



Parametric™

Leaders in Structured Portfolio Management

2008 PARAMETRIC TAX MANAGED S&P 500 COMPOSITE PRE-TAX PERFORMANCE

RESEARCH BRIEF

Winter 2009

►► SUMMARY

For 2008, the pre-tax return of the S&P 500 was -37.00% vs. Parametric's S&P500 TMC Composite of -35.91%. The pre-tax excess return for the composite over this period was +1.09%. The excess return is largely attributed to the extraordinary market volatility that began late in the 3rd quarter. We can attribute the excess return to three primary sources: AIG (+37bps), the Financials ex AIG and Energy sectors (+46bps), and cash (+24bps). Systematic biases to risk factors did not contribute materially to the YTD excess return. ►►

Rey Santodomingo

Portfolio Management

Rainer Germann

Portfolio Management

Parametric

1151 Fairview Avenue N.

Seattle, WA 98109

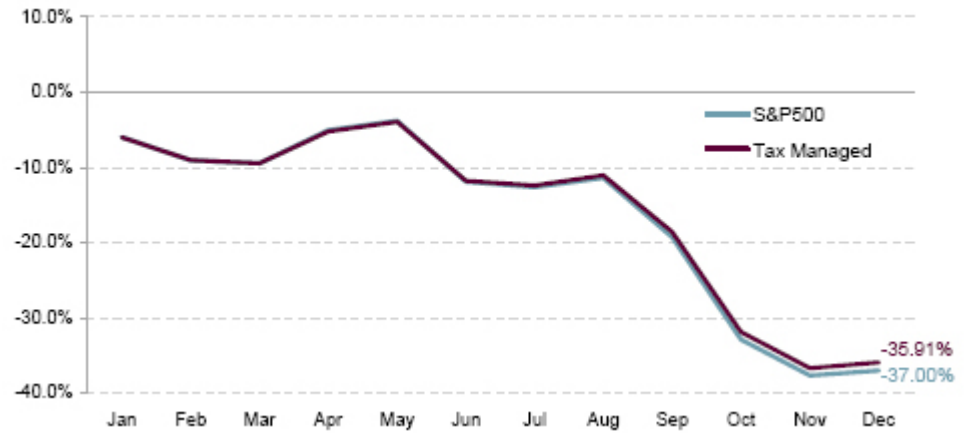
T 206 694 5575

F 206 694 5581

www.parametricportfolio.com

The 2008 relative performance suggests that the sector, industry and risk factor bias tolerances have been effective in managing deviation from the benchmark. In response to the dramatic increase in volatility, efforts to tighten security biases have been made to reduce the impact of single name events like AIG.

Figure 1:
2008 CUMULATIVE RETURN S&P 500 vs. TMC

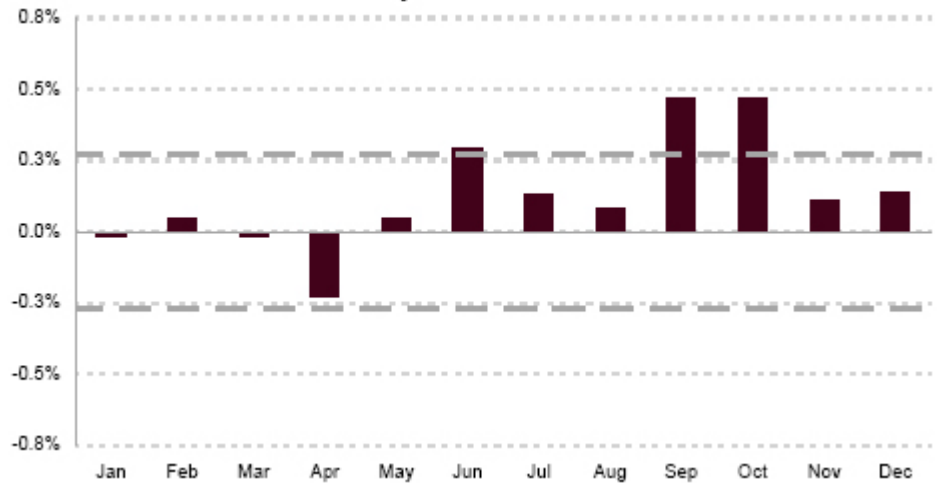


SOURCE: Parametric

►► **ATTRIBUTION**

The chart below shows the excess return of the composite for each month in 2008:

Figure 2:
MONTHLY EXCESS RETURNS 2008



SOURCE: Parametric

We can see eight consecutive months of positive excess returns beginning in May contributed to the overall positive excess return of the composite in 2008. In general, the composite portfolio has exhibited monthly return deviations consistent with the tracking error limit used to manage individual portfolios. The two exceptions over the year are September and October where the excess return of the composite portfolio was +47bps in both months. These months coincided with the period of dramatically increasing market volatility as shown by the VIX index:

Figure 3:
VIX CLOSE

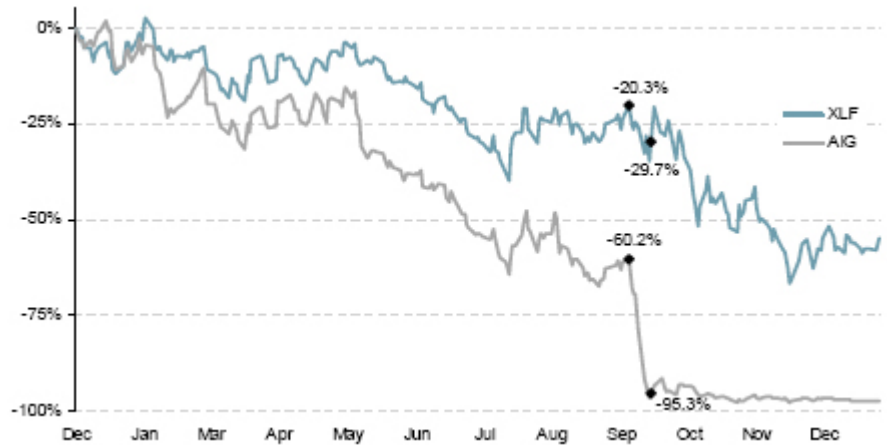


SOURCE: Parametric

►► SECURITY SPECIFIC - EXCESS RETURN IN SEPTEMBER

The large excess return in September was caused by a systematic underweight to AIG in tax managed portfolios. AIG's weak performance relative to the Financial sector in 2008 is depicted in the cumulative return chart below.

Figure 4:
2008 CUMULATIVE RETURN



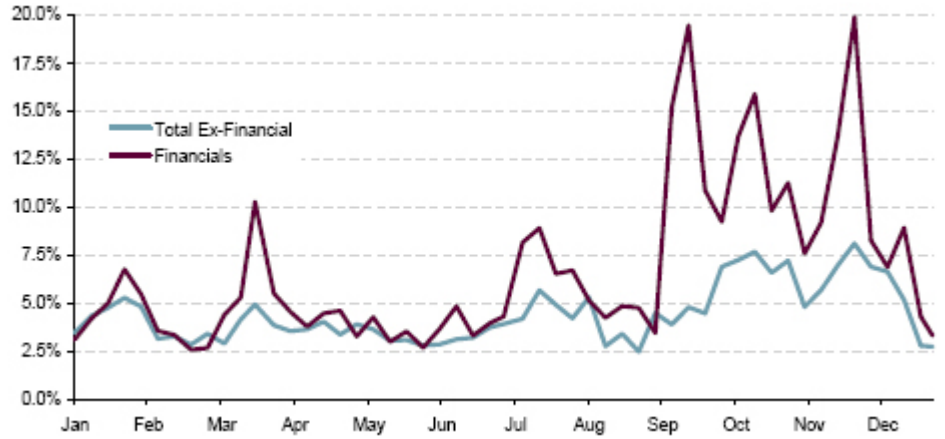
SOURCE: Parametric

The result of this return stream led AIG to be a commonly loss harvested and consequently underweighted name. This coupled with AIG's dramatic 85% decline in September caused the composite to outperform the benchmark by +37bps. Recent efforts to tighten individual security biases should reduce the impact of subsequent single name events.

►► SECTOR/INDUSTRY

The Financial and Energy sectors contributed most significantly to the excess return of Parametric's S&P500 TMC Composite in 2008. These sectors accounted for +63bps and +20bps respectively over the holding period. Among the top contributing industries were Insurance +38bps, Oil, Gas and Consumable Fuels +15bps, and Commercial Banks +10bps. The +38bps of contribution from the Insurance industry includes +37bps from AIG. We maintain neutral biases to all sectors and industries within our defined tolerances. However, we saw material security selection effects within these sectors due to relatively high cross sectional volatility in these sectors in 2008. The chart below depicts both the cross sectional volatility for Finance and the remaining S&P 500 sectors over 2008. Volatility in Finance was so extreme during September it exceeded all other sectors combined almost fourfold and continued its outlier behaviour through November.

Figure 5:
WEEKLY CROSS-SECTIONAL VOLATILITY BY GICS
S&P 500 CONSTITUENTS; 2008

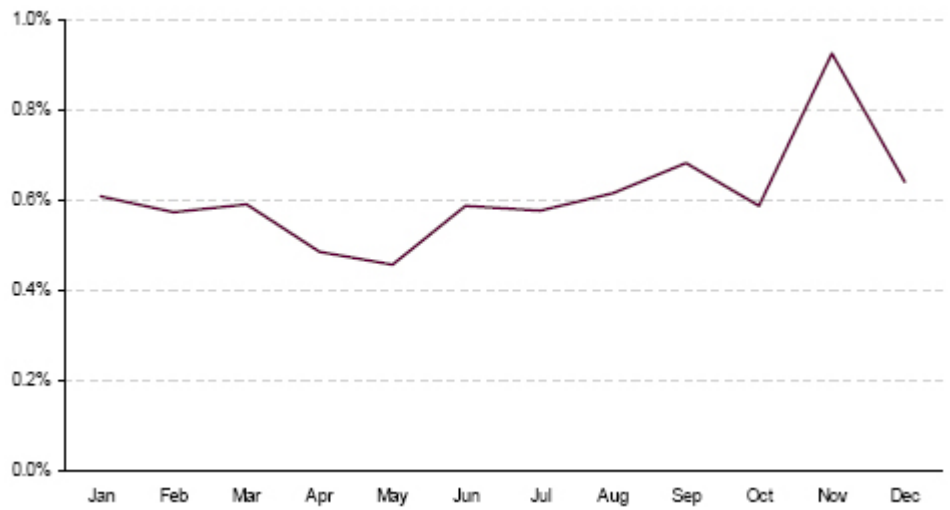


SOURCE: Parametric

►► **CASH**

For Parametric's S&P500 TMC composite, the average weight of cash was +63bps during 2008. In 2008's environment of large negative returns, being overweight cash with respect to the benchmark yielded a positive excess return of +24bps over the year.

Figure 6:
AVERAGE CASH WEIGHT IN TMC S&P 500 COMPOSITE



SOURCE: Parametric

► FACTORS - EXCESS RETURN IN JUNE

Returns due to systematic factor biases did not materially contribute to excess returns in 2008. Factor return contributions were most notable in June. In June, the momentum and volatility factors contributed +12bps of excess return. The factor returns due to biases did not contribute to the excess returns in other months.

	VOLATILITY			MOMENTUM			TOTAL (bps)
	BIAS (%)	RETURN (%)	CONT. (bps)	BIAS (%)	RETURN (%)	CONT. (bps)	
January	-1.9	-0.01	0.0	1.5	-2.95	-4.3	-4.3
February	-1.8	-0.82	1.5	-1.8	0.53	-1.0	0.5
March	-0.8	-1.70	1.4	1.7	0.27	0.5	1.8
April	-1.8	1.01	-1.8	2.5	-0.28	-0.7	-2.5
May	-1.3	NA	NA	2.1	-0.37	-0.8	NA
June	-1.9	-2.44	4.7	2.2	3.31	7.2	12.0
July	-2.2	0.23	-0.5	1.7	-1.92	-3.2	-3.7
August	-1.8	-1.22	2.3	2.2	-2.88	-6.4	-4.2
September	-1.0	-3.33	3.2	2.1	-1.35	-2.8	0.4
October	-0.6	-0.64	0.4	1.0	2.04	2.0	2.3
November	-0.3	-1.47	0.4	0.8	0.46	0.4	0.7
December	-0.8	2.35	-1.9	1.0	-0.95	-1.0	-2.9
TOTAL			9.4			-10.1	0.05

SOURCE: FACTOR RETURN DATA FROM MSCI BARRA AT WWW.BARRA.COM

► CONCLUSION

Parametric's S&P 500 TMC Composite showed an excess return of 1.09% compared to the S&P 500 index. Excess returns arose predominantly from three sources over the period:

- A systematic underweight position in AIG, where dramatic losses over a short time frame in September contributed +37bps.
- Cash bias, where a consistently strong bearish market throughout the year added +24bps.
- Selection effect due to extreme cross sectional volatility particularly in the Finance sector contributed +46bps.

Parametric Portfolio Associates, LLC, is a Registered Investment Adviser and is a majority-owned subsidiary of Eaton Vance Corp. This information should not be considered investment advice or a recommendation to buy or sell any particular security. The information in this material and any specific securities mentioned are not intended to be representative of all securities purchased, sold or recommended for clients. It should not be assumed that any of the securities or recommendations made in the future will be profitable or will equal the performance of the listed securities. Past performance does not predict future results. Parametric does not provide tax advice. Prospective investors should seek their own tax advice prior to entering into any investment strategy.