

Quarterly Investment Perspective

Balanced Strategies

A Letter From Marc D. Stern, Chief Investment Officer

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Dear Client,

Investors went one way during the first quarter, while markets went the other.

Individuals pulled billions of dollars from U.S. equity mutual funds in favor of bond funds. At the same time, stocks delivered strong gains while bond returns were near zero. Usually, a few months of healthy gains are sufficient to convince retail investors to move back into stocks. But these are not normal times: Uncertainty about macroeconomic issues is unusually high. Nevertheless, certain buyers stepped in, including corporations repurchasing their own stock, institutions adding to equities to rebalance their asset allocation weightings, and global investors deploying some of their ample liquidity.

Positive Developments

Three developments reduced the risk of a rapid deterioration in market conditions and contributed to stock market gains in the first quarter.

- **New leadership and policies in Europe.** Since becoming president of the European Central Bank last November, Mario Draghi has cut interest rates and provided substantial funding to the region's capital-starved banks. Meanwhile, newly elected "technocrats," including Italian prime minister Mario Monti, have taken preliminary steps toward raising retirement ages, adopting more-flexible labor laws, and bolstering tax collection. As a result, yields on three-year Italian bonds — a barometer of European sentiment — fell from 7.6% late last year to 3.3% by quarter end (Exhibit 1, page 2).
- **An orderly Greek debt deal.** The European Union, the central bank, and the International Monetary Fund worked together to engineer an orderly default of Greek government debt and a second bailout program. The market reaction reinforces a time-tested principle: Markets tend to preemptively factor in bad news when the downside risk is well known by all interested parties.

Exhibit 1: Three-Year Italian Government Bond Yield



As of March 31, 2012.
Source: FactSet

- **Improvements in U.S. economic data.** In the first quarter, jobless claims fell, new home traffic rose, retail sales rebounded, and business confidence improved. Moreover, the Federal Reserve's latest "stress tests" indicated the financial system is generally sound. In addition, while it remains a difficult period for many families, overall consumer debt payments as a percentage of disposable income have fallen to levels last seen in the mid-Nineties. At the same time, seven emerging markets (Brazil, China, India, Indonesia, Mexico, Russia, and Turkey), which are home to 3.3 billion people, appear on track to grow at an overall 5% rate this year.

With high-quality bonds offering little yield (often below the dividend income available from high-quality global stocks), we remain convinced that overall stock returns will meaningfully outpace overall bond returns over the next several years.

Causes for Concern

None of this suggests that risks to the global investment landscape have evaporated. While Europe appears to have averted a financial collapse, fiscal

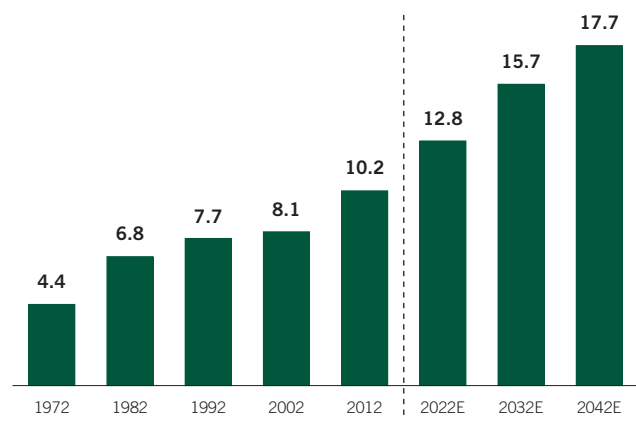
challenges remain in many countries, much of the region has entered recession, and European banks continue to be overleveraged. Elsewhere, Chinese officials face a difficult transition from runaway growth to sustainable expansion, geopolitical risk in the Middle East remains high, the U.S. election cycle is heating up, and corporate profit growth is tapering off. Markets are likely to experience sharp setbacks in the months ahead.

Longer term, another major issue looms: the U.S.'s unsustainable fiscal condition. Until 2008, government debt as a percentage of total economic activity was within historical norms. But the financial crisis led to a sharp reduction in tax revenues and substantial new spending. Debt as a percentage of GDP now tops 100%*, above the 90% level that has often brought economic difficulties to various countries historically. How policymakers respond to this serious challenge will have significant consequences for economic growth, investment returns, and the quality of life for future generations.

Even as the U.S. has endured its first ever credit rating downgrade, near-shutdowns of the government, and the failure of the so-called supercommittee, markets have been calm about U.S. fiscal health. Indeed, the country is able to finance its shortfalls at low rates of interest (e.g., 0.9% on a five-year Treasury note). But inertia brings significant risk. A notable problem is the growing burden of entitlement programs. Medicare, Medicaid, and Social Security were founded on noble intentions, but they rely on demographic assumptions that are no longer valid. As a percentage of GDP, total payouts have reached double digits and, by the government's own numbers, are headed higher (Exhibit 2, page 3). No one can know the breaking point, but that is no longer a remote outcome.

* Based on all federal debt outstanding, including debt held by the Federal Reserve and the Social Security Trust Fund. Total federal debt held by the public currently stands at 69% of U.S. GDP.

Exhibit 2: U.S. Entitlement Programs Becoming Unaffordable As a Percentage of GDP



As of December 31, 2011.
Reflects sum of Medicare, Medicaid, and Social Security as a percentage of gross domestic product.
Source: Congressional Budget Office

Some believe the government's fiscal situation cannot be fixed. We disagree. We would point (again) to the thoughtful work of the Simpson-Bowles commission, which was created by the president to make specific deficit reduction recommendations.

There are three critical aspects of the commission's plan: reining in entitlement programs (e.g., higher eligibility ages, means testing), implementing cuts in discretionary spending (e.g., defense, headcount, farm subsidies), and restructuring the tax code (e.g., loopholes, deductions). This work provided concrete steps to remedy complex fiscal problems. The question is when policymakers will have the will to take this fine plan off the shelf and act on it. Markets are likely to force action within the next two years, perhaps through a combination of higher Treasury yields and a lower U.S. dollar.

Finding Balance

This complex and changing backdrop argues against bold portfolio moves toward either aggressive growth or capital preservation. Areas of strength among corporations, consumers, and emerging-market economies are an important part of the picture, but government fiscal difficulties merit

caution. We remain focused on balanced strategies that rely on a dose of protective assets to offset the risk that comes with growth-oriented holdings.

We made several shifts to our recommended asset allocation during the first quarter. By putting cash to work in Large Cap Core and adding to our weighting in Large Cap Strategies, we increased our overall equity exposure in leading global companies with potential for attractive returns. These moves augment our growth-oriented positioning, which includes investments in small and mid cap companies, commodities and commodity-related stocks, hedge funds, and, when appropriate, private equity and real estate investments.

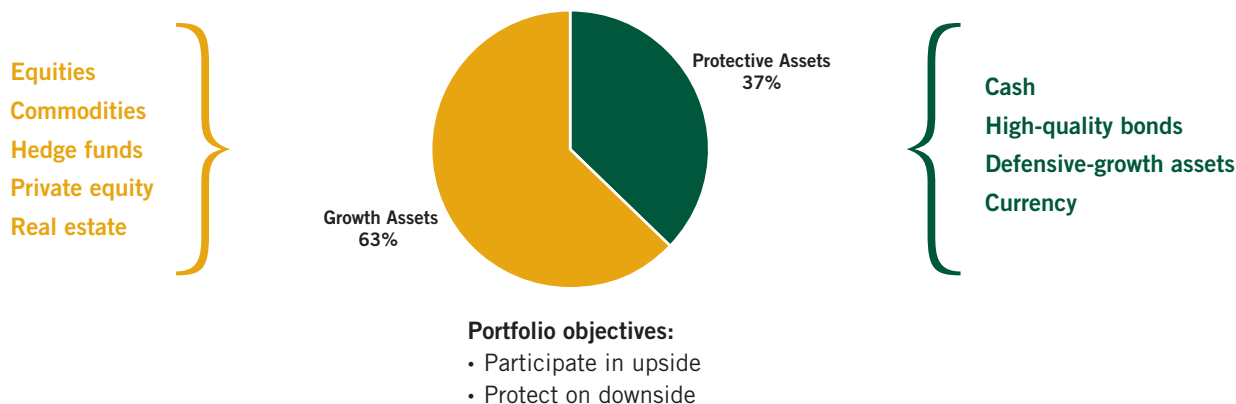
At the same time, though, we increased our allocation to more defensive areas such as credit (e.g., high-yield bonds, convertible bonds) and covered calls through Global Opportunities. These investments tend to provide solid return potential with more downside protection than equities. In addition, high-quality bonds continued to play an important defensive role in our overall portfolios despite their historically low yields, and we maintain exposure to select currencies as a hedge against potential weakness in the U.S. dollar.

At quarter end, we had invested 63% of our model Balanced Growth portfolio in growth-oriented assets and 37% in protective assets (Exhibit 3, page 4), a somewhat cautious positioning versus our normal weighting of approximately 68% growth and 32% protective.

Performance

We believe our strategy positions us to meet one of our most fundamental objectives in managing clients' irreplaceable capital: to participate in up markets, while protecting against losses in down ones. Indeed, as equity markets around the world posted healthy gains in the first quarter, all of our portfolios delivered positive results. However, our protective holdings restrained our upside.

Exhibit 3: Combining Growth and Protection



As of March 31, 2012.

This model displays Bessemer's suggested model portfolio allocation guidelines. Each client situation is unique and may be subject to special circumstances, including but not limited to greater or less risk tolerance, classes and concentrations of assets not managed by Bessemer, investment limitations imposed under applicable governing documents, and other limitations that may require adjustments to the suggested allocations. Model asset allocation guidelines may be adjusted from time to time on the basis of the foregoing or other factors.

Alternative investments, including Bessemer private equity, real estate, and hedge funds of funds, are not suitable for all clients and are available only to qualified investors.

The largest gains in the first quarter were in Large Cap Strategies, Global Small & Mid Cap, and Global Opportunities. The equities held in Large Cap Core delivered strong returns, but overall portfolio performance was held back by our gradual deployment of cash during the quarter. Most hedge funds delivered moderate returns. Smaller advances came in Strategic Currency, Real Return, and Fixed Income.

We are particularly pleased by the progress we have seen in our large cap portfolios. In the Investment Roundtable that begins on page 5, we share insights from our internal and external managers in this area. We remain convinced that the changes we made recently will benefit clients over time and help to extend our firm's long-term record of competitive overall returns with limited volatility.

Following the firm's announcement that George Wilcox and I will be named president and chief executive officer, respectively, at the end of this year, a high priority for us is recruiting an outstanding chief investment officer. While we have a number of qualified internal professionals, we like the jobs

they are doing in the roles they are in. Therefore, we are in the midst of identifying and interviewing talented external candidates from a wide range of backgrounds. Our priorities are proven investment expertise, strong experience making asset allocation decisions, and a collaborative leadership approach. We have been pleased with the significant interest from many highly qualified candidates, reinforcing our confidence that we will name a top-flight professional as our new CIO in the coming months.

In closing, our investment team remains focused on our disciplined investment approach and independent research. We believe our client portfolios are well positioned for today's market environment, with an appropriate balance of aggressive and defensive strategies. We look forward to updating you on our research conclusions, investment strategies, and performance results next quarter.

Sincerely,

Marc D. Stern
Chief Investment Officer

The Investment Roundtable: Looking into Large Cap

Michael Crawford, Bessemer Large Cap Strategies

Alex Lloyd, Bessemer Large Cap Core

Richard Oldfield, Oldfield Partners

Sunil Thakor, Sands Capital Management

Owning large, established companies is a core component of our equity investments. Bessemer clients gain exposure to this asset class through four managers with distinct investment approaches. In this roundtable, these managers discuss with Head of Investment Strategies Peter J. Langas everything from their investment philosophies to what investors are missing most in today's environment.

Langas: Each of you selects stocks using bottom-up fundamental analysis, yet you have very different investment philosophies. Can you describe your approach?

Oldfield: The things that we care most about in investing are valuations and investor behavior, and the two of course go together. You get very low valuations when investors become more and more risk averse, and that is the situation we've had over the last few years. We regard a share whose price has gone down as, at first glance, cheaper and more interesting. That's because low expectations and fear provide the fuel for markets to improve in the future. In every company, we look for at least a plausible 25% return over the next two to three years.

Lloyd: In Large Cap Core, we seek to outperform over full market cycles with less volatility than the broader equity market. Using a combination of fundamental and quantitative research, we look to build the portfolio with companies that demonstrate compelling characteristics ranging from attractive valuations and high earnings quality to disciplined use of capital and high-quality assets. These are companies for which we believe the stock market is

mispricing something about their earnings outlook. Once we have selected about 60 stocks from around the world, we use analytics in conjunction with our best judgment to weight the holdings in a way designed to achieve lower volatility.

Thakor: Because we believe growth companies are the essential building block of wealth creation, we emphasize global companies with superior prospects for rapid growth. We currently own the stocks of 39 individual businesses that are leaders in their respective industries. The biggest driver of our returns is what's going on with those businesses. Valuations will come and go over time. But ultimately, we believe that stock prices will match up with the companies' earnings power — which is driven by the success of their businesses.

Crawford: The Bessemer Strategies team seeks to invest in firms that have a durable competitive advantage, sustainable cash flow, and high returns on capital whose strengths aren't fully reflected in their prevailing stock prices. Roughly 30 of these companies compose a fundamentally driven, concentrated global large cap portfolio.

Langas: Richard, you mentioned the importance of valuation. But how do you avoid "value traps" — that is, investing in cheap stocks that are cheap because of some serious problem, and for that reason they continue to get cheaper and cheaper?

Oldfield: It's the biggest risk for the value investor, a sort of occupational hazard. You try to avoid value traps, but occasionally you stumble into them, because there is no sure method of avoidance. However, the value approach is itself a sort of control of risk. If you buy businesses for which there are low expectations, at low valuations, then there is a margin of safety and comfort.

Of course, every case is different, so you have to look at each company differently. One of our proudest moments of avoidance was an Italian company that purported to have a lot of cash on its balance sheet, yet the company was still issuing a lot of convertible debt. We didn't understand why the firm would be doing so, so we avoided it. Our suspicions proved correct: It turned out that the cash wasn't really there at all.

Langas: Sunil, how about you? As a growth investor less concerned about valuations, isn't there a risk of buying something that's already expensive?

Thakor: Yes, there's always that risk. We own a portfolio of growth businesses that tend to have relatively high valuations, which can come under pressure in a weak overall environment for equities. However, we've found that a great way to mitigate this risk is to own very high-quality assets in the first place. If you own strong businesses with sustainable competitive advantages, a weak economy can actually be quite attractive. Take, for instance, Amazon.com. Over the past two years, despite a sluggish retail environment in the U.S. and Europe, Amazon has been able to invest heavily in distribution infrastructure and free shipping for its customers — ultimately enticing them to buy more products on Amazon. That has effectively put its competition on its heels and widened the leadership gap between it and other e-commerce players.

Langas: Alex, you said earlier that controlling volatility is one of the portfolio's key goals. What type of environment, then, would be most and least favorable for the Core portfolio?

Lloyd: When we have a rapidly rising market, even though the portfolio is likely to deliver good absolute returns, it's going to be difficult for the portfolio to outperform the broader market. That's because it's designed not to fluctuate wildly — either down *or* up. Conversely, if we have a very negative market, the portfolio is designed to perform well on a relative basis. Were we to be in the middle — a

choppy market without big moves one way or the other — the portfolio will likely demonstrate a smoother return profile than the overall market. We believe all of this will contribute to outperformance over time: If you have two portfolios each with the same average annual return, the portfolio with the smoother returns will outperform because it has less ground to make up after losses.

Langas: As you go about building your portfolios, obviously you have to process a great deal of information about companies. How exactly do you go about gathering your data? What does your research entail?

Thakor: One of the most important elements of our process is field research — getting out, seeing the company, touching the product, talking to consumers, and understanding culturally why the customer wants to buy that product or not.

We had a small investment in a Chinese medical equipment company that sold patient monitoring devices in hospitals all across China. As we spent more and more time talking to hospital administrators and purchasing managers in smaller, less-developed cities in China, it became clear to us that the competitive advantage of the business and sales process were not as impressive as we had initially thought. Eventually, we visited enough hospitals and didn't see enough of the equipment that we were looking for, that we concluded that the investment case had begun to deteriorate, and we exited the position.

Lloyd: We get our information from a wide range of sources. Our investment team in New York and London spends a lot of time meeting the management of the companies that we invest in, along with customers and suppliers. Picking up on the healthcare theme, when we're considering an investment in the healthcare space, one of the first places we go to is the doctors. That's because often they're the people making the decision whether or not to use a company's device. As part of our research, we ask them if they've heard of it, if they're going to be using it, and what they think of it.

Oldfield: We agree about the importance of the field trip. We're different, I think, in that we don't spend much time with management. We're very skeptical of the value of individual meetings with management, where what they can say is very carefully regulated. Senior executives are often extremely good at spinning the company's story.

Lloyd: We agree that it shouldn't be the basis for your understanding. However, when it comes to management interaction, we find it can be valuable to meet with them after we've gained some knowledge and built a potential investment thesis on the company. We develop a list of questions and issues we'd like them to address. It's that kind of interaction that very often gives us just the one or two pieces of information that will confirm or dispel an investment case, which can make a big difference from a portfolio perspective.

Crawford: An important part of our research is learning exactly how management is incentivized; it has a big influence on how companies allocate capital. For instance, when we see company executives with a large amount of their compensation tied to how well they drive earnings per share (EPS) growth, we regard that poorly because EPS figures can be massaged through acquisitions.

However, if company leaders own large amounts of direct stock and are incentivized to increase the company's cash flow and returns on capital, that's more favorable. Pearson is a great example. Historically, the London-based publisher with brands such as the Financial Times and Penguin Books had a reputation for making large, ill-advised acquisitions. In 2005, the company named a new chairman, who subsequently encouraged Pearson's management to

Bessemer Large Cap Portfolios

In late 2011, we redefined our approach to investing in large companies. Four key principles drive our approach:

- **Thinking globally.** The world has become much more interconnected and companies compete on a global basis. Apple earns over half its profits outside the U.S., while Toyota earns a similar proportion from within the U.S. In evaluating potential opportunities, we seek to own the best companies from around the world.
- **Combining complementary strategies.** In a universe of over 1,000 companies, many different types of stocks can represent good investment opportunities. Looking for low valuations, rapid growth, or stable cash flow at reasonable prices can all be effective strategies over time. Exposure to all of these approaches can provide complementary risk profiles and a smoother performance pattern.
- **Staying disciplined.** We believe it is essential for portfolio managers to use a thoughtful investment process to identify the most attractive opportunities in the world based on a well-defined set of characteristics. The characteristics will vary by strategy, but the investment teams must apply them in a consistent manner.

- **Building concentrated equity portfolios.** Academic research has shown that high-conviction, actively managed portfolios have a higher probability of outperforming over time than portfolios that are over-diversified and tend to hug the indexes.

Large Cap Core and Large Cap Strategies strive to deliver competitive returns through investments in global companies that are thoroughly researched based on industry rather than geographical analysis. The Core portfolio seeks to control volatility, while the Strategies portfolio is more aggressive, with broader exposures through three distinct investment strategies by three different managers that complement each other.

Large Cap: Four Key Principles



hold significant direct stakes in the company and linked their compensation more closely with the company's return on capital — as it remains to this day. Perhaps as a result, the company has shown greater discipline in making acquisitions and has retained focus on its core business: educational publishing.

Langas: As you build your portfolios from the bottom up, what themes are you seeing emerge in your portfolios today?

Crawford: Three key themes have emerged in the Bessemer-managed portfolio. First, many of the holdings have powerful global brands, such as Apple, which attracted 110 million people to its stores across the world in the fourth quarter alone, and Adidas, the world's second largest producer of sporting goods. Second — and related — is that many companies in the portfolio have both wide scale and a reputation for quality, such as oilfield services firm Schlumberger. If a national oil company in a developing economy needs a firm to manage a drilling project or supply state-of-the-art drilling equipment, it might employ Schlumberger based on its reputation for quality and expertise. The third theme is a position in well-capitalized banks. At a time when many banks around the world lack sufficient capital, banks with reasonable assets and healthy capital levels such as JPMorgan face far less competition. During the Federal Reserve's recent "stress tests" of banks, JPMorgan came through well. It had enough capital to increase its dividend and buy back a significant amount of shares and still pass the stress test.

Oldfield: For us, there are a few themes. First, we have a lot of Japanese companies and see a great deal of value in Japan. Second, we like gold stocks. We've only got one, but we like it a lot. Third — and this is more of a methodological theme than a sector or geographic one — there are a lot of companies that can be valued at a large discount to the sum of their parts. For instance, if you take the French carmaker Renault, recently it was selling at a share price of €27. The value of its stake in Nissan, Volvo, and Daimler *alone* comes to €54.

Thakor: We see two very different but equally exciting sources of growth. In developed markets, we're seeing tremendous growth driven by innovation within existing markets. One such example is in mobile telephony and computing. It used to be that most people owned just a cell phone. But when I travel today I carry four different mobile devices in my bag. Each one has a chip, and we have several companies in the portfolio that are benefiting from the sales of those. As one example, we own a U.K.-based business called ARM Holdings, which sells a piece of intellectual property used by chip designers to design semiconductor chips that go into telephones. And the special thing about ARM's intellectual property is that it allows low-power consumption in mobile devices. It's a pretty important thing if you're going to carry a phone around all day. As the world consumes more and more of these devices, ARM is picking up a two- or three-cent royalty on every device sold.

Meanwhile, in the emerging markets, we're finding broad-based growth driven by the rise of the middle class. There, we're seeing billions of consumers becoming much more economically active, buying things like motorcycles in India. In China, they're upgrading from homemade noodles to instant noodles. In Brazil, they're buying more makeup than ever before. And around the world, people are spending more money on credit cards and debit cards.

Lloyd: There are three main sector themes we'd highlight: First, an underweight position in financials. We've found that many global banks don't meet our criteria in terms of earnings quality or valuation; instead, we're discovering interesting ideas in other parts of the financial sector, such as property and casualty insurance firms. Many of these companies aren't exposed to the same risks as banks and have healthier balance sheets. A second theme echoes what Richard mentioned earlier: a positive view toward gold stocks. Here, we're seeing gold equity prices not reflecting the price of the underlying gold commodity. Two of the companies in our portfolio, Canada-based Barrick Gold and Colorado-based Newmont Mining, have strong operations and current share prices

discounting a gold price significantly below our forecast. The third theme is our overweighting of the utilities sector, including less-regulated companies that could benefit from higher power prices over time.

Langas: Several of you focused not only on companies but on particular regions. Can you elaborate a little on where it is you're seeing the greatest opportunities today (Exhibit 4)?

Oldfield: While there are a lot of high-quality companies in the U.S. with attractive valuations and good potential returns, there are companies with *outstandingly* attractive valuations in Europe, which is being completely pummeled by all the problems of the euro zone. We're seeing the same phenomenon in Japan as well, which has been hurt by 20 years of decline and several new crises — such as the financial turmoil of 2008 and the tsunami of 2011.

Thakor: Conversely, those are the least interesting places to us. Quite frankly, as growth investors, we see Europe and Japan as difficult markets in which to sell stuff. They're very challenging environments from a growth perspective.

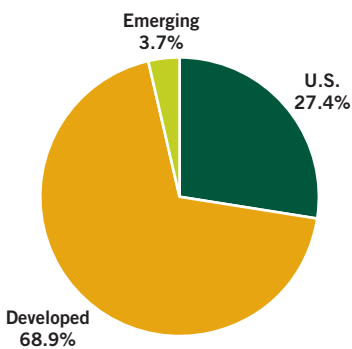
Oldfield: I'd agree, but the thing about the European companies in which we invest is that they are not necessarily terribly dependent on the European economy, which is difficult to be very optimistic

about. For example, the Italian carmaker Fiat has about 17% of its revenues from Brazil. When we invested in Fiat, the share price was €4.5; according to our calculations, the Brazilian operation alone was worth about €3 of that. In other words, a company like Fiat is not just an Italian car manufacturer — thank goodness — because if it were, it would be very difficult to be enthusiastic about it.

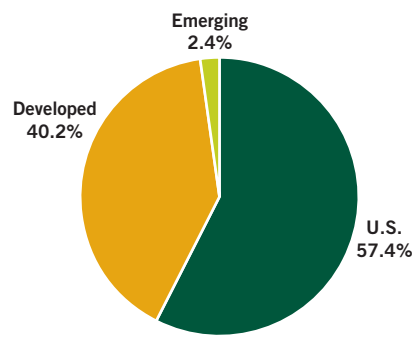
And as for Japan, it can be a very frustrating place. But we feel that there is a quiet revolution going on there in terms of corporate governance. Because of the economic battering of the last twenty years and recent crises, you have remarkably low valuations: About 60% of the Japanese stock market currently sells below book value. In Japan, there are two types of companies that we like. There are those at what I call the sharp end, like FANUC, an Oshino-based robotics company that has 40% operating margins and enough cash to pay off two years of employee expenses and all of its payables without selling another machine. Then, on the other end, you have what we call the dinosaurs, companies like the massive conglomerate Hitachi, which sells everything from consumer electronics and trains to nuclear power systems. With a management team that has recently refocused on profitability, the company is a sleeping giant that can be prodded into life — and is extraordinarily cheap.

Exhibit 4: Geographical Exposure for Large Cap Strategies

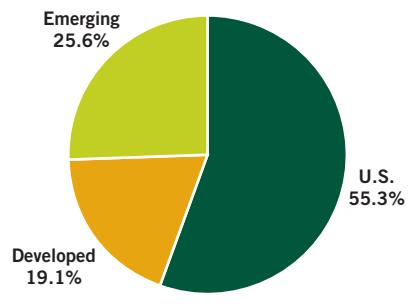
Oldfield Partners



Bessemer



Sands Capital



As of March 31, 2012. Geographical exposures exclude cash. Source: Oldfield Partners LLP, Sands Capital Management LLC

You don't expect to be able to buy companies like these so cheaply, but Japan, because it has experienced 20 years of decline, is a market that has produced tremendous bargains (Exhibit 5).

Exhibit 5: Japan's 20-Year Slump

Nikkei 225 Stock Market Index



As of March 31, 2012.
Source: FactSet

Thakor: Along with emerging markets, one of the areas that we find most exciting is the U.S. Some people find that a little bit surprising given some of the country's economic headwinds. But the businesses that we tend to own are innovators creating new markets like Amazon or Google. Another example is salesforce.com, which offers business software for managing contacts. This company's success to date attests to the rise of cloud computing — that is, running operations and storing data on external servers, and then accessing it on the Internet in real time everywhere, cheaper, faster, better, and more securely.

Langas: How about you, Alex and Michael? Are there any particular regions where you're finding opportunities today?

Lloyd: We're seeing a number of very interesting opportunities in Europe, but this is not us making a call on the European economy, which we believe is going to see very slow growth for a number of years. Rather, we're finding some world-class businesses that just happen to be domiciled in

Europe such as French pharmaceutical company Sanofi and U.K.-listed consumer staples firm Unilever (owner of brands such as Dove, Lipton, and Vaseline). Both businesses have less than 35% of their business in Europe.

Another geography we would highlight is China, where there's currently a lot of concern about the country's slowing growth. That's one of the reasons why valuations are cheap in the telecom, energy, and financial space, which will benefit as the Chinese economy expands. Many investors seem to be overlooking that the country is still on track for a robust GDP growth rate of about 8% this year — not exactly a number to sniff at. We're also investing in several companies indirectly exposed to China, such as the Anglo-Australian miner BHP Billiton.

Crawford: The Bessemer Strategies team is finding many good opportunities for firms headquartered in developed economies but with operations around the world. This lets us take advantage of Western governance standards (greater transparency and disclosure of the company's financials, for instance) while still tapping into emerging-market growth. For example, though Standard Chartered bank is headquartered in London, over 90% of the company's profits come from its operations in Africa, Asia, and the Middle East.

Langas: What do you think investors are missing most in the current environment?

Thakor: One of the most overlooked things is that there are some characteristics of human nature that don't go away, whether we're in a good economic environment or a bad one — things like ingenuity, creativity, and entrepreneurship. These qualities are as healthy today as they've ever been worldwide. As a result, despite a challenging backdrop, as a growth investor we're having no problem finding tremendous growth opportunities, through innovators ranging from South African pay-TV operator Naspers and Danish biotech firm Novozymes to U.S.-based technology giants Qualcomm and Google.

Oldfield: A behavioral psychologist named Daniel Kahneman recently published a book claiming that people are prone to extrapolate. If everything is going well, we all think that it can then continue to go well. But when everything is going badly and unpredictably, we extrapolate negatively, too. When I was living in the U.S. from 1979 to 1981, interest rates were in the double digits, inflation was 14%, hostages had been taken prisoner in the U.S. embassy in Iran, helicopters had crashed in the desert trying to get them out, and everything was about as bad as it could be for the U.S. And yet, within 10 years, America was just about the only game in town for investors after communism fell in Eastern Europe. I think that's a lesson in unpredictability and the danger of over-pessimism. What markets may be missing now is the fact that valuations are really very low, and it's from tough circumstances that you get good medium- and long-term returns.

Lloyd: The markets, more recently, are being characterized by big risk-on, risk-off periods, with investors lurching from one side of the ship to the other. We've also seen very high correlation of stocks within sectors and of sectors within the market. And that creates a big opportunity, because very often, companies are a lot more different in terms of strategy, positioning, and execution than the market is giving them credit for.

Crawford: In recent years, investors have become very focused on the macroeconomic environment, which is actually less relevant over the lifetime of a stronger company than the quality of its products or services. By focusing on the short-term macro picture, investors are ignoring the power of stronger companies to deliver returns *over multiple years*. Shorter-term risk will always be there; but as Alex said, this creates opportunities for investors to find companies that have been unfairly lumped with weaker competitors. The other thing that investors are missing is that much of a portfolio's success depends on its starting point. Ten years ago, a lot of stocks were very highly valued after the tech boom. In many cases, these stocks

struggled in the decade that followed, in part as a natural unwinding of those high valuations. But now we're seeing the opposite: Stocks are at much more reasonable values, so those with the patience to ignore short-term swings are more likely to see solid long-term returns.

Langas: To sum up this discussion, I'd say it's clear that there are diverse opportunities in the large cap universe for investors with various investment approaches. There are value opportunities in Europe and Japan, particularly among companies that are not reliant on their local economies. Growth opportunities are abundant in innovative technology companies in developed markets and in companies benefiting from the enormous potential of emerging-market consumers. Moreover, bottom-up research can uncover compelling investments in companies around the world, such as those whose franchise strength is underappreciated or whose competitive advantage is unrecognized by the market. We believe this diverse range of investment approaches and companies will deliver competitive returns over time.

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