

WOOD & WHITE

Investment Advisors, LLC

Market Commentary 1st Quarter 2008

To our clients and friends:

The global stock market correction that began in late 2007 accelerated in the first quarter of 2008. The S&P 500 closed the period with a total return of -9.47%. The month of March represented the fifth consecutive monthly decline for the S&P, marking the longest monthly losing streak for the index since October of 1990. The Dow Jones Industrial Average dropped by over 1000 points, the largest quarterly point decline on record. The sell-off, which had been largely limited to the financials and consumer discretionary sectors in 2007, spread to every corner of the equity market as recession fears grew. All 10 of the major industry sectors tracked by Standard & Poors posted negative returns for the first quarter. Stock market pain was felt worldwide, as the once red hot Indian and Chinese markets each tumbled by more than 20%.

Unprecedented turmoil in the credit markets put considerable strain on the financial services sector, spurring the Federal Reserve to take extraordinary actions to restore liquidity and confidence to the financial system. The Fed cut short-term interest rates dramatically, slashing the Fed Funds Rate by 200 basis points, to 2.25% from 4.25% at the start of the year. Perhaps of greater significance, the Fed loosened restrictions on the types of securities that it will accept as collateral when providing short-term liquidity to financial institutions and, for the first time ever, opened the discount window to investment banks.

The Fed's efforts were not enough to save the fifth largest investment banking firm in the United States. Bear Stearns, a fixture on Wall Street for 85 years and a survivor of the Great Depression, fell victim to the mortgage crisis as its liquidity dried up in breathtaking fashion. Investor and customer confidence in the firm evaporated seemingly overnight, sending the stock - which had traded at over \$170/share in early 2007 - plummeting 95% in the space of three trading days. With Bear Stearns suddenly teetering on the brink of bankruptcy, the Federal Reserve and the Treasury Department intervened at the 11th hour, engineering a take-under by J.P. Morgan Chase at the staggeringly-low initial price of \$2 per share (which was subsequently renegotiated to \$10/share, still considered by most to be a steal of historic proportions).

We have endured a very difficult period of extreme market stress in recent months. Our clients' portfolios have been subjected to a pronounced increase in volatility in the stock and bond markets. In reflecting on this extraordinary chain of market events, we would like to take this opportunity to candidly assess our effectiveness in protecting our clients' assets.

What has gone well:

- **Asset allocation:** Asset allocation is the primary determinant of a given investor's potential investment return and exposure to risk. Bonds can be "boring" when the stock market is enjoying a prolonged, uninterrupted rise, but current market conditions have once again illustrated why having some high-quality bond exposure is important for almost any investor. Our commitment to maintaining balanced portfolios (both stocks & bonds) has afforded our clients better protection than we could have hoped to achieve from security selection alone.
- **Liquidity management:** Periods of extreme short-term volatility should only prove detrimental if an investor is forced to sell securities at depressed prices to meet liquidity needs. Whenever possible, we have ensured that our clients' portfolios maintain a sufficient level of liquidity and, when necessary, a stable income stream to provide for our clients' cash needs during unforeseeable periods of market stress.
- **Durability of our core holdings:** We do not attempt to predict extreme market events, but we do expend a great deal of effort in evaluating the strength and durability of our core stock and bond holdings. We believe that our core stock holdings are well suited to endure the current environment and emerge in a stronger leadership position when conditions improve. Further, our penchant for dividend paying stocks ensures that our clients "get paid" while they wait for an eventual recovery. Our bond portfolios are of sound credit quality and have weathered the recent bond market turmoil in good shape.
- **What we have not done:** We have never invested in mortgage-backed securities. Our aversion to large sector bets has protected our clients somewhat from an overexposure to the carnage in certain areas of the mortgage and specialty finance sectors. We do not employ leverage as part of our investment strategy.

What could have gone better:

- **Financials exposure:** Our equity performance has lagged in recent months, primarily because financials represent the largest sector weighting in our clients' portfolios. Our investment in this area reflects our belief in the long-term importance of dividend income and our recognition of the irreplaceable role that financial companies play in the global economy.
- **Mr. Market:** By any practical definition, we are in a bear market. Bear markets are a normal, necessary part of long-term investing. The circumstances surrounding each bear market are always different and are impossible to reliably predict. There is very little for a long-term investor to "do" about a bear market, other than remain patient, trust one's asset allocation and seek opportunities to upgrade the quality of one's holdings.

We do not know when conditions will improve, but our sense is that the Fed's recent intervention in connection with Bear Stearns' collapse may mark a near-term bottom for the stock market. Economic challenges abound and the global deleveraging process must run its course before a sustainable recovery can commence. We continue to expect volatility and scary headlines to rule the day in the near term. However, we believe that the significant stimulus currently offered by the Fed, along with the eventual reversal of extremely negative investor sentiment, should provide fuel for a powerful recovery in the future.

The Fed is delivering massive amounts of liquidity to the financial system in creative ways. Its demonstrated commitment to intervene and insure the stability of our financial system should help restore confidence to the markets over time. The Fed's willingness to allow investment banks access to the discount window is particularly important, as a significant portion of illiquid, mortgage-related securities are owned by investment banks and hedge funds.

Many of the assets currently held on the balance sheets of the major financial institutions are not actively traded and are difficult to accurately value. U.S. accounting standards require these assets to be marked-to-market to reflect a guesstimate of their current value. The marking of these assets in the face of the current credit market turmoil accounts for a significant portion of the current losses being reported in the sector. Given the current state of panic in the credit markets, it strikes us as highly unlikely that the current mark-to-market valuations being presented accurately reflect the long-term value of these assets. Further, the associated "losses" being reported as a result of this accounting distortion are likely fostering an overly-pessimistic view of the long-term earning power of certain financial institutions.

The turmoil in the credit markets will subside at some point. Whenever this occurs, we believe there is a high probability that many of these illiquid assets will enjoy a mark-up, providing a tailwind for reported earnings and allaying capital adequacy concerns among financial companies. Our exposure to high-quality banks and insurers should serve our clients well under such a scenario.

As always, we welcome your questions and comments at any time.

Sincerely,

WOOD & WHITE INVESTMENT ADVISORS, L.L.C.



Charles B. White, CFA



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