI plans on maintaining the corporate bond exposure at the 20% level, but began taking profits in emerging market bonds in November. At year-end, emerging market debt exposure was down to 4%.

Despite beating the index benchmark by over 2% in 2002, Rogge's 1-year rank among peers is barely above average. This is due to the unmitigated success of those global managers that aggressively unhedged their currency exposure last year (something GFI did not do too well). However, GFI's 3-year record exceeds more than 2/3<sup>rd</sup>s of its peers.

- + Small cap stocks were not the strongest components of the equity market during the fourth quarter, but **Small Cap Core Manager (SCC)** posted a very strong quarterly return of 10.0%. This exceeded both its primary index benchmark- the Russell 2000 index of all small-cap stocks, and its secondary benchmark- the R2000 *Value* index. For the year, SCC's performance was more than 4% ahead of the broad small cap market (R2000), and fell just short of the small cap value index. As equity markets bounced back in the 4<sup>th</sup> quarter, led by telecom and technology stocks, SCC's tech holdings were the largest contributors to outperformance. During the quarter, SCC posted positive returns in every sector they invested in, but consumer discretionary and materials & processing stocks performed particularly well. These sectors, along with producer durables names, accounted for SCC's strong relative performance for the year.

- **Large Cap Value Manager (LCV)** is the Plan's large-cap relative value manager. LCV participated in the 4<sup>th</sup> quarter rally and advanced 7.0%. This represented below average relative performance, as its index benchmark, the Russell 1000 Value index, rose 9.2%. The full year 2002 was also a difficult one for LCV, as it lagged the benchmark by 4.5%. Unsurprisingly, LCV's ranking versus peer value managers was below the median in both cases. For the first calendar year since you hired them, LCV failed to beat its target benchmark.

The primary problem at LCV the past quarter and year has been security selection. As a relative value manager, LCV will purchase "fallen angel" stocks in any sector, providing those stocks meet their valuation criteria. In 2002, LCV's portfolio was plagued with a number of "torpedo" stocks that produced very large percentage losses. There were also a number of other stocks that were poor relative performers. We've discussed each of these names with the portfolio manager.

While it's easy to criticize after the fact, we've had similar conversations with LCV and other value managers in the past. The firm has no "stop-loss" element to its sell discipline, even after adjusting for market performance. So, it tends to hold losing positions in the belief they are getting cheaper (i.e., more attractive). This is often true, so the issue becomes how long should the manager wait? That's the same question to ask about the manager itself. As an attractively priced portfolio underperforms the market, the held portfolio should have become even more attractively priced. At some point the stocks become compelling bargains, buyers rush in, and the portfolio outperforms the market indices. At LCV, they've underperformed for three consecutive quarters. That has not happened before.

Another concern we have is the portfolio's capitalization focus. The manager estimates that 35% of the names held, comprising 25% of assets, are companies with market caps below \$10 billion (an accepted demarcation between large-cap and mid-cap styles). We suggest that 25% is quite a high exposure to mid-cap names if your assignment is large-cap. Further, the mid-cap value style sector performed substantially better in 2002 than large-cap value, yet LCV's performance went in the other direction.

We recommend watching LCV closely over the next two quarters. If relative performance does not begin to exceed their index benchmark, a reduction of exposure may be warranted. Until then, we recommend you do not make any additions to their account. But, we do recommend you *increase* your US large-cap value equity allocation. To accommodate both recommendations, we propose you add to your US large-cap value exposure at this time by placing the incremental monies into an index mutual fund designed to mirror the holdings and performance of the Russell 1000 Value or S&P Value indices. You'll obtain the desired increased exposure to large-cap value stocks, by earning a return equal to the current index benchmark.

- ± **Large Cap Growth Manager (LCG)** generated a positive quarterly result, but lagged both the R1000 Growth index and the S&P 500. As a conservative large cap growth manager, LCG has been underweight technology and overweight consumer staples for the past three years. For the majority of that time, that strategy has served them well. During the fourth quarter of 2002, it did not. Tech stocks rallied strongest, and defensive consumer staples finally gave way. Going forward, LCG will continue to overweight consumer staples and health care

stocks, as they are poised to perform well in even a moderately recovering profit environment. LCG will also look for cyclical growth opportunities in the energy service, industrial and consumer discretionary sectors.

For the year, LCG was nearly 5% ahead of the R1000 Growth target index, losing “only” 23.1% versus the index’s very poor (27.9)% result. It was a devastating year for large-cap growth stocks, with LCG’s returns ranking it in the top 30% of peers. Longer-term, LCG’s conservative, “blue chip” approach to growth stocks has helped it avoid many losing positions. It has performed very well compared to other large-cap growth managers, even as absolute returns have been terrible.

- **International Equity Manager (IEQ)** had a positive, but lagging return for the 4<sup>th</sup> quarter. For the year, IEQ underperformed the MSCI World ex US index by 5%. Currency hedging and owning XYZ stock each detracted approximately 3% of value during the year. At the beginning of 2002, IEQ reduced their currency hedging, but the minimal amount they held had a negative impact on performance in the second half of 2002, as the US\$ weakened. IEQ is taking steps to identify “torpedo” companies such as XYZ stock, by increasing quantitative screens, increasing on-site company visits and stepping up independent checks with competitors, suppliers and customers. International portfolios are positioned to take advantage of a global economic recovery, even if that recovery is slow. Half of the portfolio is invested in economically sensitive sectors, (technology and consumer discretionary), and 50% is invested defensive, less economically sensitive stocks (drug and medical stocks, integrated oil companies, consumer staples).

Sample

**Performance Evaluation  
for  
SAMPLE CHARTWELL CLIENT  
Total Fund Composite**

For the Period Ending  
December 31, 2002

Presented  
by:  
Chartwell Consulting (USA) LLC

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Executive Summary

#### Account Reconciliation

|                 | 12/31/2002<br>Qtr | 2002<br>YTD | 04/30/1998<br>Incept |
|-----------------|-------------------|-------------|----------------------|
| Beginning Value | 166,195           | 184,621     | 50,115               |
| Net Flows       | -62               | -945        | 105,332              |
| Investment G/L  | 6,523             | -11,019     | 17,210               |
| Ending Value    | 172,657           | 172,657     | 172,657              |

#### Investment Policy

| Index                             | Weight |
|-----------------------------------|--------|
| Russell 1000                      | 40.40  |
| Lehman Aggregate Bond             | 24.80  |
| Salomon World Gov't Bond - Hedged | 20.20  |
| Other                             | 14.60  |

#### Trailing Returns through December 31, 2002

|        | 1 Yr  | 2 Yr  | 3 Yr  | 4 Yr | 5 Yr | 6 Yr | 7 Yr | 8 Yr | 9 Yr | 10 Yr | 04/30/1998<br>Incept |
|--------|-------|-------|-------|------|------|------|------|------|------|-------|----------------------|
| Target | -5.99 | -3.26 | -0.96 | 1.22 |      |      |      |      |      |       | 2.18                 |
| Diff   | -7.68 | -5.40 | -3.41 | 0.19 |      |      |      |      |      |       | 1.75                 |
| Diff   | 1.69  | 2.14  | 2.45  | 1.03 |      |      |      |      |      |       | 0.43                 |

#### Calendar Year Returns

|        | 12/31/2002<br>Qtr | 2002<br>YTD | 2001  | 2000 | 1999  | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 |
|--------|-------------------|-------------|-------|------|-------|------|------|------|------|------|------|
| Target | 3.93              | -5.99       | -0.46 | 3.82 | 8.05  |      |      |      |      |      |      |
| Diff   | 5.05              | -7.68       | -3.06 | 0.69 | 11.82 |      |      |      |      |      |      |
| Diff   | -1.12             | 1.69        | 2.60  | 3.13 | -3.77 |      |      |      |      |      |      |

#### Returns in Up Markets

|        | 2 Yr  | 3 Yr | 4 Yr | 04/30/1998<br>Incept |
|--------|-------|------|------|----------------------|
| Target | 16.8  | 10.6 | 12.6 | 14.8                 |
| Ratio  | 16.7  | 14.2 | 16.1 | 18.6                 |
| Ratio  | 100.2 | 75.1 | 77.9 | 79.4                 |

#### Returns in Down Markets

|        | 2 Yr  | 3 Yr  | 4 Yr  | 04/30/1998<br>Incept |
|--------|-------|-------|-------|----------------------|
| Target | -19.9 | -11.3 | -11.7 | -12.5                |
| Ratio  | -23.3 | -18.3 | -17.1 | -17.1                |
| Ratio  | 85.1  | 62.0  | 68.3  | 73.1                 |

Inception date is April 30, 1998

All dollar values are shown in thousands.

Returns for periods exceeding one year are annualized.

Returns are net of fees.

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Quarterly Comparison Analysis (%)

| Period Ending |       | Primary Target | Diff  | Alternative Target | Diff  | CPI + 5% | Diff  |
|---------------|-------|----------------|-------|--------------------|-------|----------|-------|
| Jun 1998      | 0.09  | 1.09           | -1.00 | 1.25               | -1.16 | 1.12     | -1.03 |
| Sep 1998      | -4.77 | -4.45          | -0.32 | -4.37              | -0.40 | 1.53     | -6.30 |
| Dec 1998      | 10.53 | 11.39          | -0.86 | 11.57              | -1.04 | 1.33     | 9.20  |
| Mar 1999      | -0.73 | 1.41           | -2.14 | 1.50               | -2.23 | 1.83     | -2.56 |
| Jun 1999      | 5.08  | 3.78           | 1.30  | 3.44               | 1.64  | 1.93     | 3.15  |
| Sep 1999      | -3.65 | -2.55          | -1.10 | -2.53              | -1.12 | 2.23     | -5.88 |
| Dec 1999      | 7.50  | 9.02           | -1.52 | 8.74               | -1.24 | 1.53     | 5.97  |
| Mar 2000      | -0.01 | 3.53           | -3.54 | 3.22               | -3.23 | 2.94     | -2.95 |
| Jun 2000      | -0.11 | -1.15          | 1.04  | -1.16              | 1.05  | 1.93     | -2.04 |
| Sep 2000      | -0.32 | 0.96           | -1.28 | 1.16               | -1.48 | 1.93     | -2.25 |
| Dec 2000      | 4.28  | -2.55          | 6.83  | -2.63              | 6.91  | 1.43     | 2.85  |
| Mar 2001      | -3.96 | -5.39          | 1.43  | -5.55              | 1.59  | 2.43     | -6.39 |
| Jun 2001      | 3.03  | 3.70           | -0.67 | 3.50               | -0.47 | 2.33     | 0.70  |
| Sep 2001      | -5.84 | -7.23          | 1.39  | -6.71              | 0.87  | 1.43     | -7.27 |
| Dec 2001      | 6.84  | 6.51           | 0.33  | 6.08               | 0.76  | 0.33     | 6.51  |
| Mar 2002      | 2.08  | 0.61           | 1.47  | 0.62               | 1.46  | 2.43     | -0.35 |
| Jun 2002      | -4.06 | -4.87          | 0.81  | -4.90              | 0.84  | 1.93     | -5.99 |
| Sep 2002      | -7.63 | -8.18          | 0.55  | -7.95              | 0.32  | 1.83     | -9.46 |
| Dec 2002      | 3.93  | 5.05           | -1.12 | 5.16               | -1.23 | 1.23     | 2.70  |
| Incept.       | 2.18  | 1.75           | 0.43  | 1.71               | 0.47  | 7.31     | -5.13 |

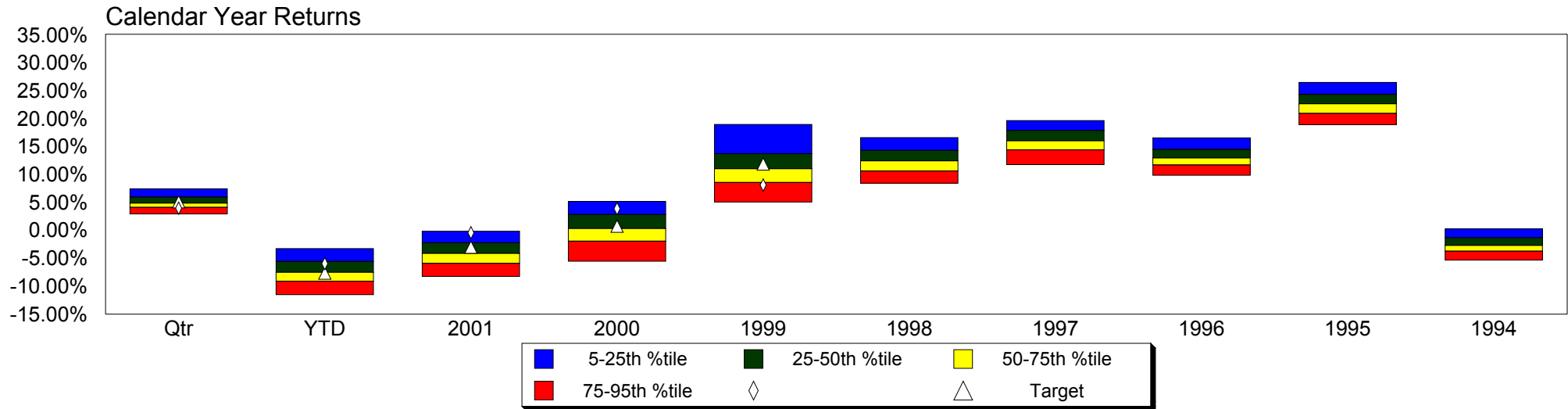
Returns for periods exceeding one year are annualized.

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Universe Comparisons

### SAMPLE CLIENT - Total Fund Composite



### Calendar Year Returns

|             | Qtr  | YTD    | 2001  | 2000  | 1999  | 1998  | 1997  | 1996  | 1995  | 1994  |
|-------------|------|--------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return      | 3.93 | -5.99  | -0.46 | 3.82  | 8.05  |       |       |       |       |       |
| %-tile      | 80   | 29     | 8     | 17    | 78    |       |       |       |       |       |
| Target      |      |        |       |       |       |       |       |       |       |       |
| Return      | 5.05 | -7.68  | -3.06 | 0.69  | 11.82 |       |       |       |       |       |
| %-tile      | 44   | 53     | 35    | 45    | 42    |       |       |       |       |       |
| Universe    |      |        |       |       |       |       |       |       |       |       |
| 5th %-tile  | 7.39 | -3.31  | -0.21 | 5.12  | 18.87 | 16.53 | 19.56 | 16.48 | 26.38 | 0.21  |
| 25th %-tile | 5.89 | -5.60  | -2.28 | 2.79  | 13.66 | 14.23 | 17.77 | 14.40 | 24.25 | -1.37 |
| 50th %-tile | 4.82 | -7.56  | -4.17 | 0.27  | 10.96 | 12.37 | 15.94 | 12.88 | 22.58 | -2.75 |
| 75th %-tile | 4.06 | -9.14  | -5.95 | -2.00 | 8.49  | 10.57 | 14.34 | 11.64 | 20.84 | -3.77 |
| 95th %-tile | 2.86 | -11.56 | -8.29 | -5.58 | 4.99  | 8.37  | 11.69 | 9.77  | 18.80 | -5.39 |

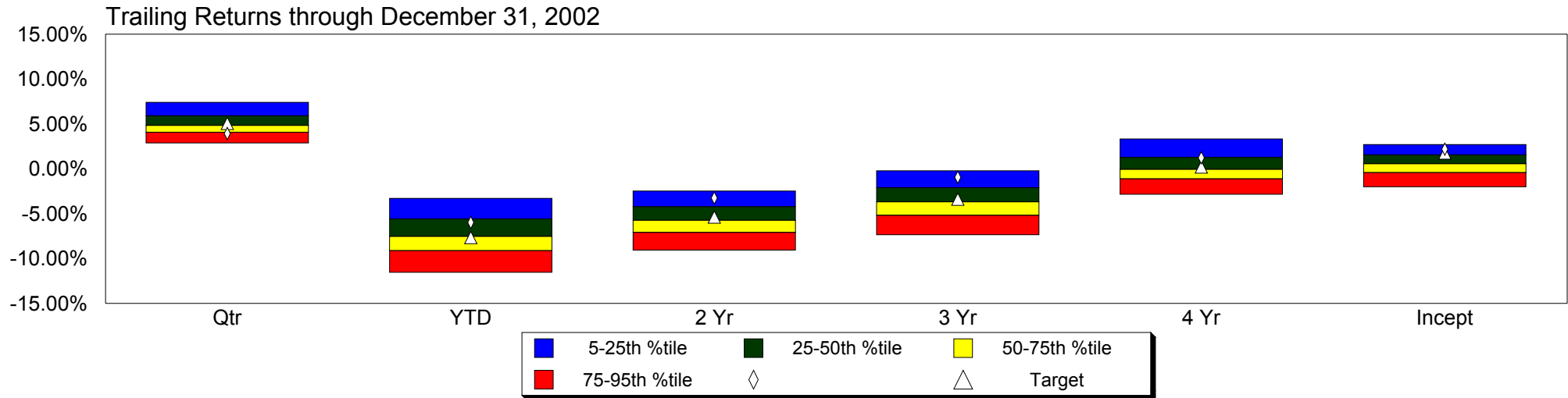
Returns are in percent. "%-tile" is the percentile ranking within the universe.  
Returns for periods exceeding one year are annualized.

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Universe Comparisons

### SAMPLE CLIENT - Total Fund Composite



### Trailing Returns through December 31, 2002

|             | Qtr  | YTD    | 2 Yr  | 3 Yr  | 4 Yr  | Incept |
|-------------|------|--------|-------|-------|-------|--------|
| Return      | 3.93 | -5.99  | -3.26 | -0.96 | 1.22  | 2.18   |
| %-tile      | 80   | 29     | 13    | 10    | 26    | 11     |
| Target      |      |        |       |       |       |        |
| Return      | 5.05 | -7.68  | -5.40 | -3.41 | 0.19  | 1.75   |
| %-tile      | 44   | 53     | 43    | 44    | 44    | 21     |
| Universe    |      |        |       |       |       |        |
| 5th %-tile  | 7.39 | -3.31  | -2.48 | -0.23 | 3.32  | 2.69   |
| 25th %-tile | 5.89 | -5.60  | -4.23 | -2.13 | 1.27  | 1.54   |
| 50th %-tile | 4.82 | -7.56  | -5.76 | -3.70 | -0.08 | 0.55   |
| 75th %-tile | 4.06 | -9.14  | -7.11 | -5.20 | -1.14 | -0.43  |
| 95th %-tile | 2.86 | -11.56 | -9.08 | -7.37 | -2.86 | -2.03  |

Returns are in percent. "%-tile" is the percentile ranking within the universe.

Returns for periods exceeding one year are annualized.

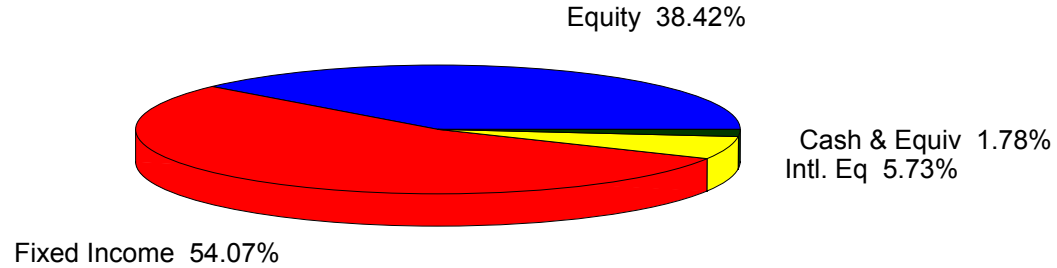
Incept is April 30, 1998 to December 31, 2002

# SAMPLE CHARTWELL CLIENT

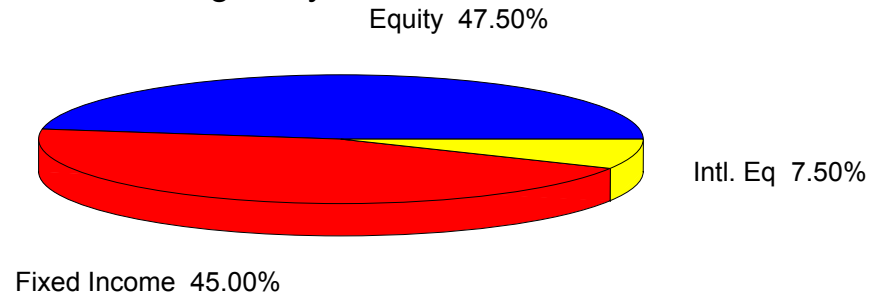
## Total Fund Composite

Style Allocation as of December 31, 2002

### Actual Style Allocation



### Target Style Allocation



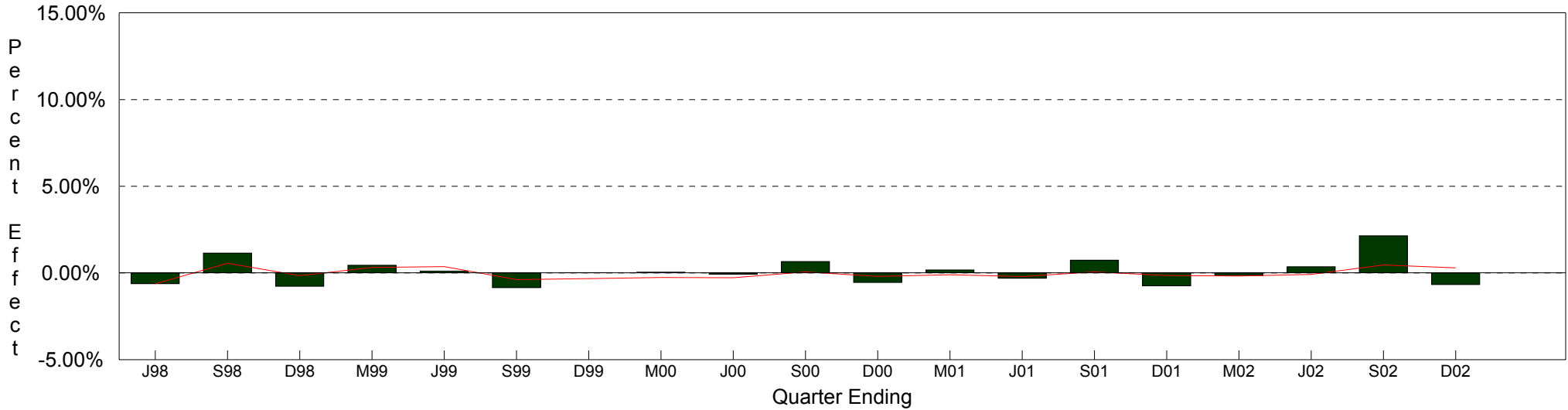
| Asset Class  | Actual (\$) | Actual (%) | Target (%) | Difference (%) | Difference (\$) |
|--------------|-------------|------------|------------|----------------|-----------------|
| Equity       | 66,327      | 38.42      | 47.50      | -9.08          | -15,685         |
| Fixed Income | 93,360      | 54.07      | 45.00      | 9.07           | 15,664          |
| Intl. Eq     | 9,899       | 5.73       | 7.50       | -1.77          | -3,050          |
| Cash & Equiv | 3,071       | 1.78       | 0.00       | 1.78           | 3,071           |
| Total        | 172,657     | 100.00     | 100.00     |                |                 |

All dollar values are shown in thousands.

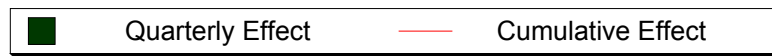
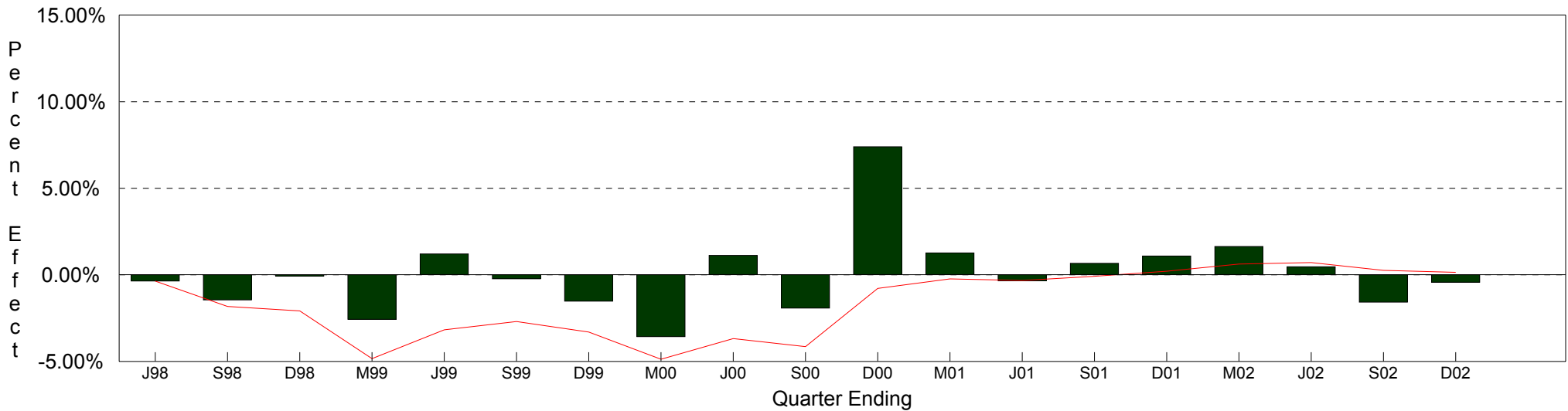
# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Asset Allocation Effect



### Security Selection Effect



# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Attribution of Returns

#### Attribution of Performance to show Manager Contribution

|                 | Primary Target | Manager Contribution |       |
|-----------------|----------------|----------------------|-------|
| Current Quarter | 5.05           | -1.12                | 3.93  |
| Year to Date    | -7.68          | 1.69                 | -5.99 |
| 2 Years         | -5.40          | 2.14                 | -3.26 |
| 3 Years         | -3.41          | 2.45                 | -0.96 |
| 4 Years         | 0.19           | 1.03                 | 1.22  |
| Incept          | 1.75           | 0.43                 | 2.18  |

Primary Target + Manager Contribution =

#### Attribution of Manager Contribution between Asset Allocation and Security Selection

|                 | Asset Allocation | Security Selection | Manager Contribution |
|-----------------|------------------|--------------------|----------------------|
| Current Quarter | -0.68            | -0.44              | -1.12                |
| Year to Date    | 1.75             | -0.06              | 1.69                 |
| 2 Years         | 0.87             | 1.27               | 2.14                 |
| 3 Years         | 0.59             | 1.86               | 2.45                 |
| 4 Years         | 0.37             | 0.66               | 1.03                 |
| Incept          | 0.29             | 0.14               | 0.43                 |

Asset Allocation + Security Selection = Manager Contribution

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Risk Measures

| 2 Yr               |       | Target | Diff  |
|--------------------|-------|--------|-------|
| # of Negative Qtrs | 4.00  | 4.00   | 0.00  |
| # of Positive Qtrs | 4.00  | 4.00   | 0.00  |
| Batting Average    | 75.00 | 25.00  | 50.00 |
| Worst Qtr          | -7.63 | -8.18  | 0.55  |
| Best Qtr           | 6.84  | 6.51   | 0.33  |
| Range              | 14.47 | 14.69  | -0.22 |
| Worst 4 Qtrs       | -5.99 | -7.68  | 1.69  |
| Standard Deviation | 9.91  | 11.00  | -1.09 |
| Beta               | 0.89  | 1.00   | -0.11 |
| Annualized Alpha   | 1.55  | 0.00   | 1.55  |
| R-Squared          | 0.98  | 1.00   | -0.02 |
| Sharpe Ratio       | -0.62 | -0.75  | 0.13  |
| Treynor Ratio      | -6.91 | -8.29  | 1.38  |
| Tracking Error     | 1.84  | 0.00   | 1.84  |
| Information Ratio  | 1.16  |        |       |

| 3 Yr               |       | Target | Diff  |
|--------------------|-------|--------|-------|
| # of Negative Qtrs | 7.00  | 6.00   | 1.00  |
| # of Positive Qtrs | 5.00  | 6.00   | -1.00 |
| Batting Average    | 66.67 | 33.33  | 33.34 |
| Worst Qtr          | -7.63 | -8.18  | 0.55  |
| Best Qtr           | 6.84  | 6.51   | 0.33  |
| Range              | 14.47 | 14.69  | -0.22 |
| Worst 4 Qtrs       | -5.99 | -11.30 | 5.31  |
| Standard Deviation | 8.53  | 9.46   | -0.93 |
| Beta               | 0.78  | 1.00   | -0.22 |
| Annualized Alpha   | 1.71  | 0.00   | 1.71  |
| R-Squared          | 0.75  | 1.00   | -0.25 |
| Sharpe Ratio       | -0.57 | -0.77  | 0.20  |
| Treynor Ratio      | -6.23 | -7.31  | 1.08  |
| Tracking Error     | 4.71  | 0.00   | 4.71  |
| Information Ratio  | 0.52  |        |       |

| 4 Yr               |       | Target | Diff  |
|--------------------|-------|--------|-------|
| # of Negative Qtrs | 9.00  | 7.00   | 2.00  |
| # of Positive Qtrs | 7.00  | 9.00   | -2.00 |
| Batting Average    | 56.25 | 43.75  | 12.50 |
| Worst Qtr          | -7.63 | -8.18  | 0.55  |
| Best Qtr           | 7.50  | 9.02   | -1.52 |
| Range              | 15.13 | 17.20  | -2.07 |
| Worst 4 Qtrs       | -5.99 | -11.30 | 5.31  |
| Standard Deviation | 8.83  | 9.73   | -0.90 |
| Beta               | 0.81  | 1.00   | -0.19 |
| Annualized Alpha   | 1.07  | 0.00   | 1.07  |
| R-Squared          | 0.79  | 1.00   | -0.21 |
| Sharpe Ratio       | -0.33 | -0.40  | 0.07  |
| Treynor Ratio      | -3.57 | -3.92  | 0.35  |
| Tracking Error     | 4.46  | 0.00   | 4.46  |
| Information Ratio  | 0.23  |        |       |

| Incept             |       | Target | Diff  |
|--------------------|-------|--------|-------|
| # of Negative Qtrs | 10.00 | 8.00   | 2.00  |
| # of Positive Qtrs | 8.67  | 10.67  | -2.00 |
| Batting Average    | 48.20 | 51.80  | -3.60 |
| Worst Qtr          | -7.63 | -8.18  | 0.55  |
| Best Qtr           | 10.53 | 11.39  | -0.86 |
| Range              | 18.16 | 19.57  | -1.41 |
| Worst 4 Qtrs       | -5.99 | -11.30 | 5.31  |
| Standard Deviation | 9.63  | 10.50  | -0.87 |
| Beta               | 0.84  | 1.00   | -0.16 |
| Annualized Alpha   | 0.71  | 0.00   | 0.71  |
| R-Squared          | 0.84  | 1.00   | -0.16 |
| Sharpe Ratio       | -0.21 | -0.24  | 0.03  |
| Treynor Ratio      | -2.44 | -2.48  | 0.04  |
| Tracking Error     | 4.16  | 0.00   | 4.16  |
| Information Ratio  | 0.10  |        |       |

# SAMPLE CHARTWELL CLIENT

## Total Fund Composite

### Market Values and Cash Flows

| Period Ending | Beginning Value | Net Flows | Investment Gain/Loss | Ending Value | Return (%) |
|---------------|-----------------|-----------|----------------------|--------------|------------|
| Jun 1998      | 50,115          | 108,173   | 143                  | 158,431      | 0.09       |
| Sep 1998      | 158,431         | -26       | -7,560               | 150,845      | -4.77      |
| Dec 1998      | 150,845         | -242      | 15,866               | 166,470      | 10.53      |
| Mar 1999      | 166,470         | 4,110     | -1,251               | 169,329      | -0.73      |
| Jun 1999      | 169,329         | -48       | 8,603                | 177,884      | 5.08       |
| Sep 1999      | 177,884         | -58       | -6,487               | 171,339      | -3.65      |
| Dec 1999      | 171,339         | 0         | 12,858               | 184,197      | 7.50       |
| Mar 2000      | 184,197         | 0         | -13                  | 184,184      | -0.01      |
| Jun 2000      | 184,184         | 4,619     | -208                 | 188,595      | -0.11      |
| Sep 2000      | 188,595         | -151      | -611                 | 187,833      | -0.32      |
| Dec 2000      | 187,833         | -200      | 8,035                | 195,668      | 4.28       |
| Mar 2001      | 195,668         | -435      | -7,738               | 187,495      | -3.96      |
| Jun 2001      | 187,495         | -7,809    | 5,497                | 185,184      | 3.03       |
| Sep 2001      | 185,184         | -1,455    | -10,731              | 172,997      | -5.84      |
| Dec 2001      | 172,997         | -201      | 11,825               | 184,621      | 6.84       |
| Mar 2002      | 184,621         | -218      | 3,837                | 188,240      | 2.08       |
| Jun 2002      | 188,240         | -304      | -7,637               | 180,298      | -4.06      |
| Sep 2002      | 180,298         | -361      | -13,742              | 166,195      | -7.63      |
| Dec 2002      | 166,195         | -62       | 6,523                | 172,657      | 3.93       |

All dollar values are shown in thousands.