

2008 INVESTMENT COMMENTARIES: 3rd Quarter, 2008 in Review

October 20, 2008

Dear Clients,

By now most of you have received your 3rd quarter statements from me and your Schwab September statements. Maybe you have looked at your statements, or maybe not, but I encourage you to open them and call me if needed.

I have been making changes all year to try to reduce the risk in your accounts. I have made some mistakes along the way that have not helped, but what I am most disappointed in regarding your investments is how some of the bonds have not withstood the problems on Wall Street and have gone down in value along with the stocks, although not quite as badly.

The two bond funds that have caused problems for me are Loomis Sayles Bond and PIMCO Developing Local Markets Fund. (Not everyone has had them in their accounts.) I sold the PIMCO fund in September because as a fund that invests in foreign government bonds, its returns are partly tied to the value of the U.S. dollar and partly tied to the credit wellbeing of other countries. This fund went from being + 5.5% on June 30th to being - 6.0% three months later. The other fund, Loomis Sayles, has been caught in the credit crisis and it is just a fact that corporate bonds are largely out of favor as institutional investors have shunned everything but treasuries. When there are more bond holders who want to sell their bonds than there are buyers, the prices go down and the values of the funds that invest in them go down. This is to be expected, but

in the years past, when stocks were down, bonds were usually up. Not this year, however. I have no plans to sell Loomis, but it is definitely causing me consternation since the bonds are what I usually use to provide portfolio protection for you. In the meantime, Loomis is paying a healthy dividend, the shares of which are being reinvested.

For most of you I have tried to add some downside protection by buying shares in various ProShares "short" funds, which go up when the markets they track go down. This strategy worked extremely well up until a week or so ago. For the past week, the stocks markets have gained value. However, I do not believe the increase in the Dow will last beyond this week, which is why I am keeping the "short" funds and staying with a lower percentage of stock funds. Should the markets continue up from today through the weekend, I will evaluate the situation at that time. If the markets do head south by the end of the week, I will probably see it as a sign that we are getting closer to a bottom and I will start to sell the "short" funds and buy regular mutual funds or exchange-traded funds to increase the equities in your portfolios.

Thank you for your business and your trust. I also appreciate the many phone calls to see how I am and, I'm guessing, just to make sure I haven't jumped off a bridge. I am here, frazzled, but I still make it to the gym three times a week which forces me to think of something other than the markets, even if it is for only 45 minutes at a time.

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