



**Smith Graham & Company**  
**Investment Advisors, L.P.**

October 1, 2002

Dear Friends of Smith Graham,

Since our founding in 1990, we have built a reputation for success by focusing on the management of fixed-income investments. Smith Graham's fixed-income products' performance year to date has been outstanding and ranks among the top managers across the country. Our strategy has always been to deliver the highest quality service by concentrating our resources in our core competencies that include identifying opportunities to broaden our service to our clients while maintaining the same high standards for performance. Given this strategy, we have been open to the possibility and the benefits of adding an equity management capability to complement our fixed-income investment management team.

We were recently approached by a group of experienced investment professionals formerly from JPMorgan Chase who together have managed equity assets, delivering outstanding performance. Our conversations explored the concept of adding that equity management capability to Smith Graham. We also identified the challenges of adding the equity component while avoiding any diversion of resources or time from our fixed-income advisory business. Our commitment has been and remains to add capabilities seamlessly with no alteration in daily operations or existing service.

We are proud to announce that effective October 1, 2002, an agreement will be signed which expands our firm to include a large-cap equity management capability. Our plan includes the additional resources required to integrate the equity team without compromising existing resource allocation.

Our agreement provides that Progress-Putnam Lovell Ventures, L.L.C. on behalf of California Public Employees Retirement Systems Manager Development Program (CalPERS MDP), the nation's largest public pension fund, will make an equity investment in Smith Graham in return for less than 25 percent interest in the firm. Additionally, CalPERS MDP will allocate \$100 million in equity investments to Smith Graham for the creation of our first large-cap equity mandate.

This is positive news for many reasons. The combination of an equity team with our existing fixed-income team is a further realization of our long-range strategic plan. It improves our ability to evaluate a broader range of opportunities and risk in the world's

financial markets on behalf of our institutional clients. The addition of an equity product also leverages our existing strengths in research, performance monitoring, and investment evaluation. Our fixed and equity components together will lead to the identification of new opportunities in the future, and the combination of fixed and equity investment professionals results in a team with depth and a consistent history of strong out performance in difficult market conditions.

Our large-cap product mandate will be managed by the members of our new equity team that have joined the firm: Jeffrey S. Phelps, CFA – Director of Equity Portfolio Management, Michael E. Garrett – Senior Equity Analyst and James Shelton – Senior Equity Analyst. Their years of experience, working relationship, and marketing contacts will be a great asset to our clients.

Jeffrey S. Phelps, our new Director of Equity Portfolio Management notes, “As a team, we’re excited to be a part of an established company like Smith Graham who is clearly committed to building and growing the equity business for the long-term. Joining Smith Graham is an ideal fit in many ways and will allow us to continue our successful equity management style and provide an opportunity to leverage the existing talent and resources from across the firm.”

Beyond benefits to you, our client, there are important benefits for our employees, who will be eligible to participate in an incentive profit interest plan of up to 10 percent equity interest in the firm. The plan comprises a significant component of our talent retention strategy and allows investment professionals and others to participate in the profits and appreciation in the value of our organization.

We are excited about these developments because they hold great promise for both our clients and our firm. We look forward to providing you with more information on our new large-cap equity mandate as we build momentum. We also would be pleased to answer any questions that you might have about our recent developments, so please call us if you would like more information.

Sincerely,

A handwritten signature in black ink, appearing to read "Gerald B. Smith". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Gerald B. Smith  
Chairman and Chief Executive Officer