U.S. Equity, Large Cap Growth
Fourth Quarter, 2008

As the closing bell rang on the floor of the New York Stock Exchange on December 31st, investors cheered as 2008 officially drew to a close, and rightfully so, as the year will go down as the second-worst calendar year ever for the S&P 500 Index (its return of -37.0% is second only to the 1931 loss of more than -43.3%). This year's decline also ended a stretch of five consecutive yearly gains for the Index. But the S&P 500 Index wasn't alone as other indices also posted record losses. The Dow Jones Industrial Average fell 33.8% while the NASDAQ declined a record 40.5% (outpacing even the 39.3% plunge following the burst of tech bubble in 2000). Even with the significant declines in the U.S. markets, international markets fared much worse. In fact, the MSCI Emerging Markets Index lost over half its value, plummeting 54.5%. Given these steep losses, investors pulled out a record $320 billion from mutual funds during the year. However, investors had a change of heart during December as equity mutual funds picked up over $23 billion in net flows. There were a few other bright moments during the quarter as the Dow enjoyed four of the five largest single daily point gains in its history. Seven of the top 10 came in calendar year 2008.

Governments around the world were quick to act in an attempt to mitigate the meltdown in the credit and equity markets in 2008. During the fourth quarter, the U.S. Federal Reserve (Fed) lowered its Fed Fund rate to the lowest point ever, targeting 0% – 0.25%, from 4.25%, where it stood only twelve months ago. Additionally, countries from Australia to Japan to the European Union also lowered their short term interest rates while U.S. President-elect Obama pledged a fiscal stimulus package of approximately $1 trillion. Even with these actions the US economy continued to weaken. In November, the labour market suffered its largest monthly loss of jobs since December 1974 as the unemployment rate crept up to 6.7%, the highest in more than 15 years. As if this wasn't enough, in December the National Bureau of Economic Research said that America officially fell into a recession back in December 2007.

For U.S. equity investors, large-cap stocks outperformed mid and small-cap stocks for the quarter with the Russell 1000 Index falling -22.5% compared to a decline of -27.3% for the Russell Midcap Index and a loss of -26.1% for the Russell 2000 Index. For the year, all three indices lost more than 30%, with midcaps declining the most (-41.5%). Stylistically, value outperformed growth across the market cap spectrum for both the quarter and year.

Risk aversion remained foremost in investors' minds, as U.S. Treasury security prices advanced (and conversely their yields plummeted). For example, the yield on 10 Year U.S. Treasury Notes declined from 3.9% to 2.2%, and 3-month T-Bill rates were priced *to yield less than 0%* at times during the quarter. With investors remaining extremely risk averse, companies with premium earnings growth rates, such as those we find attractive, were not rewarded. Consequently, it was a tough quarter for this strategy on both an absolute and relative basis. For the quarter, the lag versus the benchmark was largely attributed to underperformance in the Health Care and Consumer Discretionary sectors. On the other hand, results in the portfolio's technology sector added value versus the benchmark for the quarter. For the full year 2008, the portfolio's underperformance was largely attributed to weakness in the technology and consumer discretionary sectors. Conversely, the materials & processing sector provided modest excess return versus the benchmark.

The Summit Program

Relative underperformance in the Health Care sector was largely due to weakness in both Intuitive Surgical, a long term holding in the portfolio, and Alcon. Intuitive Surgical's stock traded lower due to concerns that the challenging economic environment would result in a general cut back in hospital capital spending plans. Intuitive's da Vinci robotic surgical system is a leading edge technology that is used as a center piece in many hospital marketing campaigns. Consequently, we used the recent weakness as an opportunity to add to this position. Shares in Alcon, a pharmaceuticals company with a focus on eye care, fell due to a significant slow down in their U.S. pharmaceutical business, and earlier than expected generic competition for Tobradex (an antibiotic used for the treatment of eye infections). We elected to sell this stock due to concerns that its earnings estimates would decline further as the year progressed.

In the Consumer Discretionary sector, the trend from previous quarters remained the same. Slower growth companies that we did not own during the period generally held the high ground, while the market tended to punish the higher growth companies that we favor. For example, well known companies that we did not own like Wal-Mart and McDonald's held up reasonably well. On the other hand, our positions in Google and video game manufacturer Activision Blizzard traded substantially lower. We continue to hold shares in these companies, as we think an improving economic environment should provide for a more favourable earnings outlook, and improved valuation for each of these companies in 2009. Also of note in this sector was the poor showing posted by Baidu – a Chinese internet search provider. We sold this company during the quarter due to concerns that its paid-search listings include unlicensed pharmaceutical companies among its top bidders for medical keywords. With the company's integrity in doubt, this company was sold.

In the Information Technology sector, the portfolio's holdings in Broadcom and Qualcomm held up reasonably well. Additionally, the portfolio benefitted from avoiding a number of household technology companies that were under pressure, such as Microsoft, IBM, Cisco Systems, and Dell. Going forward, we continue to hold an overweighted position in semiconductor companies (e.g. Broadcom, Intel and Xilinx) as we think an improving economy should ultimately lead to increased demand for chipsets going forward. Apple and Hewlett Packard are also key holdings within this sector. Apple, a well known leader and innovator when it comes to consumer electronics, is currently trading at a mid-teens price-to-earnings multiple, with an earnings growth rate in the low 20% area. Hewlett Packard has a balanced worldwide revenue profile, with what we believe are compelling cost cutting opportunities from the recent EDS acquisition. Additionally, this company also appears very attractive to us in terms of its P/E to growth rate.

Although the economic landscape will likely continue to be challenging for the next couple of quarters, the market is forward-looking and tends to rebound prior to the economy turning. In fact, looking back over the past 13 bear markets the first year average return after the decline was over 35%. In addition, the number of stocks making new lows on the NYSE peaked on October 10 and has continued to decline, which historically has proved positive for the equity markets. We think the stock market offers plenty of good opportunities, with bona fide growth stocks selling at price/earnings ratios equal to only a fraction of their long-term earnings-growth rates. In our estimation, it's likely that our economy should begin to recover by mid-2009 and earnings, the engine that drives the stock market, should improve throughout the year. And though it remains to be seen if the low of the S&P 500 Index of 752.44 reached on November 20 will in fact prove to be the low for this market cycle, we think that stocks are likely to be higher 12 months from now and, more importantly, three to five years from now and over the next decade.