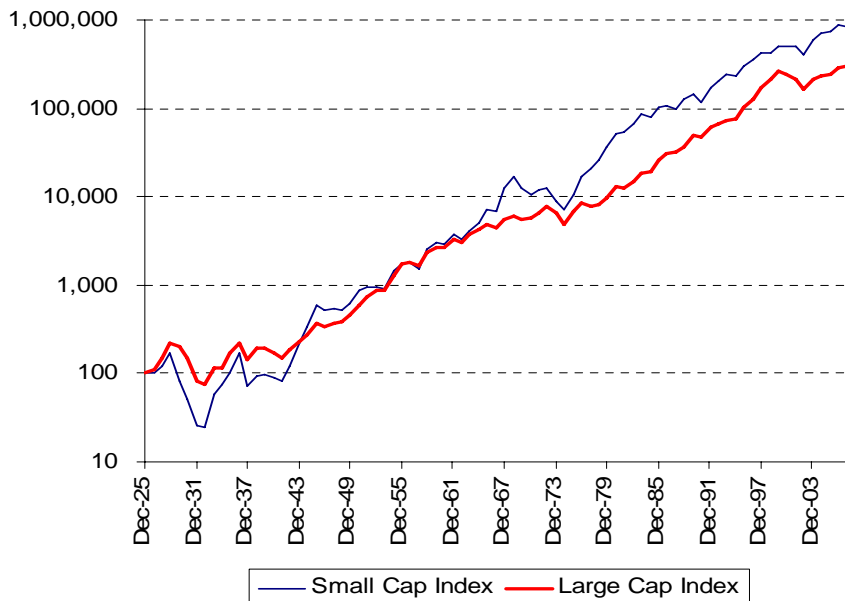


## The Case for Raising Small Cap Allocation

Small companies are the growth engine for the economy. Most new jobs are created by, and major innovations tend to come from, small companies. The stock market reflects this growth as small cap stocks have generated superior returns over the long run, even on a risk-adjusted basis. This outperformance has occurred in periods of both US dollar strength and weakness.

Small Cap & Large Cap Return

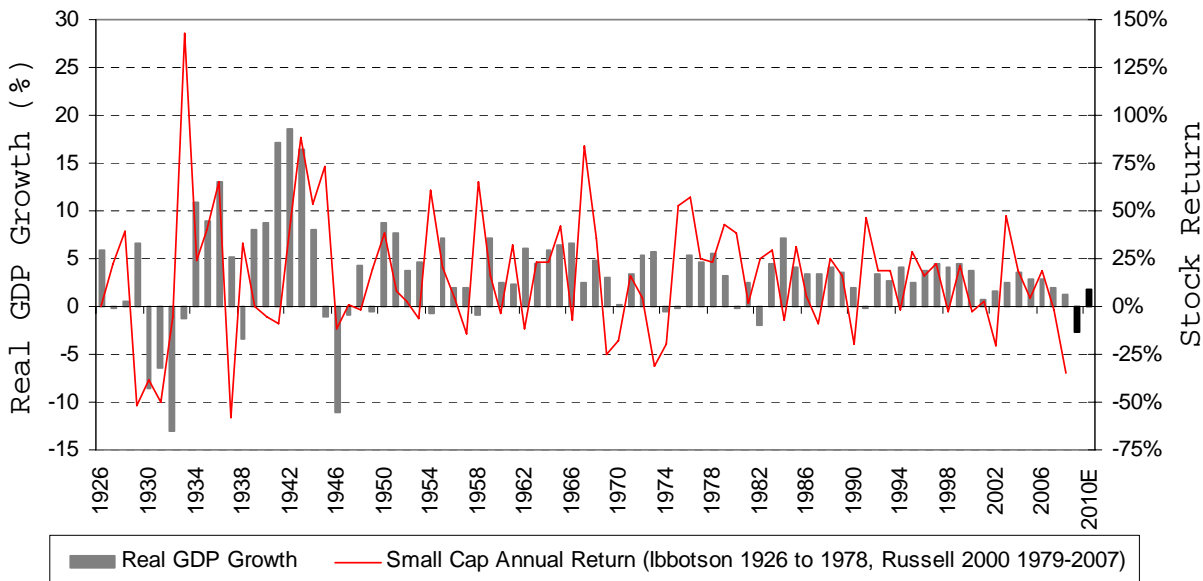


Small Cap Annual Return (Ibbotson 1926 to 1978, Russell 2000 1979-2007)  
Large Cap Annual Return (S&P 500)

### Why Focus on Small cap now?

While stocks in general turn up prior to recovery in the economy, small cap stocks tend to perform better in the early part of an uptrend. Small cap gains typically occur in the year before GDP recovers, with an average gain of 44% while GDP is still contracting in the 0% to -2% range.

Small Cap Annual Performance vs. Real GDP Trends Through 2007



**Small Cap Real GDP Test**

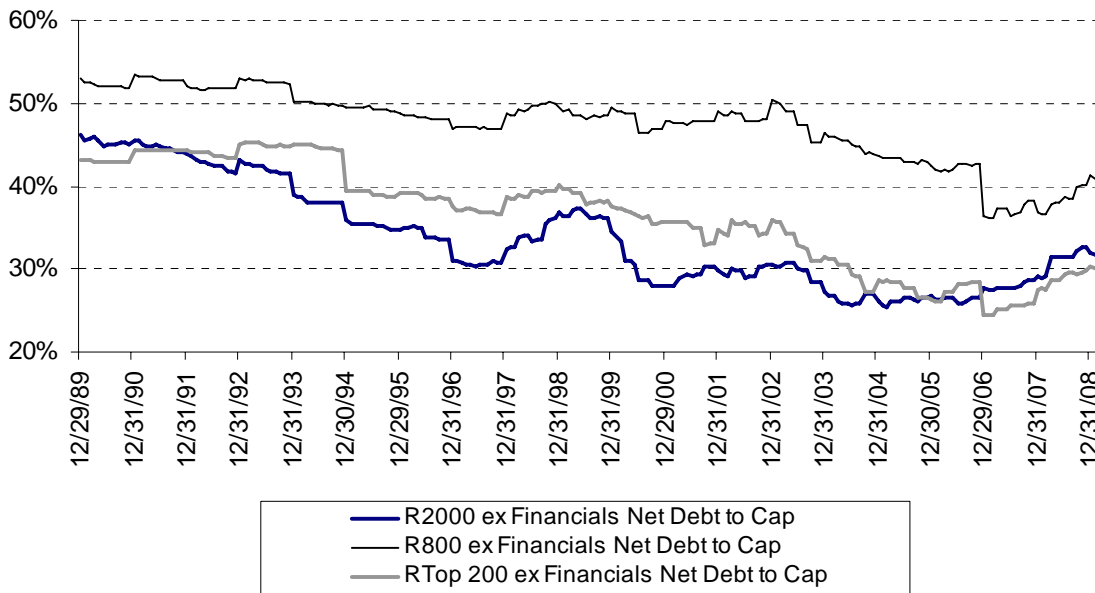
Real GDP Range	# Times	Small Cap Return				
		Avg	Max	Min	# SC Up	% SC Up
-2 to -1%	3	80%	143%	25%	3	100%
-1 to 0%	9	32%	65%	-20%	8	89%
Average		44%				

Ibbotson 1926 to 1978, Russell 2000 1979-2007

**Given the concerns about credit quality and liquidity in the financial system, aren't small caps too risky?**

On the contrary, because access to the capital markets is never guaranteed for small companies, they generally have better balance sheet integrity than large cap companies. The following chart demonstrates that small caps have historically been less levered than large companies and importantly carry higher levels of cash on their balance sheets as a percent of market cap.

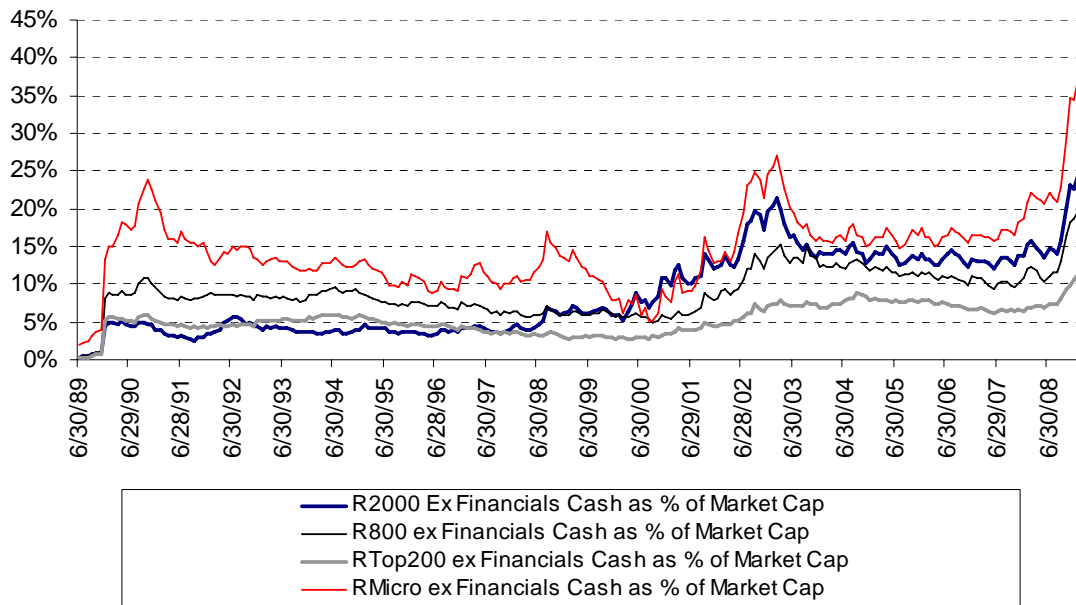
**Net Debt to Cap (ex Financials) for the Russell 2000, Russell 800 and Russell Top 200**



Source: CIR Small/Mid Cap U.S. Equity, FactSet through 2/27/2009

Currently, cash levels are higher than in the prior market trough in 2002 (See chart on next page). Furthermore, the credit crisis damaged large cap financial companies more than small cap financial concerns. In 2008, the large cap financial sector was the worst performing sector in the Russell 3000 declining, 49.9%, whereas the small cap financial sector declined 23.6% and was the third best performing sector in the Russell 2000.

## Cash as a % of Market Cap for the Russell 2000, Russell 800, Russell Top 200 and Russell Micro



Source: CIR Small/Mid Cap U.S. Equity, FactSet through 2/27/2009

### **We seem to be in a deep recession, some say the decline could be reminiscent of the 1930's. What gives you confidence that an upturn is coming?**

This country has experienced boom and bust cycles throughout its history. In most instances recovery seemed unlikely, yet through both fiscal and monetary policy the Federal government helped to find a solution for the private sector to plant the seeds for the next recovery. The new administration has been more active than any since President Roosevelt with its \$800+ billion stimulus plan. More recently the Federal Reserve announced its intention to purchase up to \$1.2 trillion in securities to inject cash into the financial system. These measures are as stimulative as any we have seen since the 1930's, yet current conditions do not come close to what the country lived through then, with 25% unemployment and no social safety nets during the worst of the Great Depression.

There are a number of signals indicating a pending upturn in the economy:

- The recent broad-based rally in stocks – led by financials
- February's +22% increase in housing starts to 583,000 units, seasonally adjusted
- Increase in retail sales, excluding autos in January and February
- Return to profitability at Citigroup, JP Morgan Chase, and Bank of America
- Doubling in Baltic Dry Index
- Upwardly sloping yield curve
- Housing Affordability index at an all time high
- Sharp increase in money supply
- \$5 trillion in liquidity on the sidelines

In conclusion, we at TAMRO Capital Partners believe the opportunities currently outweigh the much publicized concerns in the equity market, particularly for small cap stocks. Clients should benefit over the long-term by rebalancing their portfolios today back to their full equity allocation, including exposure to small cap stocks.

We would like to thank Citigroup Global Markets for their help with the enclosed charts.

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*TAMRO may or may not own any security mentioned in this paper. Nothing in this paper should be construed as a recommendation to purchase or sell any particular security or sector. Past performance is not a guarantee of future results. Performance returns presented in this paper are Index returns and include the reinvestment of income. An investor's returns would be reduced by fees. In addition to the normal risks associated with investing, investments in smaller companies typically exhibit higher volatility.*