The Lam Group
Investment Management

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The Big Picture: Air Bernanke
In a 2002 speech before becoming Chairman of the Federal Reserve Bank, Ben Bernanke famously suggested that, in a time of crisis, the Fed could drop money from helicopters to add liquidity to the financial system. With crude oil trading over $87, gold over $765 and the Euro/US dollar exchange rate solidly over 1.41, it doesn't take Radar O'Reilly (from the TV show M.A.S.H.) to tell you that the "choppers are in the air".

The primary casualty of the August injection of central bank-provided liquidity to the financial markets is the US dollar, and the resulting spike in commodities prices should come as no surprise. As the majority of commodities, such as crude oil, are paid for in US dollars, the further devaluation of our currency will have a negative effect on our country's purchasing power in a global context.

The lingering effects of subprime mortgage problems and further evidence of a slowdown in housing are likely to contribute to a more accommodative monetary policy in the coming months. This will likely further fuel inflationary pressures.

While the general stock and bond markets have also benefited from the Fed's August largesse, investors need to be mindful that in the presence of a weakening currency, a properly diversified portfolio, in addition to non-dollar investments must also include *real assets* such as commodities and commercial real estate to help preserve a portfolio's global purchasing power and to balance against inflation's corrosive effects.

How Much Purchasing Power Have We Lost?

Domestic Asset Classes	**2007 YTD**	**3yr***	**5yr***	**10yr***
S&P 500 Index (Domestic Large Cap Stocks)	+ 9.13%	+13.14%	+15.45%	+ 6.57%
Russell 2000 Index (US Small Cap Stocks)	+ 3.16%	+13.36%	+18.75%	+ 7.22%
Lehman Aggregate Bond (US Inv. Grade Bonds)	+ 3.85%	+ 3.86%	+ 4.13%	+ 5.97%
International Asset Classes	**2007 YTD**	**3yr***	**5yr***	**10yr***
MSCI EAFE Index (Int'l Large Cap Stocks)	+13.15%	+23.24%	+23.55%	+ 7.97%
MSCI EAFE Small Cap Index (Int'l Small Cap Stocks)	+ 6.62%	+23.58%	+27.56%	N/A
MSCI EMF Index (Emerging Markets Stocks)	+32.02%	+37.44%	+35.26%	+ 9.15%
Citigroup Non-$ Bond Index (Intl Bonds, unhedged)	+ 7.26%	+ 4.84%	+ 7.98%	+ 5.75%
JPM Emerging Markets Global Bond Index (EM Debt)	+ 3.54%	+ 9.73%	+14.76%	+ 9.30%
Real Asset Classes	**2007 YTD**	**3yr***	**5yr***	**10yr***
Wilshire REIT Index (US REITs)	- 4.64%	+19.63%	+21.88%	+12.80%
DJ AIG Commodities Index (Commodities)	+10.98%	+9.52%	+14.13%	+ 7.63%

* annualized returns as of 9/30/07

Real assets, when compared to financial assets, are tangible. For example, if you drop a real asset (such as a barrel of oil, a bar of gold, or an apartment building) on your foot, it will hurt; whereas a financial asset such as a stock or bond certificate will not.

Recent actions by our Federal Reserve to prevent further damage to the capital markets from subprime mortgages have essentially sent “helicopters” to blow cash all over the investment landscape, inflating asset prices and eroding the value of our currency. In this sort of liquidity whirlwind, real assets can anchor a properly diversified portfolio. History has shown that during periods of high inflation (as in the 1970s), real assets have meaningfully outperformed financial assets.

A weakening currency can be caused by excessive government borrowing (budget deficit), excessive liquidity (accommodative monetary policy), and/or importing more goods than exported (trade deficit). Any combination of these factors can lead to a “too much money chasing too few goods” scenario that is the definition of *inflation* in Economics 101.

While the US stock and bonds markets have enjoyed generally positive returns over the past 10 years, the corresponding international and emerging markets have done substantially better. A large component of this relative outperformance of non-US asset classes can be attributed to the weakening of the US dollar relative to other currencies.

	2007 YTD	**3yr***	**5yr***	**10yr***
US Dollar Index (DXY)	-7.09%	-3.83%	-6.17%	-4.36%

* annualized returns as of 9/30/07

It is worth noting that China has been slow to float their currency (the Yuan) against the US dollar. While markets are impossible to predict, there are some who believe that it is likely that the US dollar may decline further, especially after the Bejing Olympics. Why?

If China were to allow the Yuan to float freely, it would likely strengthen substantially versus the US dollar (and other developed countries currencies) and fewer foreigners would be able to afford to attend the Olympics in August 2008.

In addition to next year’s Bejing Olympics and our own Presidential election, the next 12 to 14 months will undoubtedly be volatile, unpredictable, and at times, breathtaking. In these exciting times, the importance of portfolio diversification and maintaining proper exposures to relevant asset classes cannot be overemphasized.

The Lam Group
Our portfolio strategy “tilts” our equity exposures towards smaller and more value-oriented stocks. History has shown that, while at times more volatile, small stocks outperform large stocks and value stocks outperform growth stocks.

These “tilts” are the cornerstone of our equity strategy and have served us well over the past several years. More recently in 2007, and particularly this past quarter, the small/value tilt has not outperformed the large/growth equity strategies and was central to our relative underperformance this quarter.

While markets are impossible to predict, particularly in the short-term, the historical data suggests that a small/value equity tilt is beneficial for long-term investors. It has been our policy not to chase large or growth strategies during times of relative short-term outperformance due to the corrosive effects of unnecessary capital gains taxes and transactions costs and our inability to consistently time markets.

The unpredictability of markets and increased volatility in the financial system argue more strongly than ever for a diversified and globally-balanced investment approach. We believe the market instability caused by the credit crunch in August of 2007 was temporary, and we remain firmly committed to our long-term balanced strategy.

The Lam Group continues to focus on designing and managing globally diversified investment portfolios and overseeing our client’s risks by only including investment asset classes which have low relative correlation in the context of an aggregate portfolio. Our asset allocation approach employs a highly analytical process to determine the appropriate combination of asset classes to build investment portfolios and strategies that realistically and optimally reflect the needs, risk tolerances, and investment horizons of our clients.

The Lam Group is an independent, fee-only, SEC-registered investment advisory firm with over $280 million in assets under management with clients in Oregon, Washington State, California, Connecticut, New York, and New Jersey. We offer both investment management and portfolio consulting services for taxable investors, family offices, foundations, and endowments.

The Lam Group will continue its policy of considering new clients on a referral-basis only with a $5 million initial portfolio minimum.

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Archives for The Lam Group Newsletter are available at our website: www.thelamgroup.com

Asset Class Investment Results:
All portfolios constructed and managed by The Lam Group are designed for an individual client's specific risk tolerances, income requirements and investment horizon. Our investment management approach includes the design of a customized asset allocation plan, the research and selection of the most appropriate and cost-effective asset class investments for the client's specific investment policy, and the on-going monitoring and disciplined rebalancing of the aggregate portfolio to optimize return, manage risk and minimize taxes.

As different clients have different goals, risk profiles and investment horizons, it is not useful to publish a track record of specifically-managed portfolios. The investment performance data below illustrate the returns of some of the actual mutual funds utilized by The Lam Group for specific asset class allocations in the construction of investment portfolios we manage.

Equity Asset Class Category	**3Q 2007**	**2007 YTD**	**3 Year Annualized**	**Correlation w/ S&P 500***
Domestic Total Equity Market				
-Wilshire 5000 Index (Total Dom. Eq. Market)	*+ 1.43%*	*+ 9.09%*	*+14.04%*	*+0.99*
US Total Market Fund	+ 1.54%	+ 9.18%	+13.91%	+0.99
Domestic Large Cap Stocks				
-S&P 500 Index	*+ 2.03%*	*+ 9.13%*	*+13.14%*	*+1.00*
Domestic Large Cap Value Fund	- 5.62%	+ 2.78%	+15.14%	+0.90
Domestic Small Cap Stocks				
-CRSP 6 -10 Index	*N/A*	*N/A*	*N/A*	*N/A*
-Russell 2000 Index	*- 3.09%*	*+ 3.16%*	*+13.36%*	*+0.82*
Domestic Small Cap Value Fund	- 8.59%	- 2.12%	+13.85%	+0.77
Real Estate Investment Trusts (REITs)				
-Wilshire REIT Index	*+ 1.42%*	*- 4.64%*	*+19.63%*	*+0.41*
REIT Fund	+ 1.52%	- 4.88%	+18.92%	+0.35
Real Estate Fund	- 3.12%	- 1.39%	+17.86%	+0.53
International Real Estate	+ 0.66%	+12.67%	+30.03%	+0.58
International Large Cap Stocks				
-MSCI EAFE Index	*+ 2.18%*	*+13.15%*	*+23.24%*	*+0.82*
International Large Cap Value Fund	+ 1.08%	+14.47%	+27.48%	+0.85
International Small Cap Stocks				
-MSCI Small Cap EAFE Index	*- 4.49%*	*+ 6.62%*	*+23.58%*	*+0.59*
International Small Cap Value Fund	- 2.35%	+11.28%	+27.63%	+0.48
Emerging Markets Equity				
-MSCI Emerging Markets Free Index	*+13.70%*	*+32.02%*	*+37.44%*	*+0.66*
Emerging Markets Value Fund	+10.49%	+41.79%	+45.99%	+0.66

* 5 yr correlation using monthly data

Fixed Income Asset Class Category	**3Q 2007**	**2007 YTD**	**3 Year Annualized**	**Correlation w/ S&P 500***
Domestic Investment Grade Bonds				
-Lehman 1-3 year Govt Bond Index	*+ 2.50%*	*+ 4.70%*	*+ 3.53 %*	*-0.23*
Short Duration Domestic Inv. Gr. Bond Fund	+ 1.31%	+ 3.82%	+ 3.40%	-0.16
Short Duration Domestic Muni Bond Fund	+ 0.98%	+ 2.62%	+ 2.30%	-0.20
-Lehman Aggregate Bond Index	*+ 2.84%*	*+ 3.85%*	*+ 3.86%*	*-0.14*
Domestic Investment Grade Bond Fund	+ 4.59%	+ 4.96%	+ 4.42%	+0.02
Domestic High Yield Bonds				
-CSFB High Yield Bond Index	*+ 0.05%*	*+ 3.74%*	*+ 7.48%*	*+0.42*
High Yield Bond Fund	- 2.71%	+ 4.25%	+ 8.00%	+0.50
Inflation-Linked Bonds				
-Lehman TIPS Index	*+ 4.54%*	*+ 6.35%*	*+ 4.03%*	*-0.21*
- Dow Jones AIG Commodities Index	*+ 6.24 %*	*+10.98%*	*+ 9.52%*	*-0.01*
TIPS Fund	+ 4.84%	+ 6.04%	+ 3.96%	-0.21
Commodities-Linked Fund	+ 9.91%	+13.22%	+ 8.85%	-0.08
International (non-US $) Bonds				
-Citigroup Non-$ World Govt Index	*+ 8.10%*	*+ 7.26%*	*+ 4.84%*	*-0.02*
Non-$ Bond Fund	+ 7.34%	+ 6.61%	+ 3.84%	-0.02
Emerging Markets Debt				
-JP Morgan EMBI+ Index	*+ 2.57%*	*+ 3.54%*	*+ 9.73%*	*+0.34*
Emerging Markets Debt Fund	+ 2.59%	+ 4.15%	+10.56%	+0.36

* 5 yr correlation using monthly data

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