



®

O'Shaughnessy
ASSET MANAGEMENT

Franklin Regional Retirement System
O'Shaughnessy Market Leaders Value
QUARTERLY REPORT ENDING SEPTEMBER 30, 2012

Franklin Regional Retirement System

(As of 9/30/12)

Relationship Summary

Market Value (9/30/12):	\$5,626,911.30
Strategy:	O'Shaughnessy Market Leaders Value
Inception Date:	March 1, 2012
Custodian:	Comerica

Strategy Summary

O'Shaughnessy Market Leaders Value generally seeks to provide long-term growth and some current income by investing in market leading companies with attractive valuations. First, we screen for stocks with greater than average market capitalizations and exclude Utilities. We then screen for securities with greater than average scores in our Value, Earnings Quality, Earnings Growth, and Financial Strength composites. From the remaining pool of stocks, we select those with the highest "shareholder yield"— which combines a company's annual dividend and its annual rate of stock buybacks. A portfolio typically holds approximately 50 to 80 stocks.

Performance Review

(As of 9/30/12)

		Current Month	Quarter to Date	Year to Date	Annualized Since Inception	* Inception Date
Franklin Regional Retirement System	(Gross)	1.65	4.94	4.03	4.03	3/1/2012
	(Net)	1.61	4.80	3.70	3.70	
Russell 1000® Value Index		3.17	6.51	6.54	6.54	

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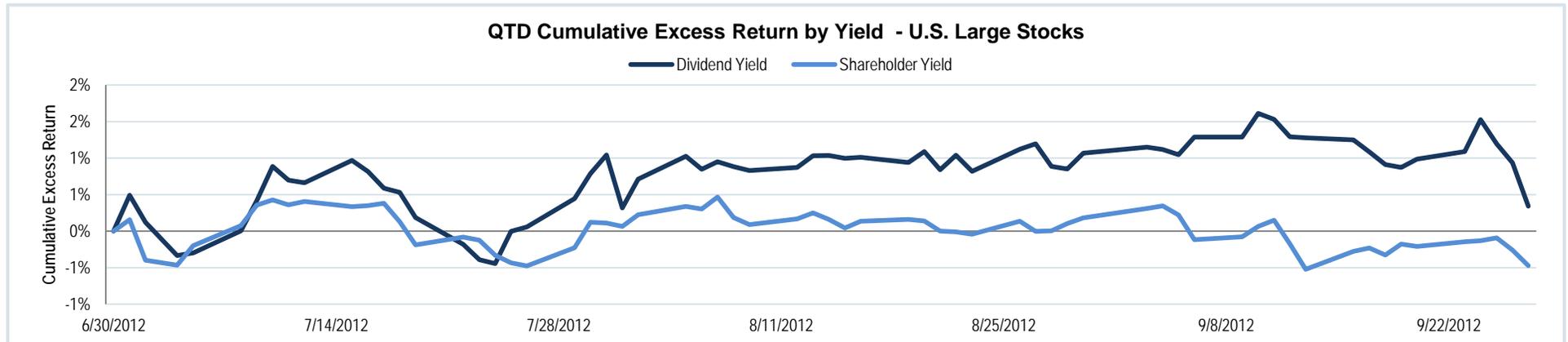
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Franklin Regional Retirement System: Commentary

(As of 9/30/12)

- During the third quarter, Dividend Yield was the stronger characteristic at +0.3%, and outperformed the U.S. Large Stocks Universe. Shareholder Yield underperformed by -0.5%.



- Year-to-date, yield strategies struggled. Shareholder Yield was the stronger characteristic, but underperformed the U.S. Large Stocks Universe by -1.3%. Dividend Yield also underperformed by -3.5%.



Franklin Regional Retirement System: Commentary

(As of 9/30/12)

Positive Contributing Factors for 3Q12:

- Our investment process emphasizes stocks with high financial strength. These stocks contributed positively to returns during the third quarter.
- Our allocation among various economic sectors, as a result of our investment process, also helped performance.
- Our model worked best in these sectors:

	Franklin Regional Retirement System			Russell 1000® Value Index			Performance Attribution		
	Weight	Total Return	Contribution to Return	Weight	Total Return	Contribution to Return	Allocation Effect	Selection + Interaction	Total Effect
OSAM GICS Sector									
Consumer Discretionary	36.47	11.61	4.10	7.74	9.37	0.71	0.77	0.77	1.53
Utilities	0.00	0.00	0.00	7.07	-0.34	-0.02	0.48	0.00	0.48

Negative Contributing Factors for 3Q12:

- During our investment process, we build an investable universe of stocks with low valuation ratios, high earnings quality, high earnings growth. These types of stocks underperformed and detracted from returns during the third quarter.
- We use Shareholder Yield as the final ranking and selection factor. Stocks with high shareholder yield held back returns. Our model worked worst in these sectors:

	Franklin Regional Retirement System			Russell 1000® Value Index			Performance Attribution		
	Weight	Total Return	Contribution to Return	Weight	Total Return	Contribution to Return	Allocation Effect	Selection + Interaction	Total Effect
OSAM GICS Sector									
Telecommunication Services	5.84	-9.70	-0.59	3.77	10.01	0.38	0.06	-1.16	-1.10
Consumer Staples	8.10	1.29	-0.07	7.26	7.95	0.58	0.01	-0.73	-0.72

Franklin Regional Retirement System: Commentary

(As of 9/30/12)

Market Outlook:

Despite a very strong third quarter, markets continue to focus more on macroeconomic and political storylines than on individual companies. Earnings have been important, but QE3, the fiscal cliff, and the health of global economies have dominated headlines. Perhaps the most pressing issue is the fiscal cliff in the United States, which will significantly raise taxes and potentially further slow economic growth if Congress does not intervene. The threat of higher taxes on capital gains (up to 20% from 15%) and especially on dividends (up to the income tax rate from 15%) continues to scare current and prospective equity investors. However, historical data on stock returns — with a focus on higher yielding stocks — suggests that the prevailing tax rates do not matter for stock returns.

Historically, large tax increases have not foretold doom for equity returns. We looked at the 10 highest year-over-year increases of the effective income tax rate on an inflation adjusted income of \$250,000. The average returns for large U.S. stocks in the 1-, 3-, and 5-year periods after the tax increase were 8.0%, 7.8% annualized, and 15.0% annualized, respectively — which are in line with long-term expectations. Only one of the 3-year periods after a large tax increase had a negative market return, following the start of World War II in 1939.

We also analyzed high yielding stocks in greater detail. Since 1926, there have been 32 years when dividends were either exempt from taxation or taxed at 15% (since 2003) and 53 years when dividends were taxed at the full income tax rate. Given the potential for a higher income tax rate on dividends to return in 2013, it is important to note how high yielding stocks have performed relative to the overall market in these two different tax regimes. Over the entire period, the highest yielding stocks beat our Large Stocks universe by 1.1% per year annualized. Surprisingly, the excess return earned by high yielding stocks was very similar regardless of tax regime, and was even slightly higher in years where dividends were taxed at full income tax rates. Volatility of returns during the fully taxable years was also lower for higher yielding stocks. Over the long-term, high yielding stocks were a slight 0.2% less volatile than the overall market, but in years where dividends were fully taxable, the highest yielding stocks were 1.8% less volatile than the market. While this evidence does not lead us to excitement over potentially large tax increases, it does quell our fears of a potential market decline as a direct result of the fiscal cliff. The historical evidence suggests that the prevailing tax rates— and large changes in those rates— do not matter for equity returns.

We continue to advocate buying higher quality stocks with attractive prices, yields, and stable momentum. A disciplined approach is essential when the macro-economic and political environment is volatile and uncertain. By focusing on companies instead of economies, we believe that our Market Leaders Value strategy will be well positioned to succeed.

Franklin Regional Retirement System: Attribution QTD as of September 30, 2012

Factors	Exposures			Factor Returns	
	Average Portfolio Exposure	Average Russell 1000 Value Exposure	Average Active Exposure	Compounded Factor Return	Compounded Factor Impact
Beta	1.04	1.10	-0.06	6.06	-0.38
Trading Activity	0.19	-0.06	0.25	-0.92	-0.32
Log of Market Cap	1.40	1.97	-0.57	0.44	-0.26
EPS Growth Rate	-0.05	-0.30	0.25	-0.98	-0.24
Revenue/Price	0.25	-0.09	0.34	-0.29	-0.11
Relative Strength	0.12	0.10	0.02	-0.23	-0.05
Earnings/Price	0.56	0.48	0.09	-0.20	-0.02
Price Volatility	-0.59	-0.65	0.07	0.32	0.00
Debt/Equity	0.29	0.11	0.18	0.23	0.03
Book/Price	-0.12	0.10	-0.22	-0.31	0.05
Dividend Yield	0.43	0.35	0.08	0.54	0.06
Industry	0.95	1.00	-0.05	-0.16	0.07
Earnings Variability	-0.29	0.19	-0.48	-0.98	0.48
Total	4.19	4.29	-0.10	-0.07	-0.68

Sectors	Franklin Regional Retirement System			Russell 1000 Value Index			Active			Performance Attribution		
	Average Weight	Total Return	Contrib. to Return	Average Weight	Total Return	Contrib. to Return	Average Weight	Total Return	Contrib. to Return	Allocation Effect	Selection + Interaction	Total Effect
Consumer Discretionary	36.47	11.61	4.10	7.74	9.37	0.71	28.72	2.25	3.39	0.77	0.77	1.53
Consumer Staples	8.10	1.29	-0.07	7.26	7.95	0.58	0.85	-6.66	-0.65	0.01	-0.73	-0.72
Energy	4.19	3.52	0.15	16.78	9.09	1.51	-12.59	-5.57	-1.36	-0.33	-0.23	-0.55
Financials	14.20	7.26	0.98	26.24	6.89	1.82	-12.04	0.37	-0.84	-0.06	0.05	-0.01
Health Care	7.67	2.09	0.13	11.64	6.03	0.69	-3.97	-3.94	-0.56	0.03	-0.32	-0.28
Industrials	17.38	5.40	1.01	9.07	5.96	0.54	8.31	-0.56	0.47	0.01	-0.13	-0.12
Information Technology	5.88	-10.06	-0.62	6.56	0.37	0.02	-0.68	-10.43	-0.64	0.08	-0.69	-0.61
Materials	0.28	2.34	0.01	3.87	7.25	0.26	-3.59	-4.91	-0.25	-0.03	0.00	-0.03
Telecommunication Services	5.84	-9.70	-0.59	3.77	10.01	0.38	2.07	-19.71	-0.98	0.06	-1.16	-1.10
Utilities	0.00	0.00	0.00	7.07	-0.34	-0.02	-7.07	0.34	0.02	0.48	0.00	0.48
Total	100.00	5.09	5.09	100.00	6.50	6.50	0.00	-1.41	-1.41	1.03	-2.43	-1.41

Source: FactSet Portfolio Analytics, with the Northfield U.S. Equity Risk Model is a third-party subscription-based tool which may base output on data provided by other databases and information service providers. Past performance is no assurance of future results.

O'Shaughnessy Market Leaders Value: Buy & Sell Examples

Stock Screening Examples (As of 9/25/12)		Buys			Sells	
		<u>Wynn Resorts Ltd. (WYNN)</u>	<u>Viacom Inc. – Class B. (VIA)</u>	<u>Motorola Solutions Inc. (MSI)</u>	<u>Dr. Pepper Snapple Group Inc. (DPS)</u>	<u>Tyco International Ltd. (TYC)</u>
Investable Universe (Approx. 3,500 stocks)						
	Market cap > Universe average, excluding Utilities					
Top half by composited score of Value, Earnings Quality, Earnings Growth, and Financial Strength Composites	Market cap	\$9.0 bil	\$25.8 bil	\$14.6 bil	\$9.2 bil	\$25.2 bil
	Value*	65	11	44	46	48
	Earnings Quality*	8	20	24	32	33
	Earnings Growth*	10	25	24	19	86
	Financial Strength*	90	61	38	69	15
Composited score of composites*	43	29	33	41	46	
Top securities by shareholder yield	Shareholder yield	21.3%	12.4%	18.6%	6.1%	2.0%
	Selected?	Yes	yes	yes	no	no

* The lower the number the better the score.

Please be advised that the information regarding our models are subject to change and is provided for informational purposes only and should not be deemed as a recommendation to purchase or sell the securities mentioned. Moreover, there can be no assurance, as of the date of publication, that the securities purchased remain in a strategy's portfolio or that securities sold have not been repurchased. Additionally, it is noted that the securities purchased do not represent a strategy's entire portfolio and in the aggregate may represent a small percentage of a strategy's portfolio.

Past performance is no guarantee of future results. Please see important disclosure information at the end of this presentation.

Franklin Regional Retirement System: Characteristics¹

(As of 9/30/12)

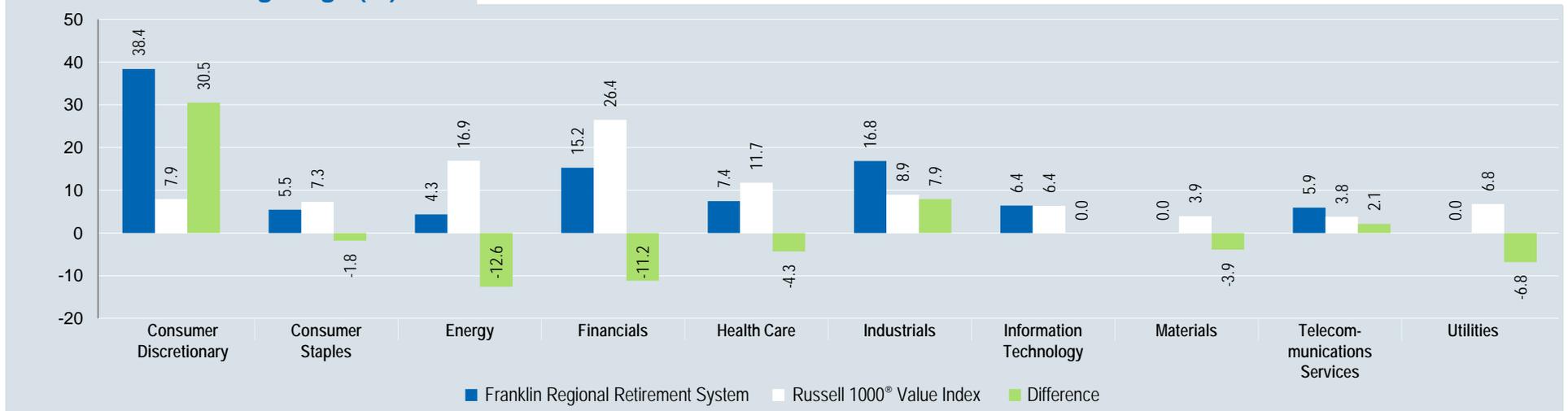
Holdings-Based Characteristics

	Franklin Regional Retirement System	Russell 1000® Value Index
Price/Earnings Ratio	12.0	13.1
Price/Sales Ratio	0.7	1.0
1-Year Historical Earnings Growth Rate (%)	14.9	34.2
Trailing 6-month Price Appreciation (%)	2.3	3.0
Trailing 12-month Price Appreciation (%)	21.9	23.4
Weighted Average Market Capitalization (\$ mil)	23,093	94,630
Median Market Capitalization (\$ mil)	13,775	4,906
Number of Holdings	54	690
Foreign Content (%)	13.0	0.6
Dividend Yield (%)	3.1	2.5
Active Share (%)	94.0	—
Cash (%)	2.4	—

Top Ten Holdings

	Percent of Portfolio
Gap Inc.	4.5
DIRECTV	4.3
ConocoPhillips	4.2
L-3 Communications Holdings Inc.	3.9
Lockheed Martin Corp.	3.9
Ameriprise Financial Inc.	3.8
Travelers Cos. Inc.	3.8
Lowe's Cos.	3.7
Kohl's Corp.	3.6
Time Warner Cable Inc.	3.5
Total	39.2

Current Sector Weightings (%)



¹ Top ten holdings and number of holdings are provided for informational purposes only and should not be deemed as a recommendation to purchase or sell the securities mentioned. Top ten holdings do not represent all of the securities that would be purchased, sold or recommended for an account and the reader should not assume that investments in the securities identified were or will be profitable. Holdings-based valuation metrics are derived from actual holdings utilizing the Factset Portfolio Analytics tool. The price/earnings and price/sales ratios are weighted harmonic averages.

Stocks with small and mid-sized market capitalizations (those defined by OSAM as less than \$10 billion) may have greater risk and volatility than those with larger market capitalizations.

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