



## Q U A R T E R L Y L E T T E R

## GENERAL MARKET REVIEW

Risk was off the table in the 3<sup>rd</sup> quarter of 2011 as investors grew increasingly despondent over the malaise of the global economy and fled equities for bonds. The markets appeared to have already priced in a global recession and displayed further concern over stalling growth in the emerging market economies leading the Dow to end down over 12%, its worst percentage decline since the 1<sup>st</sup> quarter of 2009 and causing the global small cap equities market as measured by the MSCI World Small Index, to fall more than 20% in the period. This recent quarter seemed more reminiscent of the 4<sup>th</sup> quarter of 2008 as the US teetered on the edge of default in late July and was sideswiped immediately thereafter by the S&P downgrade. Outside the US, debt concerns continue to plague the European banking system and new signs emerged that China, most notably, would not be able to maintain its strong GDP, fueling speculation over demand or lack thereof for commodities. Policymakers also had a hard time containing this fear and instigated more concern as comments they made cast a dark shadow over the global markets despite the fact that some of the slowdown in activity has been less disappointing relative to expectations. In small cap territory, as a result, intraday volatility spiked in the quarter and during the month of August and September, the US based Russell 2000® broad small cap index saw moves greater than 1% everyday; and in September, on 19 of 21 days, the index saw a move of at least 2%, levels not seen since 2009. While a drop in crude oil alleviated consumers' constrained pockets, it was not enough to materially reverse the negative market direction.

Generally, the more defensive sectors outperformed the more traditional growth sectors led by Utilities (-6%), followed by Consumer Staples (-9%), Financials and Healthcare (both -18%). Energy (-28%) suffered the worst decline in the quarter followed by Information Technology (-24%), Materials (-23%) and Industrials (-23%) – all of which were down on the compression in the commodities sector and headwinds created by the weak economic outlook. Although there continues to be much speculation over the state of the global economy, investors must now look to the 3<sup>rd</sup> quarter earnings season to give a clearer indication on the direction the markets will take.

3<sup>rd</sup> QUARTER 2011 PORTFOLIO REVIEW

The Copper Rock Global Small Cap Composite outperformed the MSCI World Small Cap Index by approximately +381 bps during a wildly volatile and negative market punctuated by headline risk and macroeconomic news, returning -8.48% versus -12.29% respectively. This result in the quarter added to the portfolio's relative outperformance since the strategy's inception of April 1, 2010 posting a return of +0.23% relative to -4.32% for the index. The broad relative outperformance in the global small cap strategy was driven by positive stock selection within the Consumer Discretionary, Information Technology, Healthcare, Telecommunication Services, and Consumer Staples sectors while there was modest underperformance from stock selection in the Industrials, Energy, and Financials sectors. In addition, the very modest overweight position the portfolio held in the Energy sector during the quarter added to the underperformance in that sector as energy prices fell in the quarter. Regionally, stock selection was especially strong in the Europe ex-UK, North America, Emerging Markets, and Pacific ex-Japan regions. Stock selection was strong in the Japanese market but the underweight allocation relative to the index detracted from performance. As we continue to see the Japanese recovery occur, we have been selectively adding to this market.

Consumer Discretionary sector holding, *Himart Co., Ltd.*, the market leader in Korean electronics and appliance retailing, was the leading contributor to performance in the quarter as the company continued to exceed on all metrics. The company, which is akin to Best Buy in the US, owns 35% of the retail electronics market and has plans to open 50 stores by the end of 2012. This plan will add to the company's scale and expand already strong margins. There is significant upside in the stock from where it presently trades at 12x 2012 multiple, and we continue to own it. Also within the same sector, *Ryohin Keikaku Company* and *Rinnai Corporation*, Japanese consumer discretionary holdings, outperformed nicely in the quarter. We have been seeing an exciting theme in Japan as the country, led by its consumers, recovers from the Tohoku earthquake. *Ryohin Keikaku Company* is a Japanese wholesaler of knitwear, food and household items distinguished by its low-overhead and minimalistic, un-branded products. The company is experiencing rapid growth overseas with a target to double international profits by 2014. In addition, it has benefited from demand for its products locally since the earthquake. The company has continually scored a top ranking in our quantitative model, and we continue to own the stock. *Rinnai Corporation* is the Japanese market leader in the manufacturing of household gas appliances. In addition to a strong base of recurring demand and a trend towards more

3<sup>rd</sup> QUARTER 2011 PORTFOLIO REVIEW (continued)

environmentally friendly gas appliances, the recent natural disaster in Japan which caused severe disruptions in electric generation and distribution has spurred demand for new gas units as part of the reconstruction effort. The stock has consistently performed well in the strategy and also has a strong ranking in our quantitative model. Within the US market, *Deckers Outdoor Corp.* has continued to excel throughout 2011 and maintains its top ranking in our quantitative model. The global designer of footwear and accessories, widely known for its UGG and TEVA brands, has seen strong sales of those brands with solid profitability supported by price increases which the company has successfully passed on to the consumer.

Within the Consumer Staples sector, *PriceSmart, Inc.*, which operates membership shopping warehouse clubs in Central America and the Caribbean, reported a strong fundamental quarter and monthly comparisons of more than 15% growth over the summer months. We continue to find this an attractive opportunity as *PriceSmart, Inc.* focuses its product offerings and format for the cost conscious consumer.

Finally, the strategy experienced solid performance from the handful of Healthcare sector holdings including *Jazz Pharmaceuticals, Inc.*, *Virbac S.A.*, *Hitachi Medical Corp.*, and *MWI Veterinary Supply, Inc.* *Jazz Pharmaceuticals, Inc.* which develops treatments for neurological and psychiatric conditions has scaled back its offerings focusing more purely on the specific niche around narcolepsy. There are high barriers to entry for the generic market and a significant opportunity to increase price coupled with sustainable double digit growth. The stock continues to trade at an attractive single digit P/E multiple and has been a consistent outperformer in the strategy.

On the downside, most of the underperformance can be attributed to the headwinds created by the weak economic picture which affected some of our holdings in the Financials sector but also to the swift decline in commodities which impacted the portfolio's holdings in the Industrials, Materials, and more specifically, Energy, sectors. First, within the Financials sector, *Jones Lang LaSalle, Inc.*, the global provider of real estate and investment management services based in the US, was down in the period. Revenues and contract win trends have remained strong though margins have been a bit lower than expectations due to higher associated incentive compensation costs. Most of the recent underperformance in the quarter, however, was because of the renewed global concerns over the financing of real estate investment. Our thesis continues to support owning this stock in the strategy because of its strong brand and efficiencies of its multi-service and global offering. The stock is still highly ranked in our quantitative model while also having a strong valuation score.

Declining oil and other commodity prices drove energy stocks and some industrials and materials stocks down in the quarter as fear of a global recession amid Europe's more severe sovereign debt problems and a slowing Chinese economy re-emerged with force. Despite these short term fluctuations, we tend to remain owners of several of the stocks that experienced these short term dislocations. *W&T Offshore, Inc.*, a US-based independent oil and gas exploration and development company that focuses on onshore and offshore production for the US market, is an example of a company that was down in the period on headline risk and the selloff in energy stocks but has since recovered. The company has pursued a strategy of buying mid-sized blocks of already producing acreage and then increasing production through additional new drilling. We continue to own this position.

Finally, within the Materials sector, despite an overall positive impact from stock selection in the quarter, there were two holdings that were down in the quarter. First, *Materion Corporation* which produces high performance engineered materials used for electronic products, was caught flat footed as fears of overcapacity in the electronics markets and slowing consumer demand hurt more cyclically oriented names. The company coincidentally started to lose quantitative support in our model as earnings revisions fell and valuation was no longer attractive relative to other superior opportunities for the portfolio. As a result, we followed our sell discipline and exited the stock. *Ilika Resources, Ltd.*, on the other hand, is an example of a stock that was down in the period as all prices for underlying commodities fell among the renewed fears of European sovereign risks, global recession and the slowing Chinese GDP. This company, which mines and processes titanium minerals and zircon - key ingredients used in many industrial processes and consumer products, continues to be a top ranking in the model. We still own this position as a unique investment exposed to structurally tight commodities with high barriers to entry and concentrated supply base.

## PORTFOLIO POSITIONING and MARKET OUTLOOK

In spite of the strong reversal in the global markets and the apparent headwinds that suggest a global GDP slowdown and possible recession in the global economy, there is no change to the fundamental investment process for the Copper Rock Global Cap strategy. We continue to seek out companies that enjoy strong underlying unit growth and profitability which operate unique business models that can sustain this growth. Similar to what we had forecast earlier in the year, we continue to believe that global GDP growth will be quite modest considering it has slowed appreciably since forecasts earlier this year. Headline risk driven by macro factors has dominated 2011 and certainly remains more abundant since the beginning of the third quarter of 2011. The ongoing focus in the markets will be on earnings and superior earnings growers and those companies with unique and differentiated products across all sectors and regions that can fund their growth in a modest to slower growth economy.

In the US, GDP has slowed appreciably and economic news remains lackluster, but we continue to invest in pockets of the economy that will withstand further economic stagnation or even pullback. Some of those companies fall within the Information Technology sector that derive benefits for corporations through the proliferation of mobile technology and applications to support that mobility. On the Consumer side, we tend to be drawn to more specialty retailers experiencing organic square footage growth with strong brand recognition both in the US and abroad and believe we will continue to find those superior companies that fit our investment strategy and are appreciated by both US and international consumers.

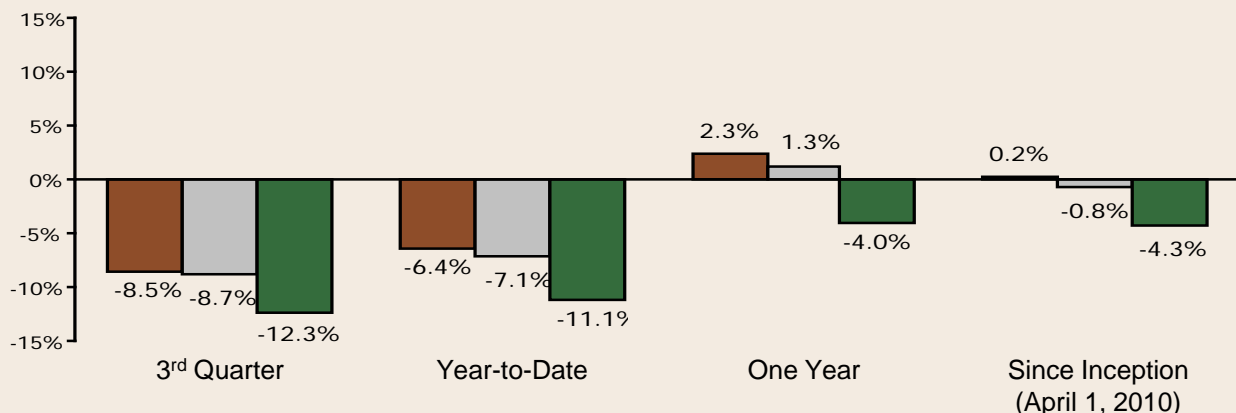
With European governments' debt in the headlines, long term stabilization will depend on Germany stepping up to support either Eurobonds or loan guarantees for financial institutions and sovereigns. We believe that Germany will rise to the occasion as it is in the country's interest to preserve the Euro currency which has been an incredibly positive driver for German manufacturing and exports. However, we recognize the difficulty the country has faced in recent weeks. In every period of stress for some enterprises there are openings for others to gain share. The European Central Bank will need to drop its hawkish stance, acknowledging that higher liquidity preferences will slow growth and inflation. This will be the backdrop that will support European exporters and, eventually, will facilitate debt restructuring. In the interim, we shall favor European companies that export, or that are gaining domestic shares at a rapid pace through unique productivity-enhancing businesses.

In Asia, specifically the Pacific Rim and Japan, the region has experienced significant growth, driven by stimulus to support internal growth. Japan has structured re-building programs in the wake of the Tohoku Earthquake and the consumer has rebounded with the pride of Japan yesteryear. China has been making a concerted effort to channel its red hot economy into broad social infrastructure and jobs as well as to deflate an over extended real estate market. As 2011 has progressed, China appears to still be working to stage a soft landing while the Japanese economy has recovered its export and domestic industries on a faster than expected time line. Regardless, we still expect China to continue to have impressive demand and constructive growth as will Japan throughout its recovery.

Despite expectations of modest global growth and headline risk, we shall continue to emphasize stock-picking over macro-driven investing – this is our normal process. Growth is out there, and even more highly-valued today than in an environment of uniform strong growth. We believe that the market will increasingly pay a premium for the growth companies on which our team focuses.

## PERFORMANCE SUMMARY: 9/30/11

- Copper Rock Capital Global Small Cap Equity Representative Portfolio Gross of Fees
- Copper Rock Capital Global Small Cap Equity Representative Portfolio Net of Fees
- MSCI World Small Cap



Performance is expressed in AU\$. The Copper Rock Global Small Cap Equity Composite includes discretionary, fee- and non-fee paying, non-wrap accounts managed in the global small capitalization equity style. The style is benchmarked against the MSCI World Small Cap Index. The composite inception date is April 1, 2010. Past performance is not indicative of future results. The MSCI World Small Cap Index is a free float adjusted market capitalization weighted index that is designed to measure the equity performance of small capitalization companies from 24 developed markets around the world including the US.

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## Q3 TOP CONTRIBUTORS\*

Himart Co., Ltd.	+52 bps
PriceSmart, Inc.	+51 bps
Jazz Pharmaceuticals, Inc.	+49 bps
Ryohin Keikaku Co., Ltd.	+45 bps
Rinnai Corp.	+42 bps

## Q3 TOP DETRACTORS\*

W&T Offshore, Inc.	-38 bps
Jones Lang LaSalle, Inc.	-28 bps
Kindred Healthcare, Inc.	-24 bps
Materion Corp.	-24 bps
Iluka Resources, Ltd.	-24 bps

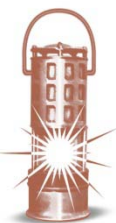
\* Data derived from a Copper Rock Global Small Cap representative account expressed in USD. Source: FactSet.

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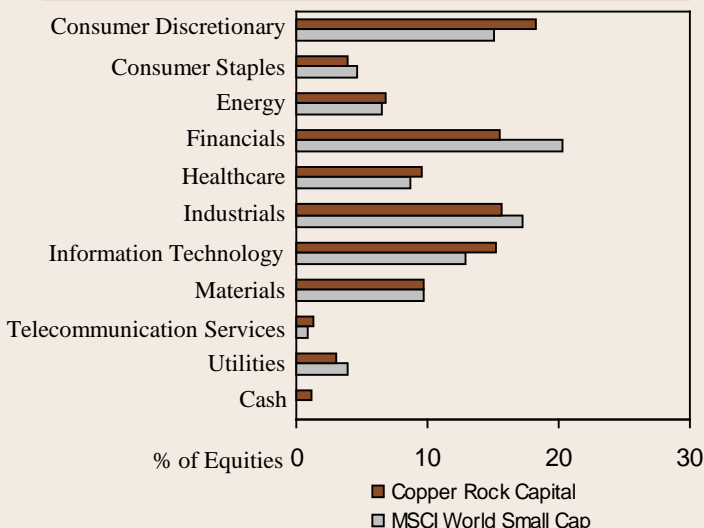


## PORTFOLIO POSITIONING as of 9/30/11

## TOP TEN COMMON STOCK HOLDINGS\*

Companies	% of Portfolio
Cadence Design Systems, Inc.	2.0
Filtrona PLC	1.8
NCR Corp.	1.8
OGE Energy Corp.	1.8
ValueClick, Inc.	1.8
Zodiac Aerospace	1.7
Rinnai Corp.	1.7
PriceSmart, Inc.	1.7
TIBCO Software, Inc.	1.7
Virbac S.A.	1.6
<b>Total:</b>	<b>17.6%</b>

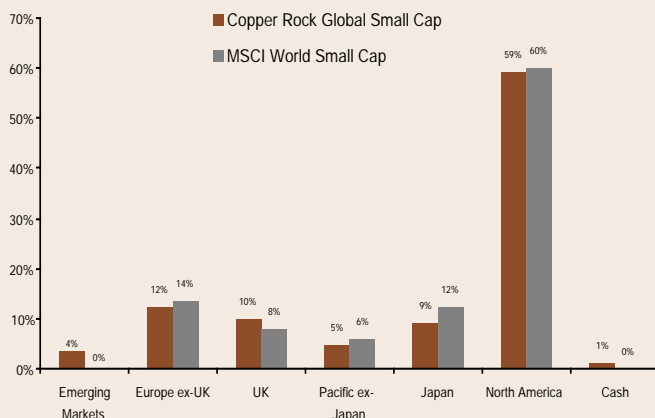
## SECTOR ALLOCATION\*



## PORTFOLIO CHARACTERISTICS\*

Characteristics	Copper Rock	MSCI World Small Cap
Price/Cash Flow	9.7	8.7
P/E (Forward 1 Year)	11.2	12.3
LT EPS Growth	27.7	12.2
ROE	17.4	11.4
ROA	8.4	5.8
Operating Margin	13.7	13.5
Yield (%)	1.3	1.6
Price to Book	2.1	1.6
Weighted Avg. Market-Cap (\$bil)	2.0	1.8
Number of Holdings	83	4,608

## REGIONAL ALLOCATION\*



\* Data derived from a Copper Rock Global Small Cap representative account expressed in USD. Source: FactSet.

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