

Investment Perspective

Third Quarter 2008

"Oh, I think confidence will come back. I will tell you this. This country is going -- be living better ten years from now than it is now." Oct 2nd, 2008 - Warren Buffett

| SFP Core Strategies* | Quarter 3 | |
|-----------------------------|-----------|----------|
| | 2008 | One Year |
| US S&P 500 | -8.27% | -21.89% |
| US Large Value | -8.24% | -22.36% |
| US Micro Cap | 0.05% | -19.33% |
| US Small Value | -1.02% | -19.15% |
| US Equity Real Estate | 5.22% | -13.08% |
| International Large Value | -17.79% | -31.60% |
| International Small Cap | -22.43% | -32.55% |
| International Small Value | -20.83% | -33.07% |
| International Real Estate | -13.32% | -36.26% |
| Emerging Markets | -20.15% | -27.32% |
| Emerg Mkts Small Cap | -24.22% | -39.03% |
| Emerging Mkts Value | -25.83% | -33.82% |
| Ultra Short Fixed Income | 0.01% | 2.80% |
| Shrt/Inter Global Fixed Inc | 0.07% | 1.67% |
| Inflation Protected Sec | -4.00% | 7.79% |
| Model Portfolios | | |
| SFP Balanced Portfolio | -6.58% | -14.93% |
| Non SFP Std Balanced | -5.63% | -12.20% |

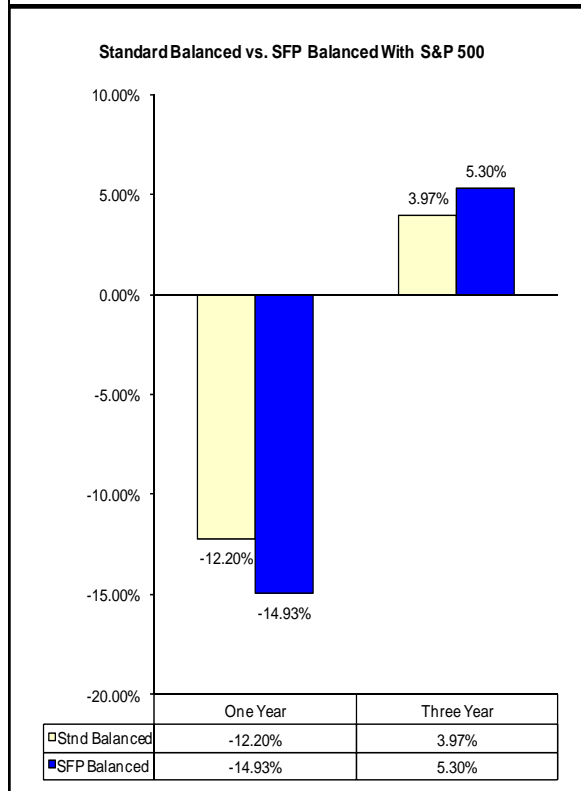
It's true that the numbers are bad. But before we report results, let us first say how we're feeling about the market. Since 2003, when we began writing this newsletter, there have been many good times during which we expressed a cautionary note. We expressed concern about the magnitude of gains, about the consistency of gains across the board, and about the lack of downside volatility. While we enjoyed gains, we feared people would forget about the risk that comes with investment. In fact, we specifically warned in our October 2004 newsletter about speculation in the residential real estate markets. (Past newsletters can be found at www.skaggsfinancialplanning.com.)

Is this situation unprecedented? It's true the popular press is pessimistic, reporting bad or worse news every day. With the Fed arranging bank mergers and with investment houses failing, it's understandable that we'd ask if we're in for unprecedented declines in the stock market, followed by years of groveling in low or negative returns. Something along the lines of *Sure, the stock market has come back before, but...*

...Is It Different This Time? Well, if you read the bad news – and worse, speculations - your answer might be yes. But, in actual fact, the market offers no evidence, at least not yet, that this decline in the markets is anything other than a garden-variety downturn. We are more positive about equity growth prospects than we have been since our firm was formed in 2002.

Of course, there is no guarantee that the worst is yet behind us. Any study of market history will show the bad times can persist. The 14 percent drop in the market during 1929 was followed by 28 percent drop during 1930, a 43 percent drop during 1931 and an additional 8 percent drop during 1932. However, the lack of leadership in Washington D.C. notwithstanding, we believe knowledge and economic tools have come a long way since those days.

For the quarter, our stock market strategies, like nearly all others, were down virtually across the board. The most painful losses took place overseas, with most strategies falling over 20 percent. Domestically, our positions in U.S. large cap stocks were down about 8 percent, while our small company positions were flat. Happily, our real estate strategy showed gains for the quarter. On the fixed-income side, we were essentially flat. These losses led the overall SFP Balanced Portfolio to fall by 6.58 percent for the quarter, bringing the one-year slide to 14.93 percent. (Please see the performance table.)



On a relative basis, the one-year performance of the SFP Balanced Portfolio underperformed the Non SFP Standard Balanced, which came in with the decline of just over 12 percent for the year, by about 2-½ percent. The three-year relative performance is still on the SFP portfolio's side, with returns of 5.3 percent versus 3.97 percent. Still, it is disheartening to see most of the gains of the last few years evaporate. You will see similar numbers reflected in your personal portfolio reports.

For many of you, the numbers won't look as bad as you might have expected given this sky-is-falling headlines we hear in the news. For others, the numbers will take you aback. Either way, we would urge you to take a look beyond just the ending dollar value of report. For your convenience, we have included a couple of pages from your account statements and highlighted some holdings at different times during the declines this quarter. Unless you took a withdrawal from the account, you will notice that the position has not changed. In fact, the number of shares you own may actually have **increased** slightly. That is, your ownership share of the underlying businesses and bonds have not changed despite the value being reported.

That's because just as part of your house is not removed when its market value falls, you do not lose your ownership of a business when the stock price falls. It's just a temporary value that changes.

Wouldn't it be better not to own securities that weren't falling in value? Yes, naturally, if we could perfectly predict the future. We would only invest in assets that were appreciating. But just as it is not sensible to avoid a brisk walk or healthy bike ride for fear of being injured by a fall, it's naïve to believe there is a way to dance between the raindrops of risk in the financial markets.

This choice may be easy for those looking to grow wealth, but what about those looking to preserve it? In that case, we have already built-in generous portions of fixed income products into your portfolio. Essentially, you have a combination of both choices that favors preservation of purchasing power. We use the term preservation of purchasing power, rather than preservation of dollar value, because there is a huge difference. The dollar value of the portfolio is simply a number, the importance of which is decreased by inflation. The purchasing power represents the portfolio's value in terms of the goods and services. It is the true measure of wealth.

Sadly for those inclined to just put their money into a savings type investment, recent government actions to get our economy back on track are likely to result in increases in inflation. In other words, the expense of the rescue package will be paid by those leaving their money in bank CDs, savings accounts and money market. No, the dollar value of their accounts will go down. But each dollar will buy fewer goods and services in the future. As the economist Milton Friedman once dryly noted, "Inflation is taxation without legislation."

During these difficult times is important to remember that the United States has made it through civil unrest, numerous wars, Enron, even the Great Depression. While we should expect and prepare for a deepening recession, we will get through this. But all the history we have – and there is a lot – demonstrates that all we have to do is wait. Waiting isn't easy, but we can do it.

Hang in there and have a great holiday season,

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.**