

A Sector Capital Management White Paper



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Passive Plus “The Investor’s Index”
*An alternative to traditional market-cap-weighted indexing
and to large cap core active management*

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Contents

Introduction	3
Problem Statement	3
Part 1	3
Part 2	4
Sector Capital Solution	5
Benefit 1	10
Benefit 2	10
Benefit 3	11
Implementation	11
Summary	13
Performance Footnotes/Disclaimer	15
References	16
About the Author	17

Passive Plus “The Investor’s Index”

Introduction

This paper explores two problems that exist with traditional market cap weighted indexes: 1) Is market-cap-weighting the best measure to represent the actual market, and 2) Is there a cost effective, disciplined and repeatable alternative to market-cap-weighted indexing in the mid-to-large cap space or an alternative that doesn't just match the market but has the ability to add excess return? This paper will clearly identify these problems as they face both institutional and individual investors. The paper explores the work conducted by Sector Capital spanning 20 years of analysis, discusses a new and innovative solution, and provides an implementation strategy.

At Sector Capital, we have always been concerned with outperforming an index since most of our clients benchmark us on a relative basis against various market indices. It is especially concerning to us in the large cap core space where the market has become highly efficient and most major news is known and disbursed immediately and effectively. As a result, common sense would lead one to believe that most large cap core strategies would overtime normalize in performance close to that of the broad market index. If that is true, what would be the advantage to pay extra fees for active management if, after paying those fees, you would essentially get the same return as the index? If we buy the index instead, aren't we essentially guaranteeing ourselves that we will always underperform the index?

These are questions that do not sit well with the highly competitive nature we possess at Sector Capital. We are not content with just matching the index in any scenario. If there is not a way to outperform the index in a cost effective, disciplined, and repeatable structure then we are simply not interested in that approach. As a result, we are constantly challenging the status quo and looking for new and innovative ways to outperform.

The large cap core segment of the stock market is a challenging place to start. For example, according to LCG Associates the median active core manager underperformed the S&P 500 Index during the last five years (as of June 30, 2010) net of fees. You would have to pick a top quartile manager to have outperformed the index in the last five years, but how hard is it to pick the manager that will be top quartile? Not one that "has been" a top quartile manager, but one that "will be" a top quartile manager? Based on our collective past experience prior to Sector Capital as plan sponsors and consultants, very hard. As we know, "past performance does not indicate future results" and many managers utilize highly subjective approaches where they may be right one year and wrong the next. Picking managers based on snapshots of performance in time is highly ineffective and usually causes you to "chase the hot dot."

What this paper identifies is a solution to these problems by introducing an alternative to both cap-weighted indexing and active core equity management.

Problem Statement

- 1) Market-cap-weighted indexes have inherent flaws stemming from their core design. For instance, the S&P 500 Index is generally made up of the top 500 U.S. exchange listed stocks by market cap, which is simply the shares outstanding multiplied by the current price. In many cases, there is an oversight committee that subjectively adds and removes

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stocks from the index based on various internally arrived at criteria. The problem is a market-cap-weighted index does not effectively take into account trading activity in the marketplace. The true benchmark of the stock market is where the largest amount of trading is taking place (where investors are buying and selling), not just where the largest market caps fall.

Specifically, if you were to rank the stocks in the S&P 500 Index by market-cap and then study the daily dollar volume (price times shares traded) of each stock you would find large discrepancies from the largest stock to the smallest stock.

	S&P 500 Market Cap Ranked	Top 500 Stocks Dollar Volume Ranked	Difference
Maximum Average Dollar Volume	\$ 5,000,000,000	\$ 5,000,000,000	\$ -
Minimum Average Dollar Volume	\$ 12,250,000	\$ 56,150,000	\$ 43,900,000
Number of Stocks Below a \$56 million			
Minimum Dollar Volume	83	0	

Exxon is the largest stock by market-cap and while it has large daily dollar volume of approximately \$1.5 billion per day, it is by far not the largest stock from a dollar volume standpoint. That honor currently goes to Apple Computer with an average of over \$5 billion traded in that stock daily. By comparison, the smallest stock in the S&P 500 Index by market cap, Meredith Corp., only trades approximately \$12 million per day. Mere peanuts compared to Apple especially when considering the billions of dollars that trade in S&P 500 Index funds or ETFs on a daily basis. As shown in the chart above, if you rank the top 500 U.S. stocks based on dollar volume, the stock with the smallest dollar volume still trades over \$56 million per day. That is almost \$44 million per day more than the smallest stock in the S&P 500 Index. In fact, there are 83 stocks in the S&P 500 Index that have daily dollar volume that falls below the \$56 million level in the volume ranked top 500.

The question you must raise then is ***“if the S&P 500 Index has stocks in it that trade such fractionally small percentages of the overall traded dollars in the market on a daily basis, is it really a good, let-alone “true” representation of the market?”***

- 2) Independent of problem one discussed above and given the current market standard benchmark is a market-cap-weighted index, how do you outperform the index? If you buy the index, you will remove the risk of getting a return much below that of the index but it will still be somewhat lower than the index itself due to any fees associated with investing in an index fund or ETF. However, you will also guarantee that you will always underperform the index. Any chance of generating positive alpha (risk-adjusted excess return) will be eliminated. Given this is the case, what alternatives are there to just buying the index in an attempt to add positive alpha?

The common method to attempt to outperform the market-cap-weighted index is by selecting an independent money management firm that actively employs a strategy to

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pick stocks that it believes will perform better as a group than the S&P 500 Index or other market-cap-weighted indexes as a whole. The problem we have experienced with this approach is that the median large cap core equity manager regularly performs either inline or below that of the market index net of fees. There may be an occasional good year when a manager makes some subjective decision or just plain gets lucky and beats the market index by a significant amount, but over time returns tend to normalize back to the median. Also, the difficulty selecting the exact manager that will have its breakout year the year you place money with them is very difficult and is mostly guess work. When selecting managers based on historical performance, there is a strong tendency to give favor to the manager that has performed well most recently, sometimes called “chasing the hot dot,” which refers to picking the manager with the most attractive point plotted on a performance chart. The problem with this is that most managers are highly style specific and styles go in and out of favor. So the manager with the best performance last year, in general, is more likely to perform middle of the pack or worse the following year. Additionally, most managers employ a subjective investment philosophy which may encounter large peaks and troughs and as a result, is not highly repeatable going forward. *Are you willing to bet your retirement savings or your investment program on a guess?*

Sector Capital Solution

Sector’s solution to address these problems was to build an alternative investment strategy to both market-cap-weighted indexing and to active core management. We call this alternative “Passive Plus” because of its passive rather than active investment discipline. We also refer to it as “The Investor’s Index” because its inherent design is built directly from the decisions investors are making by buying and selling stocks on a daily basis. Every time an investor buys or sells a stock they cast a vote about that stock. Passive Plus tracks those votes and tallies them as part of its stock selection strategy.

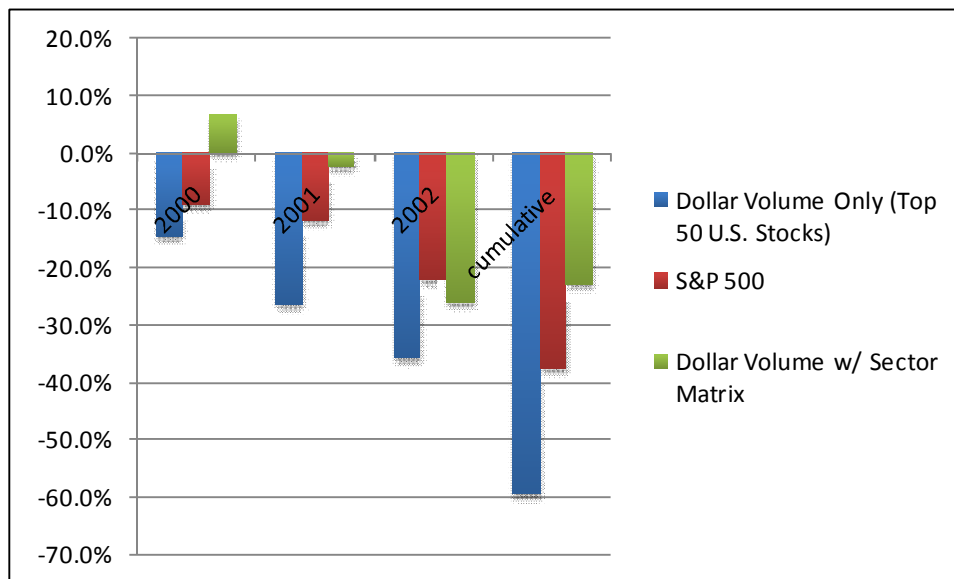
This vote tallying is actually the tracking of each stock’s “daily dollar volume,” which is an average of each trade done on a daily basis where the shares traded are multiplied by the price of the transaction. The result is a real life indication of the interest in each respective security.

We like to simplify the meaning of dollar volume for our clients by comparing it to something most people are familiar with, owning a home. And one of the most important things when selecting a home, if you ever intend to sell it someday, is its location; or as my partner, Bill Gurner, would say “location, location, location.” When buying a home you obviously want a home of good quality and a desirable layout, but if it is located near a land fill or directly under high tension power lines, are you going to be able to sell it? Probably not. Well, with medium to large cap stocks, we have found that liquidity, liquidity, liquidity is a strong driver of investor interest in a security. Stocks with little to no investor interest do not move in price and are difficult to sell. You may find a stock that is a “diamond in the rough” with great potential, but without investor interest it could take years to realize any significant gain. In contrast, stocks with strong investor interest have significant liquidity and are easy to buy or sell. An investment industry veteran and dollar volume specialist, Chih-Wei Huang, claims that there is actually an increased alpha associated with greater liquidity he calls the “Liquidity Alpha” effect. Huang

Passive Plus “The Investor’s Index”

indicates that investors have long recognized the importance of liquidity and given liquid stocks higher valuation than illiquid stocks.

At Sector Capital we have always incorporated a volume component when evaluating a security for inclusion in one of our portfolios. Fundamentals have always been the primary driver but when all else is fairly equal, the stock with greater volume would typically win out. However, over time we identified a greater level of importance from the volume component as we conducted numerous studies and back tests. Our studies revealed that in some periods the liquidity factor did provide positive alpha as Huang indicated. There were some periods where picking a portfolio on daily dollar volume alone would outperform the common indexes. However, we also found that if you go back far enough in time, (we went back to 1990) we found periods where the liquidity (dollar volume) alone actually has a negative impact on alpha. For instance, in the years following the tech bubble explosion (2000 ó 2002), we found that focusing just on liquidity or dollar volume would cause a portfolio to chase most of the high flying tech stocks of the late 1990s. These technology stocks that had little or no earnings ultimately collapsed beginning in March of 2000 and continued for the next few years.



As shown above, our back test of a portfolio of the top 50 U.S. stocks based on daily dollar volume and equally-weighted in a portfolio lost 14.4% in 2000, lost 26.4% in 2001, and lost 35.7% in 2002 compared to -9.1%, -11.9%, and -22.1% respectively for the S&P 500 Index. That is a cumulative -59% for the portfolio based on dollar volume over the three years versus a -38% for the S&P 500 Index, a 22% cumulative shortfall compared to the index. This negative alpha over three years was very concerning to us and, in our opinion, was too great to overcome with just a pure volume-only strategy. While in his 2003 article “Tracking the Real Market”, Huang makes a compelling case for considering dollar volume as an alternative to market-cap-weighting when building an index, we found that dollar volume alone did not make a suitable investment strategy for institutions and individual investors. Instead we studied the effects of incorporating our own “Quantimental” approach (a quantitative analysis of key fundamentals we call Sector Matrix™) with dollar volume. Since it was critical to us to evaluate a process that

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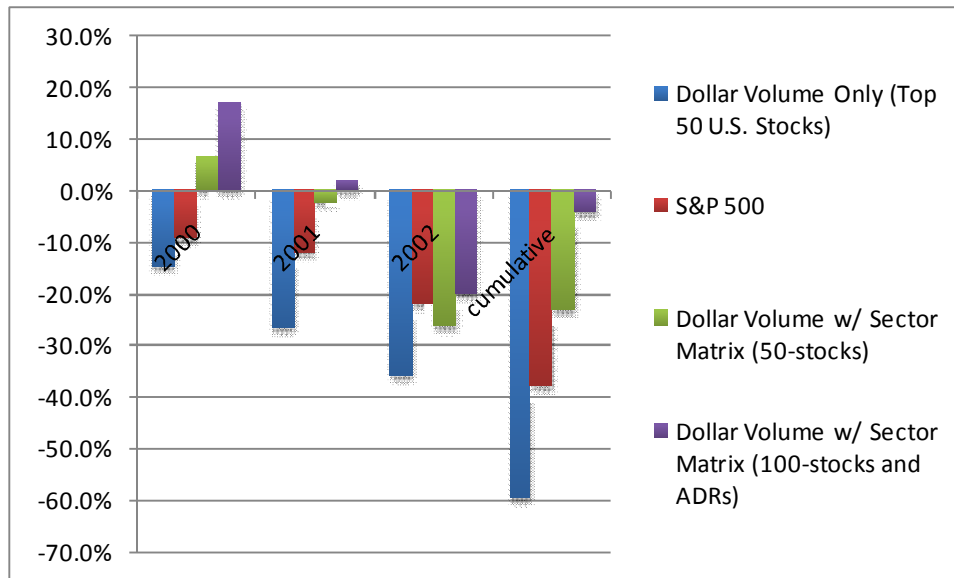
was pure, disciplined and repeatable, a process that removed any subjectivity at all, and our proprietary Sector Matrix model fit the bill.

Sector Matrix has been proven as a powerful and key component in all of Sector Capital's strategies for over five years. This matrix compiles quantitative criteria about various key fundamentals and then creates a composite score for each security. The “Quantamental” composite score can be utilized for either screening or ranking the securities. In this case, we incorporated our matrix in the screening process to ensure our universe of stocks is of high quality with real earnings, etc. Because our matrix utilizes a proprietary quantitative computer driven formula to arrive at the fundamental score we believe it was the perfect tool to incorporate fundamental analysis in a disciplined and repeatable way without subjective inputs.

We utilized the matrix to screen the universe of U.S. stocks and any stocks falling below a predefined minimum “Quantamental” score were eliminated from the analysis. From this screened universe, we simply ranked the remaining stocks by their average daily dollar volume and selected the top 50 securities. We also created a proprietary smoothing formula we utilized in calculating the dollar volume in an attempt to avoid outliers skewing our data. The portfolio was equally-weighted and there were no constraints for sector weights – sector weights were driven entirely by the investors' votes, otherwise known as average daily dollar volume. As shown in the chart on page 6, the results were eye opening. Performance improved dramatically in those difficult years of 2000-2002. The new portfolio returned 6.8% in 2000, -2.3% in 2001, and -26.2% in 2002. This calculates out to a cumulative return over three years of -23%, which is not only 36 percentage points better than the volume-only portfolio, but it is also 15 percentage points better than the S&P 500 Index during that same time period. When evaluating the full 20 year period of the back test study, we found that the passive quantitative strategy combining dollar volume and Sector Matrix outperformed the S&P 500 Index in 70% of the calendar year periods and had an annualized return of 11.2% versus 8.2% for the S&P 500 Index, an impressive 3 percentage points per year improvement. ***3% per year excess return over 20 years with compounding equates to over 80 percentage points of cumulative excess return over 20 years.***

Due to the amazing results in our 50-stock study described above, we decided to conduct a follow-on study to see what would happen if we increased the size of the portfolio to 100 stocks and also included U.S. exchange listed American Depositary Receipts (ADRs). We followed the exact same process as the 50-stock portfolio in screening, ranking, weighting, rebalancing and reconstitution. The results were even more impressive. By adding 50 more stocks and ADRs to the portfolio, the 20 year annualized return grew from 11.2% for the 50-stock portfolio to 13.4% for the 100-stock and ADR portfolio – another 2.2 percentage points of excess return per year. That works out to a total of 5.2 percentage points of excess return over the S&P 500 Index per year during the 20 year period.

Passive Plus “The Investor’s Index”



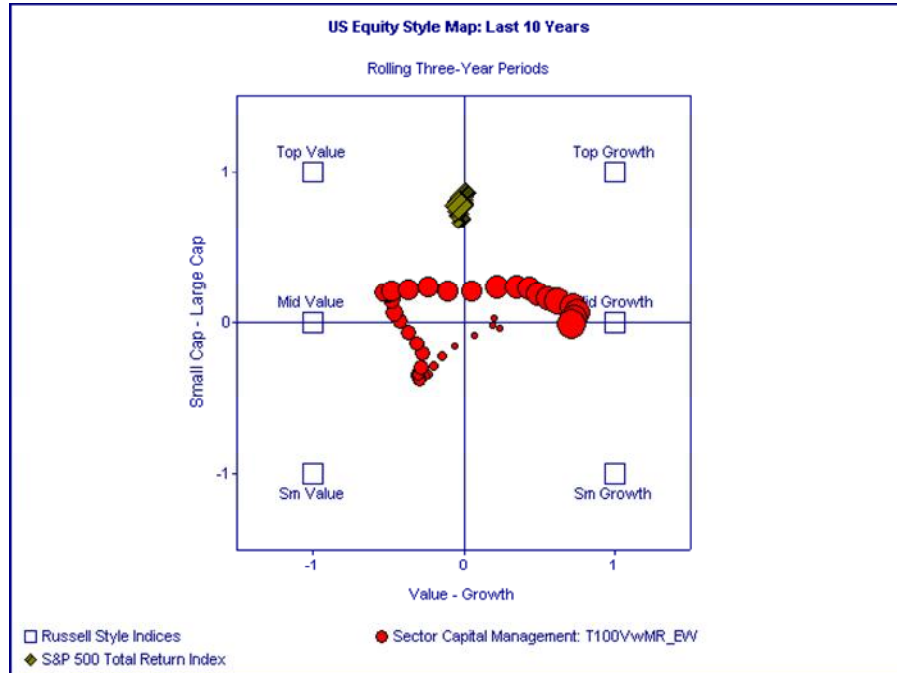
Equally impressive was the improvement in the three years following the tech bubble, as shown in the chart above. The 100-stock and ADR portfolio returned 17.33% in 2000, 2.19% in 2001, and -19.96% in 2002. In two out of those three negative years for the stock market, the 100-stock and ADR portfolio had positive returns. The cumulative return for the 100-stock and ADR portfolio during those three years was -4% versus the -38% return from the S&P 500 Index.

We found when digging into the returns further, Sector’s “Quantamental” Matrix was the more consistent alpha generator in the portfolio overtime. This wasn’t necessarily the case in every year, but in most years the Sector Matrix was the clear driver of outperformance. The dollar volume proved itself as the clear asset allocation tool or the “investor indicator” of what stocks are most appealing, what sectors are most appealing, and even what overall styles (growth versus value and mid-cap versus large-cap) are most appealing.

Our attribution analysis indicated almost half the return during the 20 year period came from the sector selection (asset allocation) decision and about half from the security selection decision. Both of these decisions were driven entirely quantitatively with the bulk of the allocation decision coming as a result of the daily dollar volume ranking, which again is a byproduct of the “investors vote” created when a purchase or sale is executed on any security.

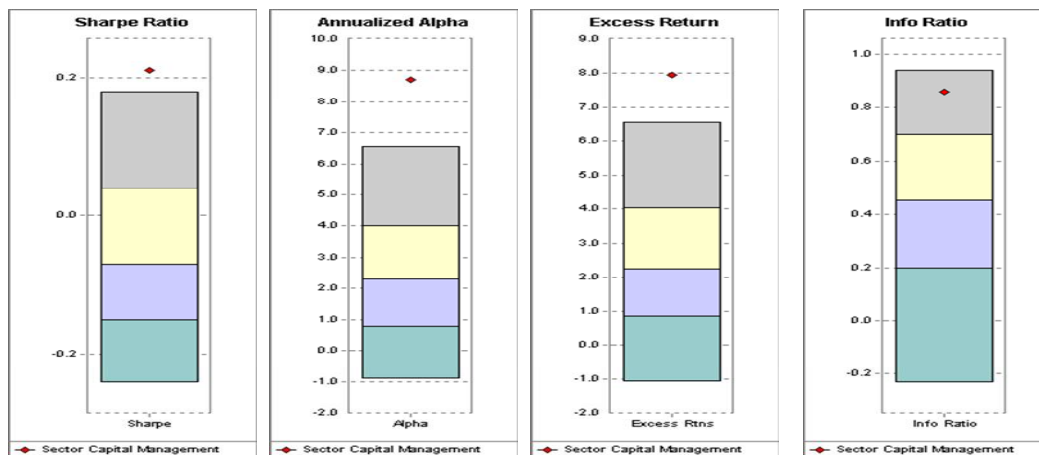
As shown in the eVestment Alliance “Style” chart below, we also found when plotting the rolling three year performance (moving ahead quarterly, each circle represents a three-year period with the smaller circles representing older time periods and the larger circles representing newer time periods) on a style analysis chart that the strategy actually shifts in style between value and growth depending on when the particular style is in favor. For instance, the strategy moved more into value in the early to mid 2000s when value was in favor and then in the later 2000s it moved into growth as growth became the dominate style from a performance perspective.

Passive Plus “The Investor’s Index”



So, therefore, rather than being a typical core strategy with an equal balance of growth and value, this passive strategy is dynamic in its style tracking and follows the investors' vote of what style is in favor versus what style is out of favor. Again, this is done purely quantitatively and without any subjective influences or constraints. As a result, the strategy is disciplined and repeatable, not left to subjective measures which could lead to inconsistency of performance like we have found with many active management strategies.

When we compared this passive strategy to the performance of active core equity managers we found it placed consistently between the top quartile and top decile of all active core managers. We also found other statistics like its information ratio, annualized alpha, and Sharpe ratio were all in the top quartile of the eVestment Alliance Large Cap Core Equity Universe during the last ten years ending 12/31/2009. Please see chart below.

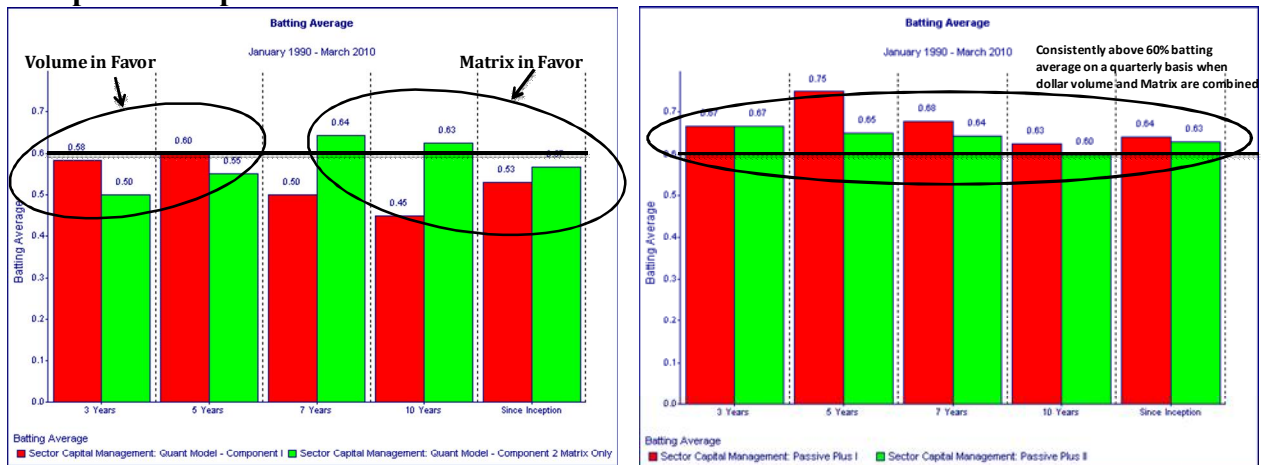


Passive Plus “The Investor’s Index”

Benefit 1

We found by blending together the two criteria (dollar volume and Sector’s “Quantamental” Matrix), the resulting portfolio was exponentially more attractive than either part taken alone. The volume by itself had some drawbacks as stated above. The matrix alone was a powerful performance contributor, but by itself it tended to create portfolios with much greater volatility and risk. Market capitalizations tended to be lower and sector concentrations tended to be higher. While this may be alright for some individual investors or as a pure alpha strategy for some institutions, we believe the strategy that combines these two factors creates the perfect core equity option for most individuals and institutions because it generates solid realizable and repeatable alpha with reasonable tracking error and reasonable standard deviation (risk). Our analysis indicated the strategy that combined the two criteria had a higher batting average and more consistently outperformed the S&P 500 Index over time than either component utilized alone. Please see quarterly batting average charts below.

Components Separated versus Combined



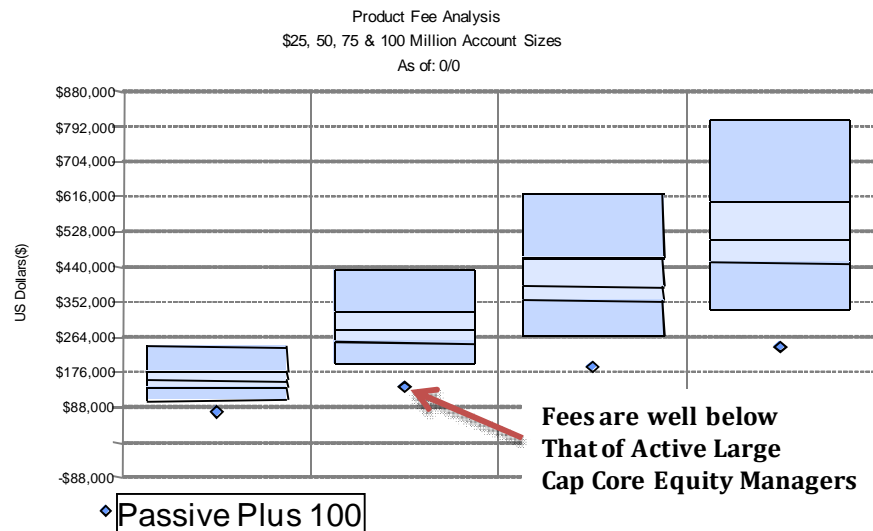
Most importantly, the passive strategy proved itself to be a much better representation of the overall market because it incorporated the stocks with the most trading activity as opposed to just the stocks with the largest market-caps. ***As such, we are confident this passive approach is an attractive alternative to traditional market-cap-weighted indexing.***

Benefit 2

Because the strategy is designed purely quantitative and managed on a passive basis, it has a highly disciplined and repeatable strategy. The strategy has shown that it not only outperforms the market (S&P 500 Index) over time, but it also outperforms most active core equity managers. Furthermore, the strategy has shown greater consistency and repeatability than most active managers. Since most managers have a significant amount of subjectivity in their approach, there is great risk from a lack of discipline which can lead to inconsistencies in style and performance. The passive strategy discussed in this paper removes the major flaws of active management, but actually retains one of the most important benefits gained from active managers in the large cap space of a strong analysis of a stock’s fundamentals. Finally, because the strategy is passive in nature, its fee structure would be well below that of active management, making it much more cost effective to implement. Please see the fee analysis chart below based

Passive Plus “The Investor’s Index”

on eVestment Alliance Large Cap Core Equity Universe manager data. The universe of active management fees is represented by the floating bars and the passive strategy is represented by the blue diamond.



As such, we are confident this passive strategy is an attractive alternative to traditional active core equity management.

Benefit 3

Lastly, because the strategy from our back test has relatively low turnover and is only traded one day per year when it is reconstituted and rebalanced, it is highly cost efficient and tax sensitive. While the cost efficiency is attractive for all investors, the tax sensitivity may only appeal to individuals or taxable investors. Regardless, it is an attractive byproduct of the strategy that gives it mass appeal. Some institutions may wonder why it is only traded once per year and since they are not tax sensitive, would it be more attractive to them to be traded quarterly? From our back test analysis, we found trading the strategy quarterly as opposed to annually did not improve returns and, in some cases, actually hurt returns somewhat. The difference was not great enough to decisively rule one way over the other, so we naturally followed the method with the lower transaction costs associated with running the strategy, annually. ***Ultimately, the passive strategy has proved it can be managed quarterly or annually with similarly impressive results versus both cap-weighted indexes and active management.***

Implementation

Based on the 20 year analysis discussed in this paper, Sector has created an investable version of the passive strategy, called Passive Plus or otherwise known as “The Investor’s Index”. It is a separately managed account composed of 100 U.S. exchanged listed stocks and American Depository Receipts (ADRs). As in the back test, the portfolio is built by first screening the universe of stocks and ADRs utilizing Sector’s “Quantamental” Matrix. The remaining stocks are then ranked by average daily dollar volume according to our smoothing formula and the top 100 are selected and equally weighted in the portfolio with 1% weights. (The portfolio could

Passive Plus “The Investor’s Index”

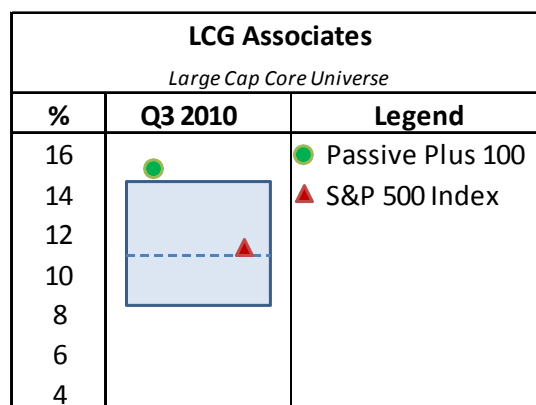
also be dollar volume weighted rather than equal weighted if there was a desire by a client to reduce tracking error to the overall market further but it would also likely lower the alpha). There are no sector or industry constraints or guidelines.

Passive Plus was started live with client money on July 1, 2010. In its first full quarter, preliminary returns have been extremely encouraging. The strategy composite was up 15.5% for the quarter versus 11.3% for the S&P 500 Index, which is 4.2% of excess return in just three months. As shown in the chart below, the strategy has outperformed the index in all three months during the quarter which included two large up months and one fairly large down month.

	Live Results as of 9/30/2010			Rolling Quarter
	Jul-10	Aug-10	Sep-10 **	
Passive Plus 100 (Live)*	7.92%	-2.67%	9.93%	15.47%
S&P 500 Index	<u>7.00%</u>	<u>-4.51%</u>	<u>8.92%</u>	<u>11.29%</u>
difference	0.92%	1.84%	1.01%	4.18%

It also compares quite favorably to a universe of active managers. According to LCG Associates, the median Large Cap Core manager earned just 11.0% for the third quarter of 2010 net of fees. Please see universe chart below.

The top quartile of Large Cap Core managers had performance between 12.1% and 14.5%. Passive Plus returned approximately 1% better than the top 5th percentile manager. This performance represents an impressive start for the product and it is consistent with expectations based on the 20 year study.



Though the current live product is mainly a large cap core equity strategy with some global exposure, preliminary “follow-on” studies have indicated other more specific products in the mid-to-large cap space could be created with similar success. Other products we have explored include style specific strategies like large cap value and growth as well as dividend focused strategies, international / global strategies, and mid cap strategies. One area where we have found the Passive Plus strategy does not exhibit the same success is in the small cap space. We found more times than not volume and historical fundamentals in the small cap space to be linked inversely to outperformance. The small cap space is much less efficient than the large cap

Passive Plus “The Investor’s Index”

space and because many of the securities are not followed by analysts, information is not as readily available. In our opinion, the small cap space among some others is still an area where active management can add realizable value-added performance over time and quantitative models are truly not as effective.

Summary

Institutions and individuals are struggling with how to treat traditional market-cap-weighted indexes. First, is utilizing a market-cap weighting structure the most effective way to represent market exposure? Just because a stock is included in a market-cap-weighted index does not mean it is widely traded by investors. And, if it is not widely traded by investors, is it a good representation of the market and does it affect my portfolio’s liquidity positively or negatively? Second, how do we incorporate core market exposure in our portfolios in an efficient manner, but also have the chance to outperform the standard indexes over time? One option is to buy the index through an index fund or ETF. However, with this approach you essentially guarantee yourself you will always underperform the index net of fees. You will track the index but will you be tracking “the market”? The second option is to hire third-party active management. However, long-term data reveals the median large cap core manager overtime to perform slightly below the index net of fees. Only managers in the top quartile outperform the index, but due to manager inconsistency from turnover, subjectivity and style specific approaches, it is difficult to find managers that plot in the top quartile on any consistent basis. It is even more difficult to identify the active manager that will plot in the top quartile looking forward over the next year. Picking a manager based on recent historical performance is akin to guessing or even gambling. *Do you want to bet your retirement on a guess?*

Sector Capital has researched these problems with the intention to find a solution for both institutions and individuals. Based on 20 years of back test studies, we have concluded one of the best alternatives to both traditional market-cap-weighted indexing and to active core equity management is to allocate to a disciplined and repeatable passive strategy. A passive strategy that combines the benefits of both average daily dollar volume and Sector’s “Quantamental” Matrix. A strategy that incorporates these two criteria in strictly a quantitative approach that is highly disciplined and therefore repeatable. A strategy that bases sector allocation decisions and style concentration not on manager subjectivity or market-cap weights, but rather on what the “investor” indicates is most attractive through the investor’s votes of buying and selling securities every day. The more the investor buys or sells a security, the greater the number of votes for the liquidity of that security. High liquidity is associated with high dollar volume and is a good indication of market interest in the mid to large cap space. Sector Capital’s research indicates that a passive strategy following this framework utilizing both dollar volume and our structured “Quantamental” matrix provides good solid core market exposure with the added benefit of adding significant alpha or excess return over time. One of the other benefits is the portfolio is extremely liquid and the companies in the portfolio tend to have the strongest balance sheets in the marketplace. So, not only do you get good core exposure with solid excess returns, but you also limit your downside by having the highest quality companies with the greatest liquidity.

Passive Plus “The Investor’s Index”

Based on this research, Sector Capital built an investable product called Passive Plus otherwise known as “The Investor’s Index”. Passive Plus follows a disciplined and repeatable strategy utilizing Sector’s “Quantamental” Matrix to first screen the universe and then utilizing average daily dollar volume to rank the universe. We select the top 100 securities (stocks and ADRs) and equal weight the portfolio. The portfolio is rebalanced and reconstituted annually, but can be quarterly for institutions if they desire more frequency of valuations and increased trading activity. This product went live with client money July 1, 2010 and in its first quarter has added over 4% of excess return versus the index and plotted above the 5th percentile in the third quarter of 2010 of the active Large Cap Core Equity Universe of managers according to LCG Associates.

Sector Capital is conducting further studies regarding this concept and have thus far found many more applications in the mid-to-large cap universe of stocks for this type of passive approach. We look forward to releasing other versions of the strategy in the near future with a style specific focus, a dividend focus, and international / global focus.

For further information, please contact Sector Capital at 901-761-4999 or visit our website at www.sectorplus.com.

Please see performance footnotes and disclaimers on following page.

Passive Plus “The Investor’s Index”

Performance Footnotes and Disclaimers

Sector Capital Management, LLC is an independent registered investment advisor. For more information on obtaining a fully compliant presentation and a complete list and description of composites, please contact us at (901) 761-4999, or (877) 826-4389 toll-free or visit our website at www.sectorplus.com for more information. Sector Capital Management’s investment strategies listed above are available via a separate account or on the Clearbrook, Investnet, Fidelity, Schwab, and TD Ameritrade platforms.

Sector Capital Management claims compliance with the Global Investment Performance Standards (GIPS). Sector Capital Management LLC’s compliance with the GIPS standards has been verified for the period January 1, 1995 through December 31, 2009 by Ashland Partners & Company LLP. All Sector Capital performance numbers are shown Gross and Net of Investment Management Fees and include the reinvestment of income. The U.S. dollar is the currency used to express performance. All returns greater than 12 months are annualized. For complete details on fees, expenses, and return calculation methodology, ask for our most current Form ADV, Part II.

Passive Plus 100 is a passively managed large cap core equity investment strategy started on June 30, 2010. It invests in 100 of the most actively traded U.S. stocks and American Depository Receipts (ADRs) that pass a minimum score on Sector Capital’s proprietary fundamental pricing model, Sector Matrix. Stocks are equally weighted and held one year. At which time, the portfolio is reconstituted and rebalanced. The performance shown is a preliminary composite of the returns for all accounts under management in the particular strategy from inception date through the ending date shown. The S&P 500 Index is a broad equity market index comprised of 500 leading companies in industries of the U.S. economy. * Inception date for the Passive Plus 100 live performance composite is 6/30/2010. ** September results for Passive Plus 100 are preliminary and do not include dividend income.

Back Test Information

The Sector Capital Management, LLC (SCM) Passive Plus model portfolio represents a hypothetical account with no actual trading activity and which may not reflect the impact that material economic and market factors might have. SCM attempts to manage this hypothetical model in a manner suitable for a taxable or tax-exempt client fund with no need for special portfolio considerations. The Passive Plus strategy can be managed in such a way that it addresses client specific considerations, however, performance under this scenario may not resemble the model performance represented in this presentation.

The investment objective for this portfolio over a three to five year time period is to exceed, by at least 2%, the compound annual rate of return available on the S&P 500 Index while owning 100 stocks selected quantitatively based on only one factor - most actively traded stocks in the index. Stocks can be equal weighted or capitalization weighted based on client preference, however, this presentation mainly reflects equal weighting. Stocks are analyzed for trading activity at the end of each calendar year and the portfolio is then reconstituted and rebalanced on the first day of the new year. These changes occur only once per annum. This hypothetical strategy is not designed to track the index but rather to outperform the index over time utilizing a passive quantitative approach selecting the top 100 most actively traded companies of all U.S. exchange listed stocks and ADRs (American Depository Receipts) that meet our Sector Matrix (a “Quantamental” pricing model) minimum score. As with most investments, there is a risk of potential loss associated with this strategy.

It is SCM’s intention to own the same securities in each client portfolio with similar objectives. However, circumstances such as market fluctuations may exist which may prevent an individual SCM client from owning one or more of the specific securities held in the Model Portfolio. Since the account is hypothetical, there can be no assurance that a SCM client would have achieved similar rates of return over the same time frame. In addition, since the time period in question is an historical one, there can be no assurance that future results achieved by the firm’s clients will in any way resemble those represented by the Model Portfolio.

The Passive Plus model returns reflected in this presentation are gross of management fees and transaction costs and include the reinvestment of income and cash. For more information, please contact us at the address or phone number listed in this paper.

Passive Plus “The Investor’s Index”

References

Papers and Briefings

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Passive Plus “The Investor’s Index”

About Sector Capital Management, LLC

Sector Capital Management, LLC is an independently-owned Registered Investment Advisor founded in 1995 by its CEO, Bill Gurner. It is headquartered in Memphis, TN. The Sector Capital Management team represents over 100 years of collective investment experience, including managing Equity Accounts for Corporations, Retirement Funds, Foundations, Taft Hartley Trusts, Endowments, High Net-Worth Individuals, and Insurance Companies.

Sector Capital's investment professionals employ a disciplined and objective investment process based primarily on a quantitative analysis of fundamental and technical factors. This innovative investment strategy is utilized in Sector Capital's different investment products that are designed to meet varied client investment objectives.

About Reed D. Walters

Reed joined Sector in May of 2009 and is the President and Chief Investment Officer. Reed works closely with the founder, Bill Gurner, co-managing the operations of Sector Capital as well as acting as a Portfolio Manager and Head Equity Analyst. Reed has nearly 20 years of investment experience as a financial analyst, portfolio manager, and investment consultant. Prior to joining Sector Capital, Reed was a partner and senior consultant at Consulting Services Group, LLC, a founder and managing partner at Renaissance Private Equity Partners, and a portfolio manager/advisor at UBS Financial Services. Reed earned his MBA and his BBA *magna cum laude* with Honors in Business from the University of Memphis. Reed also earned the Certified Investment Management Analyst (CIMA) designation in 2006. Reed is NASD Series 7, 65, and 63 licensed.