White Paper No. 35

INVESTMENT PERFORMANCE REPORTING:
JUST THE FACTS, MA'AM

White Paper No. 35 – *Investment Performance Reporting: Just the Facts, Ma'am*

Once an investment portfolio has been designed and implemented, the main job of an investor and its advisors is to monitor the portfolio to be certain it is performing as it was designed to perform. Almost nothing that can usefully be done with an invested portfolio can be done intelligently if its performance is imperfectly understood. Proper monitoring can disclose when a manager should be terminated or given more money, if the portfolio is in or out of balance versus its target strategy, whether tactical moves might be productive, whether the overall portfolio design needs to be revisited, and so on.

Unfortunately this apparently straightforward process is actually fraught with multiple perils, some of which are technological, some of which are conceptual, and some of which are behavioral. The purpose of this paper is not to present an exhaustive discussion of the vastly complex topic of investment performance reporting, but simply to outline how the process works, to identify the major challenges, and to suggest how some of the challenges might best be handled.[1]

Varieties of performance reports

First, a quick note about the kinds of performance reports investors are likely to receive, since one of the challenges we face is deciphering very different types of reports from different sources and reconciling real or apparent discrepancies among them.

Most investors will receive at least three kinds of reports: reports from the money managers themselves, reports from the custodian holding our cash and securities, and reports from an overall advisor of some kind, typically, but not always, an investment consultant.

Manager reports. All money managers send account statements to their clients, and most of these reports will be consistent with AIMR guidelines.[2] But that is the end of the similarity. Some managers send monthly reports, some send quarterly reports, some (especially some hedge funds and private equity partnerships) send only annual reports.

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[1] Parts of this paper are based on the discussion in *Creative Capital: Managing Private Wealth in a Complex World*, by Gregory Curtis (iUniverse Press, 2004), especially Chapter 16.

[2] Association for Investment Management Research, now known as the CFA Institute. AIMR guidelines are designed to ensure that managers report their returns in a manner that is both internally consistent and that is consistent from manager to manager.

Some of these reports are remarkably extensive, while others simply report the numbers. A central problem with many money manager reports is the way performance is reported against benchmarks: by manipulating the benchmark and/or by changing the measuring period, a manager can transform poor performance into ordinary performance, and ordinary performance into good performance. In addition, some benchmarks are relatively easy to beat, so it is possible for a manager to look good against its benchmark but to look very bad against peer managers. More broadly, the problem with most manager reports is that they are not customized to meet the needs of individual clients. Managers produce standard reports that go to all clients, regardless of their needs.

Bank custody reports. Most substantial investors will – or should! – have their investment assets held in custody by a large bank or, sometimes, a brokerage house. These custodians provide monthly reporting on all managers, but the reports are normally not performance reports per se, but rather reports on holdings, values, and transactions. These reports are important of course, and they are crucial for tax purposes, but they are largely useless when it comes to monitoring the performance of a portfolio. The reason, of course, is that simply showing account values says nothing about whether the increase or decrease in value during the period was a happy or unhappy outcome.[3]

Reports from an overall consultant or advisor. Investors who work with a consultant or other overall advisor, as most substantial investors now do, will also receive reports from this advisor. In fact, one of the main reasons large investors engage consultants is to ensure that they receive consolidated and informative performance reporting on their entire investment portfolio.

A good advisor's reports will show at least the following, preferably on one or two pages (plus commentary):

- The performance of each manager in the portfolio for the current period, the year-to-date, and since-inception.
- Manager performance will be compared against appropriate benchmarks for each of the periods mentioned above.
- Often, the reports will show manager performance against peer managers, although sometimes this data is not available in time to be included in the performance report.
- The performance of the client's portfolio in each sector will be compared to sector indices.

[3] An increase in account values can be an unhappy outcome, of course, if the increase would have been much greater had better strategies or managers been employed.

- The report will show the performance of the overall portfolio, usually measured against some sort of custom index.
- In addition, the best advisor performance reports will contain customized comment on the client's performance, highlighting where the portfolio is performing well and where there may be areas of concern. In particular, these comments will address areas where performance appears to be satisfactory but is actually worrisome, or where it appears to be worrisome but is in fact acceptable.
- Most advisors' performance reports will contain commentary on the various market sectors, so that clients who have a more detailed interest in market events, momentum, and valuations can place their own results in context. Importantly, these comments should include an opinion about where in the capital markets value seems to lie and where over-valuations – and hence danger – persist.
- Every performance report should show a client how the portfolio is positioned against its target asset allocation strategy.
- For clients with significant private equity commitments, a separate chart should normally be included showing (a) original commitments, (b) takedowns to date, (c) distributions, (d) remaining commitments, and (e) an internal rate of return (IRR)[4] for each investment.

The mechanics of performance reporting

The data needed to produce a first-rate investment performance report can be assembled in various ways. It is most certainly not the purpose of this paper to discuss the many technical issues associated with this enterprise, but a general understanding of how performance data is gathered and presented is useful knowledge.

As noted above, most serious investors will have their assets held in custody by a large bank or other financial institution. Individual money managers will trade securities in accounts set up for them by the bank, but the cash and securities in the account will never leave the bank's hands (unless the client requests a wire transfer). When a manager sells a stock, cash replaces the value of the stock. When the manager buys a stock, the stock replaces cash. Thus, the bank has a complete audit trail for all buys, sells, dividend payments, stock splits, transfers into and out of the account (by client request), and so on.

[4] While time-weighted returns are used to calculate the performance of traditional managers, IRRs, or cash-on-cash returns, make far more sense for private equity investments.

At the end of a quarter, lets say that Manager A reports a return of 2.3%. Our advisor should be able to look at the transaction history in Manager A's account and calculate the same return. But how does the advisor "look" at this transaction history?

The answer is that the advisor is downloading that data from the bank on a daily basis. These downloads have been authorized by the client and occur via a transfer protocol that allows the advisor's performance reporting system to recognize the transferred files.[5] Thus, at the end of the month, quarter, or any other period, the advisor knows what the custodian bank knows and can make its own return calculations for Manager A and every other manager in the client's portfolio. The advisor will also roll these calculations up so that the client can see how each sector of the portfolio performed and how the overall portfolio performed.

Advisors' presentations of these performance results can vary dramatically – the presentation of performance results is an art, not a science. Some advisors will simply use the standard reports embedded in the performance reporting system it is using, while other advisors will use special reporting systems designed to improve the presentation and accuracy of the data.[6]

The bottom line is that an accurate and understandable investment performance report requires close cooperation among a custodian, an advisor and several varieties of technology and systems.

Walking through an advisor's investment performance report

Exhibit A shows a portion of a sample investment consultant performance report, in this case for a high net worth family. Let's look more carefully at this report, focusing on the issues we have just listed.

The performance of each manager for the current period, the year-to-date, and since-inception. Looking at page 9 on Exhibit A, we can see that this particular client has engaged four US large cap active equity managers – probably an unlikely scenario in this efficient market sector,[7] but we have overloaded the sample client with managers for illustrative purposes. These four managers are investing a total of $26,468,147, or 19% of the client's entire portfolio.

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[5] The state of the art in performance reporting systems today is Advent Axys.

[6] InvestEdge is an example of this technology.

[7] In sectors of the market that are highly efficient (such as US large cap or bonds), hiring several active managers is probably a suboptimal use of investment management fees.

Note that each manager has had quite different results[8] for the current period, the year-to-date, and since-inception (assumed to be 12/31/01), although the longer term performance among the managers tends to converge. Thus the Large Cap Alpha Manager has led the pack in terms of performance for the quarter and year-to-date, but longer term his performance is rather similar to that of the Large Cap Value Manager. As it turns out, the Large Cap Alpha Manager follows a strategy of moving between growth and value styles as he sees under-valuation in one style and over-valuation in the other. As a result of the staggering over-valuation of growth stocks in the late 1990s, this manager has focused on value stocks during all of the reporting periods. And since he is a concentrated player, never owning more than 20 securities, his performance has been quite good.

Meanwhile, the second listed manager, a Large Cap Growth Manager, has struggled, producing absolute results that seem unattractive. Finally, the Large Cap Passive Manager, who controls the largest pool of capital because the client believes this sector of the market to be extremely efficient, has produced results that fall, in absolute terms, between the growth and value styles.

Manager performance will be compared against appropriate benchmarks. Below the listing of managers on Exhibit A the advisor has shown the performance of the benchmarks that are appropriate for these particular managers. Thus, we can see the following:

- The Large Cap Alpha Manager has blown away the S&P 500 Index for the quarter and year-to-date, but since inception his performance is not that dissimilar from the Russell 1000 Value Index. Because he is a concentrated manager, and therefore his results are much more volatile than the results of the other managers, it may behoove the family and their advisor to consider whether this manager is really earning his keep, despite his apparently strong performance: highly volatile managers must produce higher rates of return to compound wealth at the same rate as managers whose results are less volatile.
- Measured against the S&P 500, Large Cap Growth Manager looks pretty bad for all periods. But it is important to remember that growth stocks were badly out of style between 2001 and 2004. If we measure this manager not against the S&P 500, but against a large cap growth benchmark – in this case, the Russell 1000 Growth Index – we see that he has actually done reasonably well. It's not his fault, after all, that growth stocks are out of fashion.
- The Large Cap Value Manager has produced strong absolute results, but measured against an appropriate benchmark – in this case the Russell 1000 Value Index – he doesn't look so strong. In fact, his shorter term results are slightly below-benchmark, though longer term he has added value. These short-term results are unlikely to be

[8] Importantly, each manager's results are shown net of fees.

cause for concern, given the longer term outperformance. But in any event the advisor knows that this manager is not a deep value player, but rather a classic value player. When deep value stocks are in vogue, as was the case during the shorter term period, he will likely trail the value benchmark.

- As expected, the Large Cap Passive Manager has produced results that closely track the S&P 500 Index for all periods. His slight under-performance for most periods turns out not to be cause for concern for an interesting reason. This manager is a passive, tax-aware manager who is constantly harvesting losses that occur through natural market volatility. These losses can then be used to offset realized gains in this or other manager portfolios. Thus, while the manager has very slightly trailed the index on a gross-of-tax basis, on a net-of-tax basis the client is well ahead of the game.

Manager performance may be compared against the performance of peer managers. In this case, no peer data is shown because it was not available in time to be included in the performance report. It is possible that the advisor will issue a supplemental report showing the performance of this client's managers against peer group universes, or the client may wish to see this data only once a year. On a quarterly basis manager universe rankings are of little use.

Performance will be compared to sector indices. Notice, just above the manager listings, that the advisor's report shows the performance of the client's overall US large cap equity portfolio. In other words, the performance of the four managers has been rolled up to show how all the securities combined have performed for the periods shown. This data is important, because it shows the advisor's skill – or lack of skill – at picking managers. In this sector of the client's portfolio, it turns out that the advisor has added value: net of all manager fees, the client's US large cap equity portfolio has outperformed the S&P 500 Index.

The performance of the overall portfolio will be measured against a custom index. At the top of the performance chart the advisor has shown the performance of the client's overall portfolio for these periods. This performance has been compared to the performance of a custom index, namely, 20% S&P 500, 10% Russell 2000, 15% MSCI EAFE, 5% MSCI EM Free, 20% Lehman Muni Bond, 20% HFRI FOF, and 10% DJ-AIG Commodity. The custom index closely tracks the client's target asset allocation strategy, and in this case is a largely investable[9] custom index – in other words, the clients could themselves passively achieve the returns on this custom index by investing in index funds, exchange-traded funds, futures, and so on. By comparing the performance of the portfolio to the custom

[9] Portfolios with significant exposures to private equity will not have investable custom indices, although in fact linking PE and traditional manager performance is problematic in any event. See Note 4, above.

index, the client can get a quantitative measure of the value its advisor is adding. In this case, the since-inception numbers show that the portfolio has added 101 basis points of value over the custom index. This value has been added in part by manager selection, in part by tactical asset allocation bets the advisor has made away from the target strategy, and in part by the advisor's astute tax management of the portfolio.[10]

Customized comment on the portfolio's performance. While some individual investment managers will provide detailed commentary on how they added or subtracted value from the portfolio during the period, it is quite rare for an overall advisor to provide custom commentary on the performance of his client's portfolio. The reason is simple: it is very time-intensive to do so, and for a consulting firm time is money. Nonetheless, we believe that this sort of commentary can be useful for many clients. Few clients are expert investors, and hence simply sending a performance report containing numbers is unlikely to prove enlightening. Meeting with the client immediately after the report has been delivered can substitute for portfolio commentary, but this is not always possible. By adding even relatively brief comments about manager, sector and overall performance, clients are likely to feel far more comfortable with their portfolios, far more comfortable with their advisors, and will be far less likely to do the wrong thing in reaction to short-term market events or short-term manager under-performance. Sample portfolio commentary from this advisor is shown on pages 11 and 12 of Exhibit A.

Market commentary. Most, though not all, advisors preface their performance reports with market commentary: their take on what has happened in the markets during the current period, why it seems to have happened, and what it bodes for the future. Clients may or may not have an interest in these comments – their purpose is to put the client's own performance in broader context – but the mere fact that the advisor is forced to write commentary ensures that the firm is watching the market and developing an informed judgment about it. Sample market commentary is shown on pages 1-6 of Exhibit A.

Value and danger. One important aspect of market commentary is the advisor's views on where opportunity exists in the markets (i.e., where valuations are well below historic norms), where danger exists (i.e., where valuations are well above historic norms), and where sectors of the market appear to be fairly valued. While no serious investor should engage in market timing, investors are constantly faced with decisions about where to invest capital, where to take capital from a portfolio to meet liquidity or spending needs, when to rebalance and how far back toward the target strategy to rebalance, and so on. While investors need to appreciate the power of market momentum, the surest way to inform these decisions is to base them on a valuation discipline. A sample of this advisor's valuation views, shown in chart form, can be seen on Exhibit A at page 7.

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[10] See Greycourt White Paper No. 36, How Consultants Add (and Subtract!) Value (forthcoming).

Asset allocation versus target. Because an investor's asset allocation strategy will tend to drive long-term investment results, every investor needs to know how the portfolio is positioned against the target asset allocation strategy. On page 8 of Exhibit A we can see that the advisor has plotted the current portfolio against the target portfolio (in graph form and bar-chart form), and has also shown whether or not the family's portfolio is within the target range that was established when the portfolio was designed. In this case the family is well within their ranges and only slightly above or below the targets in each sector. This does not mean that the advisor won't recommend some kind of tactical shift in the portfolio – that will be driven by the advisor's assessment of relative valuations in the marketplace – but only that any such shifts will not be required by the portfolio's drift away from its target strategy.

Special reporting for private equity investments. Because this particular family has made substantial commitments to private equity partnerships, the advisor has included a chart (page 10) showing the information mentioned above, namely, original commitments, takedowns to date, distributions, remaining commitments, and an internal rate of return for each investment.

Reconciling the numbers

One of the most important functions of an advisor's consolidated report is to reconcile each manager's reported performance results with the value of the cash and securities in the hands of the custodian. If a manager reports his quarterly performance to be +3.2%, the advisor should be able to look at the beginning and ending account values (plus or minus account additions or withdrawals and any dividends or interest) and calculate the same number. If there is a discrepancy, then something is wrong somewhere,[11] though more often than not the difference has to do with timing or pricing protocols.

For example, when a security trade is made, the pricing of the trade is established by the trade date, but the actual proceeds change hands on the settlement date. For a money manager, it is the trade date that matters, since that date establishes the price the firm will receive from a sale or will pay on a purchase, and it is that price that becomes a part of the firm's permanent track record. Hence, managers tend to prepare account statements using trade dates.

[11] Note that some kinds of assets cannot be held in custody in the usual sense of the word. Hedge fund assets, for example, are not held by the client's custodian but by the hedge fund manager's custodian – his prime broker – and hence the hedge fund manager is the broker's client, not the investor. Private equity capital is not custodied at all, but is typically called down by the general partner as needed and used more or less immediately to invest in portfolio companies. Finally, mutual funds have their own custodians. If hedge funds, private equity partnerships and mutual funds are shown at all on custody statements, they are typically shown only as line-item entries.

From the perspective of a custodian, however, what matters is whether the proceeds from a trade are successfully received into the account, and what the value of those proceeds is. Until the proceeds from a transaction are actually received into the account, the matter is purely hypothetical. Hence, banks tend to prepare accounts using settlement dates. Managers, in other words, are engaged in a performance game, while custodians are engaged in a money-counting game.

Inevitably, some securities transactions will straddle the closing date for the preparation of custody account reports. If the trade date for a transaction is September 30, the manager who made the trade will show the proceeds of the trade in its account statements and as part of its performance record. As far as the bank is concerned, however, no proceeds from the trade have been received into the account. Hence, the bank will not show those proceeds on its account statements for that period.

Other discrepancies can arise as the result of decisions about accruing dividends and interest payments, the use of different securities pricing services, and so on. Unfortunately, when we simply look at differing balances sent to us by managers and banks, it is impossible to know whether the discrepancies are related to harmless protocol-timing issues, or whether the errors may be more serious. Very large family or institutional investors will reconcile manager and bank statements, but most investors will need to engage someone to handle this chore (and a chore it is!) on their behalf. The usual "someone" is an investment consulting firm that has built a sophisticated back office that downloads account data from the custodian on a daily basis.

The future of performance reporting

In a perfect world, *quantitative* performance reporting – calculating manager performance, sector performance and overall portfolio performance and comparing all of that to appropriate benchmarks and indices – would be a task performed by asset custodians. The custodians would share granular data on manager performance (monthly return series, for example) with client financial advisors. After all the custodian already holds the cash and securities, has already invested enormous capital in systems, and can easily make these calculations. The role of the overall advisor or consultant would then be to supply to the client the *qualitative* overlay, explaining what the performance numbers actually mean and what, if anything, the client should do about it.

But until this perfect world arrives (not in our lifetimes…),[12] investment consultants and similar advisors will continue to supply both quantitative and qualitative reporting, and thoughtful investors will find it worth their time and attention to understand how investment performance reporting happens and what it means to their investment success or failure.

GREYCOURT & CO., INC.
October 2005

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> *Please note that this presentation is intended to provide interested persons with an insight on the capital markets and is not intended to promote any manager or firm, nor does it intend to advertise their performance. All opinions expressed are those of Greycourt & Co., Inc. The information in this report is not intended to address the needs of any particular investor.*

[12] One interesting development, however, is that account aggregation systems are actually beginning to be useful. This much over-promised development, which many investors have simply given up on, looks like it could soon be close enough to reality to be worthy of serious investor interest.

EXHIBIT A

Sample Client

Performance Report: *4th Quarter 2004*

Market Performance Summary – Period Ending December 31, 2004

	Index	4th Qtr%	Year-to-Date%
Domestic Equity			
Core Market	S&P 500	9.2%	10.9%
Broad Market	Russell 3000	10.2%	12.0%
Large Cap	Russell 1000	9.8%	11.4%
Large Growth	Russell 1000 Growth	9.2%	6.3%
Large Value	Russell 1000 Value	10.4%	16.5%
Small Cap	Russell 2000	14.1%	18.3%
Small Growth	Russell 2000 Growth	15.1%	14.3%
Small Value	Russell 2000 Value	13.2%	22.3%
Technology	NASDAQ	14.7%	8.6%
International Equity			
Global Markets	MSCI All Country World	12.3%	15.8%
Developed Markets	MSCI EAFE	15.4%	20.7%
Emerging Markets	MSCI EMF	17.3%	26.0%
Fixed Income			
Taxable Bonds	LB Aggregate	1.0%	4.3%
Municipal Bonds	LB Muni Bond	1.3%	4.5%
High Yield	Merrill Lynch High Yield Master	4.5%	10.8%
Cash	Citicorp 3-month T-bill	0.4%	1.2%
Specialized Markets			
Real Estate	NAREIT Equity-REITs	15.2%	31.6%
Hedge Funds	HFRI Fund of Funds	4.4%	6.4%

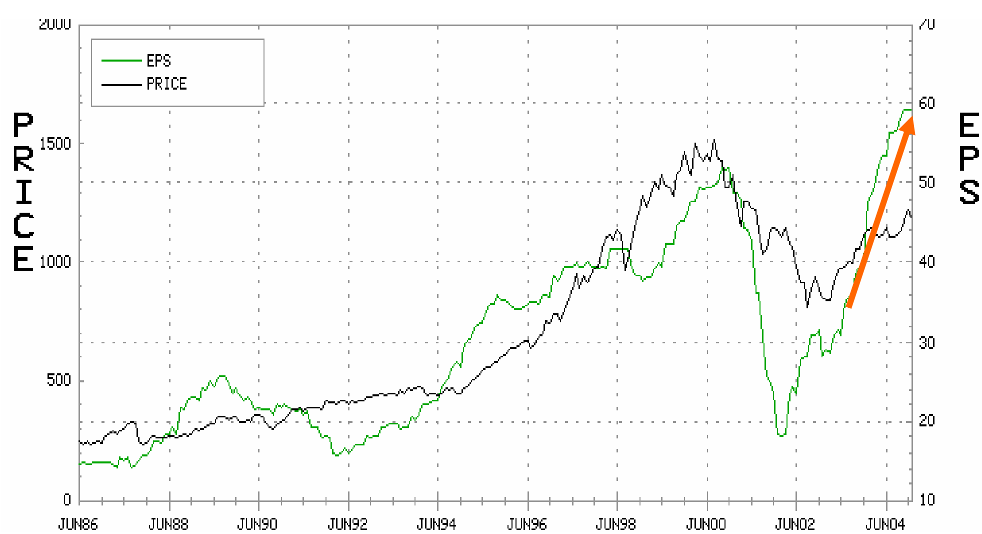
Please refer to the 'General Performance Disclosure' page for important information about these indices.

Market Overview

The wall of worry confronting corporate managers and investors alike began to crumble in early November following the decisive re-election of U.S. president George W. Bush, falling crude oil prices, continued strong corporate earnings reports and tame inflation. All of this holiday cheer resulted in a massive rally in the global equity markets. During the last 60 days of 2004, the S&P 500 Index jumped 7.6%, the Russell 2000 Index was up 11.3% and non-US stocks soared by 10.9%. By contrast, during the bulk of 2004 (January through October) equity markets rose only a meager 5.6%.

We find it puzzling that equity markets rose so sharply near year-end. After all, forecasts of corporate earnings growth continue to fall while interest rate levels are simultaneously forecasted to rise. Since stock market prices are driven by a combination of expected earnings, expected interest rates and changes in investor confidence, we must conclude that investors simply feel that investing in equities is less risky today than it was prior to November. Are investors correct? Is the risk of investing in equities falling? Unfortunately, we think that investors are under estimating the magnitude and nature of risks confronting the stock market today. In particular, we remain concerned about the following:

1. Interest rates are likely to rise persistently throughout most of 2005 as the Federal Reserve seeks to achieve a more neutral monetary posture. Despite strong global GDP growth, today's rates are still stimulative – money market yields are below the prevailing rate of inflation (i.e., the real rate of return on cash assets is negative).
2. Alan Greenspan retires in 2006. Markets will begin to react to speculation of this iconic Fed chairman's replacement.
3. Oil prices are likely to remain high (and volatile) as demand from Asia is unlikely to slow.
4. The U.S. dollar remains vulnerable to further declines as the U.S. continues to generate huge current account and budget deficits.
5. Over-leveraged and aging consumers will be hard pressed tocontinue to spend as freely as they have in the past. Savings rates are low, retirement looms for baby boomers and high gasoline prices sap consumers' pocket books.



Earnings growth since June 2002 has been remarkable. This should be no surprise given the magnitude of the fiscal and monetary stimuli applied in 2002. However, pressure on the US dollar, tired consumers and rising oil prices are likely to slow future growth.

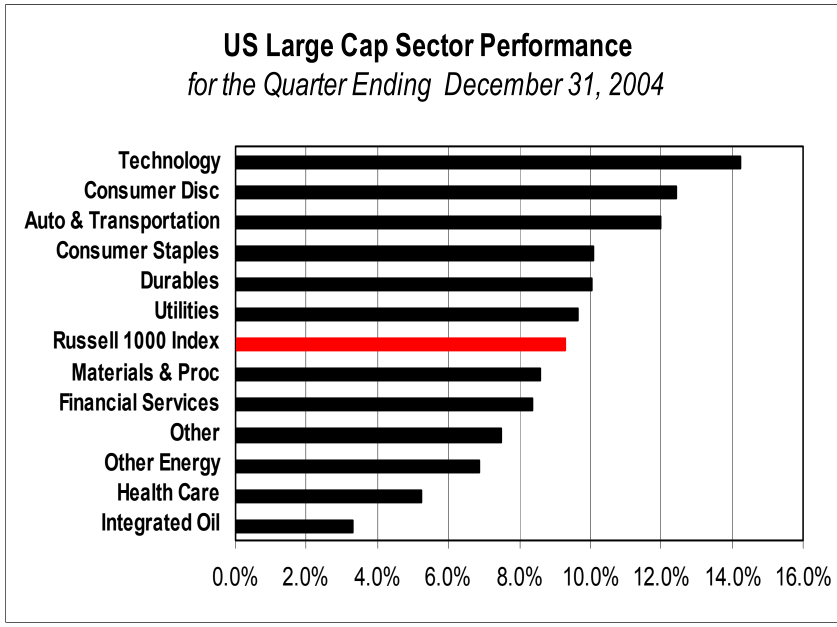
US Equity

4th Quarter 2004

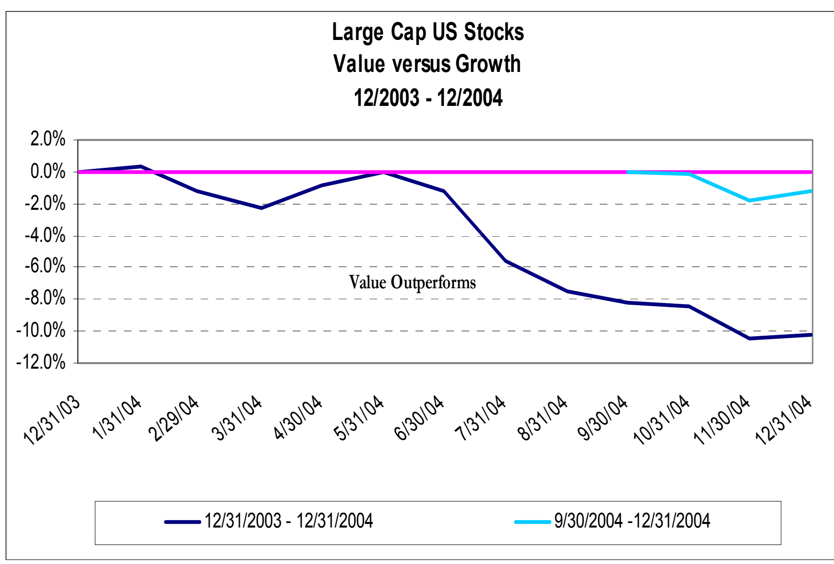
❖ Thanks, in part, to the largest post-election bounce since 1952, the S&P 500 grew 9.2% for the quarter. After nominal gains in October, the index rose by 4.1% and 3.4% the last two months of the year, pushing total returns for the year to 10.9%.

❖ All sectors were up for the quarter, with technology and consumer durables/non durables being the primary beneficiaries of a rejuvenated consumer. Financial stocks under-performed on a relative basis as interest rates rose but rallied somewhat at year-end as many of the major investment banks had a record year. After a torrid couple of quarters, energy stocks caught their breath as oil prices slipped almost 20% in December.

❖ While the S&P 500 is still 20.7% off its 2000 peak, it is interesting to note that almost two-thirds of the stocks within the index are trading higher. This fact again reminds investors how concentrated performance had been in 2000, especially due to the influence of the technology sector.



Source: Frank Russell & Company



Source: Bloomberg, Frank Russell Co.

This chart represents the return of the Russell 1000 Growth Index less the return of the Russell 1000 Value Index.

US Equity

4th Quarter 2004

- After a difficult period in the middle of the year, economic results showed greater staying power than many had anticipated. Third quarter GDP improved to 4% and consumer spending rebounded to approximately 5%. According to The Conference Board, consumer confidence jumped to 102.3 in December (forecast had been for 94), a good sign for continued spending in early 2005.

- However, the news was not quite as bright as we headed into the New Year. After a 2004 in which Fed policy was relatively easy to anticipate (the targeted federal funds rate ended the year at 2.25%, exactly where many had predicted) 2005 should be more difficult to forecast. Record trade and budget deficits, the continued weakening of the dollar, and mixed economic news, have many estimates ranging from 3.5% to 4%.

- CPI for the twelve months ending in November stood at 3.5%, almost twice that of the year before.

- Consumer spending makes up almost two-thirds of US economy and with imports at 16% of GDP and exports only 11%, it will be extremely difficult to reduce the trade deficit (now almost 6% of GDP) without slowing the economy.

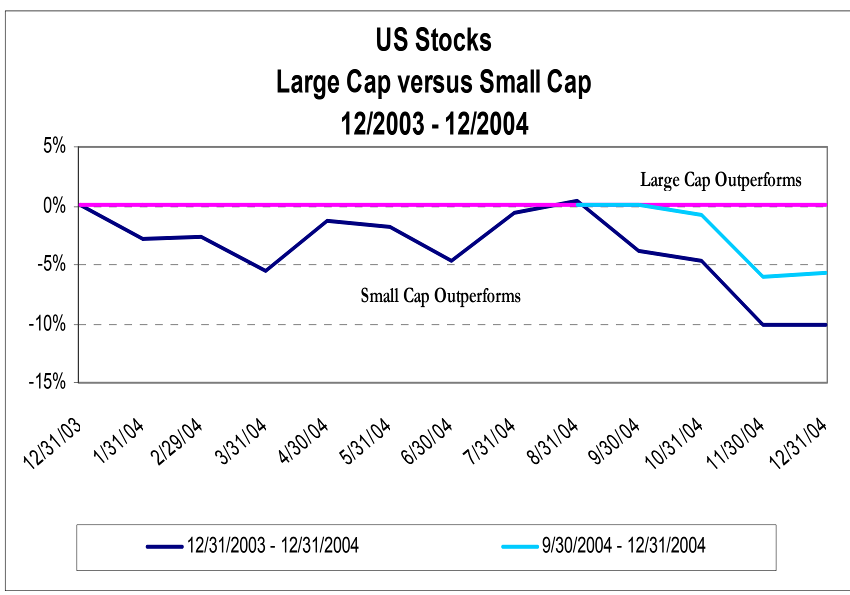
Key Economic Statistics

Economic Statistic	Index as of 9-04	Index as of 10-04	Index as of 11-04	Index as of 12-04
Gross Domestic Product (annualized)	4.0%	*	*	3.1%
Consumer Price Index ex food & energy (MoM)	0.3%	0.2%	0.2%	0.2%
Producer Price Index (MoM)	0.1%	1.7%	0.5%	-0.7%
Leading Economic Indicators (MoM)	-0.3%	-0.3%	0.3%	0.2%
ISM Manufacturing Index	59.1%	57.5%	57.6%	57.3%
Unemployment Rate	5.4%	5.5%	5.4%	5.4%
U. of Michigan Survey of Consumer Confidence	94.2%	91.7%	92.8%	97.1%
Capacity Utilization	78.0%	78.5%	78.6%	79.2%

* Data available quarterly, only.

Source: Bloomberg

This chart represents key economic statistics for the most recent time periods.



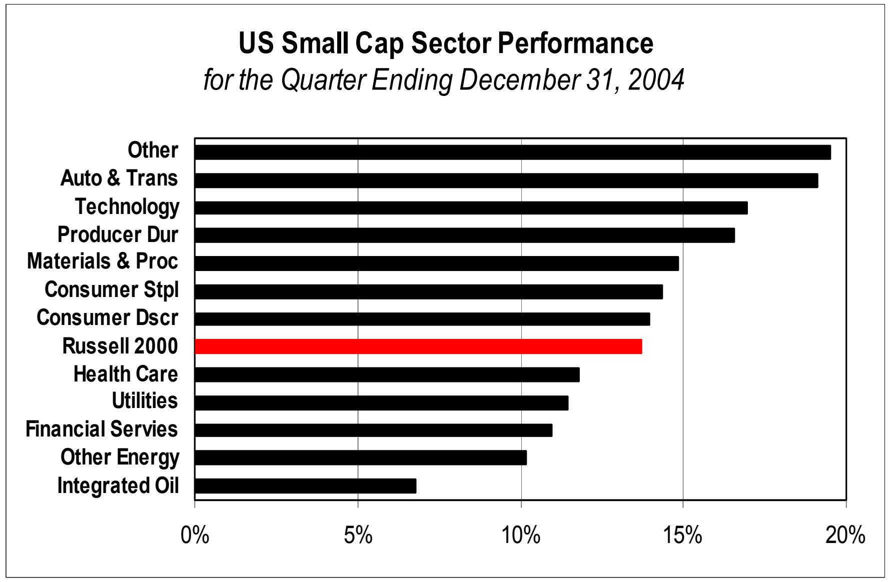
Source: Bloomberg

The chart above seeks to illustrate how large caps have done relative to small caps by comparing the performance of the Russell Top 200 ("Mega Cap") Index to the performance of the Russell 2000 ("Small Cap") Index.

US Equity

4th Quarter 2004

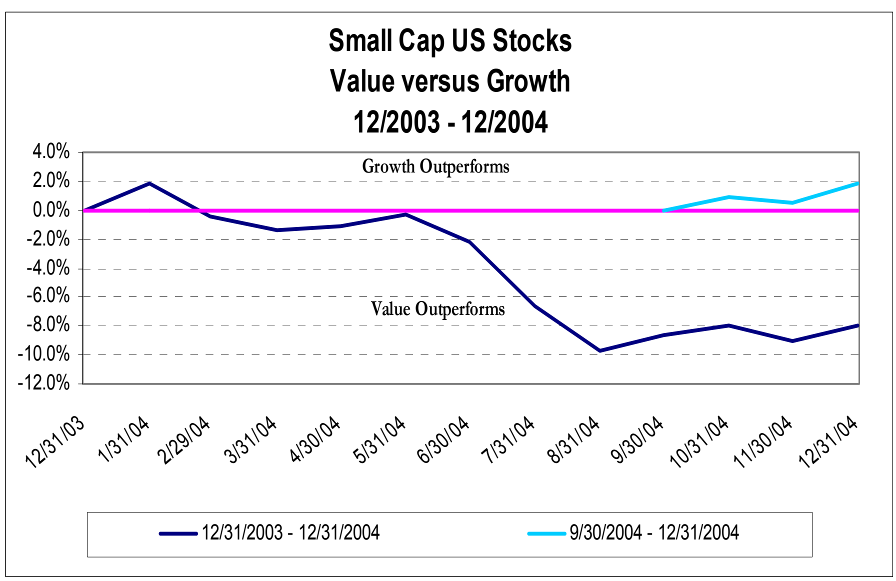
- Improving economic news and consumer confidence found their way to technology and consumer sectors during the quarter, pushing the Russell 2000 up 14.2% for the quarter.



Source: Frank Russell Co.

- After both a second and third quarter that saw large caps out perform, the more economically sensitive small caps used the momentum of the post-election bounce and improved economic news to provide a more attractive return for the quarter and the year. While pleased with 2004 returns (Russell 2000 was up 18.3% and has beaten the S&P 500 for almost six years), we firmly believe that prices have gotten ahead of themselves and that large caps are more attractive prospects going into 2005.

- A late year rally in more cyclical sectors such as technology (which makes up 19% of the growth index in comparison to only 5% in value) led to small cap growth out performing value for the quarter; however, it still trailed significantly for the year.



Source: Bloomberg, Frank Russell Co.

This chart represents the return of the Russell 2000 Growth Index less the return of the Russell 2000 Value Index.

Non-US Equity

4th Quarter 2004

[Balance of market commentary has been excised]

Asset Class Summary

Tactical Views

The table below summarizes the consensus views of Greycourt's Managing Directors and Senior Consultants regarding the most likely prospects for selected asset classes over the next one to two years. Asset classes we deem "Attractive" have a likelihood of generating near-term returns above our projections of their long-term sustainable rate of return[(a)], "Fairly Valued" asset classes are expected to perform in line with long-term estimates and "Over Valued" asset classes are expected to underperform.

December 2004 Tactical View

Attractively Valued	Fairly Valued	Over Valued
	Fixed Income	
		Gov't Bonds
		High Yield Bonds
		Corp Bonds
		Muni Bonds
	Equity	
	US Large Core	
	US Large Growth	
		US Large Value
		US Small Core
		US Small Growth
		US Small Value
	International (Developed)	
	Emerging Markets	
	Hedge	
		Non-Directional Fds
		Directional Funds
	Private Equity & Other	
	International PE	Real Estate
	Mid-Market Buyout	Large Buyout
	Venture Capital	
Secondary Funds		

(a) **Greycourt Long-Term Pretax Asset Class Forecasts**

Asset Class	Index Proxy [(1)]	Total Return (%)	Yield (%)	Appreciation (%)	Std Dev (%)
Inflation	*CPI , NSA*	2.75			0.59
Cash Equivalents					
3-MonthT-Bill	*Salomon 3-Month Treasury Bill*	4.00	4.00		0.30
Taxable MMKT	*Salomon 3-Month CD*	5.00	5.00		0.40
Tax-Exempt MMKT	*Salomon 3-Month CD *(1-.35)*	3.00	3.00		0.40
Fixed Income					
US Government Bonds	*Merrill Lynch Treasuries 10+YR*	5.75	5.75		8.00
Taxable Bonds	*Lehman Government/Credit Intermediate*	6.80	6.80		4.00
Tax-Exempt Bonds	*Lehman Municipal Bond Index*	5.00	5.00		5.00
High Yield Bonds	*Merrill Lynch High Yield Master II*	8.45	8.45		6.00
Equities					
US Large Stocks	*Russell 1000*	9.00	3.00	6.00	16.00
US Small/ Mid Stocks	*Russell 2500*	10.00	1.75	8.25	19.00
Non-US Stocks	*MSCI EAFE Index*	9.50	3.00	6.50	18.00
Emerging Markets Stocks	*MSCI EM (Emerging Markets)*	11.50	2.00	9.50	25.00
Alternative Assets					
Private Equity	*NASDAQ*	14.00			28.00
Real Estate	*Wilshire R. E. Operating Co. Index*	9.55	6.80	2.75	13.00
Directional "Hedge"	*HFR Equity Hedge Index*	15.00		15.00	10.00
Non-directional "Hedge"	*HFR Market Neutral Index*	10.00		10.00	5.00

[(1)] *Index proxies are used to estimate risk and asset correlations.*

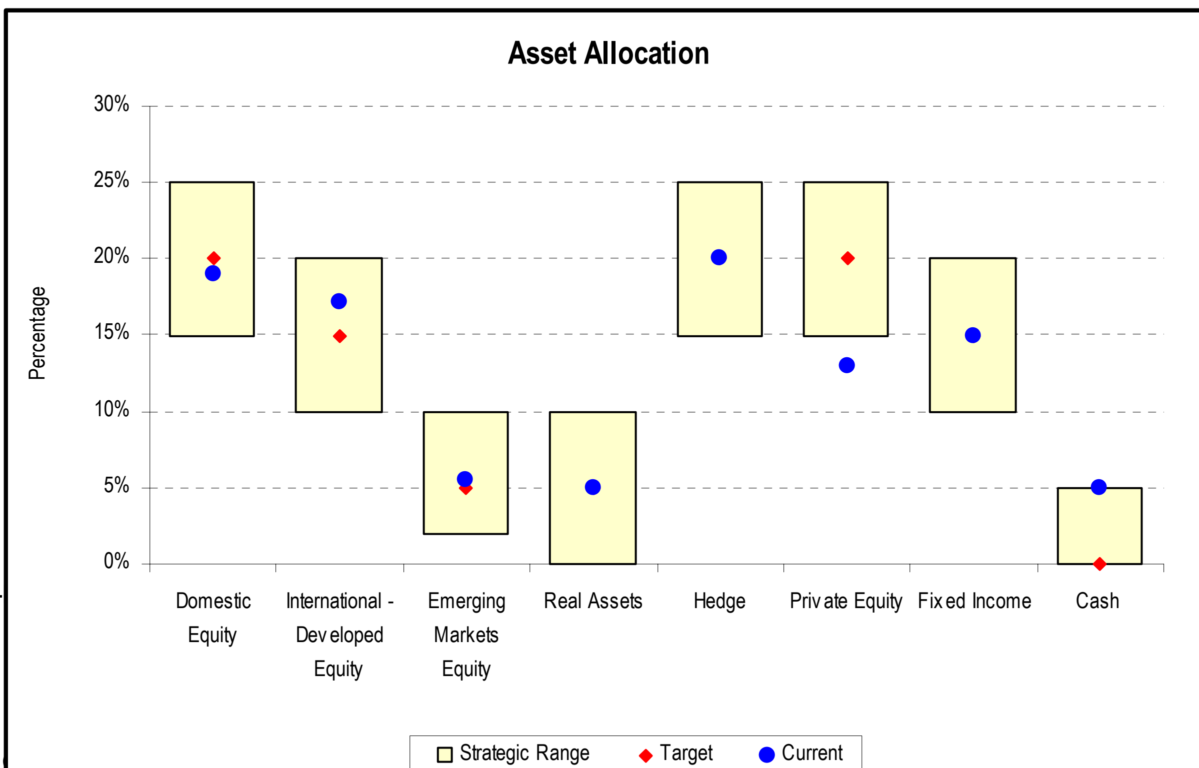
See 'General Performance Disclosure' page for important information about this chart.

Sample Client Portfolio

Current Asset Allocation vs. Target Asset Allocation

As of 12/31/04

Asset Class	Current Allocation	Long Term Targets	Difference	Strategic Range Min	Strategic Range Max
Domestic Equity	19%	20%	(1%)	15%	25%
International - Developed Equity	17%	15%	2%	10%	20%
Emerging Markets Equity	6%	5%	1%	2%	10%
Real Assets	5%	5%	0%	0%	10%
Hedge	20%	20%	0%	15%	25%
Private Equity	13%	20%	(7%)	15%	25%
Fixed Income	15%	15%	0%	10%	20%
Cash	5%	0%	5%	0%	5%
Total	100%	100%			



INVESTMENT PERFORMANCE REPORT

Quarter Ending December 31, 2004
Sample Client Portfolio

		Ending Balance	*Portfolio Percentage*	*Return This Qtr*	*YTD Return*	*Annualized Since Inception*
Total Portfolio (5/31/00)	**$**	**139,635,081**	**100%**	**8.4%**	**8.6%**	**6.7%**
Custom Index (1)				8.1%	8.7%	5.6%
U.S. Equity-Large Cap						
-U.S. Large Cap Equity	**$**	**26,468,147**	**19.0%**	**10.0%**	**13.1%**	**5.0%**
>Large Cap Alpha Manager (12/31/01)	$	5,723,226	4.1%	13.4%	20.8%	8.8%
>Large Cap Growth Manager (12/31/01)	$	5,630,001	4.0%	8.8%	6.0%	-0.1%
>Large Cap Value Manager (12/31/01)	$	5,449,531	3.9%	9.3%	16.2%	8.9%
>Large Cap Passive Manager (12/31/01)	$	9,665,389	6.9%	9.1%	10.8%	3.5%
-S&P 500 (12/31/01)				*9.2%*	*10.9%*	*3.6%*
-Russell 1000 Growth (12/31/01)				*9.2%*	*6.3%*	*-0.2%*
-Russell 1000 Value (12/31/01)				*10.4%*	*16.5%*	*8.6%*

[BALANCE OF REPORT HAS BEEN EXCISED]

XYZ Client
Investment Partnership Summary
December 31, 2004

Partnership	Type of Investment	Monthly IRR	Date of Initial Inv	Original Commitment	Drawn	Remaining Commitment @ 12/31/2004	Current Value @ 12/31/2004	Total Distributions	Total Value @ 12/31/2005	Total Value over Capital Contributed	Valuation Date Notes	Value @ 12/31/03	Cost w/Step-up @ 12/31/03	
Partnership A	Fund of Funds	4.64%	3/24/1997	2,000,000	2,000,000	-	733,560	1,610,079	2,343,639	343,639	12/31/03 Final	81,591	641,129	
Partnership B	Venture Capital	18.80%	3/30/1998	753,300	755,119	(1,819)	1,412,109	1,162,815	2,574,924	1,819,805	12/31/03 Final	754,672	661,321	
Partnership C	Venture Capital	94.55%	1/2/1997	100,000	100,000	-	21,322	1,082,667	1,103,989	1,003,989	12/31/03 Final	44,804	641,129	
Partnership D	LBO	-2.18%	3/27/2002	2,000,000	1,027,938	972,062	774,631	229,783	1,004,414	(23,524)	12/31/03 Final	326,097	2,374,937	
Partnership E	Real Estate	4.82%	4/22/1999	5,000,000	4,795,369	204,631	2,486,420	3,018,882	5,505,302	709,933	12/31/03 Final	(24,446)	(24,446)	Estimate
Partnership F	Venture Capital	8.80%	1/4/1993	450,000	450,000	-	66,123	991,224	1,057,347	607,347	12/31/03 Final	112,189	769,023	
Partnership G	LBO	20.87%	4/25/2001	2,000,000	2,000,000	-	1,587,036	1,522,290	3,109,326	1,109,326	12/31/03 Final	294,602	459,424	
Partnership H	Fund of Funds	16.01%	1/1/1997	1,000,000	1,000,000	-	274,039	1,276,207	1,550,246	550,246	N/A			
											12/31/03 Final	1,012,108	3,511,653	
											12/31/03 Final	220,229	858,088	
				[BALANCE OF PRIVATE EQUITY REPORT HAS BEEN EXCISED]							12/31/03 Final	204,125	664,251	
Total				**$ 13,303,300**	**$ 12,128,426**	**$ 1,174,874**	**$ 7,355,241**	**$ 10,893,946**	**$ 18,249,187**	**$ 6,120,761**		**$ 3,025,970**	**$ 10,556,509**	

YOUR PORTFOLIO PERFORMANCE

Comments on Your Performance

2004 turned out to be a better-than-average year in the equity markets – but if you had missed the last quarter you would never have known it. Here is what the major equity markets would have looked like without the blowout final quarter:

Market	*Full Year Return*	*Without 4th Quarter*
S&P 500	10.9%	1.7%
Small cap	18.3%	4.2%
EAFE	15.8%	3.5%

As is so often the case, patience and the willingness to stick with markets despite lackluster progress paid off handsomely.

Your fourth quarter portfolio performance was good almost across the board, due in part to asset allocation and in part to strong manager performance. Since inception (5/31/00), your portfolio has added 101 basis points to the return of the custom benchmark. The only disappointment to date has been in the hedge fund sector, where your three managers have, collectively, underperformed the benchmark (Treasury bills + 5%) since inception. Given the low return environment and markedly low volatility we have experienced, this performance is not surprising. In any event, the hedge funds have added significant value to the overall portfolio Since Inception by outperforming your equity portfolio.

In the US large cap sector you beat the S&P 500 by a comfortable margin for the quarter and year-to-date, thanks mainly to the strong performances of Large Cap Alpha Manager and Large Cap Value Manager. The decision to move toward a slight over-weight position in growth hurt the portfolio modestly this quarter, but we believe that it remains a sensible tactical decision. Although we have no concerns about any of your individual managers, we believe that this sector of your portfolio could be more efficiently structured. See the discussion below under "recommendations."

[BALANCE OF COMMENTARY HAS BEEN EXCISED]

Recommendations

As we suggested last quarter, our only two thoughts about your otherwise very well-positioned portfolio are the following:

- As we have mentioned before, we believe that the cost of your US large cap manager portfolio is too high for the returns you have been generating. In this highly efficient sector of the market, it is useful for investors to separate beta – simply achieving market return – from alpha – risk-adjusted excess return above the market return. The market return could be generated very inexpensively, leaving significant fee budget for alpha-seeking managers. At present the portfolio suffers from "deadweight," that is, indexed exposure on which you are paying active management fees. If you approve, we propose to submit a suggested restructuring of the US large cap portfolio for your review.

- [BALANCE OF RECOMMENDATIONS HAS BEEN EXCISED]

As always, please do not hesitate to call us with questions or comments about this report. It has been a pleasure to work with you this quarter.