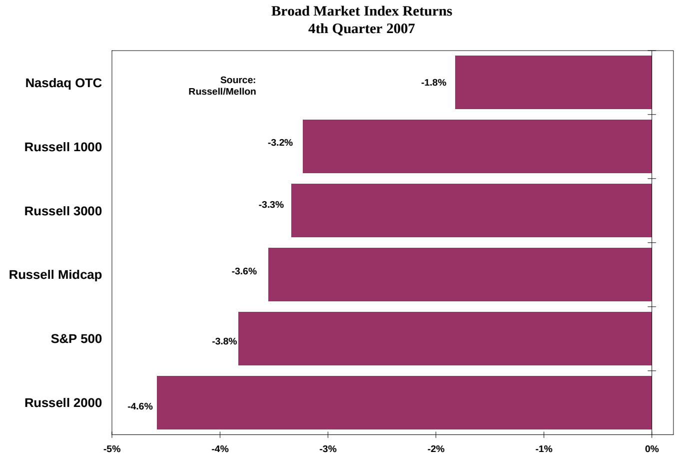
Fourth Quarter 2007 Market Summary



Economy

The fourth quarter of 2007 may go down as the most interesting from an economic perspective since the third and fourth quarters of 1998, during which the financial system was stressed by the collapse of hedge fund Long-Term Capital Management and the Russian financial crisis. The fourth quarter was marked by a continuation – and deepening - of the credit turmoil that bubbled up in the previous quarter. Liquidity issues resulting from the subprime fallout caused an economic slowdown that is likely to border on being recessionary, and will continue into at least the first part of 2008. The consensus estimate for GDP growth in the fourth quarter is approximately 1% and 2.5% for the entire year.

The effects of the crisis were widespread. Mortgage lenders were not the only ones hit hard; large money center banks and investment banks – big investors in securitized packages of mortgage obligations – announced multi-billion dollar write-downs of these assets on a weekly basis. Significant write-downs at Citigroup and Merrill Lynch cost the CEOs of those firms their jobs.

The Fed lowered rates twice in an effort to boost the slowing economy and to avert a recession. The Federal Open Market Committee (FOMC), the Fed's policy-making arm, lowered the federal funds rate from 4.75% to 4.25% during the quarter, and has dropped rates by 1.00% since the reduction program began in September. The Fed also announced shortly after its December meeting that it had put together a consortium of international central banks to free up credit to a tight market. The plan called for the banks to make available up to $40 billion for banks to borrow at favorable rates. The availability of liquidity in the system does not seem to be much of an issue; financial institutions' willingness to lend the funds appears to be more of a concern. Such reluctance likely will only be overcome through the passage of time.

The dollar continued its downward spiral relative to other currencies. There are both positive and negative implications of the declining dollar. On the positive side, the dollar's decline makes it easier for US manufacturers of goods to compete effectively against countries with lower labor costs, helping our trade imbalance. Negative implications include less foreign appetite for owning dollar-denominated assets, which may eventually prompt foreign central governments – large holders of US government securities – to scale back their investments.

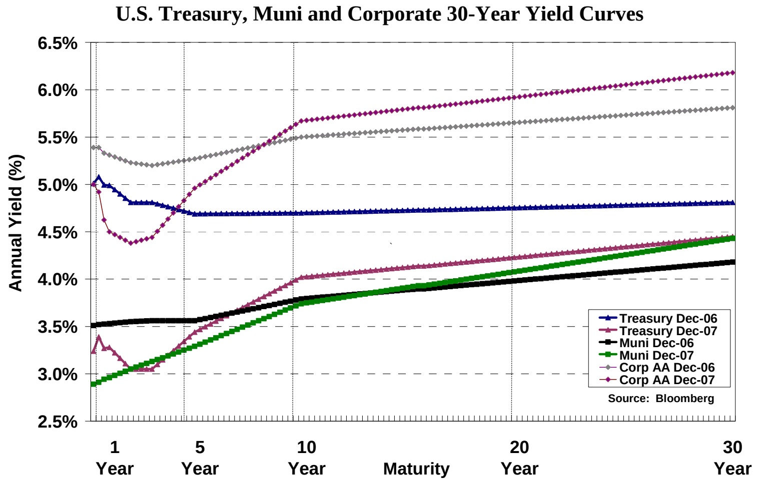
The housing sector also continued to deflate. According to economy.com, the volume of existing home sales is off as much as 40% since the beginning of 2006. Many economists and housing analysts believe the workout of the housing problems will continue through most of 2008, with prices not leveling off until sometime in 2009. Indeed, the latest home price data available shows that prices in 10 major metropolitan areas in October were down 6.7% from a year earlier, marking the largest year-over-year decline on record.

Inflation is expected to remain benign into 2008. The "core" component of the Consumer Price Index (i.e., CPI ex-food and energy) jumped more than had been expected in November, but this is likely to be a temporary blip because of slowing economic growth.

The risk of recession remains elevated. Consumer and business confidence is eroding. In the fourth quarter, some measures of consumer confidence hit their lowest levels since the early 1990s. Business investment is also lagging, endangering continued expansion. Perhaps the biggest threat to sustained economic growth is the housing situation. Economy.com estimates that the housing recession will eliminate an estimated $2.5 trillion in household wealth. A continued housing recession is the most significant threat to the economic expansion.

Interest Rates

As one might expect, bonds continued a strong recovery in the fourth quarter, primarily due to the expectation of the Fed's accommodation in order to sustain growth. There was a significant divergence between performance of taxable and municipal bonds. In the taxable universe, yields across the maturity spectrum declined dramatically in the quarter: the yield on the 2-year Treasury fell from 3.97% to 3.05%; the yield on the 5-year note declined from 4.23% to 3.44%; the yield on the 10-year note dropped from 4.59% to 4.03%; and the 30-year long bond saw its yield slip from 4.83% at the beginning of the quarter to 4.45%. The yield curve steepened further in the quarter, making for a better environment for lenders' financial statements.

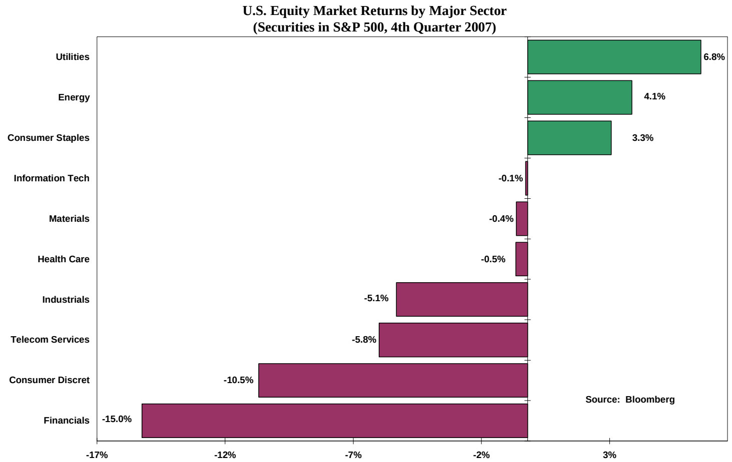


Municipal bond issues, however, did not fare as well as taxable bonds. At best, yields were unchanged during the quarter, reflecting the softening in the economy. Composite yields on 2-, 5-, 10- and 20-year ended the quarter approximately 10-30 basis points higher. The significantly expanded spread between taxable and municipal yields has many investors looking for opportunities in select municipals.

Equity Markets

The uncertainty engulfing the overall economy marked a volatile quarter for equities. All-time highs were established in many of the major indices early in the quarter based on expectations that the Fed's actions would prove to be the antidote for the subprime mess. However, the depth of the credit market's problems quickly became evident, and the stock market's foray into record territory was followed almost immediately by what has come to be known as an "official" correction of 10% during the quarter. It was the first correction since the current bull market began in the third quarter of 2002.

The fourth quarter witnessed a continuation of the relative outperformance of Large Cap stocks over Small Caps, and Growth over Value, typical for this point in the economic and market cycles. The Russell 1000 index declined 3.23% for the quarter and gained the 5.77% for the year, while the Russell 2000 index of Small Cap stocks posted a decline of 4.58% for the quarter and lost 1.57% for the year.



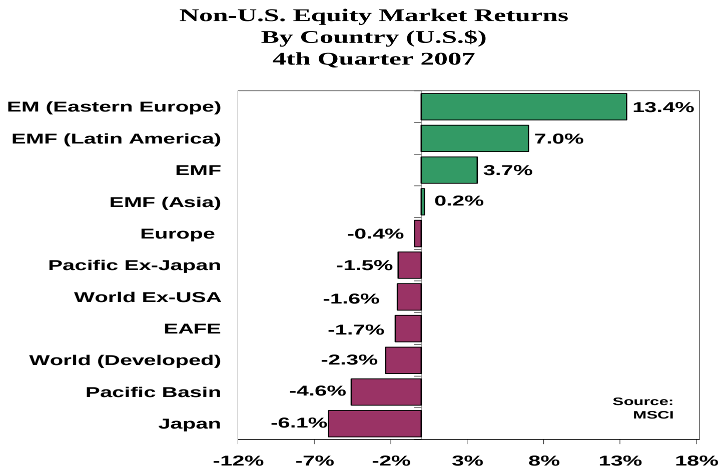
Domestic and international equities fared similarly in the fourth quarter and for the full year. International developed markets, as measured by the MSCI EAFE index, declined 1.71% in the fourth quarter, resulting in a total return for the year of 11.63%. Emerging markets continued their strong relative performance in the fourth quarter, posting a gain of 3.66%. For the year, emerging markets gained 39.78%.

The financial sector remained the poorest performer on a relative basis in the fourth quarter, as well as for the entire year. Consumer services stocks, in particular the home improvement retailers, also fared poorly in the quarter as the housing recession has dampened consumers' willingness to spend.

As we have been anticipating, the recent decline in stock prices, particularly in the financial sector, is beginning to attract savvy investors seeking bargains. Many solid companies with strong franchises have seen a precipitous drop in the value of their stock, and contrarian investors are taking advantage. Three recent cases indicate that the stock market may be stabilizing. First, the investment arm of the government of Abu Dhabi invested $7.5 billion in Citigroup preferred shares, making the Arab emirate the bank's largest individual holder. Citigroup shares have declined significantly this year, and analysts have touted the Abu Dhabi investment as a bargain. In a second situation of a deep-pocketed investor seeking to exploit low stock prices, Citadel, the large Chicago-based hedge fund, agreed to invest $2.5 billion in E-Trade, which has been beleaguered by its subprime loan portfolio. Finally, Merrill Lynch received an infusion of $4.4 billion from Singapore's investment arm, Temasek, at an extremely favorable valuation. Expect to see more such deals involving sharp investors, particularly if the market continues to have difficulty finding its bearings.

Outlook

If history is a guide, 2008 may shape up to be a positive one for equities, particularly if recession can be averted. To be sure, there is a great deal of uncertainty casting a pall over the market: the stock market recently underwent a 10% decline from its high, the "official," but arbitrary, level of a correction. Financial headlines are pessimistic. The economy is having difficulties. Yet, in many ways the current environment is one containing promising opportunities for astute advisors and their clients.



As noted above, a sign that the dust is starting to settle is that sophisticated investors are beginning to rummage through the carnage of beaten down stock prices to buy into perceived bargains. This is the type of environment where track records and reputations can be made, and each one of these deals supports equity prices and provides a shot of confidence to the markets.

Another reason we are optimistic is that equity valuations are reasonable, if not attractive, even when factoring in an economic slowdown. The price/earnings (P/E) multiple on S&P 500 operating earnings is approximately 16.5, far lower than the 27.8 multiple prior to the market's slide in 2000. Therefore, there is downside protection in the form of attractive valuations.

Market action during previous interest rate reduction programs by the Fed also can provide insight as to possible stock price activity going forward. There have been three distinct periods of interest rate reductions since 1990, one beginning in October 1990, another in July 1995, and the third in January 2001. In the first two instances, which were similar from a valuation perspective to the current environment, stocks rallied strongly in the 12 months following the initiation of the rate reduction program, with gains in the S&P 500 of 33.5% and 26.0%, respectively. Following the onset of the 2001 program, stocks declined approximately 12%, but valuations were much higher at the time.

Finally, for whatever reason, stocks have enjoyed positive returns in every presidential election year – with the exception of 2000 **-** since at least 1976. Performance in 2000 should probably be discounted because of the excessive valuations prevailing at the time.

In short, we anticipate moderate gains for equities in 2008 due to a climate that looks relatively promising in spite of the current psychology. A vigilant Fed expected to provide adequate liquidity to the financial system, rising exports, and continued capital spending by corporations should enable the economy to avert a recession. Reasonable valuations should serve to moderate any share price declines.