STRATEGIC INVESTMENT PARTNERS LLC QUARTERLY COMMENTARY – JULY 2008

MARKET OVERVIEW

United States

Not since 2002 has the stock market delivered such a crushing blow. The first bear market in stocks in six years has finally crossed investors' paths. Bear markets, which are defined by a 20% drop in the major stock market averages, are unfortunately inexorable. Since 1960, there have been nine bear markets in total. Since that year, the average bear market has lasted about 14 months and has resulted in stock declines averaging 28% at the bottom. The mildest bear market took place in 1991. It featured a 21% drop in the major markets. Bear markets can be sparked by any number of problems -- inflated stock values, mounting inflation, rising interest rates, or a recession. The two largest on record took place during the 1970s and 2000s, and resulted in near 50% drops. The last bear market, which was due to the technology boom and bust, was due to overvaluation. This time, problems are related to three economic segments; housing, banking, and inflation. Record oil prices and rising commodities have taken a substantial toll on the U.S. consumer and sparked rising worries of inflation. At the same time inflation has perked up, U.S. economic growth is now slumping to near recessionary levels. Economic growth averaged only 1% in the first quarter of 2008. Growth expectations for the second quarter, even considering the economic stimulus checks, are also just over 1%. However, this anemic growth has not restrained inflation, as the price of oil and food stock continues to march upwards. Banks, usually a stalwart of our economy, are teetering with loan losses that are piling up faster than snow in Buffalo. Citigroup, one of the largest banks in the world, hit a 10-year price low in late June. The banking company has lost more than $180 billion in stock market value in the past eighteen months. The resulting crisis within our banking system has made credit harder to get for the average American, thus putting more pressure on the beleaguered real estate and housing markets. All this doom and gloom is showing up in the surveys that measure consumer confidence. One of the best followed surveys is the "expectations index" which looks ahead to quantify how consumers see their future. In June 2008, this index hit 41, the lowest it has been on record. Yes, at this point in time, U.S. consumers feel *more* hopeless about the future as they did in the days of the 1970s oil shock, in which gas was rationed, Watergate bloomed, Vietnam

U.S. Growth Leaders Portfolio Top-Ten Holdings

1) **Abbott Labs**
2) **Oracle**
3) **Schering Plough**
4) **Xilinx**
5) **Google**
6) **Novartis**
7) **Bank of New York**
8) **Accenture**
9) **Wells Fargo**
10) **Medtronic**

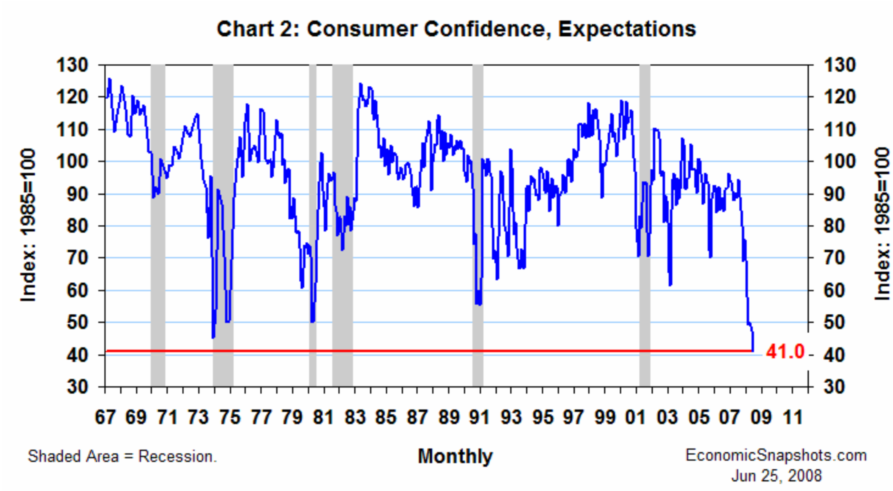
U.S. Value Leaders Portfolio Top-Ten Holdings

1) **Staples**
2) **ChevronTexaco**
3) **Johnson Johnson**
4) **ConocoPhilips**
5) **Wyeth**
6) **Microsoft**
7) **Amerisource**
8) **Merck**
9) **USB Bank**
10) **Hershey**

Global Balanced Portfolio Top-Ten Holdings

1) **Medtronic**
2) **Sanofi Aventis**
3) **Novartis**
4) **Microsoft**
5) **BP PLC**
6) **Abbott Labs**
7) **Teva Pharma**
8) **Schering Plough**
9) **Toyota**
10) **Mitsubishi Tokyo**

raged, and our own President of the United States was about to be impeached. No doubt about it, in the summer of 2008, gloom and doom are thick enough to cut with a knife. This gloom can be primarily attributed to the price of oil. Three of the four previous lows in consumer confidence occurred when oil prices had soared; 1974, 1991, and today. Additionally, food price acceleration has also added a layer of aggravation to consumers' sour sentiment. After nearly two decades of low food inflation, prices for staples such as bread, milk, eggs, and flour are surging at double-digit rates. Milk prices, for example, increased 26 percent over the past year. Egg prices jumped 40 percent. But wait a minute! Perhaps I can give you, our clients, a lifting of your spirits. All this news is disheartening and worrisome, true. But in stock market analysis, investor and consumer sentiment is considered a *contrary* indicator. That is, confidence is always at an extreme of optimism at economic and stock market tops. At major stock market lows, sentiment is always at extreme negative levels. An examination of history will prove my point.



Let's look back at the three previous episodes of dreadful consumer sentiment. Each was accompanied by a dramatic fall in the stock market to bear market levels. First, March 1974. The year presented the second lowest expectations confidence reading on record (chart 2). Over the next twelve months, consumer confidence remained low and did not break the 60 level until later the following year. However, although confidence remained low throughout 1975, the stock market leapt nearly 30 percent. The second period when confidence fell below a 60 reading was in April 1980. The year also had a recession that was brought on by credit controls aimed at restraining inflation. Consumer confidence turned up rapidly in 1981 as Ronald Reagan implemented his economic programs. In the next 12 months, the stock market rose 25 percent. The third time began in November 1991, when housing starts were down 27 percent over the previous two years and the savings and loan crisis broadened. Our country was also worried about the cost and the outcome of the Gulf War in Iraq. In this case, American victory in the war the following winter did not immediately do much to restore consumer confidence. While the consumer confidence numbers bounced around, they did not rise above 60 for good until November 1993. Nonetheless, the first year after the numbers fell that low, the stock market rose 18 percent. The question in 2008, or 2009, therefore, is not "if" the stock market will recover from the 20% drubbing, but when. Severe readings in consumer confidence always mark a low in the stock market within a six month time frame. This does not imply that we will turn around this summer or end up positive for the balance of 2008. We are skeptical of that.   But it does indicate, with a high degree of accuracy, that buying soon with a minimum two year horizon will almost certainly lead to outsized profits in the stock market.

Europe

The gloom was quite intense in Europe, with benchmark stock indexes in the United Kingdom, Germany and France each falling by single digits. These results pushed all major European markets into bear market territory. Germany's DAX stock index fell 1.8% for the quarter and is off 20.4% for the year. The U.K.'s FTSE 100 fell 1.3% for the quarter and is off 12.9% for the year. Big European companies like Siemens AG, whose shares are down 34% this year, and Unilever, down 27%, are among the casualties of falling expectations in Europe. Such large market declines around the world illustrate how far-flung financial markets have become correlated. As global investors have expanded their range, they have deepened the connection between various stock exchanges. The correlation of the major world stock exchanges has increased each decade. As the stock markets get more volatile -- as they have in the latest six months -- they have all tended to move in the same direction - down. One factor that has remained constant into the start of 2008 is the slide of the U.S. dollar. When overseas stocks were rising, the weakening dollar increased returns for U.S. investors, as profits were worth more converted back into dollars. Now it is cushioning the blow as foreign stock prices fall, because lower proceeds in foreign currencies still buy more dollars than they used to. Thus the returns to U.S. investors of European stocks have been better than those on the continent.   However, fears are mounting that a supercharged euro will make life more difficult for European companies that sell goods and services overseas. This could put further pressure on the shares of European stocks.   We have maintained our position in European stocks at 10%. We added one new European name this past quarter, National Bank of Greece.

Asia

We have shown concern for the Chinese stock markets for well over a year. Many of the region's stocks have finally succumbed under the weight of their own expectations. The Chinese stock market is now down an astounding 48% so far this year as higher raw-materials costs and a strengthening currency are squeezing profits. China's corporate profits were up 17.4% in the first quarter of 2008, compared to 49.4% profit growth last year. But this quarter, the number of unprofitable companies has more than doubled, and they now account for 15.4% of listed Chinese companies. The profit declines were exacerbated by the fact that the bottom lines of many companies had been fattened by gains from their own stock investments.

Elsewhere in Asia, Hong Kong, Mumbai and Singapore stock markets dropped 21%, 34% and 15%, respectively, so far this year, while smaller markets like the Philippines, Vietnam and New Zealand have fallen 32%, 57% and 21%, respectively. Many of them added to a bad first quarter in the last three months. India took another big beating for the quarter. India was down 14% for the past three months, and for the year has declined over 30%. Double-digit inflation has spooked foreign institutional investors, who have pulled out more than $6 billion so far this year. One exception to all this carnage is Japan, where earnings have been strong and inflation tame. The Nikkei Stock Average rebounded strongly and was up 7.6% in the second quarter after losing 18% in the first quarter.

PORTFOLIO & SECTOR REVIEW

Morningstar Sector	2008 2nd Quarter Return	2008 YTD Return
Energy	14.91%	6.26%
Materials	4.19%	0.49%
Consumer Staples	-5.96%	-8.57%
Technology	3.32%	-12.56%
Consumer Discretionary	-7.27%	-13.06%
Health Care	-2.68%	-14.30%
Industrials	-11.40%	-15.36%
Real Estate	-1.68%	-18.03%
Telecommunications	-8.00%	-21.38%
Financials	-17.25%	-29.39%

Health care is a classic defensive sector. No matter how bad the economy is, the argument goes, people still get sick. And they'll pay for medical care before they'll pay for almost anything else. It has always been our thesis that an erudite investor will always have a strong position in this group. The performance of the sector over the past thirty years has been above that of all other sectors in the economy. But in 2008, something unusual has occurred. Healthcare is not the defensive stalwart in this market collapse. It is in the bottom half of all major sectors for performance, falling 14.3% year-to-date. Pharmaceuticals, normally the most defensive industry with the healthcare sector, has fallen on desperate times, falling over 16% in value in 2008. Managed care stocks, such as HMOs, are doing far worse, down 31% for the year through June 30, making it one of the worst-performing industries out of the 129 that Morningstar tracks. Why all the heartburn in healthcare? In pharmaceuticals, the pipelines of new drugs are scant. And post-Vioxx, the Food and Drug Administration (FDA) is unfortunately on new-approval lockdown. Last year, it approved the lowest number of new drugs (19) since 1983. Moreover, analysts also fear that if the Democrats sweep the elections in November, they'll ultimately limit price increases on medications. In managed care, rising medical costs have been cutting into these companies' profit margins, leading to some high-profile reductions in earnings forecasts. Such fears, combined with company-specific issues, have taken a major toll on top managed-care players. The industry's two largest companies, UnitedHealth Group and Wellpoint are down 38% and 45%, respectively, for the year.

Nonetheless, health care stocks could use some healing in the latter half of 2008. The sector is so bedraggled, top to bottom, that any good news could start a rally. We have been prudent with our health care selections, focusing more on biotechnology and medical devices in 2008. Several of our top holdings have faired well in the first half of the year. Abbott Labs, Gilead Sciences, Genentech, Wyeth, Medtronic, and Novartis are all positive on the year. As many of the top companies in the sector have fallen hard, we did add to our stake in healthcare as well, picking up the previously mentioned UnitedHealth Group and Merck to our list of positions in our value fund. Both are big turnaround stories whose shares are at multi-year lows. But each company does have merits we believe will serve a long term investor well. As for Merck, our attraction are two recently approved and launched drugs, Januvia for diabetes and the Gardasil vaccine against human papillomavirus virus. Both drugs represent market potentials of well over $3 billion and will maintain monopoly positions for several years. By 2012, we anticipate these products will generate over $8 billion in annual sales, representing roughly 35% of earnings and enabling Merck to more than offset an ongoing patent expiration cycle. We believe cost cutting also remains a core piece of the Merck story and we see operating margins actually improving by 2012 despite two major patent expirations (Fosamax, Cozaar). For UnitedHealth Group the story is a depressed valuation. UnitedHealth now trades at a price/earnings ratio of 7, about half of the overall market. The stock has collapsed from $70 a share to $26. Even if we project out a reduction in earnings of over 20% in the next two years, i.e. worst case scenario, UnitedHealth's stock will still be priced at less than 10 times earnings. We think this dominant HMO company can cut costs and re-price contracts to stabilize its earnings.

The technology sector has held up remarkably well during 2008. The sector was positive in the second quarter of 2008, rising 3%. The sector has been favored as the earnings of many large technology companies have not fallen off. Several companies we own in your portfolios had solid returns for the past few months including Accenture, Oracle, Google, and EMC. All had positive investment returns year-to-date. Accenture was one of the top performers in the portfolio, rising nearly 20% in the past three months alone. The company, which we purchased over three years ago, continues to dominate the technology service industry. The firm is very diversified, offering everything from management consulting to software application development to business process outsourcing. The scope of its industry knowledge (covering 17 groups, including auto, media, chemicals, and capital markets) also protects Accenture, as few rivals can challenge the firm as deeply in these categories. This domination has allowed the company to post above-average growth in the past few years. Even in a period of stagnant economic growth, Accenture actually raised their projections for 2008 earnings and revenue in June. Accenture and the always steady Oracle are our two favorite technology stocks for the rest of 2008.

The energy sector continues to excel in 2008. No doubt the $140 price of oil has greatly engorged the profits of the large energy firms. The sector returned 15% during the past three months and is now up 7% year-to-date. Most of all our energy stocks had double digit gains for the quarter including Schlumberger (up 24%), ConocoPhilips (up 22%), Total (up 15%), Transocean (up 12%), and BP (up 11%). When will this tremendous run in energy stocks stall? It is quite difficult to predict. We realize that the energy sector is approaching "bubble" valuations, but that does not guarantee that a major turn will come anytime soon. Just as technology stocks continued to rise in the late 1990s, energy stocks could carry on for quite some time. Predicting the actual top is impossible. The ratiocination behind our continued position in energy stocks, despite the rise in value, is simply diversification. Energy stocks provide an excellent buffer against inflation and economic chaos. Now, we have gradually sold out of energy firms as time has progressed and share prices have skyrocketed. Exxon was sold earlier this year as it went beyond even our most optimistic forecasts. We find it prudent to slowly sell into this feeding frenzy. Our value portfolio currently maintains a slightly below market weighting of 12% in energy, whereas the growth portfolio holds only a 6% weight in energy. We are content with our current positioning within the sector.

The financial sector, ah what a mess. It is the worst performing sector for the past month, quarter, year-to-date, year, and two year period. The monumental collapse of the sector is evident across the board. Banks are down over 50% as a group in the past year. Citigroup and Wachovia, two banking behemoths, are down 65% apiece. SunTrust and Capital One have fallen 55% each. Even American Express and Prudential, two of the most revered financial firms that have limited exposure to the housing market, are down 38% each. The list goes on and on. Unfortunately, we have purchased some of the above companies with the best of intentions, but with a limited degree of success in regard to timing. Although we did not buy at the top, we also did not catch these stocks at the bottom. One item of conviction is these listed financial companies will not go bankrupt. This is a certainty after our Federal Reserve Bank stepped in to save investment bank Bear Stearns earlier this year. This assured us that our government will not let a major financial company fail. Despite this salvation, it does not guarantee against another round of price depreciation. This is the gray area we are dealing with. We know that there is tremendous value within the financial sector. The unknown is how many of their loans will actually go bad over the next couple of years. Despite our nervousness, we have slowly put capital to work in the financial sector. We have generally focused on what we believe are market leaders that have the best chance of a quick turnaround. The two financial firms we purchased during the past three months fit this pattern; Wells Fargo and National Bank of Greece. We purchased Wells Fargo in May and National Bank of Greece in June. Wells Fargo is considered one of the top three managed banks in the U.S. In reviewing key financial statistics, Wells Fargo sets the standard in many areas. The bank is the nationwide leader in accounts per customer. Currently, the bank averages 5.6 different accounts per customer in its retail bank. This allows the bank to maintain a high level of customer retention and also the ability to attract a substantial amount of low-cost deposits. Low cost deposits allow Wells Fargo to maintain an average net interest margin (The dollar difference between interest income and interest expenses) of 4.9%, tops among all major U.S. banks. Charge offs on bad loans are also one of the industry’s lowest, at less than 1%. National Bank of Greece (NBG) is an unorthodox purchase in our growth fund. We have been eyeing this hidden gem for years, and with the price falling by 35% in the past few months, we felt it would make a great addition to the portfolio. This is a bank that is actually growing earnings and revenue at a double-digit pace, far greater than the average growth of a U.S. bank. The Greek bank also has scant exposure to the U.S. housing market. NBG is the largest bank in Greece with a network of 580 branches and a 33% market share in deposits. NBG is rapidly expanding its presence across southeastern Europe, principally through acquisitions. It now operates in Turkey, Romania, Bulgaria, Serbia, Macedonia, Cyprus, and Albania. NBG earned 36% of its profits abroad in 2007, which it hopes to increase to 50% by 2010. We applaud this strategy as southeastern Europe's demand for financial services is growing rapidly, and we think NBG management's experience give the bank the skills necessary to profit from this development. June financial results for the Greek bank were excellent, with nearly 20% growth in net income. Currently priced just below $9 a share, we think the bank’s share price can double within three years.

ECONOMIC REVIEW & OUTLOOK

The economic query at the mid-year point of 2008 is what should we fear most, inflation or recession? Although growth has been sub-par for the first half of 2008, at about 1%, it still is positive. Most economists had predicted a recession when we began the year. It was not to be the case. In examining the reasons the U.S. skirted a recession, one has to look no further than trade policy. With an open trade policy, U.S. exports have not only survived, but thrived. Multinational companies based in the United States, like the previously mentioned Accenture, have thrived as nearly half of their revenue and earnings are derived from outside the U.S. It is the growth from countries like China, India, Brazil, and Russia (so called BRIC countries) that have bailed out our nation. A recession is off the table as the greatest threat for our Federal Reserve Chairman, Ben Bernanke. However, a new sword of Damocles has come to the forefront; inflation. We have mentioned inflation as the largest menace in the past couple of quarterly client letters. It is our belief that inflation is dramatically understated by our government. The government reports inflation through its consumer price index, or CPI. But CPI understates food and energy costs, while counting the price drop of a computer as a major item. I don't think most Americans are buying a new computer each week. Chairman Bernanke understands this conundrum and is attempting to manage inflation expectations in the public arena. He knows the government cannot keep reporting CPI increases of only 3 and 4%, when the true cost of basic goods that people actually buy on a weekly basis is climbing by 5 to 6%. Thus Chairman Bernanke, in his closed door meetings with his fellow Federal Reserve Board members, is setting his sights on inflation. Inflation will play the largest impact in the outlook for economic growth in 2009. To slow down inflation, Bernanke can attempt to "talk up potential interest rate increases" or actually pull the trigger. But pulling the trigger would risk extending the housing slump and the credit crunch, and it would then lessen the chances for a solid economic recovery next year. There is also an outside chance that it might also push us into a full-out recession.

How much growth Chairman Bernanke is willing to sacrifice next year if he raises interest rates will depend on the seriousness of the inflation threat. And despite our own concerns, in general, economists are sharply divided over whether our government should lift rates to keep prices of oil and food down. Many believe the weak economy will slowly mitigate the soaring energy and food costs more broadly. Historically, economic slowdowns kill inflation because they depress demand, hammer the job markets, and keep higher wages from pushing up prices in an upward spiral. Other economists aren't so sure, and for good reason. This is not your ordinary inflation threat because globalization may have changed the economic rulebook. This time the pressures are coming from outside the U.S. The push is not only from oil, but also from a variety of commodities and other imports, and it is unlikely to subside soon. Plus, rapidly growing markets for U.S. exports are supporting domestic growth and limiting the inflation-dampening effects of the national slowdown. It's unclear whether the current period of weakness is sufficient to hold down the inflation spiral. Global inflation has already hit a nine-year high of nearly 5% annually, and it will rise further as the latest jump in oil prices works its way through world markets. Emerging-market economies are one of the biggest culprits to the inflation resurgence. Emerging markets, such as the BRIC countries, now account for half of world gross domestic product and provide a market for half of all U.S. exports. While the inflation fighters under Chairman Bernanke are preparing for the inflation battle, developing nations are still partying, with few signs that their monetary authorities are ready to take away the growth bowl. Growth in emerging markets, fueled by booming domestic demand in China and other hot economies, is zipping along at about 7%, with overall inflation in China is now running at more than 7%. With tight labor markets in nations like China and India driving up wages, it indicates a broad problem.

Inflation abroad is also pressuring U.S. prices via the weaker dollar and import prices. Imports now make up about 16% of America's domestic demand, double their importance in the early 1990s. Excluding petroleum, import inflation is running at 6.6% in May, the highest since records began in 1990. Imported raw materials aren't the only culprit. Prices of imported autos are up 3.1%, and those for all other consumer goods are up 3.6%, the fastest increases in more than a decade. Given these growing pressures, keeping inflation under wraps in 2009 may require an extended period of weak economic growth. If the housing slump rebounds before inflation is tamed, Chairman Bernanke will be forced to raise interest rates. This is what we believe will occur in 2009, interest rates will be climbing even higher. To prepare for a continuing problem with inflation, we have maintained our large position in the Profunds Rising Rates Fund (*benefits when interest rates rise*) as protection for your stocks and bonds. The economists' call for rising interest rates will not go down easily with the public. Not exactly what a new President will want during his opening year of office.

MARKET OUTLOOK

We expected 2008 to offer investors a challenging year. But we never imagined a bear market taking place. We thought the declines would be limited to 10%, as corporate profits were strong and interest rates tame. But the housing market has not recovered as expected and oil and energy prices have continued to rise. This has slowly eroded consumer confidence to an abyss and taken down the stock market with it. Although the previously mentioned consumer sentiment numbers are quite dire, we are not convinced the next few months will offer a quick turnaround. We do understand the longer term significance of such ominous consumer confidence numbers. We can say with a high degree of certainty that the stock market will do well over a one or two year period. But, we simply cannot ignore the lethal combination of problematic inflation numbers and grim housing statistics. As the Dow Jones Industrial Average has fallen over 10% in June alone (*the worst monthly June return since the Depression*), a rebound in July or August is highly probable. We have thus positioned your stock portfolios with a few new companies, and have purchased some positions in financial and healthcare in our hedge fund. But any bounce, we believe, will be short-lived. As the election approaches and inflation continues to rear its ugly head, we feel the stock market will continue to struggle until late this year. We have refigured our overall outlook for 2008, turning less sanguine about a positive market year. We will attempt to be opportunistic in adding and subtracting from positions to take advantage of both the ups and downs in the market.

We appreciate your continued trust and confidence. Please call with any questions regarding your portfolios.