M W INVESTMENT STRATEGY GROUP

APRIL 2008

In the worst quarterly performance by the US stock market since 2002, the S&P 500 index lost 9.5% for the three months ended March 31. Foreign markets declined in tandem. Treasury bonds rose during the quarter with gains of between 2.0-3.0%. Lesser-quality bonds underperformed and shorter-term Treasuries outperformed in a characteristic flight to quality. Municipal bond prices fell during the quarter, a further consequence of the ongoing turmoil in the credit markets.

Model Portfolio Performance[1]

Our four model portfolios declined by between 2.6-9.6% in the first quarter. Each model matched or exceeded its benchmark for the period.

MUTUAL FUND MODEL PORTFOLIOS CURRENT PERFORMANCE[i]

Model	Risk Benchmark	1st Qtr	Trailing 12 Mos	Cumulative since Jan 99
All Equity	100% Stocks	**-9.6%**	**-5.4%**	**92.5%**
Growth	80% Stocks 20% Fixed Income	**-7.4%**	**-3.1%**	**84.3%**
Balanced	65%Stocks 35% Fixed Income	**-5.1%**	**-0.1%**	**90.0%**
Conservative	40%Stocks 60% Fixed Income	**-2.6%**	**2.9%**	**79.1%**
S&P 500		-9.5%	-5.2%	24.0%

All our equity mutual funds were in the red, with declines ranging from 16% at the recently-added Kinetics Paradigm to 3.5% at Fairholme. High-quality bonds were the best performing asset class in early 2008, leading to the superior relative performances by our more conservative portfolios. All our bond funds (with the exception of a small loss at Loomis Sayles Bond) had strong performances, with our core bond holding, Pimco Total Return, earning a 3.3% gain for the three months. Pimco Total Return and Pimco Developing Local Markets have returned 10.4% and 14.7% respectively over the past twelve months.

Clients who hold muni funds in taxable accounts in place of Pimco Total Return experienced slightly lower performance due to the sell-off in municipal bonds. We viewed this price decline as an over-reaction to the credit market distress and were able to take advantage of some attractive values in higher-rated muni bonds and funds.

Current portfolio positioning:

At the end of March, we eliminated the small allocation to commodities that we had held in our Conservative and Balanced models, adding the proceeds to the Pimco Developing Local Markets fund. These positions were intended as an inflation hedge and had been funded by a reduction in fixed income allocations. In recent months, the inflation-hedge value of commodities was increasingly overwhelmed by the speculative fervor driving the asset class. We are still considering the possibility of adding commodities as a longer-term risk-diversifier to our portfolios.

[1] *See disclosures on pages 4 of this letter*

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There were no other changes to our portfolio allocations during the quarter. Within our US equity allocations, we retain a substantial overweight to Large Cap vs. Small Cap stock funds. Within our foreign stock exposure, we have a small emphasis on Emerging Markets. We remain overweight foreign currency vs. the US dollar through our selection of specific mutual funds.

During March, we took the opportunity to rebalance client account allocations towards their target values, reducing fixed income and increasing equity mutual fund positions, the latter of which had declined with the falling market. This rebalancing practice, essentially buying low and selling high, is one of the less visible ways in which we are able to enhance the longer-term performance of our client accounts.

Looking ahead

In the coming quarter, we will be replacing our positions in TCW Select Equities, a major holding that we have owned in client accounts for almost nine years, due to the unexpected departure of the second of the fund's original three managers.

Real estate (REITs) and high yield (e.g. junk) bonds are approaching sufficiently depressed valuation levels that we can envision adding these asset classes back to our portfolio allocations sometime later this year.

Buy? Sell? A dilemma

It has been a tough three months for investors as collapsing home prices in 2007 began an avalanche of problems in the credit markets, both here and abroad. As of this writing, home prices continue to decline, but the credit markets are attempting to stabilize.

By quarter's end, stock markets were rebounding in a show of relief over the perceived diminishing possibilities of an "Armageddon" economic outcome, e.g. a severe deflation ala Japan or worse. While the risks of this dire scenario may in fact be fading, we remain concerned that we have yet to see the end to the cycle of deleveraging and economic weakness. In the face of significant economic uncertainty, we rely on our investment discipline that is based in the valuation and scenario analysis we receive from Litman Gregory. Their valuation work suggests that, in spite of the potential for further market declines, the long-term return potential of equities is strong enough relative to other opportunities that any underweighting would reduce our clients' eventual returns. Policy makers (and the Federal Reserve in particular), are loudly signaling that they will do whatever they deem necessary to reverse the crisis of confidence in credit markets.

Considering all scenarios, it is also possible that the stock market is correct and that a market bottom is at hand. Reducing equity exposure poses the risk of being underweighted to equities in a market rebound, which has the potential to be quick and sharp. As is true in all bear markets, rational market analysis can provide long-term confidence, but offers no short-term assurances. Markets are often driven more by emotion than economic fundamentals, and in bear markets that emotion is fear.

In the event of a further sell-off of 10% or more in the US stock market, we plan to increase equity exposure to at least a 5% overweight to US Large Cap stocks in our allocation models. While we cannot be sure of buying at a market bottom, a further decline of this magnitude would

bring valuations to a very compelling level. Lower stock prices mean that stocks are, as Warren Buffet likes to say, "on sale." Our intention would be to be a buyer at those prices, buying more aggressively in our All Equity and Growth models and with more restraint in our Conservative and Balanced models.

How to take advantage of possible capital gains tax changes

On another note entirely, the opportunity to take advantage of an historically low 15% rate on long-term capital gains may be ending soon. Greg Valliere, Chief Political Strategist for the Stanford Washington Research Group, speaking at a recent financial advisor forum, noted that a tax hike – on capital gains and dividends – is almost a certainty for 2009 with (he said) a likely Democratic President in the White House and Democratic majority in Congress. Currently, the 15% rate on long-term gains is scheduled to revert to its prior 20% rate at the end of 2010. However, Valliere thinks the tax code may be revised even before then.

For investors with substantial unrealized capital gains in securities or real estate and who do not plan to hold these assets indefinitely, we suggest consulting with your tax advisor as to whether it makes economic sense to realize some or all of the gains and pay the taxes while the 15% rate is still in effect.

Another strategy worth revisiting for 2008 is gifting appreciated securities to anyone who might fall into the 10% or 15% income tax brackets. (A married couple with no more than $65,100 in taxable income and single filers $32,550 or less in 2008 fall into these brackets.) These taxpayers qualify for a **zero capital gains tax rate in 2008**. This zero rate represents a valuable tax-saving opportunity for those providing, or wishing to provide, financial support to children, parents or others. An important caveat is the newly expanded "kiddie tax" rules that eliminate the tax-savings in the case of full-time students between the ages of 18-24, and for all minors. Note that the expanded kiddie tax rules add to the advantages of utilizing 529 plans in place of Gifts to Minors accounts for college savings.

Conclusion

The disruption in the credit markets is as severe as any in post-war history. Home prices are in their worst decline since the Great Depression. The US economy has almost certainly entered a recession. Any one of these circumstances by itself should have been enough to cause a far greater stock market sell-off. That stocks have held up as well as they have is a testament to the robustness of the US and global economies, and to the fact that valuations (other than residential real estate) are not wildly over-optimistic as they were in the late 1990s. However, if the record of similar major credit crises is any guide, there is more market volatility and the possibility of further market downturns ahead.

We continue to employ the same "all-weather" approach that has served us well through previous downturns. Our portfolio models and client accounts are behaving as expected and should hold up in the face of any further market weakness. While we have no ability to predict the shorter-term, we are confident that stocks are likely to outperform investment-grade bonds over a five-year period and, at current levels, represent at least a reasonable value for longer-term investors.

Martin Weil
President

Model Portfolio Performance Disclosures:

a) Performance data is for model portfolios and is not a composite of actual client accounts.
b) All MWI managed client accounts are based on one of these four diversified mutual fund model portfolios. The models are geared to differing levels of investor risk tolerance, expressed as a one-year maximum loss thresholds - for Conservative (-5%), Balanced (-10%), Growth (-15%) and All Equity (per the US market).
c) New accounts are invested following one of these models, typically using dollar-cost averaging over a period of months, not to exceed one year. Once an account is fully invested, it is expected to track the performance of its underlying model. Exceptions will include accounts with restrictions such as: client-directed retention of legacy holdings and/or excess cash; substantial withdrawals or additions. Accounts smaller than $100,000 are restricted by purchase minimums at certain mutual funds we employ and the performance of these accounts may differ somewhat from the models. Taxable accounts employing municipal bond funds in place of the taxable bond funds used in the models may underperform on a pre-tax basis.
d) Benchmarks are custom created following the neutral asset allocation shown for each portfolio. Components of the benchmark allocations are Vanguard's S&P 500 index fund, iShares Russell 2000 index, Vanguard Total International and Total Bond index funds, and cash. S&P 500 index data is based on the performance of the Vanguard S&P 500 fund and includes dividends.
e) Net of fees: The performance for MWI model portfolios is calculated net of our maximum annual management fee. The returns of the portfolio benchmarks and market indices do not include these management charges. All returns assume dividends and income are reinvested.
f) Rebalancing: Model portfolios are routinely rebalanced every six to twelve months on the last day of a quarter. Actual client accounts may be rebalanced at other times. With tax-efficiency a part of our decision criteria, taxable accounts may be rebalanced less often and/or less completely than retirement and other accounts not subject to current taxation. This may result in performance discrepancies between taxable and non-taxable accounts managed following the same portfolio model.
g) Model allocation changes: Changes to model allocations are infrequent but can and do occur at any time. When a model is changed, allocations to client accounts are changed as soon as is practical. However, changes to the model portfolios are only recorded, for performance purposes, on the last day of any quarter.
h) Closed funds: From time to time, mutual funds that form part of MWI model portfolios close to new investors. Clients already owning closed funds will generally continue to hold and/or add to their positions. New client accounts will be invested in alternate funds. At year-end, MWI will substitute in its models for any funds that have closed during the year with alternate funds available at that time to new clients. As a result, performance disparities may develop between older and newer client accounts, and between older client accounts and current model performance.
i) Historical performance is not a guarantee of future results. While the performance period since January 1999 includes both rising and falling stock markets, there can be no assurance that the portfolios will perform as well under future market conditions. In particular, the cumulative performance of our Conservative and Balanced models relative to the S&P 500 index reflect outperformance by these two models during the bear market in US stocks during 2000-2002. In rising equity markets, the Balanced and Conservative models would be expected to underperform a similar investment in the S&P 500.