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The Big Picture: The Randomness of Asset Class Returns
Following a difficult 4th Quarter in 2007, the 1st Quarter of 2008 was even more challenging, especially for the global equity markets. In these volatile times, portfolio diversification is essential.

With the broad equity indices (MSCI All-Country World) down over 9% for 1Q2008, portfolios with positions in commodities (up over 9%), domestic and international bonds (up over 2% and 10% respectively), and US REITs (up over 2%) experienced considerably less volatility during the quarter than less diversified portfolios.

Having the right ingredients in a diversified strategy is important, and recently, asset classes such as commodities and non-dollar bonds have been important contributors to portfolio performance.

Should investors buy more commodities and/or foreign currency-related assets now?

Probably not. While these specific asset classes have been on quite a rally of late, rallies never last as long as everyone would like, in the same way crises never last as long as everyone fears. Markets are impossible to predict.

Table 1 illustrates the annual returns for each asset class that we employ in our balanced and globally diversified investment strategy:

Table 1: Annual Asset Class Returns 1998 – 2007, 1Q2008

1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	1Q2008
28.6%	21.0%	-9.1%	-11.9%	-22.1%	28.7%	10.9%	4.9%	15.8%	5.5%	-9.4%
-2.6%	21.3%	-3.0%	2.5%	-20.5%	47.3%	18.3%	4.6%	18.4%	-1.6%	-9.9%
20.0%	27.0%	-14.2%	-21.4%	-15.9%	38.6%	20.2%	13.5%	26.3%	11.2%	-8.9%
5.4%	17.7%	-9.2%	-14.3%	-9.6%	57.8%	28.1%	23.9%	17.4%	-0.4%	-6.2%
-27.5%	63.7%	-31.8%	-4.9%	-8.0%	51.6%	22.4%	30.3%	29.2%	36.5%	-11.3%
-17.0%	-2.6%	31.0%	12.3%	3.6%	36.2%	33.2%	13.8%	36.0%	-17.6%	2.1%
8.7%	-0.8%	11.6%	8.4%	10.3%	4.1%	4.3%	2.4%	4.3%	7.0%	2.2%
0.6%	3.3%	-5.2%	5.8%	3.1%	27.9%	12.0%	2.3%	11.9%	2.7%	-2.9%
17.8%	-5.1%	-2.6%	-3.5%	22.0%	18.5%	12.1%	-9.2%	6.9%	11.5%	10.9%
-27.0%	24.3%	31.8%	-19.5%	25.9%	23.9%	9.1%	21.4%	2.1%	16.2%	9.6%
3.9%	2.4%	13.2%	7.9%	16.6%	8.4%	8.5%	2.8%	0.5%	11.6%	5.2%
-11.5%	24.2%	14.4%	1.4%	13.1%	25.7%	11.7%	10.7%	9.9%	6.3%	0.6%

Can you guess which asset class is represented by each color?

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Table 2: The Answers: Asset Classes by Color

Asset Class
S&P 500 Index (Domestic Large Cap Stocks)
Russell 2000 Index (Domestic Small Cap Stocks
MSCI EAFE Index (International Large Cap Stocks)
MSCI EAFE Small Cap Index (International Small Cap Stocks)
MSCI Emerging Markets Index (Emerging Markets Stocks)
Dow Jones Wilshire REIT Index (Domestic REITs)
Lehman Brothers Aggregate Bond Index (Domestic Inv. Grade Bonds)
CSFB Credit Suisse HY Bond Index (Domestic HY Bonds)
Citi World Govt Bond (Non-$ Bonds)
Dow Jones - AIG Commodity Index (Commodities)
Lehman Brothers US TIPS Index (Treasury Inflation Protected Securities)
JPM EMBI Global Debt Index (Emerging Markets Debt)

As you can see from Table 1, over the last 10 years, each asset class has had its day in the sun and periods of relatively stormy weather.

Table 3 ranks asset class returns over each of the last 10 years. This colorful presentation illustrates the randomness of asset class returns: a top performing asset class is as unlikely to maintain its relative superiority as a poorly performing asset class is likely to remain in the doghouse on a long-term basis.

Table 3: The Randomness of Annual Asset Class Returns 1998 – 2007, 1Q2008

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	1Q2008
1	28.6%	63.7%	31.8%	12.3%	25.9%	57.8%	33.2%	30.3%	36.0%	36.5%	10.9%
2	20.0%	27.0%	31.0%	8.4%	22.0%	51.6%	28.1%	23.9%	29.2%	16.2%	9.6%
3	17.8%	24.3%	14.4%	7.9%	16.6%	47.3%	22.4%	21.4%	26.3%	11.6%	5.2%
4	8.7%	24.2%	13.2%	5.8%	13.1%	38.6%	20.2%	13.8%	18.4%	11.5%	2.2%
5	5.4%	21.3%	11.6%	2.5%	10.3%	36.2%	18.3%	13.5%	17.4%	11.2%	2.1%
6	3.9%	21.0%	-2.6%	1.4%	3.6%	28.7%	12.1%	10.7%	15.8%	7.0%	0.6%
7	0.6%	17.7%	-3.0%	-3.5%	3.1%	27.9%	12.0%	4.9%	11.9%	6.3%	-2.9%
8	-2.6%	3.3%	-5.2%	-4.9%	-8.0%	25.7%	11.7%	4.6%	9.9%	5.5%	-6.2%
9	-11.5%	2.4%	-9.1%	-11.9%	-9.6%	23.9%	10.9%	2.8%	6.9%	2.7%	-8.9%
10	-17.0%	-0.8%	-9.2%	-14.3%	-15.9%	18.5%	9.1%	2.4%	4.3%	-0.4%	-9.4%
11	-27.0%	-2.6%	-14.2%	-19.5%	-20.5%	8.4%	8.5%	2.3%	2.1%	-1.6%	-9.9%
12	-27.5%	-5.1%	-31.8%	-21.4%	-22.1%	4.1%	4.3%	-9.2%	0.5%	-17.6%	-11.3%

This predictability of the unpredictability of markets is a strong argument for a disciplined portfolio rebalancing strategy in combination with a globally-balanced and diversified portfolio.

A regular rebalancing strategy focuses investors on a “buy low and sell high” framework for portfolio asset classes *regardless* of the uncertainties surrounding the economy, the outcome of the Presidential election, or the duration of the current credit crisis. This focus is critical to managing aggregate portfolio risk and optimizing overall investment return.

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The Lam Group: China
As many of our clients, friends and readers know, we spent the last two weeks of 1Q 2008 touring China (visiting Bejing and Xian as well as a cruise down the Yangtze River to see the Three Gorges Dam) in advance of attending the Harvard Alumni Association Global Conference in Shanghai. Our trip was inspirational in many respects and we received first hand exposure to many of the good and the bad aspects of the tremendous growth China is experiencing.

On one hand, China's population is enormous and its middle class is growing and consuming. This increased level of consumption will make their economy less reliant on manufacturing and export over the long run. On the other hand, China's growing environmental problems and labor issues will become significant factors in China's social landscape which will undermine the country's ability to continue as a global manufacturing powerhouse.

It is worth noting that the majority of our emerging markets equity exposure has been achieved with limited direct investment in China. As many emerging markets countries (such as Korea and Brazil) and developed countries (such as the US and Japan) have enormous business and trade with China, direct investment in China has not been necessary to benefit from China's extraordinary growth. It has always been our policy to take our international and emerging markets equity exposures in countries which have developed and relatively-sophisticated capital markets. We continue to believe China's capital markets are still in nascent stage and their policies on property right and contract enforceability have a long way to go before meaningful direct investments in China can be made. We will continue to monitor China's evolution as a country worthy of direct investment during these exciting times in the global equity markets.

The Lam Group continues to focus on designing and managing globally-diversified investment portfolios and overseeing our clients' 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 $265 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, and foundations. In 2008, we will continue its policy of considering new clients on a referral-basis only with a $5 million initial portfolio minimum.

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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.

All data is as of 3/31/08

Equity Asset Class Category	1Q 2008	12 Mo.	3 Year Annualized	Correlation w/ S&P 500*
Domestic Total Equity Market				
-Wilshire 5000 Index (Total Dom. Eq. Market)	*- 9.61%*	*- 5.82%*	*+ 6.45%*	*+0.99*
US Total Market Fund	- 9.46%	- 5.72%	+ 6.30%	+0.99
Domestic Large Cap Stocks				
-S&P 500 Index	*- 9.45%*	*- 5.08%*	*+5.85%*	*+1.00*
Domestic Large Cap Value Fund	- 7.68%	-12.00%	+ 5.89%	+0.93
Domestic Small Cap Stocks				
-CRSP 6 -10 Index	*-10.67%*	*-14.98%*	*+ 4.19%*	*+0.87*
-Russell 2000 Index	*- 9.90%*	*-13.00%*	*+ 5.06%*	*+0.86*
Domestic Small Cap Value Fund	- 5.88%	- 18.50%	+ 4.27%	+0.83
Real Estate Investment Trusts (REITs)				
-Wilshire REIT Index	*+ 2.14%*	*-18.83%*	*+12.03%*	*+0.51*
REIT Fund	+ 2.30%	-19.61%	+11.02%	+0.51
Real Estate Fund	- 6.36%	-17.05%	+ 8.09%	+0.72
International Real Estate	- 4.32%	-17.88%	N/A	N/A
International Large Cap Stocks				
-MSCI EAFE Index	*- 8.91%*	*- 2.70%*	*+13.32%*	*+0.83*
International Large Cap Value Fund	- 8.20%	- 3.65%	+15.98%	+0.87
International Small Cap Stocks				
-MSCI Small Cap EAFE Index	*- 6.24%*	*-11.19%*	*+11.15%*	*+0.67*
International Small Cap Value Fund	- 3.66%	- 9.07%	+13.74%	+0.68
Emerging Markets Equity				
-MSCI Emerging Markets Free Index	*-11.32%*	*+18.90%*	*+26.27%*	*+0.67*
Emerging Markets Value Fund	- 9.51%	+22.68%	+32.25%	+0.73

* 5 yr correlation using monthly data

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All data is as of 3/31/08

Fixed Income Asset Class Category	1Q 2008	12 Mo.	3 Year Annualized	Correlation w/ S&P 500*
Domestic Investment Grade Bonds				
-Lehman 1-3 year Govt Bond Index	*+ 2.97%*	*+ 8.76%*	*+ 5.41%*	*-0.36*
Short Duration Domestic Inv. Gr. Bond Fund	+ 0.68%	+ 4.63%	+ 4.15%	-0.10
Short Duration Domestic Muni Bond Fund	+ 0.68%	+ 3.39%	+ 2.93%	-0.02
-Lehman Aggregate Bond Index	*+ 2.17%*	*+ 7.67%*	*+ 5.48%*	*-0.11*
Domestic Investment Grade Bond Fund	+ 3.32%	+10.81%	+ 6.54%	-0.16
Domestic High Yield Bonds				
-CSFB High Yield Bond Index	*- 2.90%*	*- 3.23%*	*+ 4.89%*	*+0.67*
High Yield Bond Fund	- 2.39%	- 2.59%	+ 4.07%	+0.60
Inflation-Linked Bonds				
-Lehman TIPS Index	*+ 5.18%*	*+14.54%*	*+ 6.75%*	*-0.18*
- Dow Jones AIG Commodities Index	*+ 9.61%*	*+21.80%*	*+12.10%*	*+0.05*
TIPS Fund	+ 5.54%	+14.85%	+ 6.73%	-0.18
Commodities-Linked Fund	+14.38%	+34.08%	+14.15%	-0.03
International (non-US $) Bonds				
-Citigroup Non-$ World Govt Index	*+10.93%*	*+22.31%*	*+ 7.40%*	*-0.01*
Non-$ Bond Fund	+10.05%	+20.21%	+ 6.37%	-0.01
Emerging Markets Debt				
-JP Morgan EMBI+ Index	*+ 0.64%*	*+ 4.44 %*	*+ 9.64 %*	*+0.36*
Emerging Markets Debt Fund	+ 1.53%	+ 5.00%	+10.09%	+0.37

* 5 yr correlation using monthly data

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