

Small-cap emerging market equities have outperformed their large- and mid-cap peers by significant margins over the past ten years.

Emerging Market Small-Cap

Overview

Emerging markets investing has come a long way in the last decade. When the “gold rush” to emerging economies began in the 1990s, investors initially limited their interest to blue chip stocks from the largest emerging markets. However, as broad-based and size-specific indices have flourished for emerging markets, new investment opportunities have opened up and global funds have flowed to small-cap stocks in addition to large-cap stocks. This changing investment pattern has been reflected in equity performance during recent years.

Key highlights:

Small-cap emerging market equities have outperformed their large- and mid-cap peers by significant margins over the past ten years, as of September 30, 2010.

Despite the relatively strong performance of small-cap emerging market equities, it is rare for investors to have dedicated small-cap exposure within emerging markets.

Significant performance differentiation between small-caps and large- and mid-caps within emerging markets and the possibility of greater diversification provide a compelling argument for investors to carve out dedicated allocations for emerging market small-cap.

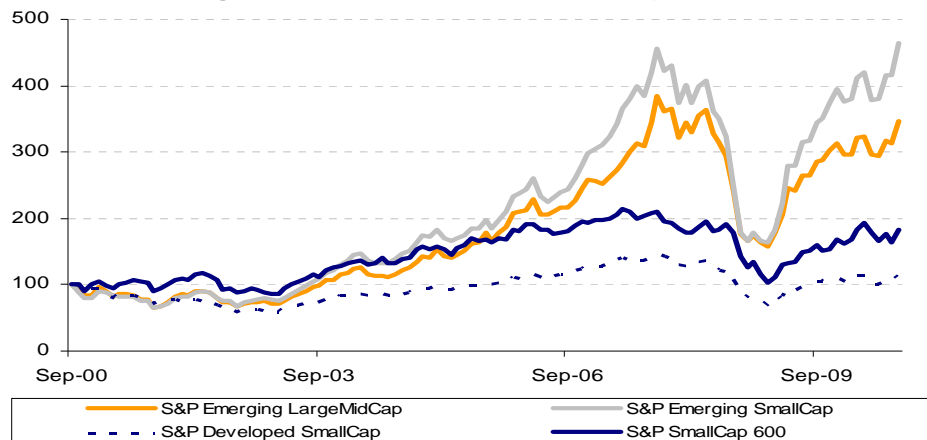
As seen in the U.S. and other developed equity markets, emerging market small-cap stocks have generated significantly larger gains than their large- and mid-cap peers. Furthermore, small-cap outperformance does not appear to be driven by regional, sector, or style biases as the phenomenon generally holds across regional, sector and style indices.

Note: This analysis utilizes data from the S&P Global BMI (Broad Market Index) Series. The index series has approximately 10,000 constituents and consists of the S&P Developed BMI index, which includes 26 developed markets and the S&P Emerging BMI index, which includes 19 emerging markets. The index can be further broken down by size (e.g. S&P Emerging SmallCap), region (e.g. S&P Europe BMI); sector (e.g. S&P Emerging BMI Financials) and style (e.g. S&P Emerging BMI Growth or S&P Emerging BMI Value).

The Emergence of Small-Caps

As illustrated in Figures 1 and 2 on the following page, emerging market small-cap equities have outperformed large- and mid-cap emerging market equities by a wide margin in recent years. In fact, the S&P Emerging SmallCap index posted a 16.6% ten-year compound annual growth rate (CAGR) as of September 30, 2010. This compares to a 13.2% CAGR for the S&P Emerging LargeMidCap index. In addition, the S&P Emerging Small Cap index has beaten the S&P Emerging LargeMidCap index in eight out of the last ten years, as of September 30, 2010.

Figure 1: 10-Year Performance Comparison



Source: Standard & Poor's. Data as of September 30, 2010. Charts and graphs are provided for illustrative purposes only. Index returns do not include payment of any sales charges or fees an investor would pay to purchase the securities the index represents. Such costs would lower performance. It is not possible to invest directly in an index. Past performance is not an indication of future results.

Figure 2: Comparative Annual Total Returns (2001-2010)

Year	S&P Emerging SmallCap (%)	S&P Emerging LargeMidCap (%)	Variance (%)
2010 (YTD as of [9/30/10])	17.2	10.9	6.3
2009	120.6	78.6	42.0
2008	-58.5	-52.0	-6.5
2007	44.9	41.3	3.6
2006	41.6	37.7	3.9
2005	20.4	31.7	-11.2
2004	34.1	23.8	10.3
2003	68.7	57.1	11.6
2002	-3.1	-11.6	8.4
2001	0.5	-2.3	2.8

Source: Standard & Poor's. Year-to-Date data as of September 30, 2010. Charts and graphs are provided for illustrative purposes only. Index returns do not include payment of any sales charges or fees an investor would pay to purchase the securities the index represents. Such costs would lower performance. It is not possible to invest directly in an index. Past performance is not an indication of future results.

However, in the earlier days of emerging markets investing when investors were largely focused on large, blue chip companies, small-cap stocks did not generate such impressive performance in comparison to their large- and mid-cap counterparts. In fact, the S&P Emerging LargeMidCap outperformed the S&P Emerging SmallCap for six consecutive years between 1995 and 2000.

Figure 3: Comparative Annual Total Returns (1995-2000)

Year	S&P Emerging SmallCap (%)	S&P Emerging LargeMidCap (%)	Variance (%)
2000	-38.5	-31.5	-7.0
1999	48.6	77.1	-28.5
1998	-25.2	-22.4	-2.8
1997	-6.9	5.4	-12.3
1996	2.2	4.7	-2.5
1995	-12.2	-5.5	-6.7

Source: Standard & Poor's. Charts and graphs are provided for illustrative purposes only. It is not possible to invest directly in an index. Past performance is not an indication of future results. The S&P Emerging LargeMidCap and the S&P Emerging SmallCap were launched on December 31, 1997 and all data presented prior to that date reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information on indices and the inherent limitations associated with back-tested index performance.

Sector Exposures

As shown in Figure 4 below, there are significant sector variances between large- and mid-cap stocks and small-cap stocks within emerging markets. The S&P Emerging SmallCap index is currently significantly underweight in Energy, Financials, and Telecommunication Services – sectors typically dominated by large multinational companies. Likewise, it is overweight in Consumer Discretionary, Consumer Staples and Industrials.

Figure 4: S&P Emerging LargeMidCap and SmallCap Sector Weights

Sector	9/30/2010		9/30/2005	
	LargeMidCap (%)	SmallCap (%)	LargeMidCap (%)	Small Cap (%)
Consumer Discretionary	5.2	17.6	3.7	14.1
Consumer Staples	6.6	10.8	5.2	7.8
Energy	15.9	2.2	19.3	3.8
Financials	27.1	15.5	21.1	17.9
Health Care	1.0	5.1	2.1	4.1
Industrials	6.2	15.8	5.2	11.9
Information Technology	11.7	12.2	13.2	14.6
Materials	14.2	13.4	14.0	16.2
Telecomm Services	8.5	1.6	12.9	5.7
Utilities	3.5	5.8	3.3	3.8

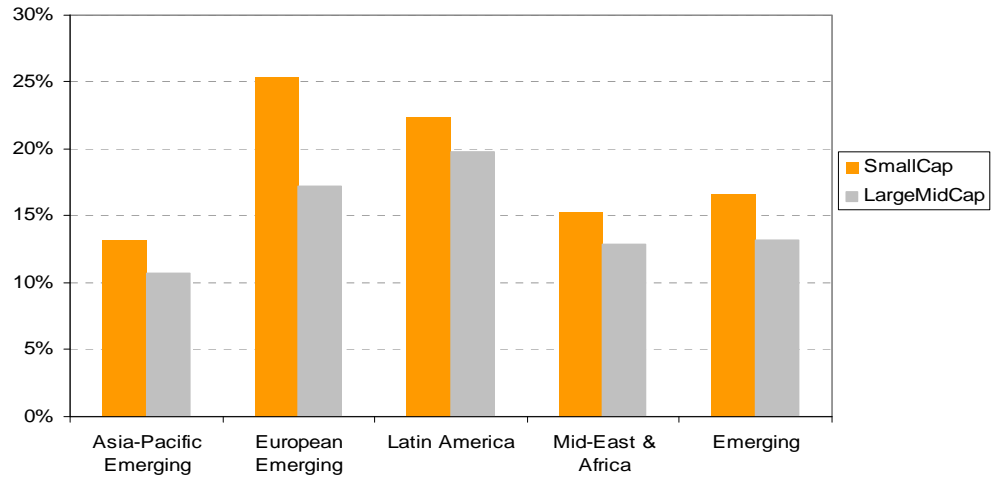
Over the past ten years ending September 30, 2010, small-caps have outperformed their large- and mid-cap peers across all four major regions.

Source: Standard & Poor's. Charts and graphs are provided for illustrative purposes only. It is not possible to invest directly in an index. Past performance is not an indication of future results. The S&P Emerging LargeMidCap Sector and the S&P Emerging SmallCap Sector were launched on September 19, 2005 and all data presented prior to that date reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information on indices and the inherent limitations associated with back-tested index performance.

Small-Cap Outperformance Across Regions

As shown in Figure 5 on the following page, small-cap outperformance has also generally occurred across regions. In fact, over the past ten years ending September 30, 2010, small-caps have outperformed their large- and mid-cap peers across all four major regions. This trend has also been consistent over shorter periods as the S&P Asia-Pacific SmallCap index, S&P European Emerging SmallCap and S&P Latin America SmallCap have outperformed their LargeMidCap counterparts in all instances over the year-to-date, three- and five-year periods as of September 30, 2010. The only period in which the S&P Mid-East & Africa SmallCap lagged its LargeMidCap version was the three-year period ending September 30, 2010.

Figure 5: Annualized 10-Year Regional Performance Comparison



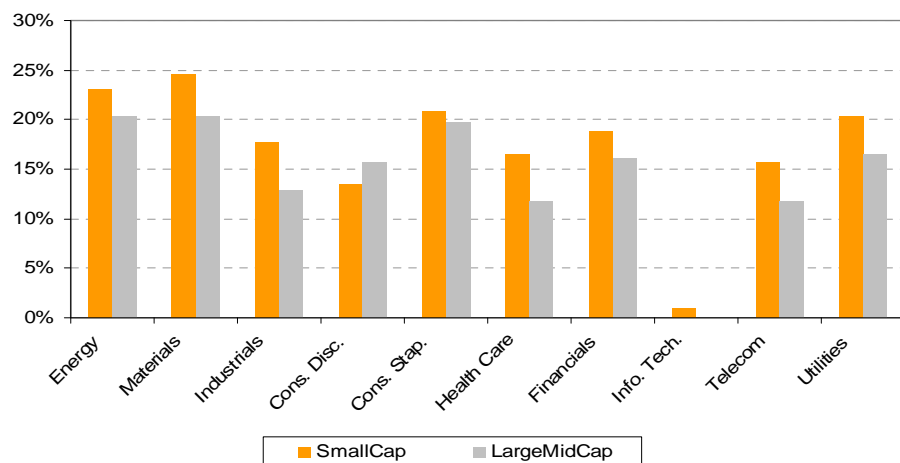
Over the past ten years ending September 30, 2010, nine out of ten sectors within the S&P Emerging SmallCap Sector Indices have outperformed their LargeMidCap counterparts.

Source: Standard & Poor's. Data as of September 30, 2010. Charts and graphs are provided for illustrative purposes only. Index returns do not include payment of any sales charges or fees an investor would pay to purchase the securities the index represents. Such costs would lower performance. It is not possible to invest directly in an index. Past performance is not an indication of future results.

Small-Cap Outperformance Across Sectors

Over the past ten years ending September 30, 2010, nine out of ten sectors within the S&P Emerging SmallCap Sector Indices have outperformed their LargeMidCap counterparts. Once again, this suggests that small-cap outperformance has been broad-based and not driven by sector biases within the small-cap indices. Over shorter time periods, the broad-based dominance of small-cap sector indices is not quite as overwhelming. However, the general trend of small-cap outperformance is also still present in most of the sectors over these periods.

Figure 6: Annualized 10-Year Sector Performance Comparison



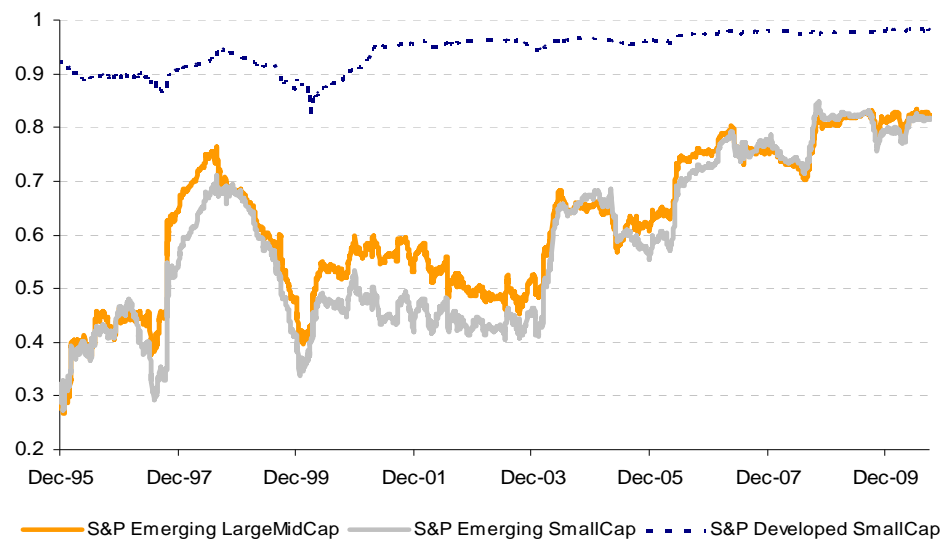
Source: Standard & Poor's. Data as of September 30, 2010. Charts and graphs are provided for illustrative purposes only. It is not possible to invest directly in an index. Past performance is not an indication of future results. The S&P Emerging LargeMidCap Sector and the S&P Emerging SmallCap Sector Indices were launched on September 19, 2005 and all data presented prior to that date reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information on indices and the inherent limitations associated with back-tested index performance.

Emerging Small-Caps as a Source of Portfolio Diversification

Although correlations have increased in recent years, emerging market equities continue to provide a valuable source of diversification for investors. As illustrated in Figure 7 below, correlations between emerging market equities of all sizes and developed market equities remain well below those of small-cap developed market equities. Additionally, over time, small-cap emerging market equities have exhibited lower correlations to the developed markets (albeit modestly) relative to large- and mid-cap emerging market equities. This suggests that investments in emerging market small-caps may generate a greater diversification impact than investments in large- and mid-caps.

Correlations between emerging market equities of all sizes and developed market equities remain well below those of small-cap developed market equities.

Figure 7: Rolling 12-Month Correlation to the S&P Developed BMI



Source: Standard & Poor's. Data as of September 30, 2010. Charts and graphs are provided for illustrative purposes only. It is not possible to invest directly in an index. Past performance is not an indication of future results. The S&P Emerging LargeMidCap and the S&P Emerging SmallCap were launched on December 31, 1997 and all data presented prior to that date reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information on indices and the inherent limitations associated with back-tested index performance.

Conclusion

As capital flows to emerging markets have increased in recent years and many investors have ventured beyond the largest companies, small-cap stocks have outperformed large- and mid-cap stocks by significant margins. Despite this trend, however, many investors do not have dedicated small-cap exposure within their emerging markets portfolios. Significant performance differentiation between small-caps and large- and mid-caps within emerging markets and the possibility of greater diversification provide a compelling argument for investors to carve out dedicated allocations to emerging market small-caps.

In addition, as financial markets continue to deepen in emerging markets, equity performance is likely to further differentiate beyond size ranges. Historically, emerging market economies and equity markets have primarily been driven by

export-oriented growth stemming from sectors such as Energy and Materials. While these sectors will undoubtedly continue to be important drivers of growth in these markets, emerging market economies will likely continue to diversify. As the wealth of local populations increases, sectors such as Consumer Staples, Consumer Discretionary and Health Care may increase in importance as organic demand for these goods and services grows within these markets.

Emerging Markets Investment Tools		
Index Name	ETF Name	ETF Ticker
S&P Emerging BMI <US\$2bn	SPDR S&P Emerging Markets Small Cap ETF	EWX
S&P Emerging BMI	SPDR S&P Emerging Markets ETF	GMM
S&P Developed ex/US US\$2bn - US\$5bn	SPDR S&P International Mid Cap ETF	MDD
S&P Developed ex/US BMI <US\$2bn	SPDR S&P International SmallCap ETF	GWX
S&P Asia-Pacific Emerging BMI	SPDR S&P Emerging Asia Pacific ETF	GMF
S&P Emerging Europe BMI	SPDR S&P Emerging Europe ETF	GUR
S&P Latin America BMI	SPDR S&P Emerging Latin America ETF	GML
S&P Middle East & Africa BMI	SPDR S&P Emerging Middle East & Africa ETF	GAF
S&P BRIC 40	SPDR S&P BRIC 40 ETF	BIK
S&P Latin America 40	iShares S&P Latin America 40	ILF
S&P China BMI	SPDR S&P China ETF	GXC
S&P Russia BMI Capped	SPDR S&P Russia ETF	RBL

Additional Resources

S&P Indices Practice Essentials: www.SPindices.com/4solutions
 S&P Indices Market Attributes®: www.marketattributes.standardandpoors.com
 S&P Indices Thought Leadership Center: www.SPindices.com
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Performance Disclosure

Indices are not collective investment funds and are unmanaged. It is not possible to invest directly in an S&P index. Past performance of an index is not an indication of future results.

The inception date for the S&P Emerging LargeMidCap and the S&P Emerging SmallCap, as well as their corresponding Regional Indices (S&P Emerging LargeMidCap Regional, and S&P Emerging SmallCap Regional) is December 31, 1997 at the market close. The indices were not in existence prior to that date and all data presented prior to that date are back-tested. The back-test calculations are based on the same methodology that was in effect when the indices were officially launched. Complete index methodology details are available at www.indices.standardandpoors.com.

The inception date for the S&P Emerging LargeMidCap Sector and S&P Emerging SmallCap Sector is September 19, 2005 at the market close. The indices were not in existence prior to that date and all data presented prior to that date are back-tested. The back-test calculations are based on the same methodology that was in effect when the indices were officially launched. Complete index methodology details are available at www.indices.standardandpoors.com.

Prospective application of the methodology used to construct the S&P Emerging LargeMidCap, S&P Emerging SmallCap, S&P Emerging LargeMidCap Regional, S&P Emerging SmallCap Regional, S&P Emerging LargeMidCap Sector, and S&P Emerging SmallCap Sector indices may not result in performance commensurate with the back-test returns shown. The back-test period does not necessarily correspond to the entire available history of the indices. Please refer to the methodology paper for these indices, available at www.standardandpoors.com for more details about the indices, including the manner in which it is rebalanced, and the timing of such rebalancing, criteria for additions and deletions and index calculation. The indices are rules based, although the Index Committee reserves the right to exercise discretion, when necessary.

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