

Fund Commentary

Forward International Small Companies Fund Market Review First Quarter 2007

Average annual returns (in %) as of 3/31/07

	1YR	3YR	5YR	10YR	Since Inc.*
<i>Forward International Small Co. Fund</i> – Institutional	21.55	26.75	25.09	16.15	14.44
HSBC World ex-U.S. Smaller Companies Index	24.05	27.76	27.40	11.44	10.87
MCSI EAFE Small Cap Index	15.91	23.74	24.76	9.86	8.23

*2/7/1996

	Gross Exp.	Net/Actual Exp.
<i>Forward International Small Co. Fund</i> – Institutional	1.46%	1.26%

The performance quoted represents past performance, does not guarantee future results and current performance may be lower or higher than the data quoted. The investment return and principal value of an investment will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Performance quoted does not reflect the non-recurring redemption fee of 2% that may be charged if shares are sold or exchanged within 180 days of the purchase date. If these fees were reflected, the performance quoted would be lower. Investment performance reflects fee waivers in effect. In the absence of fee waivers, total return would be lower. Total return is based on NAV, assuming reinvestment of all distributions. Performance does not reflect the deduction of taxes that a shareholder would pay on fund distributions or the redemption of fund shares. Performance data current to the most recent month end may be obtained at www.forwardfunds.com.

Market Review

After the sharp market correction of late February, equities recovered much of their losses in March, with the MSCI World ex-US index gaining 2.2%. Small caps fared a little better, with the benchmark index rising by 3.9% over the month, extending their YTD out-performance. Despite the tangible problems of the Middle East and further signs of deterioration within the sub-prime US mortgage market, it was the rather more arcane pronouncements of the US Federal Reserve which seemed to be the main focus of investor interest. Following the March meeting of the Federal Open Market Committee, markets sparked to life as the earlier reference to “additional firming” in interest rates was dropped from the accompanying statement. With the impact of some greater uncertainty about US growth and the position of the Federal Reserve with regard to future interest rate policy, combined with a further rise in the oil price to nearly USD 66 per barrel (WTI), it is perhaps surprising that the markets have made such a quick recovery. Asia was strong, most European markets made at least modest headway, but once again Japan was a notable laggard. The Fund modestly lagged the benchmark over the month, rising by 6.1%. Returns were slightly disappointing in Continental Europe which outweighed good stock selection in the UK and Japan. Over the first quarter, the return of 6.1% also slightly lags the benchmark (+6.7%).

Economic Background

The economic outlook in the U.S. has certainly deteriorated during recent weeks with the problems in residential real estate continuing to hang over the market with February showing new home sales at a seven year low. There also seems to be some evidence that lower confidence in the economic outlook is feeding through into corporate spending plans, with capital spending showing a degree of weakness.

Retail sales figures however show that the consumer continues to spend despite the gloomier outlook. A key factor to watch in the months ahead will be the employment data, which should provide an indication if corporations are reducing their willingness to hire workers. A slowdown in employment growth would likely result in a rapid deterioration in investors risk appetite and cause a more sustained sell-off in equities. One remaining bright spot for markets has been the continuing level of M&A activity. According to data collated by Dealogic, global M&A activity was in excess of U.S.D1,000 bn during the first quarter of the current year. The continuing low level of interest rates, strong corporate balance sheets, record private equity deals and the need to respond to competitive threats within consolidating industries remain strong drivers of activity. Within Europe, Germany and the UK remain at the forefront of activity with British companies particularly being involved both as targets and as acquirers of foreign businesses. On the buy-side Vodafone's U.S.D13bn acquisition of a majority stake in Hutchison stake in Essar and Imperial Tobacco's U.S.D 18.7bn approach for Altadis was followed by the initial approach for ABN Amro by Barclays. Buy-outs by British companies amounted to over U.S.D166bn in the first quarter according to Dealogic, accounting for 15% of global M&A deals. Such a level of activity throughout Europe as well as the U.S. does not look like stalling any time soon unless interest rates rise to unforeseen levels and this fire-power should continue to provide a safety net that would help underpin equity markets in the face of further market turbulence. We continue to be strongly in favor of equities relative to bonds, taking the view that the current slowing in the U.S. economy is not a precursor to recessionary pressures taking hold. We believe it is likely that the Federal Reserve will maintain a steady-state as regards interest rates for some time, as the inflation data only slowly improves. The resilience in the price of commodities (including oil), reflecting still strong growth in Asia and elsewhere, may well be an additional factor that cautions the U.S. central bank from any early action to lower rates. Equity valuations remain reasonable and although earnings growth is likely to slow in the U.S. this seem to be accepted in the minds of investors. Geopolitical shocks remain a threat to equities, but in the absence of the situation in the Middle East becoming sufficiently critical to cause a sustained spike in oil prices, any market set-back should prove short-lived.

Portfolio Strategy

As we have mentioned previously, we continue to believe small caps can offer investment opportunities despite several years of exceptional performance, and so far this year they continue to outperform. Even now, the valuation of small caps relative to large caps does not fully reflect their higher growth potential and the momentum of positive earnings revisions. We outlined our positive medium term view on European small cap equities: there is robust macro-economic background, healthy corporate profits and balance sheets, and potential for more M&A activity. Furthermore, European growth looks poised to decouple from the U.S., helped by plenty of pent-up internal demand and we believe that the recovery is just beginning. This view has recently been vindicated by an IMF report in which its revised estimate of European growth (2.3%) exceeds that of the U.S. While in some the European countries, the valuation gap for small versus large cap has been closed, there continues to be no shortage of exiting investment ideas at reasonable valuations. Although we are also positive on the prospects for Japan, we have been investing cash elsewhere in the last few quarters, thereby eroding our previous modest overweight position there towards a more neutral stance. In our view, there is potential upside to the strength of the domestic economy and corporate profits. Our emphasis is still with capital goods rather than consumer discretionary, as wage rises are not coming through as fast as many had anticipated, leaving consumer spending lackluster. We maintain a significant overweight position in the rest of Asia which has continued to confound expectations, maintaining its status as the world's fastest growing region with a stable growth rate of 7%. China has failed to slow significantly, so our overweight stance in the region has been beneficial. Macro-economic growth, industry themes (such as outsourcing and the rise of the Chinese consumer) have been positive. This overweight is balanced by our moderately cautious stance on the UK. Recent macro data has been mixed, suggesting that inflationary pressures are persisting, while economic growth is moderating. As mentioned previously, the housing market has shown surprising strength over the last few months, but the support that this tends to give to retail spending has been reduced by the unprecedented levels of household debt. The above factors suggest that the MPC is likely to raise interest rates further over the next few months, putting additional pressure on consumers. The key factor supporting the market

continues to be abundant liquidity which, combined with the comparative openness of the UK economy, has led to a surge in M&A activity which has continued into this year. We are retaining our long term underweight in the UK, and are particularly wary of consumer-related stocks, preferring industrials and financials. After five years of out-performance by value stocks, we believe that stock picking in 'Delivered Growth' companies should be more rewarding than in thematic 'Sector Plays'.

You should consider the investment objectives, risks, charges and expenses carefully before investing. A prospectus with this and other information about the Fund may be obtained by calling (800) 999-6809 or by downloading one from www.forwardfunds.com. It should be read carefully before investing.

Investing in foreign securities generally involve certain additional risks, including exchange rate fluctuation, less liquidity, greater volatility and less regulation. Small company stocks are generally riskier than large company stocks due to greater volatility and less liquidity. There are risks involved with investing, including loss of principal. Past performance does not guarantee future results.

The HSBC World Excluding U.S. Smaller Companies Index is a market capitalization weighted index designed to represent performance of smaller companies available in developed stock markets outside the United States and Canada. The index figures do not reflect any deduction for fees, expenses or taxes. It is not possible to invest directly in an index.

The MSCI EAFE Small Cap Index is an unmanaged, market-weighted index of small companies in developed markets, excluding the U.S. and Canada. The index figures do not reflect any deduction for fees, expenses or taxes. It is not possible to invest directly in an index.

The MSCI World Index ex U.S. is a free float-adjusted market capitalization index that is designed to measure global developed market equity performance.

The MSCI Europe Index is a free float-adjusted market capitalization index that is designed to measure developed market equity performance in Europe.

The MSCI Pacific Index ex Japan is a free float-adjusted market capitalization index that is designed to measure equity market performance in the Pacific region.

The MSCI Japan Index is designed to broadly and fairly represent the full diversity of business activities in Japan.

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