INVESTMENT
MANAGEMENT

Schwab Fundamental Index* Mutual Funds and ETFs

Schwab Fundamental Index mutual funds and ETFs provide investors with access to an innovative indexing approach that offers a complement to traditional cap-weighted indexing and active management, helping to create the potential for more attractive risk-adjusted portfolios.

An Innovative Approach to Index Investing

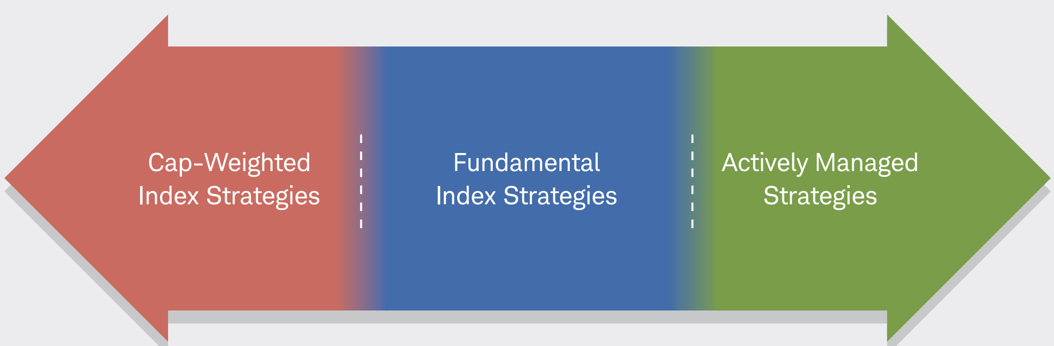
Following more than 50 years of finance theory and indexing convention, the vast majority of stock indexes determine a company's weight based on the market value of its stock—its "market capitalization." Cap-weighted indexes rely on market sentiment that can drive stock valuations to excessive levels in either direction, leading indexes to overweight stocks that the market has overvalued and underweight those it has undervalued, resulting in portfolios that can be vulnerable to pricing bubbles and subsequent corrections.

Fundamental Index® strategies attempt to address these aspects of traditional cap-weighted indexes while offering greater diversification of core equities along with the opportunity for attractive risk-adjusted returns over longer periods of time. Instead of selecting and weighting companies based on their market capitalization, Fundamental Index strategies weight companies based on **objective** financial measures of company size, essentially breaking the link with stock price. This methodology employs a disciplined approach that counters the constantly shifting sentiments of the broader market while preserving the chief benefits of traditional cap-weighting: capacity, liquidity, diversification and broad market participation. During periods of strong market performance, however, Fundamental Index strategies may lag their cap-weighted counterparts.

As a pioneer in Fundamental Index strategies, Charles Schwab Investment Management, Inc. (CSIM) created a partnership with Fundamental Index creator Research Affiliates, LLC (RAFI) and was the first to launch index mutual funds following a RAFI methodology in 2007. CSIM subsequently launched a series of Exchange Traded Funds (ETFs) in 2013. Both the Schwab Fundamental Index Funds and ETFs passively track certain indexes within the Russell RAFI Index® Series, which is based on Research Affiliate's methodology.

A complement to traditional indexing and active management

Fundamental Index strategies fall along a continuum spanning index and active strategies by focusing on fundamental measures similar to many active stock-picking strategies.



Three Industry Leaders; One Strategic Alliance

Research Affiliates, LLC
Developing the methodology

Research Affiliates LLC is the pioneer of the Fundamental Index methodology. Founded by Rob Arnott in 2002, Research Affiliates is a leader in asset allocation and indexing strategies, with approximately $169 billion in assets managed using its investment strategies ($130 billion of which are in Fundamental Index–based strategies).[1]

Frank Russell Company
Creating the indexes

With more than four decades of experience, Frank Russell Company is a premier institutional index provider whose indexes are used to benchmark more than $6.7 trillion in investor assets.[2] Russell indexes combine the firm's rigorous index construction methodology with best-of-class thinking to serve as a trusted source of index intelligence.

Charles Schwab Investment Management
Providing access via mutual funds and ETFs

With $316 billion in assets under management,[3] Charles Schwab Investment Management (CSIM), a subsidiary of The Charles Schwab Corporation, is one of the nation's largest asset management companies and the third-largest provider of retail index funds. Since 1991, CSIM has delivered passive, core strategies to investors, providing convenient, low-investment-minimum access across key categories of cap-weighted and alternative index strategies through both mutual funds and ETFs.

What's Behind the Fundamental Index Methodology?

Cap-weighted indexes that select and weight their constituents according to market-determined prices are inherently momentum-driven, assigning the largest weights to companies whose stocks the market has rewarded. By overweighting overvalued stocks and underweighting undervalued ones, traditional cap-weighted indexes tend to favor companies trading at high multiples and exclude those trading at distressed, deep-discount prices.

In seeking to avoid such biases, Rob Arnott and his company, Research Affiliates, created a transparent approach to investing that seeks to break the link between price and portfolio weight, focusing instead on financial measures that objectively anchor a stock's weighting in a broad-based index. Constituents in RAFI strategies are selected and weighted according to fundamental metrics of company size, such as adjusted sales, retained operating cash flow and dividends plus buybacks to determine index weights. These weights, which can often differ significantly from a company's market capitalization, tend to be relatively stable over time.

Additionally, the RAFI strategies rebalance periodically to reset the preceding period's price drift, trimming exposure to stocks that have performed best and adding to positions that have lagged, and bringing sector, country and individual companies back to their objectively derived anchor weights. This periodic rebalancing exercise enables the RAFI strategies to take advantage of the theory of "mean reversion"—a theory that has been observed in the returns of investment securities since the beginning of markets—that prices eventually return to their mean, or average. In the context of the RAFI strategies, prices would move away from inflated or deflated market expectations and toward their inherent value based on objective, quantifiable metrics, minimizing the impact of ever-shifting market forces. Fundamental Index strategies offer many of the advantages of index investing, while helping to create the potential opportunity, over time, for more attractive risk-adjusted returns when paired with traditional cap-weighted index and actively managed strategies.

Two Views on Markets

Traditional cap-weighted indexes are based on the premise that markets are efficient and that stock prices reflect all relevant information and, thus, that stocks are fairly priced. Fundamental Index strategies have roots in the Graham & Dodd[4] economy-centric premise that prices are fluid, so overpricing and underpricing are possible.

	Market-centric (cap-weighted)	Economy-centric (Graham & Dodd[4])
Premise	▪ Markets are efficient; prices reflect true valuations ▪ Departures from cap-weights are active bets; inherently a zero-sum game	▪ Markets are constantly seeking fair value, but prices are rarely right ▪ Some companies can get over-priced; some underpriced ▪ The market itself makes active bets
Beliefs	▪ It's difficult to beat a cap-weighted index	▪ Cap-weighted indexes overweight overpriced stocks and underweight underpriced ones; the result is a return drag relative to its opportunity set
Tactics	▪ Invest in companies proportional to market valuation ▪ Seek equity-risk premium[5], not alpha[6]	▪ Create valuation models of companies and invest in those that offer the best rate of return

The Russell RAFI Index Series

In constructing the Russell RAFI Index Series, Frank Russell Company starts by developing a list of potential securities from a large, global investment universe. Research Affiliates then scores those companies by three fundamental measures: adjusted sales, retained operating cash flow, and dividends plus buybacks. The metrics are widely accepted and consistently derived; they are not intended to be predictive of future size or value; and are uncorrelated with stock prices. The data is easily accessible and broadly available across countries. Research Affiliates then equally weights the three factors to produce an aggregate score for each company. From this data, Russell creates multiple Fundamental sub-indexes along such dimensions as geography, size and state of market development. The Russell RAFI Indexes are recalculated annually. The subsequent changes to the indexes are then implemented on a quarterly basis.

Russell RAFI Index Ranking Factors

	Adjusted Sales		Retained Cash Flow		Dividends & Buybacks		
	Weight	Rank	Weight	Rank	Weight	Rank	Fundamental Weight
Company A	5.4%	1	2.6%	2	7.2%	1	5.1%
Company B	3.5%	2	2.1%	4	1.9%	7	2.5%
Company C	1.9%	3	1.7%	9	1.8%	8	1.8%
Company D	0.9%	16	0.5%	35	3.6%	2	1.7%
Company E	0.3%	70	2.9%	1	1.7%	9	1.6%

Source: Research Affiliates LLC. Actual company names have been concealed.

Implementing the Strategy

Schwab Fundamental Index mutual funds and ETFs are designed to serve either as standalone core investments within a portfolio or as complements to existing equity index holdings and/or active strategies. They are transparent, offer broad diversification and have competitive expenses.

Since cap-weighted indexes are the broadly accepted measure of the overall market, the addition of incremental holdings of Schwab Fundamental Index mutual funds and ETFs may help improve portfolio diversification.

Why Schwab Fundamental Index Mutual Funds and ETFs

- When used in **combination** with traditional cap-weighted index and actively managed strategies, Fundamental Index offers the potential for more attractive risk-adjusted returns over time
- Uses **multiple fundamental measures** of company size which may provide greater investment opportunity than single-metric methodologies, such as those that focus only on dividends or earnings
- Broad offering of 12 ETFs and mutual funds across **various asset classes**
- Preserves the **benefits of index investing**: lower expenses, lower turnover, full market participation, broad diversification across sectors and a high level of investment capacity as compared to many actively managed products

The Lineup

Schwab Fundamental Index ETFs	Ticker	Expense Ratio
Schwab Fundamental U.S. Broad Market Index ETF	FNDB	0.25%
Schwab Fundamental U.S. Large Company Index ETF	FNDX	0.25%
Schwab Fundamental U.S. Small Company Index ETF	FNDA	0.25%
Schwab Fundamental International Large Company Index ETF	FNDF	0.25%
Schwab Fundamental International Small Company Index ETF	FNDC	0.39%
Schwab Fundamental Emerging Markets Large Company Index ETF	FNDE	0.40%[7]
Schwab Fundamental Index Mutual Funds	**Ticker**	**Expense Ratio**
Schwab Fundamental US Large Company Index Fund	SFLNX	0.25%
Schwab Fundamental US Small Company Index Fund	SFSNX	0.25%
Schwab Fundamental International Large Company Index Fund	SFNNX	0.25%
Schwab Fundamental International Small Company Index Fund	SFILX	0.39%
Schwab Fundamental Emerging Markets Large Company Index Fund	SFENX	0.39%
Schwab Fundamental Global Real Estate Index Fund	SFREX	0.49%[8]

For more information

Visit: www.csimfunds.com

Call: 1-877-824-5615

* Schwab is a registered trademark of Charles Schwab & Co., Inc. Fundamental Index is a registered trademark of Research Affiliates LLC.

1 As of 12/31/2016; based on estimates. Includes asset managed or subadvised by Research Affiliates or licenses using RAFI, Enhanced RAFI® or GTAA strategies.

2 Data as of 12/31/2015. Source: Russell Research, U.S. Equity Indexes: Institutional Benchmark Survey.

3 As of 03/31/2017, CSIM Monthly Performance and Fund Net Assets Report. As of March 31, 2017, CSIM managed approximately $302.5B on a discretionary basis and approximately $13.6B on a non-discretionary basis.

4 In their 1934 book, *Security Analysis*, Benjamin Graham and David Dodd laid the intellectual foundation for what became known as "value investing," criticizing investment analysts for their myopic focus on earnings and identifying alternate metrics for valuing stocks.

5 The excess return that an individual stock or the overall stock market provides over a risk-free rate. This excess return compensates investors for taking on the relatively higher risk of the equity market.

6 The abnormal rate of return on a security or portfolio in excess of what would be predicted by an equilibrium model.

7 Includes 0.01% of acquired fund fees and expenses (AFFE), which reflect the fees and expenses incurred indirectly by the fund through its investments in other investment companies during its prior fiscal year.

8 The investment adviser and its affiliates have agreed to limit the total annual fund operating expenses (excluding interest, taxes and certain non-routine expenses) of the fund for so long as the investment adviser serves as the adviser to the fund. This agreement may only be amended or terminated with the approval of the fund's Board of Trustees. This agreement is limited to the fund's direct operating expenses and does not apply to acquired fund fees and expenses.

Please note that ETFs and mutual funds are separate and distinct products.

Investors should consider carefully information contained in the prospectus, or if available, the summary prospectus, including investment objectives, risks, charges and expenses. You can request a prospectus at www.csimfunds.com or by calling 1-877-824-5615. Please read the prospectus carefully before investing.

There can be no assurance that the Fundamental Index methodologies will achieve their desired outcomes. Each investing strategy brings with it its own set of unique risks and benefits. Past performance does not guarantee future results.

Frank Russell Company (Russell) and Research Affiliates LLC (RA) have entered into a strategic alliance with respect to the Russell RAFI Index Series. Subject to RA's intellectual property rights in certain content, Russell is the owner of all copyrights related to the Russell RAFI Index Series. Russell and RA jointly own all trademark and service mark rights in and to the Russell RAFI Index Series. Schwab is not affiliated with Russell or RA. Schwab Fundamental Index Funds are not sponsored, endorsed, sold or promoted by Russell or RA, and Russell and RA do not make any representation regarding the advisability of investing in shares of the funds. Russell and RA are not responsible for and have not reviewed the Schwab Fundamental Index Funds nor any associated literature or publications, and Russell and RA make no representation or warranties, express or implied, as to their accuracy, or completeness, or otherwise. RA is the owner of certain intellectual property (see all applicable rights disclosures and notices at http://www.researchaffiliates.com/Pages/legal.aspx#d, which are fully incorporated herein.) Effective December 1, 2016, the name of the index series and all associated index names were changed by the index provider. No other changes to the series or the indices have occurred.

Investment returns will fluctuate and are subject to market volatility, so that an investor's shares, when redeemed or sold, may be worth more or less than their original cost. Unlike mutual funds, shares of ETFs are not individually redeemable directly with the ETF. Shares are bought and sold at market price, which may be higher or lower than the net asset value (NAV).

Diversification does not eliminate the risks of investment losses.

Charles Schwab Investment Management, Inc. (CSIM) is the investment advisor for Schwab Funds and Schwab ETFs. Schwab Funds are distributed by Charles Schwab & Co., Inc. (Schwab), Member SIPC. Schwab ETFs are distributed by SEI Investments Distribution Co. (SIDCO). CSIM and Schwab, are separate but affiliated companies and subsidiaries of The Charles Schwab Corporation, and are not affiliated with SIDCO.

00194445