Quality Mix: More Than the Sum of Its Parts

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MSCI

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State Street Global Advisors
What is Factor Investing?

- Simply said, a “factor” is a characteristic that is important in explaining risk and return.
- Factor investing is the investment process that aims to capture such risk and return.
- Extensive financial research has shown that six key factors have historically earned a persistent premium over long periods of time relative to cap-weighted indexes.
- Factor Indexes may provide investors with a transparent, rules based, flexible and cost-effective approach to passively seek systematic exposure to factors.
- Factor Indexes are complementary to Market Cap Indexes and play key roles in asset allocation.
Multi Factor Indexes

- **Address the cyclicality of single factor returns across business cycles**
  - Single factors cyclicality can lead to periods of underperformance

- **Multi factor indexes have historically led to:**
  - Lower volatility and higher Sharpe Ratios
  - Higher information ratios and lower tracking errors
  - Less regime dependency over business cycles

- **Allocations to multi factor strategies are increasing**
  - Ability to express views on more than one factor
  - Diversification and potential for improved risk-adjusted returns
  - Clear attribution
  - Implementation flexibility
  - Internal crossing at rebalance
MSCI Quality Mix Indexes

- Equal weighted combination of the MSCI Value Weighted, Minimum Volatility and Quality Indexes

**MSCI Quality MIX**

**MSCI Value Weighted Index**
- Re weights parent index according to four fundamental variables: Sales, Earnings, Cash Flow, Book Value
- Semi-annual rebalancing

**MSCI Quality Index**
- Identifies quality growth stocks within parent index by calculating a quality score based on: high return on equity, stable earnings growth and low leverage
- Semi-annual rebalancing

**MSCI Minimum Volatility Index**
- Identifies stocks from the parent index with the potential to provide lowest total risk and superior risk-adjusted performance
- Constructed using minimum variance optimization
- Semi-annual rebalancing

Source: MSCI
Quality, Value and Volatility Have Different Performance Cycles

MSCI World Quality, MSCI Minimum Volatility (USD) and MSCI Value Weighted Relative Performance

During the long bull-run, Value Weighted outperformed, Minimum Volatility tracked the benchmark and Quality lagged.

Both Minimum Volatility and Quality outperformed during the recent crisis, Value Weighted performed cyclically.

Performance through April 2014
Factor Cyclicality

Individual factor performance is cyclical and can underperform for long periods

Combining the three factors may dampen the effect of business cycles due to their correlations

<table>
<thead>
<tr>
<th></th>
<th>MSCI World Quality Mix</th>
<th>MSCI World Quality</th>
<th>MSCI World Value Weighted</th>
<th>MSCI World Minimum Volatility</th>
</tr>
</thead>
<tbody>
<tr>
<td>MSCI World Quality Mix</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI World Quality</td>
<td>0.65</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI World Value Weighted</td>
<td>0.40</td>
<td>-0.02</td>
<td>1.00</td>
<td></td>
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<tr>
<td>MSCI World Minimum Volatility</td>
<td>0.80</td>
<td>0.24</td>
<td>0.13</td>
<td>1.00</td>
</tr>
</tbody>
</table>

Correlations of Excess Monthly Returns from June 1988 to March 2014. Source: FactSet

Pre-Inception Index Performance shown above is back-tested. Market indices are unmanaged and are not subject to fees and expenses which could lower returns. Index performance is not intended to represent the performance of any particular exchange-traded fund or product managed by SSgA Funds Management, Inc. Actual performance may differ substantially from the back-tested performance presented, as the performance was calculated with the benefit of hindsight, and is not a guarantee of future results. SSgA compensated MSCI for the calculations noted herein. Investment Professional Use Only. Not for Public Distribution. State Street Global Advisors (SSgA) and MSCI are not affiliated.
Relative Performance of the MSCI Quality Mix Indexes

- MSCI World Quality Mix Index has historically outperformed MSCI World
- Combining the 3 Factor Indexes diversifies returns during periods of volatility

Simulated history from May 1988 to February 2014.
MSCI Quality Mix Key Potential Benefits — Risk versus Return

Quality Mix presents an attractive risk versus return profile relative to individual factors.

**MSCI World Factor Performance Characteristics**

- **Annualized Return (%)**
- **MSCI World Quality Mix**
- **MSCI World Quality**
- **MSCI World Value Weighted**
- **MSCI World Minimum Volatility**
- **MSCI The World Index**

Source: MSCI, FactSet

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MSCI Quality Mix Key Potential Benefits — Diversification in Volatile Markets

These historical benefits have been particularly important during volatile market conditions.

Based on MSCI Quality Mix Index data, approx. 90% of the returns in up markets are captured while only enduring 80% of the returns in down markets, leading to drawdown benefits.

MSCI World Quality Mix versus MSCI World Index Drawdown Comparison

<table>
<thead>
<tr>
<th>Index</th>
<th>Upside capture</th>
<th>Downside capture</th>
</tr>
</thead>
<tbody>
<tr>
<td>World Quality Mix versus World</td>
<td>88.73%</td>
<td>80.17%</td>
</tr>
<tr>
<td>EAFE Quality Mix versus EAFE</td>
<td>92.55</td>
<td>80.87</td>
</tr>
<tr>
<td>EM Quality Mix versus EM</td>
<td>95.82</td>
<td>85.41</td>
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</table>

Period: 11/30/2001 to 03/31/2014

Source: MSCI, FactSet
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### MSCI World Historical Performance from 1998 to 2014

<table>
<thead>
<tr>
<th></th>
<th>MSCI World</th>
<th>MSCI World Quality Mix</th>
<th>MSCI World Value Weighted</th>
<th>MSCI World Quality</th>
<th>MSCI World Minimum Volatility (USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Return</strong> (%)</td>
<td>4.9</td>
<td>6.4</td>
<td>6.3</td>
<td>5.9</td>
<td>6.4</td>
</tr>
<tr>
<td><strong>Total Risk</strong> (%)</td>
<td>16.0</td>
<td>13.5</td>
<td>16.9</td>
<td>14.1</td>
<td>11.2</td>
</tr>
<tr>
<td><strong>Return/Risk</strong></td>
<td>0.31</td>
<td>0.47</td>
<td>0.37</td>
<td>0.42</td>
<td>0.57</td>
</tr>
<tr>
<td><strong>Sharpe Ratio</strong></td>
<td>0.22</td>
<td>0.34</td>
<td>0.30</td>
<td>0.30</td>
<td>0.39</td>
</tr>
<tr>
<td><strong>Active Return</strong> (%)</td>
<td>0.0</td>
<td>1.5</td>
<td>1.4</td>
<td>1.0</td>
<td>1.5</td>
</tr>
<tr>
<td><strong>Tracking Error</strong> (%)</td>
<td>0.0</td>
<td>3.4</td>
<td>3.5</td>
<td>4.4</td>
<td>7.7</td>
</tr>
<tr>
<td><strong>Information Ratio</strong></td>
<td></td>
<td></td>
<td>0.43</td>
<td>0.39</td>
<td>0.24</td>
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<tr>
<td><strong>Historical Beta</strong></td>
<td>1.00</td>
<td>0.84</td>
<td>1.03</td>
<td>0.85</td>
<td>0.63</td>
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<tr>
<td><strong>Turnover</strong> (%)</td>
<td>3.0</td>
<td>21.0</td>
<td>18.1</td>
<td>22.7</td>
<td>26.8</td>
</tr>
<tr>
<td><strong>Price to Book</strong> ***</td>
<td>2.2</td>
<td>2.5</td>
<td>1.7</td>
<td>4.5</td>
<td>2.5</td>
</tr>
<tr>
<td><strong>Price to Earnings</strong> ***</td>
<td>18.6</td>
<td>18.1</td>
<td>18.0</td>
<td>16.8</td>
<td>18.7</td>
</tr>
<tr>
<td><strong>Div. Yield</strong> *** (%)</td>
<td>2.3</td>
<td>2.4</td>
<td>2.6</td>
<td>2.1</td>
<td>2.6</td>
</tr>
</tbody>
</table>

* Gross returns annualized in USD for the 12/31/1998 to 04/30/2014 period

** Annualized one-way index turnover for the 12/31/1998 to 04/30/2014 period

*** Monthly averages for the 12/31/1998 to 04/30/2014 period

The definitions of all statistical parameters are available in the Appendix.
Potential Cost Effectiveness of Multi-Factor Indexes

- Combining factor indexes into a single composite may reduce turnover
  - Exploiting natural internal “crossing” opportunities at each rebalancing
  - May reduce the need to reallocate capital across managers
- An allocation to portfolios tracking two or more factor indexes can be implemented in two ways
  1. Separate investments: three different asset managers, three separate indexes
  2. Combined investment: one portfolio tracking a combined index

<table>
<thead>
<tr>
<th></th>
<th>MSCI World</th>
<th>MSCI Quality</th>
<th>MSCI Minimum Volatility</th>
<th>MSCI Value Weighted</th>
<th>Separate Investments</th>
<th>Combined Investment</th>
<th>Reduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover (%)</td>
<td>3.00</td>
<td>22.71</td>
<td>26.82</td>
<td>18.09</td>
<td>24.78</td>
<td>20.68</td>
<td>4.10</td>
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<tr>
<td>Performance Drag in bps (at 50 bps)*</td>
<td>0.03</td>
<td>0.23</td>
<td>0.27</td>
<td>0.18</td>
<td>0.25</td>
<td>0.21</td>
<td>0.04</td>
</tr>
</tbody>
</table>

Annualized from Dec 1998 to Feb 2014

*Performance drag aims to represent the total two-way annualized index level transaction cost assuming various levels of security level transaction cost.
MSCI Quality Mix Indexes: 3 Key Benefits

1. Emphasize **quality, value** and **low volatility** stocks, which have historically outperformed the market over time

2. Typically provide **reduced concentration in individual names** compared to market cap weighted indexes

3. Offer the benefits of **broad market exposure** with diversification across different business cycles
MSCI Quality Mix Indexes: Additional Benefits

- **Quality Mix Indexes offer efficiencies vs. traditional market cap weighted benchmarks**
  - Investors may experience **less tracking error risk** while also benefiting from Factor premiums
  - Multi-Factor Indexes may offer **lower turnover** than combining indexes from various providers
    - Consistent universes
    - Synchronized rebalancing schedules
  - **Seamless integration** with other MSCI Indexes
    - Quality Mix Indexes are based on parent MSCI Indexes, used by a large number of advisors and institutions
SPDR MSCI Quality Mix Products

**SPDR Regional Quality Mix ETFs (Gross Expense Ratio = 0.30%)**

- SPDR MSCI World Quality Mix ETF (QWLD)
- SPDR MSCI EAFE Quality Mix ETF (QEFA)
- SPDR MSCI Emerging Markets Quality Mix ETF (QEMM)
- SPDR MSCI Australia Quality Mix ETF (QAUS)
- SPDR MSCI Canada Quality Mix ETF (QCAN)
- SPDR MSCI Germany Quality Mix ETF (QDEU)
- SPDR MSCI Japan Quality Mix ETF (QJPN)
- SPDR MSCI Spain Quality Mix ETF (QESP)
- SPDR MSCI United Kingdom Quality Mix ETF (QGBR)

The gross expense ratio is the funds total annual operating expenses ratio. It is gross of any fee waivers or expense reimbursements. It can be found in the funds most recent prospectus.
How to use SPDR MSCI Quality Mix ETFs

The asset allocation decision of a SPDR MSCI Quality Mix ETF to a market cap weighted benchmark can be viewed as either:

A supplementary — replace existing cap weighted exposure with an SPDR MSCI Quality Mix ETF

Or complementary — augment existing regional exposure with a small allocation to a SPDR MSCI Quality Mix ETF

The allocation decision depends on:
  – Investors Factor Conviction
  – Time Horizon
  – Market Exposure Style
  – Risk Tolerance
  – Return Expectations
How to use Single Country SPDR MSCI Quality Mix ETFs

Single Country Quality Mix Model Portfolio

Complimentary Approach

MSCI ACWI IMI Strategic Quality Mix Country

This portfolio is an example of how an investor could potentially use the single country Quality Mix ETFs as a strategic or tactical holding.

As an example: to implement a strategic view similar to a country rotation, an investor could weight the single country Quality Mix ETFs by the average country GDP forecast to compliment a core MSCI ACWI IMI holding.

The average GDP can then be re-weighted by the country index weight in the MSCI ACWI IMI parent index to reduce country exposure differences.

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Country</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>Average Forecast</th>
<th>Country Weight in MSCI ACWI IMI</th>
<th>Average Weighted GDP</th>
<th>Weight</th>
<th>Portfolio Weight</th>
</tr>
</thead>
<tbody>
<tr>
<td>QJPN</td>
<td>Japan</td>
<td>1.3</td>
<td>1.3</td>
<td>1.1</td>
<td>1.23</td>
<td>7.42%</td>
<td>0.09</td>
<td>17%</td>
<td>3.35%</td>
</tr>
<tr>
<td>QGBR</td>
<td>United Kingdom</td>
<td>2.8</td>
<td>2.4</td>
<td>2.4</td>
<td>2.53</td>
<td>7.76</td>
<td>0.20</td>
<td>36</td>
<td>7.21</td>
</tr>
<tr>
<td>QCAN</td>
<td>Canada</td>
<td>2.3</td>
<td>2.5</td>
<td>2.8</td>
<td>2.53</td>
<td>3.74</td>
<td>0.09</td>
<td>17</td>
<td>3.47</td>
</tr>
<tr>
<td>QAUS</td>
<td>Australia</td>
<td>2.8</td>
<td>2.9</td>
<td>3.4</td>
<td>3.03</td>
<td>2.80</td>
<td>0.08</td>
<td>16</td>
<td>3.12</td>
</tr>
<tr>
<td>QDEU</td>
<td>Germany</td>
<td>1.9</td>
<td>2.0</td>
<td>1.7</td>
<td>1.87</td>
<td>3.29</td>
<td>0.06</td>
<td>11</td>
<td>2.25</td>
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<tr>
<td>QESP</td>
<td>Spain</td>
<td>0.9</td>
<td>1.5</td>
<td>1.55</td>
<td>1.32</td>
<td>1.24</td>
<td>0.02</td>
<td>3</td>
<td>0.60</td>
</tr>
</tbody>
</table>

Source: IMF, SSgA, MSCI, Bloomberg L.P., as of March 31, 2014.
Past performance is not a guarantee of future results.
Model Allocations and Weights are as of the date indicated, are subject to change, and should not be relied upon as current thereafter.
The model portfolio shown was created by SPDR ETF Sales Strategy Group. Methodology is Weighted Average. The model portfolio performance does not reflect actual trading and does not reflect the impact that material economic and market factors may have had on SSgA's decision-making. The results shown were achieved by means of a mathematical formula. Please see the Appendix for additional disclosure. The calculation method for value added returns may show rounding differences.
# Index Characteristics

## MSCI World Quality Mix Index — Sector and Country

<table>
<thead>
<tr>
<th>MSCI World Quality Mix Index</th>
<th>MSCI World Index</th>
<th>SECTOR %</th>
<th>SECTOR %</th>
<th>O/U</th>
</tr>
</thead>
<tbody>
<tr>
<td>Energy</td>
<td>Energy</td>
<td>8.64</td>
<td>9.53</td>
<td>-0.88%</td>
</tr>
<tr>
<td>Materials</td>
<td>Materials</td>
<td>4.14</td>
<td>5.74</td>
<td>-1.61</td>
</tr>
<tr>
<td>Industrials</td>
<td>Industrials</td>
<td>9.91</td>
<td>11.33</td>
<td>-1.42</td>
</tr>
<tr>
<td>Consumer Discretionary</td>
<td>Consumer Discretionary</td>
<td>12.94</td>
<td>11.94</td>
<td>1.00</td>
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<tr>
<td>Consumer Staples</td>
<td>Consumer Staples</td>
<td>12.78</td>
<td>9.82</td>
<td>2.96</td>
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<td>Health Care</td>
<td>Health Care</td>
<td>14.10</td>
<td>11.68</td>
<td>2.42</td>
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<td>Financials</td>
<td>Financials</td>
<td>14.92</td>
<td>20.92</td>
<td>-6.00</td>
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<tr>
<td>Information Technology</td>
<td>Information Technology</td>
<td>13.65</td>
<td>12.24</td>
<td>1.41</td>
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<td>Telecommunication Services</td>
<td>Telecommunication Services</td>
<td>4.55</td>
<td>3.54</td>
<td>1.01</td>
</tr>
<tr>
<td>Utilities</td>
<td>Utilities</td>
<td>4.37</td>
<td>3.27</td>
<td>1.11</td>
</tr>
</tbody>
</table>

As of March 31, 2014, MSCI

<table>
<thead>
<tr>
<th>MSCI World Quality Mix Index</th>
<th>MSCI World Index</th>
<th>COUNTRY %</th>
<th>COUNTRY %</th>
<th>O/U</th>
</tr>
</thead>
<tbody>
<tr>
<td>AUSTRALIA</td>
<td>AUSTRALIA</td>
<td>1.60</td>
<td>3.23</td>
<td>-1.63%</td>
</tr>
<tr>
<td>AUSTRIA</td>
<td>AUSTRIA</td>
<td>0.08</td>
<td>0.12</td>
<td>-0.04</td>
</tr>
<tr>
<td>BELGIUM</td>
<td>BELGIUM</td>
<td>0.22</td>
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<td>-0.28</td>
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<td>CANADA</td>
<td>CANADA</td>
<td>4.91</td>
<td>4.14</td>
<td>0.78</td>
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<td>DENMARK</td>
<td>DENMARK</td>
<td>0.82</td>
<td>0.56</td>
<td>0.26</td>
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<td>FINLAND</td>
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<td>-0.11</td>
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<td>FRANCE</td>
<td>FRANCE</td>
<td>2.17</td>
<td>4.26</td>
<td>-2.09</td>
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<td>GERMANY</td>
<td>2.18</td>
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<td>ITALY</td>
<td>0.76</td>
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<td>JAPAN</td>
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<td>NEW ZEALAND</td>
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<td>0.05</td>
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<td>NORWAY</td>
<td>0.20</td>
<td>0.34</td>
<td>-0.14</td>
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<td>PORTUGAL</td>
<td>PORTUGAL</td>
<td>0.06</td>
<td>0.08</td>
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<td>SINGAPORE</td>
<td>SINGAPORE</td>
<td>1.04</td>
<td>0.60</td>
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<td>SPAIN</td>
<td>SPAIN</td>
<td>0.90</td>
<td>1.46</td>
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<td>SWEDEN</td>
<td>0.84</td>
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<td>SWITZERLAND</td>
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<td>3.82</td>
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<tr>
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<td>UNITED KINGDOM</td>
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<td>8.66</td>
<td>-0.43</td>
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<td>UNITED STATES</td>
<td>59.33</td>
<td>54.77</td>
<td>4.56</td>
</tr>
</tbody>
</table>

As of March 31, 2014, MSCI

Source: MSCI

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Appendix: Important Disclosures
Important Disclosures

FOR INVESTMENT PROFESSIONAL USE ONLY. Not for use with the public.

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ETFs trade like stocks, are subject to investment risk and will fluctuate in market value. The investment return and principal value of an investment will fluctuate in value, so that when shares are sold or redeemed, they may be worth more or less than when they were purchased. Although shares may be bought or sold on an exchange through any brokerage account, shares are not individually redeemable from the fund. Investors may acquire shares and tender them for redemption through the fund in large aggregations known as creation units. Please see the fund’s prospectus for more details.

The Fund invests by sampling the index, holding a range of securities that, in the aggregate, approximates the full Index in terms of key risk factors and other characteristics. This may cause the fund to experience tracking errors relative to performance of the index.

Non-diversified funds that focus on a relatively small number of securities tend to be more volatile than diversified funds and the market as a whole.

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