

What's New at Arrowstreet?

We hope this issue finds you enjoying a relaxing summer break. In this issue of the Journal we highlight a recent Arrowstreet research piece, ESG (Environmental, Social & Governance) and Portfolio Returns. It comes from a talk John Capeci gave at our 2010 Client Conference.

Q2 2010 Review:

World equity markets weakened during the second quarter after peaking in mid April. Sovereign debt concerns in Europe spread through global markets resulting in speculation about the Euro-zone's ability to remain in tact.

Business Growth:

During the second quarter, Arrowstreet gained five new client relationships and firm-wide assets under management reached \$24.7 billion.

Team Members:

In this edition of the Journal, we profile Ruxanda Nedelciuc and Jeffrey Li, who joined Arrowstreet's portfolio management and research teams in 2010. Please turn to page 3 of the Journal to learn more about Ruxanda and Jeff.

As always, we are interested in your views and encourage your feedback. Please email your thoughts to us at: info@arrowstreetcapital.com

ESG (Environmental, Social & Governance) and Portfolio Returns

John Capeci, Ph.D., Partner, Portfolio Management

Environmental, Social, and Governance (ESG) criteria are employed by many institutional investors as part of socially responsible investing programs. The approaches used by investors vary, both with regard to the types of criteria considered, and with regard to approach. In some instances, responsible investing objectives are implemented using screening criteria on allowable holdings. In other cases, investors may modify the benchmark used to measure a manager's performance, in order to reflect large target exposures to socially responsible firms. With either approach, it is in our interest as managers to understand both the return and risk implications of applying the ESG quality criteria.

In this white paper, we examine the impacts of ESG quality criteria by looking at the empirical relationship between ESG quality and various measures of corporate performance. We also investigate the relationship between ESG quality measures and stock level measures of risk. The data we use are contained in a 7 year data set on ESG ratings for a sample of over 5000 globally traded companies, produced by a commercial vendor of ESG rankings. This information is then related to firm level data on profitability (Cash Flow Return on Capital, or CROC), valuation ratios (Book-to-Price), and total returns.

For a complete version of this article, please visit:
http://www.arrowstreetcapital.com/research_whitepaper.htm
For complete versions of other white papers, please contact us.

The Arrowstreet Journal is provided for informational purposes only and is not intended as investment advice. References to recent portfolio activity and holdings are not intended as investment advice. Arrowstreet Capital, Limited Partnership may have already bought or sold or may in the future buy or sell these securities on behalf of its clients. There can be no assurance that an investment in the securities of these issuers, or in any investment recommendation, has been or will be profitable to Arrowstreet's clients. A complete list of buys and sells is available upon request.

June 2010 Investment Outlook Global/International Equity Strategy

Developed Markets Overview: 2nd Quarter 2010

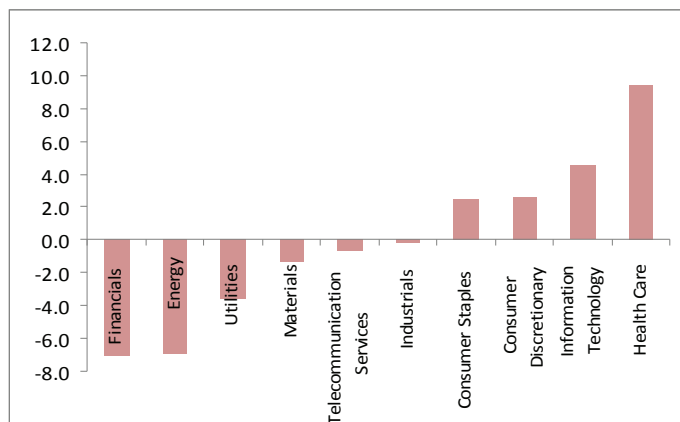
World equity markets weakened during the second quarter after peaking in mid April. Continued concern over sovereign crises resulted in speculation about the ability of the Eurozone to remain intact with Greece receiving a bail out from the European Union and International Monetary Fund. Germany has been calling for an end to stimulus spending and a renewed focus on austerity, expecting reduced government budget deficits will result in growth. The recent G20 summit witnessed mixed views on the subject with the Obama administration advocating for additional spending and government stimulus to promote growth. The final communiqué from the summit offered varied advice saying that appropriate policy responses would necessarily change depending on a country's situation. Weak economic performance may contribute to further political turmoil. Japan's Prime Minister Hatoyama's resignation showed the effects of a loss of confidence and fear of a Greek style financial crisis in the face of a growing deficit.

China began to address their currency valuation problems on two fronts during the quarter. First, they intend to increase the Yuan's flexibility, which should appease US officials demanding immediate adjustment and should reduce calls of manipulation. Second, China moved to raise the minimum wage in the country, indicating its intention to promote wage growth.

Denmark was the best performing developed country in local currency terms during the second quarter of 2010. The country index advanced 4.5% over the three-month period. Denmark's outperformance was paced by the Health Care sector, where Novo Nordisk constitutes 90% of the MSCI basket. The worst performing developed country was Greece, whose MSCI country index declined by more than 34% in the second quarter, highlighted by a 20% drop in the month of May. Greek Financials were the laggard in the country index, dropping 41% in the second quarter.

All ten sectors in the MSCI World index posted negative returns in the 2nd quarter of 2010, with five sectors posting double-digit losses. Energy stocks posted the biggest loss as the sector dropped more than 14% during the quarter. BP Plc plunged 48% after one of its off-shore rigs exploded and initial cleanup efforts proved ineffective. Uncertainty as to when the crisis in the gulf will be resolved and pending litigation against the company weighed on BP shares throughout the quarter. The Financials sector lost more than 13% in the 2nd quarter as sovereign debt concerns continued to loom in the Euro region. UK bank, Barclays Plc, saw its shares plummet 24% in the 2nd quarter. Spain's Banco Santander posted its second consecutive negative quarter, losing 11%. The best performing sector in the 2nd quarter was Telecommunications Services, down 5% over the three month period.

**June 2010 Active Sector Weights (%)
(MSCI World)**



Developed Markets Strategy Performance Attribution

Two country/sector baskets that impacted the performance of Arrowstreet's developed markets portfolios during the quarter are described here:

Sweden Telecommunications: Swedish telecommunication company, Ericsson, had its share price jump 10% at the end of April, as the company reported that its first-quarter North American revenues doubled. The price climbed also during the second half of June on reports that Sony Ericsson had developed new mobile phones. Our overweight position in the stock was motivated by basket level momentum.

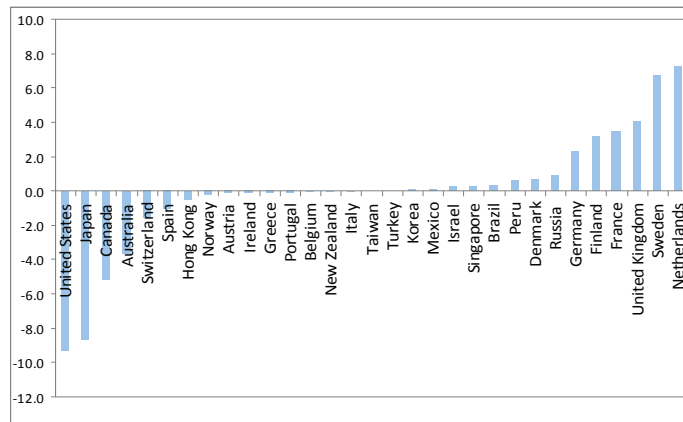
UK Healthcare: United Kingdom drug maker, AstraZeneca PLC, saw shares rise sharply at the end of the second quarter as U.S. courts ruled to prevent generic-drug makers from producing competitors to AstraZeneca's successful cholesterol drug, Crestor. The ruling protects the company's patent on the active ingredients in Crestor through 2016. Our overweight position in the stock was motivated by basket level earnings and basket level value terms.

Specific opportunities that we believe will offer attractive return potential include:

Sears Holdings Corp. (US Consumer Discretionary): Stock level value signals are the primary driver of our overweight position in Sears Holdings Corp. The retail chain with stores in the US and Canada saw its stock price fall by 40% in the previous quarter. While the stock remains disfavored by analysts, various valuation measures indicate the stock's outperformance going forward. The share price rose toward the end of July after reaching its lowest levels in nearly a year earlier in the month.

Renault SA (France Consumer Discretionary): French automobile company, Renault SA, designs, produces, and markets passenger cars and lightweight commercial vehicles. In June, Renault Chief Executive, Carlos Ghosn, announced that the company was open to collaborating with a United States' carmaker, implying that Renault may seek ties with Ford Motor Co. or General Motors. Half-year light vehicle sales for France's second largest carmaker rose 22% to 1.35 million units as the company improved its full-year sales forecast for the European market. Our positive outlook on the stock is based on stock level value and basket level momentum signals.

**June 2010 Active Country Weights (%)
(MSCI World)**



Data provided above is for Arrowstreet's longest standing representative portfolio for the Global Equity strategy as of the end of June 30, 2010.

June 2010 Investment Outlook Emerging Markets Equity Strategy

Emerging Markets Overview: 2nd Quarter 2010

Among emerging market countries, Indonesia was the best performing in USD currency terms during the second quarter of 2010. The country index advanced 4.5% over the three-month period. Indonesia's outperformance was paced by the Consumer Discretionary sector, where Astra International constitutes 100% of the MSCI basket. The worst performing developing country was Hungary, whose MSCI country index declined by more than 30% in the second quarter in USD terms. The underperformance was driven by the Financials sector, where OTP Bank constitutes 100% of the MSCI basket.

All ten sectors in the MSCI Emerging Markets index performed negatively in the 2nd quarter of 2010. Materials stocks posted the biggest loss as the sector dropped more than 13% during the quarter. Russian metals and mining company Mechel OAO plummeted 36% after releasing negative production results for the first quarter, mostly attributable to a seasonal decline in demand. The Energy sector lost 11% over the last three months, making it the worst performing sector year-to-date. Information Technology stocks sank 10%. Shares of Chinese internet company, Tencent Holdings Limited, fell 16% in the second quarter after the stock was downgraded to "neutral" at Susquehanna. Consumer Staples was the best performing emerging markets sector, finishing flat for the quarter after a relatively strong June where the sector posted a positive return of 5%.

Emerging Markets Strategy Performance Attribution

Two country/sector baskets that impacted the performance of Arrowstreet's emerging markets portfolios during the quarter are described here:

Brazil Materials: Vale SA is a Brazil-based company that produces and sells iron ore, gold, copper, and other metals. The company also owns and operates railroads and maritime terminals. Share prices of Vale sank 23% during the second quarter as the company announced the resignation of its chief financial officer and investor relations officer, Fabio de Oliveira Barbosa. Also weighing on share prices was China's growing concern that its own real estate boom may lead to government tightening of property development. As the Chinese government became more vocal about this

concern, materials stocks took a hit globally. Our underweight positioning added value and was motivated by negative basket level momentum signals and poor basket level value terms.

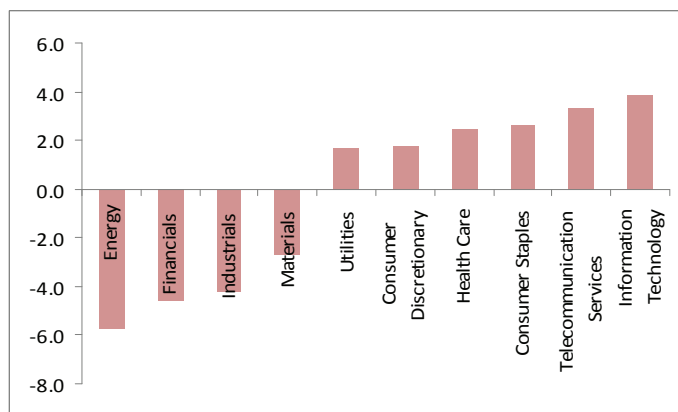
China Telecommunications: China Mobile, the world's largest mobile telecommunications company, saw its price rise during the first half of April on news that it would invest US\$300 million in Pakistan and that it had teamed up with Xinhua News Agency to launch a mobile digital newspaper. China Mobile's price climbed again during the second half of June following reports, on June 11, that the company would become a strategic investor in government-backed People's Daily Online and, on June 22, that the company would invest RMB 70 billion to enlarge the communication networks in China's rural areas. Our underweight position in the stock hurt performance and was motivated by basket level momentum and country level macroeconomic signals.

Specific opportunities that we believe will offer attractive return potential include:

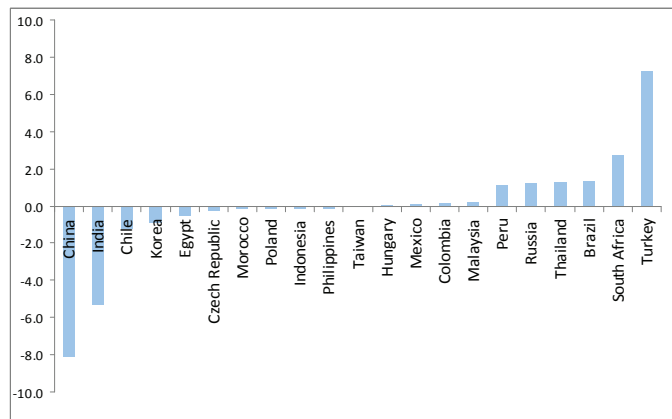
Turkiye Vakiflar Bankasi T.A.O (Turkey Financials): State run bank Turkiye Vakiflar Bankasi has announced plans to expand growth throughout 2010 and beyond. The bank will aim to expand its size from 575 to 620 branch offices this year, with the goal of operating 850 branches in three years. The bank also plans to hire 900 people by the end of the year. The bank plans to sell approximately \$190 million worth of non-financial assets, including some real estate. We view the shares as attractive based on basket level momentum and stock level value terms.

Standard Bank (South Africa Financials): Standard Bank, Africa's largest bank in terms of assets, plans to increase its product range to capitalize on the continent's increased trade with other developing countries. Standard Bank was named the best investment bank in Africa recently at the Euromoney Awards for Excellence. In June, Standard announced that it would partner with GAIN Capital Holdings to launch a retail FX platform, the first offering of its kind by a South African bank. We have a positive outlook on Standard Bank shares due to favorable basket level momentum and country level macro signals.

June 2010 Active Sector Weights (%) (MSCI EM Index)



June 2010 Active Country Weights (%) (MSCI EM Index)



Data provided above is for Arrowstreet's longest standing representative portfolio for the Emerging Markets Equity strategy as of the end of June 30, 2010.

Employee Profiles



Ruxanda Nedelciuc

Associate, Portfolio Management

Ruxanda is involved in various trade support tasks, from corporate actions and trade settlement to forecast review and custom client reports. Ruxanda worked as a summer intern within Arrowstreet's portfolio management team in both 2008 and 2009. She joined full time in June 2010 after graduating from Oberlin College with a degree in Applied Math and Economics.

Jeffrey Li

Associate, Research

Jeff works in the Research Team and is responsible for the development, enhancement, and integration of the firm's data and forecasting systems. Prior to joining Arrowstreet, he worked as an Economic Consultant at Cornerstone Research for a year and interned as a Software/Mechanical Engineer at Raytheon Company for four years. Jeff received his B.S. in Computer Systems Engineering and M.A. in Economics in 2009 from Boston University, which he attended on full academic scholarship.

