

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Portfolio Review and Outlook

The American Fund returned -10.23% for the second quarter, modestly ahead of the benchmark S&P 500 at -11.43% and also the Russell 3000 at -11.32%.

During the quarter:

The Brown Advisory U.S. Equity Growth Fund returned -7.88%;

The Brown Advisory U.S. Equity Value Fund returned -11.93%;

The Brown Advisory U.S. Small-Cap Fund returned -11.25%.

Please see the individual strategy reports for a more detailed review of the second quarter.

Portfolio Review and Outlook: U.S. EQUITY GROWTH STRATEGY

While markets sputtered as concerns about a “double-dip” recession were heightened by both economic issues in Europe and sluggish job recovery in the U.S., the portfolio performed relatively well, declining significantly less than its benchmark.

While we don’t spend a great deal of time on broad equity market strategy (preferring instead to focus on company-specific fundamentals), we offer a few thoughts that are probably at odds with a majority of the broad market commentary like CNBC and the *New York Times*, or the popular press at large:

1. Jobs recovery always lags; the market today feels a lot like ’02-’03 when we were bemoaning the potential for a “jobs-less recovery.” We shall see, but let’s not despair quite yet.
2. The markets are not expensive, even if 2011 estimates ultimately come down.

3. Some note that the “European situation is a disaster which has the capacity to bring us all down.” The equity growth portfolio only has roughly 15% exposure to Europe, so a really weak European economy would not spell the end of the world for our portfolio. Also, it is unclear right now how bad the situation really is. In the latest *Businessweek*, Ajay Banga, the CEO of MasterCard states that “It’s almost like a tale of two Europes, we read about the debt crisis and sovereign debt issues. (But) I don’t see any real impact (on our business) yet.”

With regard to our specific investments, although the end of the quarter was highly volatile in reaction to a spate of economic data, our portfolio was fairly consistent, with few changes made amongst names during the last three months. This has less to do with inactivity on our part and more to do with the high-quality nature of the portfolio as we have found numerous opportunities to buy superior business models at attractive valuations over the past year.

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Portfolio Review and Outlook: U.S. EQUITY VALUE STRATEGY

After a strong stock market recovery and rising expectations, renewed concerns over the financial health of Europe and the daily grind of the Gulf oil tragedy made for an abrupt reversal in both investor attitude and stock prices during the second quarter. Notwithstanding the high quality global nature and low absolute valuation of our portfolio, we posted negative returns for the quarter and were also slightly below the broad benchmarks.

Our key investments in the energy and technology industries were hardest hit. The largest loss was in Transocean, the world's leading rig company. Our investment thesis for Transocean rested on its ability to sustain acceptable returns during the downturn, to better manage capital deployment and to exceed expectations that appeared too pessimistic. The Company performed well until the accident. Our downside risk case had assumed low activity and prices, but we had not assumed a catastrophic loss that continues to linger with an unknown liability. Given the uncertain legal and political costs, we elected to sell our position in favor of other depressed energy investments.

Although government actions are designed to restart the credit cycle via bank support, zero interest rates, and consumer

spending incentives, we believe that they will not, nor should not, be especially successful. What is needed, from our common sense perspective, is time. As such, we believe the reward/risk ratios for many credit-based financials and consumer discretionary stocks remain unattractive.

We remain confident in the fundamentals of the companies in the portfolio. Their leadership position, global orientation, innovative culture, strong financial condition and absolutely low valuations should offer the potential for solid long-term returns with a manageable level of risk. Whereas global economic realities may mean that the future is very different from our postwar experience, we have been especially circumspect about what growth may look like and remain especially vigilant with respect to the risks we are willing to assume.

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Portfolio Review and Outlook: U.S. SMALL-CAP STRATEGY

The state of macroeconomic events continues to be the dominant factor influencing equity portfolios. The result has been a historically high correlation between individual stock movements and the broader market of approximately 80%. In essence, stock picking has presently taken a clear back seat to market timing. However, correlations of this magnitude tend to be relatively short-lived. As long-term investors focused on fundamental security selection, we believe history will prove a reasonable guide to future behavior.

The second quarter of 2010 was disappointing, particularly given the strong start to the year by our strategy in the first quarter. In sum, the portfolio relinquished all of the out-performance it produced early in the year, finishing the most recent period flat with the Russell 2000 Growth benchmark on a year-to-date basis. Mostly random fluctuations in individual holdings and an overweight in energy heading into the Gulf of Mexico oil spill explain the variation in our returns compared to our broader investment universe. Given our two- to three-year investment horizon, a single quarter is not a statistically significant period from which to judge our stock selection. That said, we do realize that the long term is comprised of a series of short-term intervals, so we attempt to do our best to maximize near-term results without compromising our multi-year investment views.

The only stock-specific items worth highlighting in the quarter were the continuation of a heightened level of M&A activity within the portfolio. Two more portfolio holdings, Sybase and Argon ST, were acquired by strategic buyers in 2Q10, equaling the number of “take-outs” in the first quarter. Although the probability of a strategic buyer unlocking value was considered in each of these investments, the primary consideration upon purchase was the quality of the business model, the capability and honesty of management team, and the sustainability of its competitive advantages. In other words, we attempt to buy sound businesses where internal fundamentals will drive value, attracting suitors; we are not attracted to businesses simply because they are rumored to be “take-out” candidates.

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Sector Diversification vs. S&P 500 Index

Sector	Portfolio Q2 '10	Benchmark Q2 '10	Difference	Portfolio Q1 '10	Portfolio Q2 '09
Consumer Discretionary	5.81	9.99	-4.18	8.97	9.00
Consumer Staples	4.75	11.53	-6.78	3.81	5.03
Energy	11.94	10.69	1.25	12.61	9.70
Financials	10.14	16.52	-6.38	10.31	10.61
Health Care	17.47	12.09	5.38	16.16	16.64
Industrials	18.08	10.45	7.63	19.37	16.65
Information Technology	28.46	18.54	9.92	25.71	23.38
Materials	2.97	3.44	-0.47	2.74	4.41
Telecommunication Services	0.30	3.00	-2.70	0.27	0.25
Utilities	0.00	3.76	-3.76	0.00	0.00

N.B.: Figures may appear not to add up due to rounding.

Source: Brown Advisory

Benchmark: S&P 500

Holdings and allocations are subject to change.

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Quarterly Attribution Detail by Sector vs. S&P 500 Index

Sector	Portfolio		S&P 500		Attribution Analysis			
	Average Weight	Total Return	Average Weight	Total Return	Allocation Effect	Selection Effect	Interaction Effect	Total Effect
Consumer Discretionary	7.35	-15.36	10.25	-10.67	0.07	-0.47	0.09	-0.31
Consumer Staples	4.26	-2.35	11.21	-8.13	-0.21	0.62	-0.39	-0.01
Energy	12.37	-18.92	10.93	-12.75	-0.01	-0.70	-0.09	-0.80
Financials	10.12	-10.81	16.61	-13.43	0.13	0.39	-0.18	0.34
Health Care	16.59	-9.41	11.76	-11.78	0.06	0.28	0.08	0.42
Industrials	18.39	-8.17	10.62	-12.27	-0.05	0.46	0.33	0.74
Information Technology	27.32	-9.02	18.78	-12.31	-0.12	0.64	0.31	0.83
Materials	3.18	-5.83	3.48	-14.98	0.00	0.32	-0.02	0.30
Telecommunication Services	0.26	-5.71	2.83	-4.24	-0.19	-0.01	0.00	-0.19
Total	100.00	-10.36	100.00	-11.43	-0.60	1.54	0.12	1.07

Allocation Effect: Measures the impact of the decision to allocate assets differently than those in the benchmark.

Selection Effect: Measures the effect of choosing securities that may or may not outperform those of the benchmark.

Interaction Effect: Measures the effect of allocation and selection decisions, i.e. did we overweight the sectors in which we underperformed.

Portfolio Review: American Fund

Second Quarter 2010



BROWN ADVISORY

Quarterly Contribution to Return

Top Five Contributors

	Name	Avg. Weight	Total Return	Contribution to Return
SRCL	Stericycle Inc.	1.36	20.33	0.25
NTAP	NetApp Inc.	1.18	14.66	0.17
CRM	Salesforce.com Inc.	1.05	15.27	0.14
SY	Sybase Inc.	0.42	38.70	0.13
STST	ARGON ST Inc.	0.33	28.86	0.11

Bottom Five Contributors

	Name	Avg. Weight	Total Return	Contribution to Return
RIG	Transocean Ltd.	0.96	-46.36	-0.57
QCOM	QUALCOMM Inc.	2.34	-21.31	-0.51
CSCO	Cisco Systems Inc.	2.28	-18.13	-0.43
BK	Bank of New York Mellon Corp.	2.07	-19.82	-0.43
CVD	Covance Inc.	2.11	-16.40	-0.33

N.B.: Figures may appear not to add up due to rounding.

Source: Brown Advisory

Holdings and allocations are subject to change.