

Investment Perspective

Fourth Quarter 2007

J.P Morgan, when asked what the stock market will do, replied, **It will fluctuate.**

SFP Core Strategies*	Quarter 4	
	2007	One Year
US S&P 500	-3.35%	5.44%
US Large Value	-5.39%	-2.76%
US Micro Cap	-6.91%	-5.22%
US Small Value	-8.81%	-10.75%
US Equity Real Estate	-14.50%	-18.67%
International Large Value	-3.69%	10.24%
International Small Cap	-5.56%	5.66%
International Small Value	-7.49%	2.95%
International Real Estate	-11.21%	NA
Emerging Markets	3.25%	36.02%
Emerg Mkts Small Cap	0.06%	38.02%
Emerging Mkts Value	2.71%	45.64%
Ultra Short Fixed Income	1.26%	5.19%
Shrt/Inter Global Fixed Inc	1.31%	5.22%
Inflation Protected Sec	5.27%	11.84%
Model Portfolios		
SFP Balanced Portfolio	-2.47%	3.70%
Non SFP Std Balanced	-0.34%	6.41%

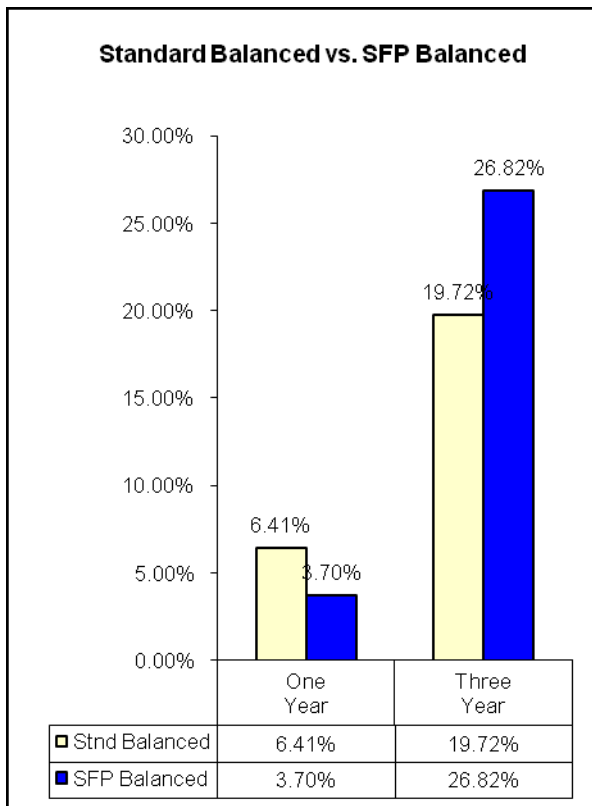
Recently, Morningstar announced its fund manager of the year awards. When the world's leading research firm for mutual funds annually names the best fund manager, I like to take a peek. But this year, after a rough final quarter, I wasn't exactly thrilled about hearing how much money someone else made. What started off as a good year turned topsy-turvy in the third quarter and downright dark in the fourth quarter.

The previous newsletter discussed the bottleneck in the credit markets and pointed out that problems continued to linger despite Federal Reserve Bank actions. Then the stock market had staged a recovery and it appeared things might straighten out. But the fourth quarter didn't cooperate.

News increasingly indicated a strong potential for a recession in the United States, a recession that may already be occurring. The Fed once again lowered interest rates, but their actions weren't enough to quench the market's thirst for a strong statement to quell fears about recession and credit issues. The end result? Negative quarterly results. High-quality bond issues, that is, those not related to the subprime mortgage meltdown, and the Emerging Markets avoided trouble, but our other strategies declined.

Despite the quarterly losses in most areas, our SFP Balanced Portfolio happily still made money for the year, returning 3.7 percent, and was down just 2.47 percent during the fourth quarter. That was thanks largely to the significant investment in those boring bonds that previously had been doing little for us over the last several years. (Please see the performance chart.)

On a relative basis, our SFP Balanced portfolio underperformed the Standard Balanced Portfolio by about 2 percent for the quarter and 2.7 percent for the year. This was largely due to the underperformance of Small and Value stocks in the world's developed markets. Our three-year relative performance is still dominating, so we're not complaining. For some investors, it has been much worse.



We earlier made a conscience decision to go with low-yielding, conservative, Fixed Income investments. Our view is that bonds should provide safety, not growth. Some unfortunate investors didn't take that approach. In fact, some of the worst performing mutual funds for 2007 were bond funds. Unbelievably, Regions Morgan Keegan Select's High Income fund and their Intermediate Bond funds lost 60 percent and 50 percent for the year, respectively.

It must be terrible to see your bonds losing money just when you need them to diversify and cushion investors from stock market turbulence. These investors probably did not realize the bonds they were choosing were exposed to the same types of risks that affected their stocks. They were just attracted to the higher interest rates being offered. Avoiding these situations is why we insist on using very structured investment vehicles whenever possible. We're trying to achieve a specific balance for your portfolios and that's not easily achieved with an average investment product.

Morningstar's fund managers for 2007, Will Danoff, Kakan Castegren, and Bill Gross, did have great returns for 2007, it's true. Their funds earned from 9.58 percent to 19.4 percent. While these numbers are not eye popping, remember that the award was not solely based on 2007 returns. According to Morningstar, these managers "all have delivered strong absolute and relative returns for huge numbers of investors over many years."

How can one argue with success? The goal is to make money, not to create some ideal structure. If a fund manager is good at making money, you shouldn't handcuff them, right? And it seems that an endorsement from the premier provider of fund research is a pretty good indication they can make money.

So we decided to look at some of these past winners and how they did in the year following their award. The table below shows funds managed by the 2004, 2005 and 2006 winners, and their performance figures for the year following their Morningstar award, plus an appropriate benchmark (Russell, MSCI, and Lehman indexes) to compare them to. Fund managers that did outperform their benchmarks the following year are highlighted with blue, while those that underperformed are highlighted in yellow.

Year of Award	Fund	Subsequent Annual Return	Benchmark
2004	T Rowe Mid-Cap Growth	14.82%	12.09%
2004	Dodge & Cox Intl Stock	16.75%	13.80%
2004	Western Asset Core Bond	1.91%	2.43%
2005	Selected American	15.19%	15.46%
2005	Davis NY Venture	15.12%	15.46%
2005	Wset Total Return Bond	6.99%	4.66%
2005	ICAP International	24.30%	30.38%
2006	Longleaf Partners Fund	-0.40%	5.77%
2006	Longleaf Partners Small Cap	2.80%	-9.78%
2006	Oakmark International	-0.50%	5.96%
2006	Oakmark International Small	-8.30%	-9.78%
2006	TCW Total Return Bond	6.60%	6.97%
Average Return		7.94%	7.79%

There are a total of 12 funds listed. Five funds outperformed in the subsequent year, but in the case of seven funds, more than half of these superstar managers could not beat the index in the year following their award. When we look at a simple average of the returns listed, the superstars earned 7.94 percent while the indexes returned 7.79 percent - **essentially the same number**. Once again, we find that picking the winners after the race is over is much easier than picking them ahead of time.

The most important lesson is that one should be extremely cautious in giving up structure and discipline in search of superior returns. Going with longtime industry experts because they were recognized by industry authorities simply isn't good enough. As we look toward what are potentially dark skies ahead, we know that preparation cannot eliminate all risks, but it can minimize them.

Wishing you good health, happiness and good fortune in 2008,

Sincerely,

Brian J. Skaggs, CFP

The information in this newsletter should not be construed as investment advice. Investment advice is only given in the context of individualized interactions that ideally result in the development of a continually evolving financial plan. *Total returns as measured by the performance of associated DFA funds - advisor fees not included in strategy performance. Advisor fees are subtracted from model portfolio performance at 8.3 basis points per month. This information is believed to be reliable, but we do not guarantee the accuracy of the information. **Past performance is not an indication or guarantee of future performance.**