

BEACON POINTE

ADVISORS

BEACON'S POINT: A RARE AND DYING BREED

DECEMBER 31, 2010

CONFIDENTIAL - PROPRIETARY



These materials are confidential and being furnished solely to clients and prospective clients for informational purposes only and are not to be distributed. The materials may not be reproduced or disseminated without the express prior consent of Beacon Pointe Advisors, LLC. This information is obtained from internal and external research sources that are considered reliable, but the information's accuracy is not guaranteed by Beacon Pointe Advisors. Neither the information nor any opinion that may be expressed constitutes a solicitation, an offer to sell, or advertisement by Beacon Pointe Advisors, LLC. This material has been prepared for the general information only. It does not take into account the particular investment objectives, financial situation or needs of individual or the institutional investors. Before acting on any advice or recommendation in this material, you should consider whether it is suitable for your particular circumstances. Opinions expressed are the author's current opinions as of the date appearing on this material only. While the author may strive to update on a reasonable basis the information discussed in this material, there may be some factors or reasons that may prevent the author from doing so.

A Rare and Dying Breed

One of Beacon Pointe's core tenets is our belief in active, fundamentally-driven investment management. Despite the rapid ascent of index funds and ETF investing during the past decade, we contend that carefully researched and selected active strategies offer the best opportunities for our clients to achieve their investment objectives while taking the least amount of risk possible. Our conviction is based on past experience, the depth and discipline of Beacon Pointe's manager research and selection process, and our analysis of manager performance in the context of "active share", an objective new measure introduced by Yale School of Management's Cremers and Petajisto in a 2006 academic paper discussed below.

By the researchers' definition, active share is a measure of the percentage of stock holdings in a manager's portfolio that differ from the benchmark index. It is calculated by taking the sum of the absolute value of the differences in weight for each holding in the manager's and index' portfolios and dividing by two. The example below (courtesy of Goldman Sachs Asset Management) helps illustrate the mathematics behind active share. Simplifying the example further, suppose that a benchmark index includes only one stock. If a Portfolio Manager decides that he or she likes the stock, but wants to invest only half the portfolio in that stock and half in another stock, then the active share of that portfolio would be 50%.

Definition

Active Share is the percentage of the portfolio that is different than the benchmark. An active share above 60% is considered active. (The benchmark is 0%).¹

	Benchmark (00 Holdings)	Portfolio A (10 Holdings)	Overweight/ Underweight	Portfolio B (30 Holdings)	Overweight/ Underweight
IBM	9.5%	0.0%	9.5%	1.2%	8.3%
3M	6.0	7.9	1.9%	2.4	3.6
Chevron	5.6	0.0	5.6	4.5	1.1
United Technologies	5.0	9.0	4.0	3.9	1.1
Exxon Mobil	4.9	9.7	4.8	1.1	3.9
Johnson & Johnson	4.7	0.0	4.7	2.1	2.6
McDonalds	4.5	0.0	4.5	4.9	0.4
Procter & Gamble	4.4	0.0	4.4	2.6	1.7
Coca-Cola	4.1	18.0	13.9	4.4	0.3
Caterpillar	4.1	0.0	4.1	5.0	0.9
Boeing	3.9	7.0	3.1	6.0	2.1
Wal-Mart	3.9	0.0	3.9	2.0	1.9
Hewlett-Packard	3.7	0.0	3.7	3.9	0.1
Travelers	3.6	0.0	3.6	4.7	1.1
JPMorgan	3.0	14.0	11.0	9.5	6.5
American Express	2.9	0.0	2.9	1.7	1.2
Merck	2.6	0.0	2.6	4.1	1.5
DuPont	2.4	12.0	9.6	3.7	1.3
Verizon	2.4	0.0	2.4	1.3	1.1
Walt Disney	2.3	0.0	2.3	4.1	1.8
Microsoft	2.2	7.3	5.1	5.6	3.4
Home Depot	2.1	0.0	2.1	1.1	1.0
AT&T	2.0	6.1	4.1	3.6	1.6
Kraft Foods	2.0	0.0	2.0	3.0	1.1
Cisco Systems	1.7	0.0	1.7	1.5	0.3
Intel	1.5	0.0	1.5	2.9	1.5
Pfizer	1.3	9.0	7.7	2.4	1.1
Alcoa	1.2	0.0	1.2	2.3	1.2
General Electric	1.1	0.0	1.1	2.2	1.1
Bank of America	1.1	0.0	1.1	2.0	0.9
Total	100%	100.0%	130%	100%	55%

For illustrative purposes only.
Source: GSAM

1 Source: Cremers, M. and Antti Petajisto, 2009. "How Active Is Your Manager? A New Measure That Predicts Performance," Yale ICF Working Paper No. 06-14.



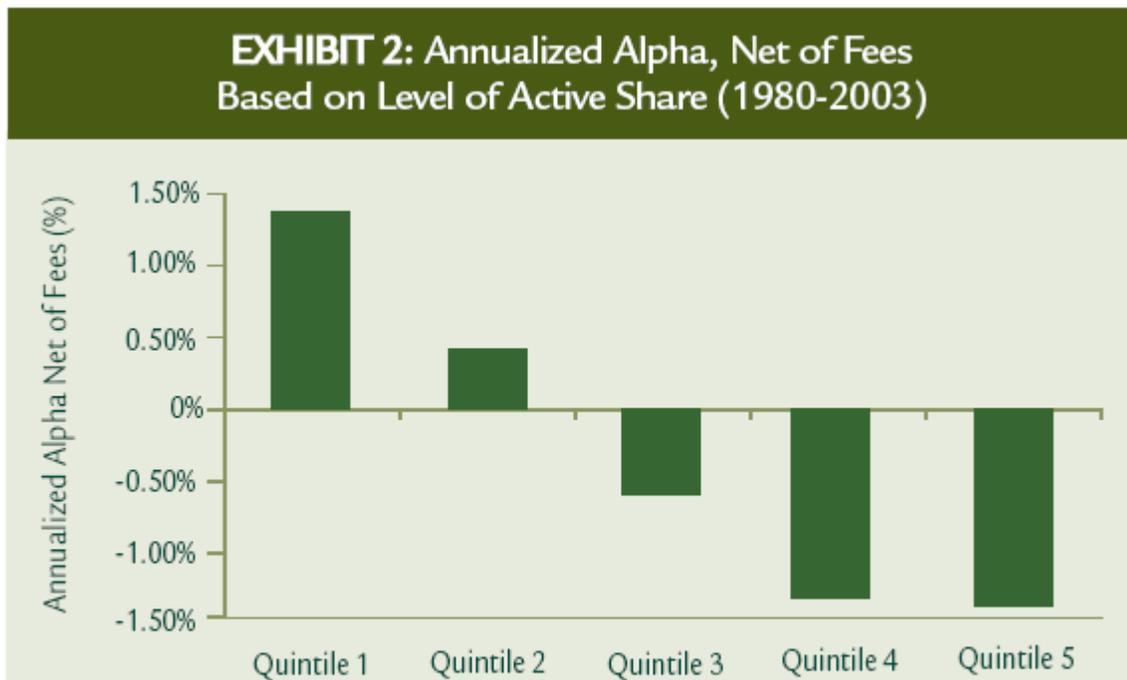
Source: Goldman Sachs Asset Management

Unlike tracking error, which is based on past returns, active share is holdings-based and forward looking. It is found by analyzing the manager's actual portfolio and comparing its holdings to the benchmark index. By measuring active management in this way, investors can get a better understanding of what exactly a manager is doing to drive performance, rather than drawing conclusions from past performance. In essence, active share takes into account all "active" decisions by Portfolio Managers in constructing their portfolios. The stock selection and portfolio weighting decision reflect the entirety of research views formulated by the investment team regarding valuation opportunities, future company prospects, and securities' risk/reward profiles. Naturally, if a manager's views differ from consensus expectations, the

fundamentals-driven, actively-managed portfolio would look quite different from the broad market, the relevant benchmark, and the majority of its peers.

Generally, strategies with active share of 60% or higher are considered "truly active". Passive strategies typically have an active share of 0%-20%. Products with active share between 20% and 60% fall into the "closet indexer" category -- these are managers who claim to be active, but whose portfolios are very similar in composition to the benchmark portfolio. This is an important distinction, because "closet indexers" charge active fees, yet produce results that are similar to -- and often below -- those of the benchmarks.

The first important finding of the 2006 Yale study was that active share is a powerful tool for indentifying potential future outperformers. Examining the returns of 2,650 mutual funds from 1980 to 2003, Cremers and Petajisto found that **the highest ranking active funds (those with an active share of 80% or higher) beat their benchmark indexes by 2.0%-2.7% before fees and by 1.5%-1.6% after fees**. The researchers concluded that "active share significantly helps predict fund performance". Importantly, the authors also found that active share and excess returns are higher among funds with lower levels of assets under management. The following table compares the alpha (outperformance or underperformance) of mutual funds, broken into five groups based on their level of active share (quintile one comprises funds with the highest active share, while quintile five includes the funds with the lowest active share).



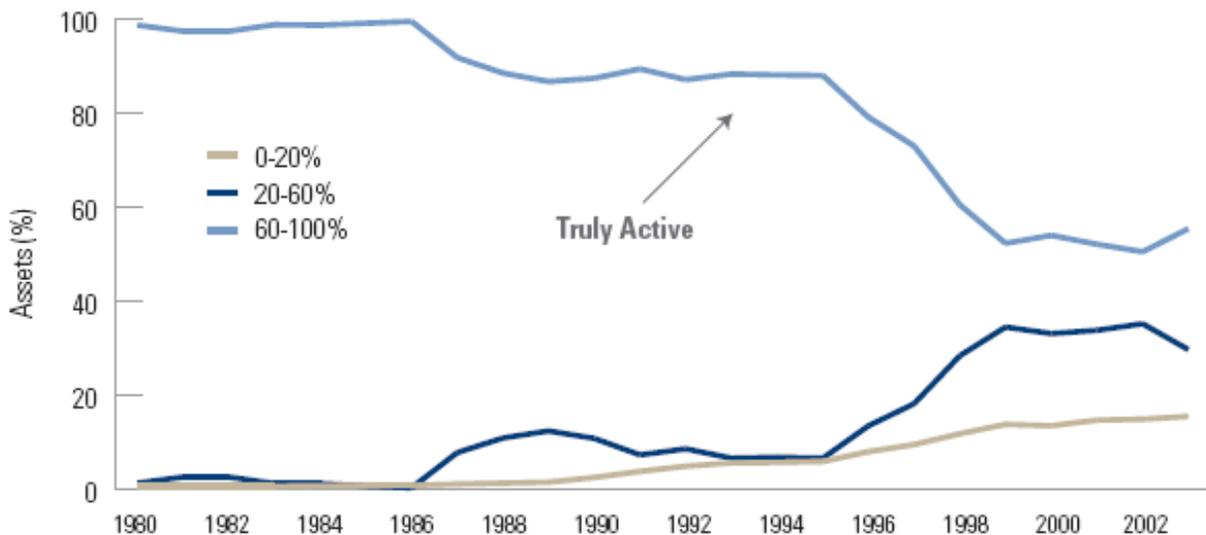
Source: Cremers, Martijn and Antii Petajisto. "How Active is Your Fund Manager? A New Measure That Predicts Performance." October 3, 2006.

Source: Brandes Investment Partners

The second important finding of the 2006 Yale study is that **over time the investment management industry has reduced its active share and become more index-like**. Specifically, the percentage of assets under management with active share of less than 60% increased from 2% in 1980 to 41% in 2003. Correspondingly, the percentage of assets under management with active share greater than 80% went down from 58% in 1980 to 28% in 2003. Are active managers "a rare and dying breed"? These data

certainly seem to indicate a shift in the money management world towards passive and quasi-passive strategies. Since the growing number of closet indexers are included in most performance studies of the broad active management universe (which do not take active share into account), their results materially skew the overall results. It is not surprising, therefore, that many draw the conclusion that the average active manager underperforms after fees. In contrast, the incorporation of active share in the research of Cremers and Petajisto shows that truly active managers are able to generate benchmark-beating returns consistently over the long term.

Percentage active share of equity mutual fund assets over time (1980-2003)⁴



⁴ Cremers, M. and Petajisto, A. 2007 "How Active Is Your Manager? A New Measure That Predicts Performance," Yale ICF Working Paper No. 06-14

Source: Goldman Sachs Asset Management

As with any other statistical study, a cautious interpretation of the results is warranted. While the average return of the group of managers with high active share is easily above the benchmarks, not every manager with high active share outperformed its respective index. Furthermore, the incorporation of active share in the manager search and selection process requires a patient and long-term oriented approach. It is well known that even top-performing managers occasionally experience short-term periods of underperformance. For instance, some of Beacon Pointe's recommended managers have lagged during the strong up-market of 2009-2010. This is not surprising, given our preference for more conservative investment styles and the nature of the market rally off the March 2009 lows. These managers' superior results during the 2008 bear market and in past challenging market environments have produced superior long-term results even if their upside capture is less than 100%.

Beacon Pointe's research efforts have always focused on investment managers that are "truly active" -- those that are benchmark-agnostic, construct concentrated portfolios; focus on capital preservation in difficult markets (the "make more by losing less" philosophy) with adequate upside participation; are committed to a strong valuation discipline with a "margin of safety" requirement; and exhibit a willingness to be contrarian and move against consensus. The Yale study on active managers and their historical results further validated our research work on our recommended managers. Active share, which we can now calculate through our analytical and database software program Morningstar Direct, gives us a valuable tool we can use going forward for identifying and evaluating potential candidates that fit Beacon Pointe's requirements. In addition, active share confirmed that the managers we already recommend in client portfolios are "truly active" as shown in the tables below.

Beacon Pointe Advisors: Focus List Managers' Active Share

Data as of 6/30/2010 (Source: Morningstar Direct)

BPA Large Cap Value/All Cap Value Managers*		
Large Cap Value Manager A	Russell 1000 Value	95%
All Cap Value Manager A	Russell 3000 Value	94%
All Cap Value Manager B	Russell 3000 Value	93%
All Cap Value Manager C	Russell 3000 Value	93%
All Cap Value Manager D	Russell 3000 Value	93%
All Cap Value Manager E	Russell 3000 Value	90%
All Cap Value Manager F	Russell 3000 Value	85%
Large Cap Value Manager B	Russell 1000 Value	81%
Large Cap Value Manager C	Russell 1000 Value	77%
Large Cap Value Manager D	Russell 1000 Value	75%

BPA Large Cap Growth/All Cap Growth Managers*		
Large Cap Growth Manager A	Russell 1000 Growth	94%
Large Cap Growth Manager B	Russell 1000 Growth	87%
Large Cap Growth Manager C	Russell 1000 Growth	84%
Large Cap Growth Manager D	Russell 1000 Growth	82%
Large Cap Growth Manager E	Russell 1000 Growth	80%
Large Cap Growth Manager F	Russell 1000 Growth	79%
All Cap Growth Manager	Russell 3000 Growth	77%
Large Cap Growth Manager G	Russell 1000 Growth	74%
Large Cap Growth Manager H	Russell 1000 Growth	74%
Large Cap Growth Manager I	Russell 1000 Growth	70%
Large Cap Growth Manager J	Russell 1000 Growth	68%

** Beacon Pointe's approved manager list is confidential information. However, we would be happy to discuss any particular manager or recommendation upon request.*

Our rigorous manager evaluation process is designed to identify those active managers that will generate market outperformance over the long term combined with strong downside protection. The typical active manager we work with has a lower risk profile and better risk-adjusted returns than the benchmark index and its universe of peers. Our intensive and thorough due diligence, backed by our robust quantitative analytical capabilities (including active share), give us a high degree of confidence when recommending managers to our clients.

Please feel free to call Beacon Pointe at 949-718-1600 should you need additional information or have any questions.