

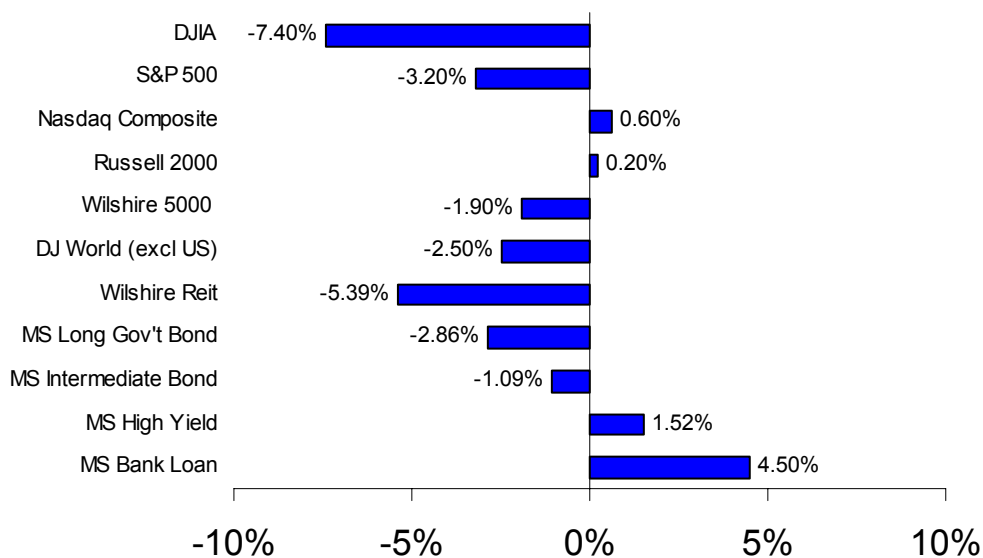
Second Quarter 2008 Investment Summary
Trinity Wealth Advisors
Values and Performance as of 6/30/08

Market Update

Financial markets struggled for a third straight quarter, as investors continued to sift through the lingering effects of the credit crisis, and increasing inflation concerns from higher energy and food prices. Stocks peaked in May after the Fed took steps to shore up battered investment banks including Bear Stearns last March. The markets were up nearly 9% in early May, before economic concerns grew and accelerated in June. The S&P 500 index fell 8.4% for the month of June. Overall the U.S. markets declined 2-4% during the quarter with the Dow Industrials down 7.4% due to their heavier concentrations in financials and auto stocks. Technology stocks (Nasdaq) and smaller stocks (Russell 2000) were slightly positive for the quarter, but had underperformed the broader markets at times prior to the second quarter. International stocks also declined during the quarter (2-3%) as many countries were dealing with inflation concerns and slower economic growth. Year to date, the U.S. markets and international markets are down 11-13%.

Bond markets showed some readjustments in the second quarter after investors moved aggressively into safer U.S. Treasuries in the first quarter. The Fed's actions to shore up liquidity alleviated investors' fears and a rally in the markets for higher yielding debt began. This is reflected in the negative returns seen in U.S. Government and intermediate bonds (down 1-3%) and positive returns for high yield (+1.5%) and bank loan debt (+4.5%). This trend began to reverse a bit in June as a shift back to higher quality bonds and government treasuries began when concerns magnified.

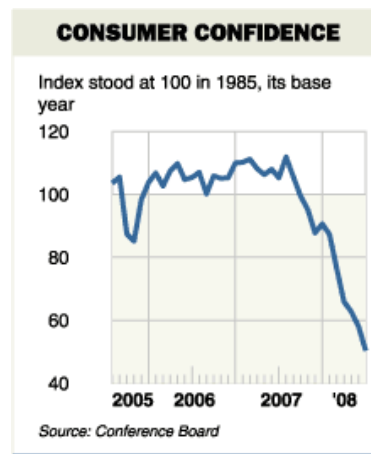
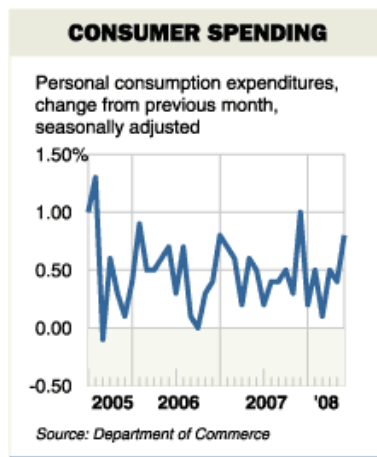
2nd Qtr 2008 Market Returns



Sources: Frank Russell Company, Standard & Poors, Wilshire Associates, Morningstar, Lipper, Wall Street Journal
 Past performance is no guarantee of future results

As the year began expectations were that a slowdown and possibly a recession would occur during the first two quarters followed by an improving financial sector and corporate earnings in the second half of the year. It now appears that GDP growth is likely to be positive in the first three quarters of the year, but the financial sector and corporate earnings will be slower to ramp up and may not be as strong as had been hoped until the fourth quarter. Equity analysts have reduced their forecast for 2008 earnings growth from 16% at the beginning of the year down to 8% currently

So far consumer spending and improvements in the trade deficit have kept GDP growth positive. If current forecasts hold up then economic improvements should start to unfold toward the end of the year. However, as resilient as the U.S. economy is, consumer spending is starting to show signs of weakness that could cause a change in growth trends. The combination of housing and financial sector problems, along with gasoline prices at more than \$4 per gallon is impacting consumers' discretionary spending in more significant ways. Recently, consumer confidence slumped to its lowest level in more than 16 years. If these trends continue to deteriorate then we could realize an additional slowdown more typical of a recession.



Inflation concerns have affected global markets as well. Global inflation rates are nearing 5.5%, up from 3.5% since the beginning of the year, thanks to soaring food and energy costs. Central banks around the world have begun to raise interest rates to stem rising commodity prices. The EU, Brazil and China have already tightened their monetary policy, and more than three quarters of the world's central banks have also tightened.

In times of crisis, global stock markets often move in sync. Money managers in Europe are starting to worry about an economic slowdown caused by the combination of elevated inflationary pressures, higher oil prices, strong exchange rates, weakening global growth and tight credit conditions. European recession fears grew as Denmark became the first EU country to slip into a technical recession. Italy, Spain, Portugal and Ireland are the most at risk of following Denmark into recession.

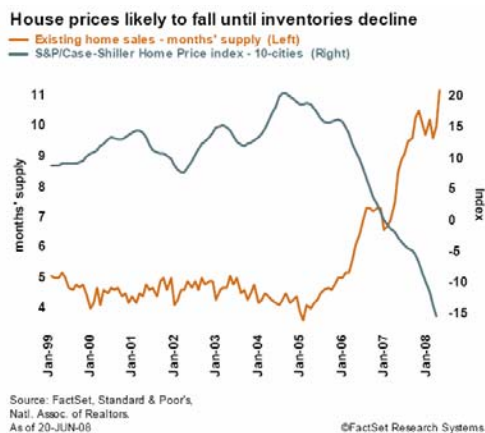
Much of the economic concerns are centered on two core problems affecting the consumer. Notably the housing and credit crisis that intensified last year, and inflation concerns due to soaring energy and food prices.

Housing and Credit Crisis

Housing figures suggest the real estate sector is still under pressure. Home prices in 20 major metropolitan areas were down 15% from a year ago in April. Prices are still worse in "bubble" areas,

with more stable conditions elsewhere in the country. Gasoline prices are beginning to reduce the desirability of housing in outlying regions.

We are seeing some glimmers of an end to the crisis, though a housing recovery may be some distance off. Construction of new homes fell 3.3% in May to their lowest level since 1991 which means that new supply isn't rapidly being added to the saturated housing market. Home lenders announced a more aggressive plan with homeowners who are having trouble making their payments. This could impact the numbers of foreclosures that continue to add unneeded inventory of homes on the market. Recent stronger than expected sales could indicate that bargain hunting is beginning, which would be a sign that we are approaching bottom. Sales of existing homes, which account for close to 90% of the combined sales, advanced 2% during May.



Presently, the mortgage crisis is dealing with the slow, steady wave of mortgage delinquencies and the erosion of value in the underlying homes. Additionally, the loss by bond insurers MBIA and Ambac Financial Group of their triple-A credit ratings has forced banks and brokerages to revalue or even unload assets those firms backed. Expectations were that write-downs would be done by the second quarter but it looks like it's going to be awhile longer.

The number of houses available for sale remains high, while foreclosures show few signs of abating. Housing continues to pose a risk to the economy due to the large unsold inventory levels which continue to put pressure on home prices to fall. Foreclosures rose to a record 2.5% in the first quarter and represent 27% of the inventory of unsold homes, up from 18% a year ago. Since it may take as much as a year for today's foreclosures to be placed on the market, this bloated inventory problem may be around for some time. Lower prices may be the quickest means to that end.

Oil and Inflation

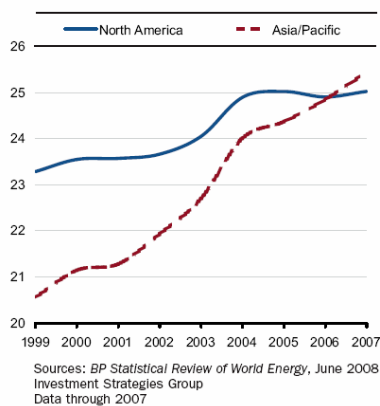
Oil prices continue to be a dominant factor in overall market sentiment. Over the past year, oil prices have more than doubled to \$140+ per barrel, and the increase is at the heart of many of the issues the market is dealing with at the present time. The oil rally is now bigger than the Nasdaq composite's run during the internet stock bubble, and the energy sector is now the second biggest by market value in the S&P 500 index, at 15.6%, three times larger than it was in March 2000. The financial fallout is hard to ignore and that's why Congress is holding energy hearings and considering changes in legislation designed to curb speculation.

There are many factors that have created the quickly rising oil prices. Supply concerns and geopolitical uncertainty has added a risk premium to oil prices. Demand has been on the rise until recently, especially in Asia, as Asia recently eclipsed North America as the largest consumer of oil. (see left chart below) The

dollar's decline has added to the cost as well. And speculation chasing the next "hot" theme has also pushed prices higher, making it difficult to ascertain when the expected correction may come. The amount of money that has flooded into commodity speculation is staggering and can be demonstrated in these two examples: 1) Investments in all funds tied to oil futures have risen to \$260 billion, from \$13 billion in 2003. 2) The total outstanding value of over-the-counter commodity derivatives rose from \$1 trillion in December 2004 to \$8.4 trillion in December 2007.

With total world energy expenditures relative to global GDP exceeding highs seen in the late 1970s (see right chart below), we expect today's oil prices to increasingly reduce demand. U.S. demand for oil has declined 2.3% compared to the same period in 2007. With economic growth around the world softening, we anticipate a parallel track of declining global demand for oil.

Exhibit 2 — A new world energy order in the making
(Regional oil consumption, annually, millions of barrels per day)



High oil costs poised to slow spending



World-wide, countries are making efforts to reduce consumption. Higher prices led some Asian nations to relax energy subsidies. Record oil and gasoline prices have prompted Americans to buy smaller and more fuel-efficient cars. Consumers drove less, as gasoline in the U.S. surpassed \$4 a gallon. Total U.S. vehicle miles traveled posted a 4.3% decline in March from a year ago, the biggest yearly drop since the data were first reported in 1942.

Global interest rates are starting to increase due to rising inflation concerns. The European Central Bank has recently increased their key lending rate by .25%. The Federal Reserve has focused on core inflation, which excludes food and energy, and has kept rates at the same level. Inflation in Asia is particularly high and many Asian central banks have begun to raise rates.

Some Positive Economic News and Perspective

Consumer spending growth is slowing, not contracting. Business investments are expected to add growth. Government spending is accelerating. And exports, which now impact our economy more than twice as much as residential construction, should continue growing. The slowing economic trends to date have been less than what is typical during a recession, yet the market is already priced 10% below current growth expectations. Improvements with oil prices or the housing market could quickly restore confidence in the U.S. economy. Speculation has been a significant contributor to rising oil prices. That could change quickly should global demand continue to slow or should legislation begin to put limits on the type of leverage or trading that can be done with particular commodities.

The U.S. Economy comprises 26% of the world GDP today. Recently revised global GDP expectations have been reduced to 3.5-4% for 2008. Whatever the final outcome, it is clear nothing like the new

“Great Depression” is at hand. While many fear a U.S. slowdown will drag the global economy lower, it has been global economic growth that has supported the U.S. through this period.

Stock valuations around the world are trading at a multiple of 13 times expected earnings for 2008. The last time global economies headed into a significant downturn in the earnings cycle (2000) the market was trading at over twice that level.

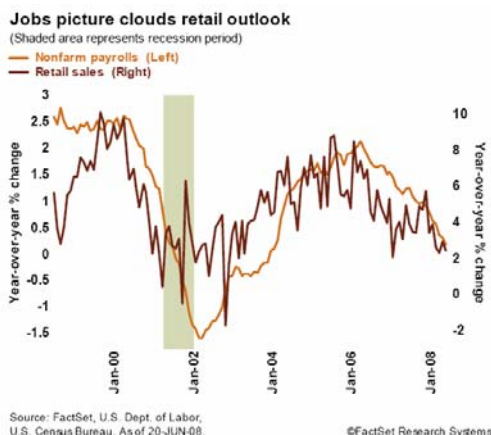
Global stock earnings yields remain above bond yields globally. This creates an environment for continuing to reduce stock supply. Larger firms can still borrow cheaply and acquire competitors for cash or buy back firm shares. 2008 has seen more than 3,000 mergers and buyouts totaling \$530 Billion, which is more than 2007 through June. Some of the larger transactions include: 1) InBev offers \$46.3 Billion for Anheuser-Busch; 2) Mars, Buffet buying Wrigley for \$23 Billion; 3) HP to Buy EDS for 12.6 Billion in challenge to IBM; These deals are being transacted in cash, which means stock supply will be reduced as these transactions are completed.

Investment activity is also being seen in the bond markets. May set a record for new investment grade bond issues, raising \$141 billion dollars. Companies with weaker credit ratings crept back into the market to issue new bonds after months of nearly no new deals.

Summary:

The third quarter will offer many distractions. The official presidential campaign heats up, and investors will be digesting specific proposals on issues that affect corporate profits, including trade, taxes, health care and defense spending. The problems that have plagued the market aren't expected to go away quickly. Financial firms are still raising billions in new capital to shore up their books and appear to be anticipating more uncertainty in the second half of this year.

Markets are bucking strong economic headwinds: tight credit markets, a slowing economy, high energy costs, and rising inflation. These are the four factors investment managers picked as most likely to affect equity performance during the latter half of 2008. The slowing of payrolls and spending in the chart below is evidence that this slowdown is significant but not inevitable to turn into a recession.



The consumer will be the determining factor of whether this economy will improve later this year, or whether we see a more extreme decline in spending and layoffs that could result in a recession late in 2008 or early 2009. Energy and home prices are likely to play a key part in what happens.

Jim Evens
Investment Director