

### US Small-Cap

Within U.S. small-cap equity the active management fee levels have fallen, similar to products higher up on the market capitalization spectrum. The area that has seen the most significant drop in fee level over the last three years, based on investment style, were U.S. small-cap growth managers. Furthermore, across the differing investment styles we found that the average discount of actual fees compared to the stated fee level has been meaningfully lower. In contrast, the small market capitalization space demands more diversified portfolios in comparison to the large market capitalization area. U.S. small-cap managers have not been immune to the fee pressure we've seen throughout the equity landscape.

U.S. small-cap growth equity managers have seen their fees drop more dramatically over the most recent three-year period compared to core and value managers (Figures 22, 23, and 24). In a similar study conducted ten years ago by State Street Analytics and the ICC (Independent Consultants Cooperative), U.S. small-cap growth saw their fee level fall by 10% between 2004 and 2005. The reason for the fall 10 years ago was performance related. From 2013 to 2015 the growth equity managers' median fee level went from 93 basis points to 87 basis points, for those managers that do not offer performance fees. This decrease has happened during a time where growth stocks have been in favor, outperforming both core and value stocks in each year shown. Conversely, value managers have seen their fee levels maintained over this time period. Historically, we've seen small-cap growth products fee levels rise significantly before coming back in line with both value and core products, like we are seeing today. When looking at those asset managers that offer performance based fees we found that across all styles the median fee level has fallen.

We saw significant differences between stated and actual fee levels in U.S. small-cap. The value products had an average discount of 19 basis points. Approximately, sixty percent of each investment style universe within U.S. small-cap equity had a lower actual fee compared to their stated fee, this is shown below in figure 25. Core and growth equity managers have an average discount of

Figure 22.

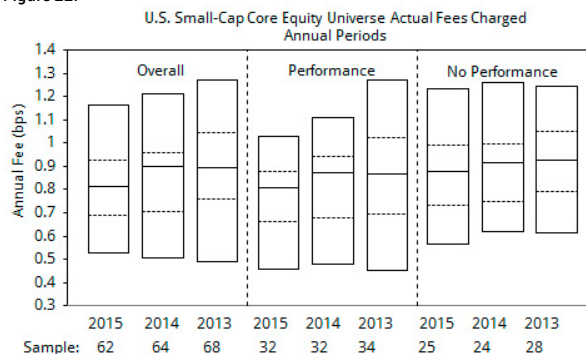


Figure 23.

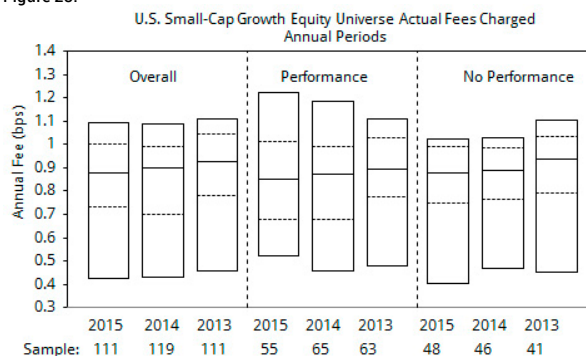


Figure 24.

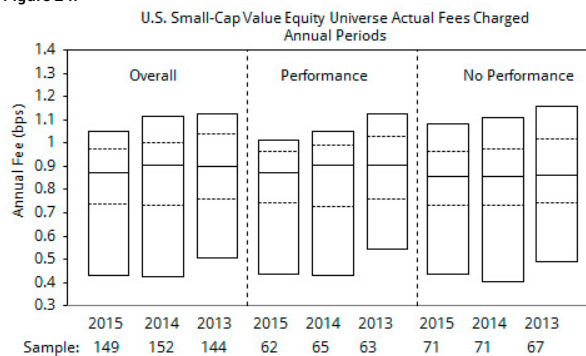
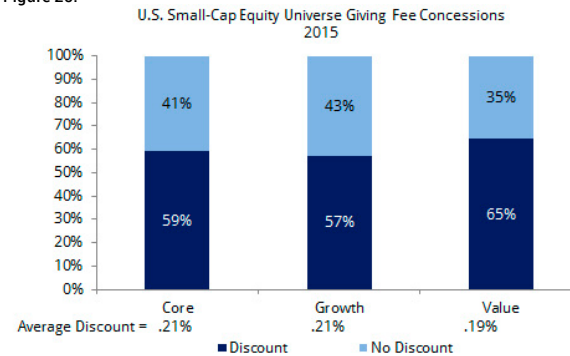


Figure 25.

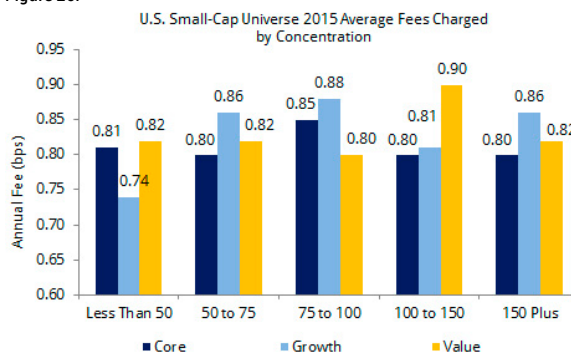


21 basis points based on 2015 fees. Meanwhile, value managers had the largest percentage of their universe offering discounts to their stated fee level at 65%.

A difference within the U.S. small-cap space in comparison to the large-cap space is the demand has been for more diversified portfolios (Figure 26). Those portfolios that have between 75 and 150 holdings were the ones that earned the highest fees in 2015, when comparing products by concentration segments. Small-cap growth and core managers saw the highest fee levels in the 75 to 100 holdings range, earning 85 basis points and 88 basis points respectively. Small-cap value managers saw the highest fees, on average, from those portfolios that held between 100 and 150 securities with 90 basis points. The volatility and breadth of the small-cap universe leads to a higher demand for more diversified portfolios.

The year-to-date asset gainers in the U.S. small-cap space saw moderate differences between their calculated fees and the median fee level of their competitors (Figure 27). A value manager was the top asset gainer and the fee differential was only 8 basis points between their actual fee and the median competitors' fee, based on concentration segments. Second on the winners list was another value manager, however, this asset manager's actual fee is 20 basis points greater than their competitors. The average

Figure 26.



fee difference of the top ten asset gainers was slight at 5 basis points lower when comparing them to their competitors based on concentration levels.

Below are the top performers within our calculated fee universe over the most recent three year period as of September 2015 (Figure 28). Many of the top U.S. small-cap performers had fee levels above their product's style median fee level. Additionally, the performance from this segment of the market has been very strong over the most recent period.

Within the U.S. small-cap equity space growth managers saw the largest reduction of fees in the most recent three-year period. Also, more diversified portfolios were preferred to more concentrated portfolios, which is in contrast to the larger capitalization area.

Figure 27. U.S. Small-Cap Equity Year-To-Date Top Asset Gainers

	Tax-Exempt Assets Gained YTD 2015	Average Account Size (Assets Gained)	Style	Holdings	Actual Fee	Difference vs. Median by Concentration
1	\$653	\$327	Value	100	1.00	0.13
2	\$649	\$324	Core	288	0.76	-0.04
3	\$455	\$227	Value	121	1.00	0.12
4	\$374	\$62	Value	95	0.90	0.02
5	\$363	\$52	Growth	90	0.69	-0.18
6	\$310	\$31	Value	75	0.99	0.16
7	\$272	\$68	Core	148	0.68	-0.20
8	\$255	\$127	Value	140	0.68	-0.20
9	\$201	\$50	Growth	48	1.00	0.12
10	\$175	\$58	Value	60	0.69	-0.14

Figure 28. U.S. Small-Cap Top Performers

	Process	Style	3 Year Return	2015 Fee	Difference vs. Overall 2015 Style Median
1	Fundamental	Growth	30.68	0.90	0.02
2	Fundamental	Growth	26.35	0.88	0.00
3	Quantitative	Growth	19.97	0.93	0.05
4	Fundamental	Growth	19.80	0.59	-0.29
5	Fundamental	Core	19.50	0.91	0.10
6	Fundamental	Value	19.02	1.05	0.18
7	Fundamental	Growth	19.00	0.85	-0.03
8	Fundamental	Core	18.65	0.82	0.01
9	Fundamental	Core	18.32	0.72	-0.09
10	Fundamental	Core	17.82	0.73	-0.08