Capital Market Review • Third Quarter 2007

The third quarter of 2007 was a bumpy ride for the major averages. After a tough July, the major indices bounced back in September to finish the quarter in positive territory with the Russell 2000 Index being the lone exception. The Lehman Brothers Aggregate Bond Index, a representation of the overall bond market, provided the best return and was the only index to record a gain for every month in the quarter. It was up 2.8% for the third quarter and now stands at 3.9% year to date. The international market, represented by the MSCI EAFE Index, gained 2.2% during the quarter to bring its gain for 2007 to 13.2%. The S&P 500 Index, an index representing large company stocks, finished the quarter with a gain of 2.0% after a July loss of 3.1%. The S&P 500's return for the year is now 9.1%, trailing only the MSCI EAFE. Dow Jones Wilshire REIT Index, an index of real estate companies, barely finished in positive territory for the third quarter with a 1.4% gain. After a June and July loss of 16.5%, the index came back strong with gains in August and September of 5.9% and 3.9%, respectively. It is still the only major index with a negative return year to date losing 4.6%. Further evidence of the rotation from small caps to large caps can be seen in the third quarter return of the Russell 2000 Index. The Russell 2000 Index, an index of small company stocks, couldn't recover from a June loss of 6.8% and finished the quarter down 3.1%. The index's gain year to date now stands at 3.2%, almost 6% behind the S&P 500. The S&P 500 has outpaced the Russell 2000 on a three month, six month, year to date, one year, and two year total return basis. The three year total return has the Russell 2000 just ahead.

The month of September provided some much needed relief to the markets as July and August saw worries about subprime mortgages come to a head. The continued weakness in the housing market and rising delinquencies of homeowners finally made its way to the bottom line of financial corporations. Many financial institutions took huge write-offs on these risky securities and unease about the extent of the exposure sent the markets reeling. Investors shunned anything that was mortgage related leading to a liquidity crisis in the commercial paper market. Lenders refused to lend money to even borrowers with good credit. The Federal Reserve came to the rescue and lowered the discount rate, the rate among which banks lend to each other, by 50 basis points in mid-August and 50 basis points in mid-September mainly to restore confidence. The Fed lowered the federal funds rate by 50 basis points to 4.75% in mid-September as well. The markets responded well to the news and rallied back toward the end of the quarter. However, uncertainty remains, which should lead to more volatility in the short-term.

The housing market and liquidity crisis weren't the only issues that investors had to worry about during the quarter. Oil prices hit all time highs. Oil started the quarter at $70.68/barrel and finished at $81.66/barrel. It was up nearly 34% year to date at the end of the quarter. Homeowners will no doubt see higher heating bills this winter due to the spike in price. It is too early to tell if consumer spending will drop leading some to worry that the U.S. could go into a recession. The U.S. consumer now makes up 70% of the United States GDP and 20% of the World's GDP.

The decline of the U.S. Dollar to the Euro also was at the top of the headlines during the quarter. The Dollar continued to lose ground against the Euro falling another 5.3% from $1.3535 at the beginning of the quarter to $1.4259 at the end. The Wall Street Journal reported that this is the weakest the U.S. Dollar has been since the Federal Reserve index began to track the Dollar in 1973.

STOCK MARKET

The third quarter was mixed with most of the indices finishing in positive territory. The Lehman Brothers Aggregate Bond Index provided a safe haven away from the volatile equity markets leading the major indices with a gain of 2.8%. The index is now up 3.9% during the first nine months of the year. The MSCI EAFE Index built on gains from the prior quarter to finish up 2.2%. The MSCI EAFE remains the highest returning index year to date with a return of 13.2%. It is interesting to note that the S&P 500 is beating the MSCI EAFE on a third quarter and year to date basis when you take out the currency effects. In local dollars, the MSCI EAFE is down 2.5% for the quarter and up 7.1% year to date. That compares to the S&P 500 Index's 2.0% gain this quarter and its year to date gain of 9.1%. Also, see the returns for the MSCI EAFE compared to other regions of the world.

After a roller coaster third quarter, the Dow Jones Wilshire REIT Index finished the last three months with a 1.4% gain. This comes on the heels of a 9.5% loss in the second quarter. The gain in the third quarter still leaves the index under water with a 4.6% loss. The poorest performing index for the third quarter and the only one failing to post a gain was the Russell 2000 Index, representing small cap stocks. The index lost 3.1% giving up about half its gains of 2007. The Russell 2000 now has a 3.2% gain year to date.

Market Returns

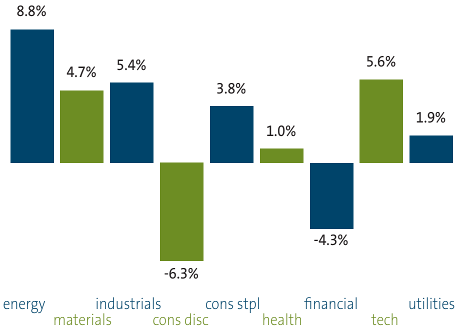
	3 months ended 09/30/07	YTD ended 09/30/07
T-Bills	1.2%	3.8%
Lehman Bros. Aggregate Bond Index	2.8%	3.9%
S&P 500	2.0%	9.1%
Russell 2000	-3.1%	3.2%
EAFE	2.2%	13.2%
Wilshire REIT	1.4%	-4.6%

Returns by Equity Manager Style

	3 months ended 09/30/07	YTD ended 09/30/07
Large Value	-0.5%	6.7%
Large Growth	5.4%	13.9%
Small Value	-6.1	0.6%
Small Growth	0.8%	11.4%
International	3.1%	14.9%
Real Estate	1.6%	-2.9%

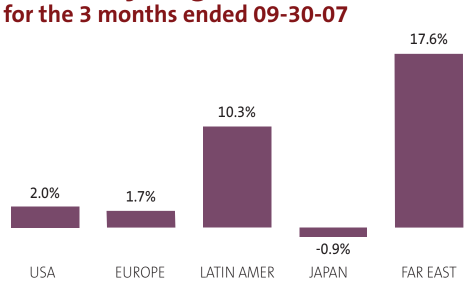
The equity styles for the third quarter showed mixed results. Both value styles, large and small, were the only styles to finish down. Small Value ended the quarter with a loss of 6.1% plunging its overall year to date return close to unchanged at 0.6%. Large Value also finished down for the third quarter posting a 0.5% loss, but still remains in positive territory for 2007, up 6.7%. Both Small Growth and Large Growth have been considerably stronger than their value counterparts for the quarter and year to date. Large Growth surged 5.4% for the third quarter bringing its nine month return to 13.9%. Small Growth rose slightly during the quarter up 0.8% and now stands at 11.4% for 2007. International Equities built on its strong gains during the first half of the year to finish the quarter up another 3.1% and posting a 14.9% return year to date. Real Estate was the most volatile equity style in the quarter, but still managed to gain 1.6%. The style, however, wasn't able to get into positive territory year to date and remains the only equity style posting a loss. It is now down 2.9% for the nine month period.

Stocks by Sector
for the 3 months ended 09-30-07



Most sectors of the stock market had positive returns for the quarter and year to date. Energy led the way last quarter and also led the way for the last nine months. The sector returned 8.8% helped by the surging price of oil. It now has returned an impressive 28.7% for 2007 making it the best performing stock sector. Technology built on its strong first half performance returning another 5.6% for the quarter bringing its total return year to date to 16.3%. Materials and Industrials built on strong second quarter gains to post returns in the third quarter of 4.7% and 5.4%, respectively. The impressive returns of the third quarter now put Materials and Industrials behind only Energy year to date with gains of 22.2% and 17.9%, respectively. Consumer Staples, Health, and Utilities were the last of the sectors to finish the quarter positive returning 3.8%, 1.0%, and 1.9%, respectively. The year to date returns for Consumer Staples, Health, and Utilities finished the nine month period at 8.7%, 7.0%, and 10.8%, respectively. Consumer Discretionary and Financials failed to participate in the gains of the third quarter. Financials were particularly hurt by the sell off in July and August and weren't able to recover. The sector finished the three months losing 4.3% and remains in the red year to date losing 5.2%. Consumer Discretionary gave back more than Financials during the quarter with a loss of 6.3% pushing its year to date return into negative numbers at -3.7%.

Stocks by Region
for the 3 months ended 09-30-07

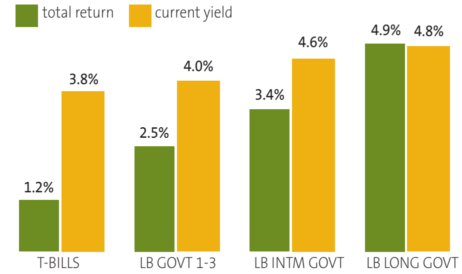


With Japan being the lone exception, the other major regions of the world posted gains during the quarter. The Far East ex. Japan was the best place for investors' money during the quarter. It had another impressive quarter returning 17.6%, easily outpacing the other regions. Even with that double digit return during the quarter and now 35.9% year to date, it wasn't able to overtake Latin America for 2007. Latin America did trail only the Far East region this quarter with a gain of 10.3%. Latin America's year to date return still remains the best region in the world for investors' money this year. Europe and the USA continued its solid performance to gain 1.7% and 2.0%, respectively for the third quarter. Europe has now returned 14.4% year to date with the USA gaining 9.1%. Japan can't seem to keep any momentum going. After a positive return in the first quarter, a losing second quarter and third quarter, the region is up only 2.0% year to date. Investors continue to be unimpressed by the region, finding better opportunities elsewhere around the world.

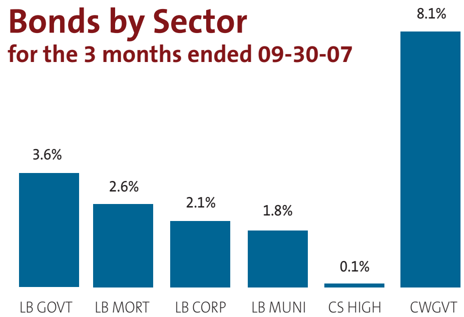
BOND MARKET

The Federal Reserve stepped in during the liquidity crisis and volatility in the markets to lower the Fed fund's rate to 4.75% after leaving the rate unchanged for over a year. The Fed also decided to lower the discount rate twice during the quarter by 50 basis points each time to improve confidence and make the lending between banks cheaper. Investors are now expecting the Fed to cut rates one, possibly two, more times this year. Bonds were the place to be during the quarter as yields declined across the board with the expectation of more rate cuts and investors found safety from the equity market. The Lehman Brothers Aggregate Bond Index, a broad fixed income benchmark, returned 2.8% this quarter and is now up 3.9% year to date. The longer end of the bond market was the best place to be for government bonds in the quarter. The Lehman Brothers Long Government Index gained an impressive 4.9% for the last three months, but was still unable to push into positive territory year to date losing 0.4%. The Lehman Brothers Intermediate Government Index also had a good showing gaining 3.4% for the third quarter and sits up 2.4% year to date. The shorter end of the government bond market, represented by the Lehman Brothers 1-3 Year Index, returned less than its intermediate and long counterparts, but still pushed 2.5% higher and has now returned 3.1% for 2007. T-bills had another strong quarter gaining 1.2% and are now outpacing all government bonds year to date with a return of 3.8%.

Bonds by Maturity
for the 3 months ended 09-30-07



Bonds by Sector
for the 3 months ended 09-30-07



Every sector of the bond market finished up for the quarter and all six showed gains year to date. World Government bonds bounced back sharply from a disappointing first half of the year surging 8.1% for the last three months pushing the year to date return to 7.3%. This makes World Government bonds the best sector in the bond market for 2007. Government bonds, as talked about earlier, finished up 3.6% for the quarter and 4.8% year to date trailing only World Government for those time periods. After posting losses across the board, Mortgages, Corporates, and Municipals came back strong and gained 2.6%, 2.1% and 1.8%, respectively. Mortgages gained 3.7% for the first nine months of the year, while Corporates returned 2.9% and Municipals were up 2.0%. High Yield bonds were essentially unchanged during the quarter gaining 0.1%, but it was the most volatile bond sector to be in. After losing 3.14% in July, it bounced back with a 1.04% return in August and 2.23% return in September. High Yield bonds are up 3.7% for the first nine months of 2007.

COMMODITIES MARKET

The Dow Jones AIG Commodity Index moved higher during the quarter in large part due to the unexpected rise in the price of oil. The index gained 6.2% pushing its year to date return into double digits, up 11.0%. Gold was another big winner in the commodities market gaining 15% to close the quarter at $742.80 on fears of a recession in the U.S. Copper also rose 5.1% in the quarter and Wheat surged to its highest price ever to return 61% for the quarter. ■