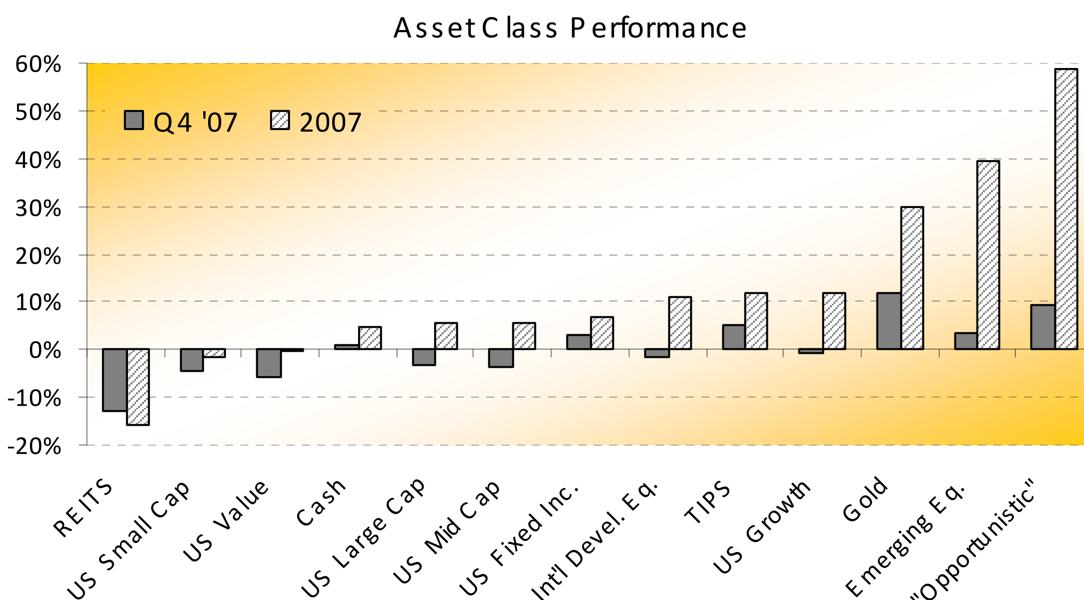
A Brief Look Back at 2007

Without a doubt, the investment topic of the year in 2007 was the subprime mortgage meltdown. No one can say they didn't see it coming, but the breadth and severity of the fallout surely were underestimated by most market observers. What began as an unwinding of excesses built up in a synthetic, specialized type of financial instrument broadened to a general credit crunch and general loss of appetite for risk.

Surging oil and food prices reignited inflation concerns while at the same time the Federal Reserve continued lowering short-term interest rates in an effort to ease the credit malaise and stave off a recession. The dollar plummeted against major currencies. The equity market reacted sharply to each piece of economic data, as it pushed the needle a-little-to-the-left or a-little-to-the-right on the recession-probability meter. Volatility skyrocketed, making daily swings of +/– 2%, 3% and even 5% the norm for equity benchmarks.

What Did This Mean for the Markets?

With all of this negative news, an investor might have expected a pretty dismal year from markets, but this wasn't the case across the board. Certainly there were areas of weakness: U.S. Value equities suffered in 2007 ending 7 consecutive years of besting the Growth benchmark; and U.S. Small Cap equities not only posted a negative annual return, but performed significantly worse than Large Caps for the first time since 1999. However, many other asset classes posted decent, if not significant, gains. In fact, the S&P 500 gained 5.5%, the MSCI EAFE index rose more than 11% in U.S. dollar terms, and the MSCI Emerging Market index soared almost 40%. The index of emerging BRIC countries (Brazil, Russia, India and China), which we define as an "opportunistic investment", rose nearly 60% in the year.



Copyright © 2008 Miracle Mile Advisors

Hindsight is 20/20

At the outset of 2007 many investors believed that the long, dominant runs of Value stocks and Small Caps were more than overdone, however many had said the same thing for several years running, and were wrong. Would anyone have predicted that in a year marked by volatility, a reduced tolerance for risk and a credit crunch, emerging markets would gain 40% with some of the riskiest "frontier markets" up more than double that figure?

One lesson to be taken from the year behind us is that past performance is no guarantee of future returns. Just ask your neighbor who gained over 20% per year in Real Estate Investment Trusts (REITS) from 2000 to 2006. Markets are predictably unpredictable, and the best course of action is to maintain a well-diversified portfolio that can smooth out the volatility inherent in a single asset class.

Looking Ahead to 2008

Deju Vu, All Over Again

What's in store for 2008? As is the case at the start of each year, it's impossible to know. There are a multitude of factors that will affect the markets in 2008, but the question is, to what degree? Will the Fed continue to lower rates? Will inflation pressures take precedence? Will slowing growth and the slumping housing market trigger a recession? Will exports be bolstered by the weak-dollar and help keep the economy in the black? What unknown problem is just around the corner in 2008?

Below we discuss some of the issues facing the markets in 2008. Regardless of how these issues play out in the months ahead, Miracle Mile Advisors believes that the best solution is to stay ***globally diversified***. We advocate maintaining broad exposure to the equity markets for growth, holding bonds for income and diversification, and carefully selected alternative and opportunistic investments for an enhanced risk-reward tradeoff. Here are our thoughts on the hot topics, and how we are investing for our clients in the year ahead.

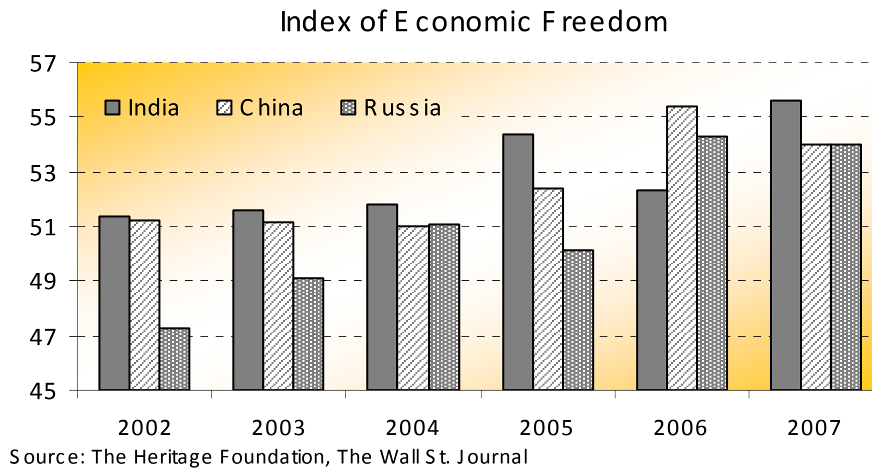
Emerging Markets

We believe that the strength we've seen in Emerging Markets has room to run.

- They held up remarkably well as the credit crisis took its toll on the western world. The debt products at the heart of the sub-prime mortgage crisis were largely absent from emerging market economies, and for once the baby did not go out with the bathwater.
- Thanks to technological improvements and more transparent markets, it has become much easier to invest and trade in emerging markets. New ETFs continually are debuting in the marketplace providing access to markets previously untouchable.

Copyright © 2008 Miracle Mile Advisors

- The much-hyped "emerging middle class" story in China and India has undeniable power. The sheer number of educated people coming into the workforce, acquiring wealth and investing it in their home countries will have a self-reinforcing, positive impact on these economies. Foreign investment in India *doubled* in 2007, hitting a record $17 billion, as global investors anxiously fed this growing domestic demand. The *Index of Economic Freedom*, published by the Wall Street Journal and The Heritage Foundation, is trending upward for these economies, reflecting their increasing accessibility and viability.



- China is on the verge of replacing the U.S. as India's largest trading partner. According to the Chinese Commerce Ministry, bilateral trade between the two countries increased 56% from 2006 to 2007, reaching $38.6 billion.

☑ We expect the "de-coupled" movement of developed and emerging markets and economies to continue. While we acknowledge that no global economy is immune to difficulties in the U.S., we look for emerging countries to maintain their superior market performance relative to the U.S. in year ahead. In particular, the "BRIC" countries (Brazil, Russia, India and China) have successfully lessened their degree of economic dependence, which should allow them to cope with disturbances in Western economies without disastrous domestic repercussions. We expect to shift some developed market equity allocation toward broadly diversified emerging markets to maintain capital growth in the portfolios. We favor index-like exposure to high growth economies to offset any potential regionalized market disturbances.

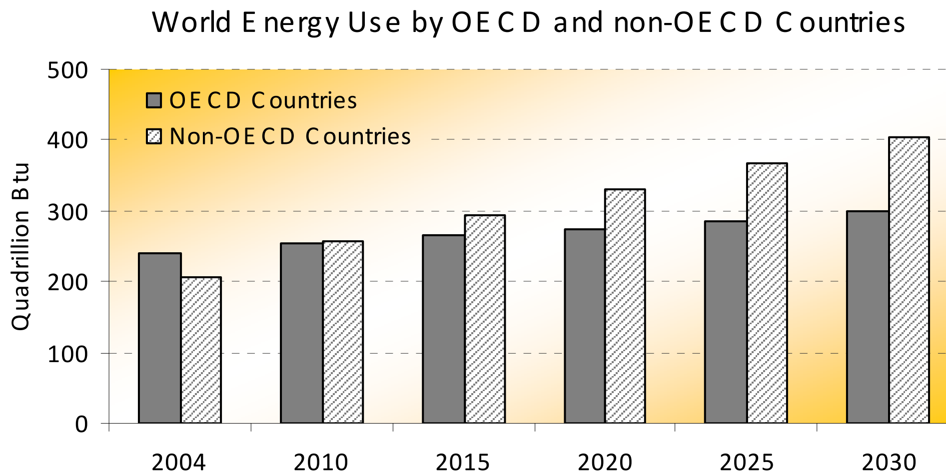
Oil

It's likely that we will see oil prices remain elevated even as the U.S. economy slows.

- Oil prices are determined by the overall supply/demand relationship like any other good. While growth and demand in the U.S. are falling off, global demand for oil is booming. According to OPEC, total world demand for crude oil rose by 1.5% (1.2 million barrels per day) in 2007.

Copyright © 2008 Miracle Mile Advisors

- Analysts at Cambridge Energy Research Associates (CERA) claim that oil in the ballpark of $100 "is an exclamation point for two major trends: the rapid rise of Asia and the shift in economic power to exporting countries." The industrialized nations of the OECD (Organization for Economic Cooperation and Development) actually reduced consumption during the same period that total world demand for crude oil rose by 1.5%. This growth is originating from countries like China, which alone increased consumption of crude oil by nearly 36% from 2005 to 2007.



- And what about the exporting countries? Between 1997 and 2007, six Middle Eastern OPEC member countries boosted production by a total of 2.5 million barrels per day. During the same period, these countries increased consumption by 1.9 million barrels per day, meaning that 75% of the production increase remained in the region. These countries are benefiting from increasing world demand, investing in local development and infrastructure, and thereby further stimulating demand for oil resources.

- Looking forward, the trends that boosted demand in 2007 are still intact. OPEC projects that in 2008, world demand for crude will rise an additional 1.3 million barrels per day. Of this increase, they project that non-OECD countries will account for about 80% of the total, with China alone responsible for 30%. Despite how Americans reduce their dependence on oil, either through slower growth lowering demand or through alternative fuel technologies, the rest of the world is more than taking up the slack.

- On the supply side, OPEC decided to keep production steady for the time being at their Abu Dhabi conference on December 5th. They did agree, however, to meet again on February 1st to re-evaluate their decision in light of the unfolding world economic situation and the impact of speculative market activity.

Copyright © 2008 Miracle Mile Advisors

- ☑ While the U.S. economy slows, the rest of the world, led by the emerging economies, will increasingly demand crude oil to fuel expansion. High(er) fuel costs will continue to affect American consumers at the gas pump and through the indirect cost of bringing goods to the marketplace. This reduces the amount of disposable income Americans have to pump back into the U.S. economy, potentially hurting domestic equity markets. This structural phenomenon could also direct more emphasis and funding toward developing alternative energy sources, and boost sectors of the economy focused on developing green technologies. We are exploring opportunistic investments in clean energy technologies and natural resources to enhance capital growth and provide portfolio diversification.

Alternative Energy

As world demand for energy grows, governments will direct funding toward alternative energy research. In the U.S., particular importance is placed on energy security and independence as the geo-political threat to oil supplies in the Middle East remains.

- There is an unprecedented amount of research and innovation in all types of energy-related areas, and given the current small percentage of energy considered to be "renewable" there is much room for growth.

- The base long-term scenario for Cambridge Energy Research Associates, which they call the "Asian Phoenix", estimates that demand for world energy will grow about 50% over the next 25 years. While much of that demand may be met by increased efficiency as well as conventional energy sources, the expectation is that renewable forms will become much more prevalent.

- The global Renewable Energy Policy Network for the 21st Century (REN21) states that global investment in renewable energy exceeded $100 billion in 2007, with about 2/3 of those dollars going toward added capacity. At least 58 countries have implemented targets for renewable energy use, including 13 developing countries and all EU member countries.

Growth Rates – Alternative Energy Production	
Wind	25-30%
Solar PV	50-60%
Solar hot water	15-20%
Biofuels	15-20%

Source: Renewable Energy Policy Network for the 21st Century, "Renewables 2007: Global Status Report". Growth rates for 2006.

Copyright © 2008 Miracle Mile Advisors

- ➢ Renewable energy is important not only for countries like the U.S., but also for countries like India, where inadequate traditional energy supplies cannot keep pace with demand growth, and millions of people are under-served by commercial energy sources.

- ➢ A growing awareness of climate change and environmental concerns has moved into the mainstream, and is even creeping into pop culture. NBC recently launched its "Green is Universal" campaign with an entire week dedicated to environmentally themed shows, including cameo appearances by former Vice President Al Gore. According to data from Ward's Auto, total reported sales of hybrid vehicles in the U.S. rose 36% year-on-year in December, despite the fact that sticker prices of hybrid models are typically thousands of dollars more than their gas-only counterparts.

- ☑ Out of both necessity and conscience, Americans are embracing cleaner, greener ways of life. Presidential candidates in both major parties are championing this trend, promising funds for research, development and deployment of alternative energies, energy independence, reductions in greenhouse gas emissions, and carbon-neutral construction. Regardless of the results of the U.S. Presidential election in November, we expect that environmental concerns will be a priority for the new administration. We are exploring opportunistic investments in clean energy technologies and natural resources to enhance capital growth and provide portfolio diversification.

The Presidential Election

We do not believe that the U.S. Presidential election will have a major impact on the broad market in 2008.

- ➢ Right now it's anybody's ball game, and with the primary season in full swing candidates are pandering to the extremes of their respective parties. At this point it's unclear what the priorities will become for the new administration. Candidates from both parties, however, are in some way embracing universal healthcare as well as environmentally conscious programs.

- ➢ "It's the economy, stupid" is *sooo* 1992. It hasn't been a major campaign issue. Not yet, anyway. The focus is on change, change and more change. That spells uncertainty, uncertainty, and more uncertainty so we'll have to wait for the national campaign to gear up before we can get a better idea of what to expect from the candidates' mainstream platforms.

- ☑ For those who remember the health care reform fiasco of President (Bill) Clinton's first term, don't rush out to make any bets on health care stocks just yet. We think the environmental play is a better bet, more consistently supported across party lines and more of a global issue.

Copyright © 2008 Miracle Mile Advisors

Inflation

Inflation is on the rise, and American consumers are feeling the pain. Investors need to protect against rising price levels in their portfolios.

- Soaring food and energy prices brought inflation in November to 4.3% year-on-year, as measured by the Consumer Price Index. As we discussed in our November publication, "What's the Story with Inflation?" these price increases are hitting consumers in their every day purchases of milk, gasoline and other basic necessities.

- The Federal Reserve continues to lower interest rates to ease the credit crunch, putting inflation concerns on the backburner. Domestic growth is slowing, but this is not the case everywhere on the global stage. Developing countries are driving world demand growth for oil, making it possible that elevated oil prices are here to stay for the foreseeable future.

- ☑ Gold, other commodities and Treasury Inflation Protected Securities (TIPS) serve as a defensive position against rising prices. At the end of 2007, we allocated the model weighting previously held in REITS to both TIPS and real assets, particularly gold. This change serves two purposes: First, it reduces exposure to real estate, which we think will remain depressed until well after the subprime issues are worked out of the markets. And two, it allows us to structure our model portfolios more defensively to protect against rising prices and the falling U.S. dollar.

Subprime Mortgage Crisis

The mortgage meltdown that reintroduced volatility to the markets took a hefty toll on investors during the second half of 2007. While the housing markets that were most inflated, like Miami and Southern California, took a hard and fast hit, there is still a good deal of unwinding to come in many areas of the country.

- It's not over. The aftershocks of the crisis have widespread implications not just for homeowners who have lost their homes, or even those just trying to sell in a dismal market. The subprime crisis has also shaken some of the biggest financial institutions in the world to their core, generating huge losses and major shakeups at the highest levels of management.

- Despite the toll the mortgage fiasco has taken on western financial markets, as discussed above, Emerging Markets held up surprisingly well.

Copyright © 2008 Miracle Mile Advisors

- The value of the so-called "teaser-freezer" bail out plan announced by the Bush Administration in December depends on perspective. It's a positive for homeowners who qualify for the interest rate freeze. Borrowers who received a mortgage between January 2005 and July 2007 and are facing an interest rate reset between January 2008 and July 2010 qualify for a rate freeze, subject to certain restrictions. It's too late, however, for borrowers who have already experienced an interest rate reset prior to January 1. From a free-market perspective, we believe that the plan is a negative. A bail out that restricts the housing market from correcting naturally could maintain artificially inflated prices, thus keeping some credit-worthy borrowers priced out of the housing market for an extended period of time.

- The U.S. is not alone. The U.K. and Canada are suffering from similar, if slightly lagged, scenarios of a bubble in housing, overextended borrowers, weakening currencies and slowing growth.

- From a contrarian perspective, maybe the worst is behind us. The American Dialect Society named "subprime" its word of the year in 2007. An article posted on the MSNBC.com website says that the sheer number of stories in the media about subprime mortgages has changed the word from adjective to verb status — loosely defined as the ability to completely dig one's self into a hole and then expect a bailout. For example, a high school student might say, "I completely subprimed my Algebra test yesterday. Instead of studying, I played Xbox, and just hoped the answers would come to me." Once something hits the popular media, chances are its days are numbered.

☑ For diversification, rely on investments in markets not unduly exposed to the continued unfolding of the subprime debt crisis and/or housing slump, i.e. not the U.S. and the U.K. We have reduced exposure to REITS, financial instruments designed to invest in the real estate market. Trying to time when it's safe to re-enter particular sectors such as Financials is risky. Maintain broadly diversified equity exposure.

The U.S. Dollar and Gold

The U.S. dollar is in structural decline. The Fed will continue lowering rates in the year ahead, which will keep downward pressure on the dollar. We do not expect a significant recovery in 2008.

- A weak dollar makes investments based in foreign currencies more attractive in U.S. dollar terms, boosting total returns for U.S.-based investors.

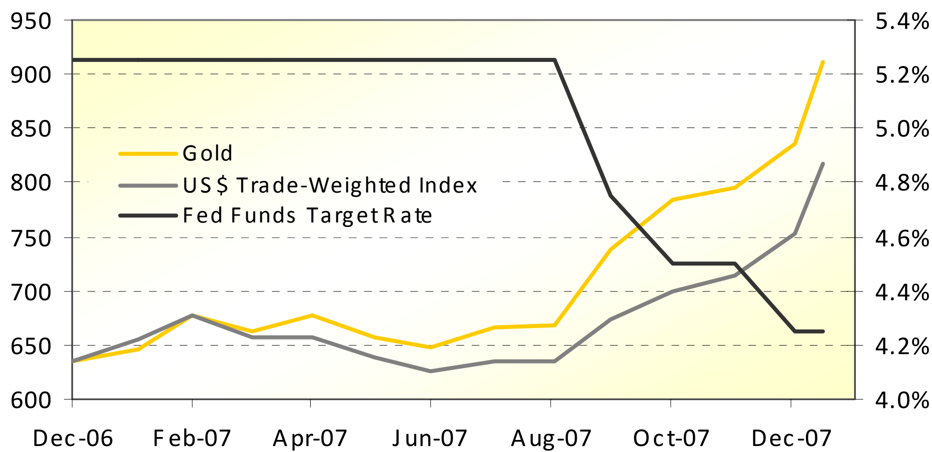
- A weak dollar also increases the attractiveness of U.S. goods abroad, which could help boost exports. Strength in this area of the economy could help mitigate the slow down in domestic growth.

Copyright © 2008 Miracle Mile Advisors

- Gold has surged as a type of alternative "currency" to the U.S. dollar. The metal is priced in U.S. dollars, and therefore is now much cheaper to buy in other currencies.

- Another tailwind for gold is the opening of gold futures trading on the Shanghai Futures Exchange as of January 10, 2008. Experts are calling this one of the most significant market events since the launch of gold ETFs several years ago.

☑ Investing opportunistically in country-specific ETFs provides both total return and foreign currency exposure. Another consideration is investing directly in currency-basket ETFs; however, we feel that this is a riskier path to obtaining non-dollar exposure. Gold is an excellent investment option, both as an inflation hedge and a defensive play against the falling dollar.



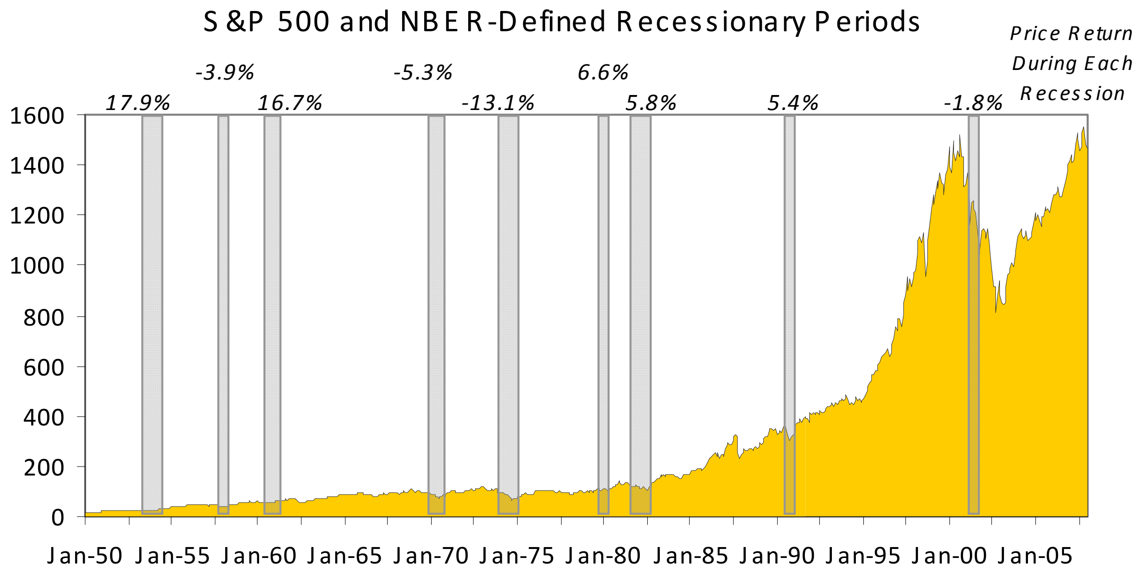
The U.S. Economy

Without a doubt, economic growth in the U.S. is slowing. But let's not get caught up in semantics. Whether it becomes a full-blown "recession", or remains a euphemistic "mid-cycle slowdown", the investment implications are the same: non-U.S. markets should outperform in 2008.

- Let's address the dreaded "r word" up front. We typically don't know that we're in a recession until after the fact. The official definition of a recession is two consecutive quarters of negative growth in GDP. And given the lag in reported GDP data, we would have to be well into the second quarter of a recession before knowing that a full quarter of negative growth had occurred. Federal Reserve Chairman Ben Bernanke acknowledged that when he was a member of the NBER Business Cycle Dating committee they wouldn't even try to determine whether a recession occurred until 6 months after the data was released and revised. As investors our goal is to position our portfolios to benefit from dislocations between expectations and reality, not position for what already happened 6 months ago.

Copyright © 2008 Miracle Mile Advisors

- Several decades ago, economist Paul Samuelson quipped that "the stock market has predicted 9 of the last 4 recessions." Behind this witty observation is an important point: The stock market is a poor leading indicator of the economy. Do we even care about predicting a recession? It doesn't always translate into simultaneous weakness in financial markets. There have been 9 NBER-defined recessions during the past 50 years, and during 5 of those the S&P 500 actually climbed, with an annualized average increase of 13% on a price-only basis. If we include the other 4 recessions during which the market fell, the annualized average return was still positive at 5%.



- Regardless of the label, we know that growth is slowing. Chairman Bernanke admitted that "incoming information has suggested that the baseline outlook for real activity in 2008 has worsened and the downside risks to growth have become more pronounced." He bluntly stated that the central bank was ready to act aggressively: "We stand ready to take substantive additional action as needed to support growth and to provide adequate insurance against downside risks." We expect that the Fed will cut the target interest rate a half a percentage point at its next meeting January 29-30. But it's important to remember that *changes in monetary policy impact the economy with a significant lag, possibly up to a year or more*. The Fed only began the current easing cycle in September, so it may take several more months before the effects of monetary stimulus take hold.

- The American consumer has been remarkably resilient during the current business cycle, reminiscent of Mark Twain's famous quote, "reports of my death have been greatly exaggerated." Perhaps this is because the wealthiest 20% of Americans, whose disposable income is less impacted by rising gasoline prices and higher mortgage rates, are responsible for 40% of consumer spending. While the combination

Copyright © 2008 Miracle Mile Advisors

of higher oil prices, reduced wealth from the weak stock market and falling home values are surely impacting the average consumer, there are still areas of support.

- Deteriorating labor market conditions are both a real and psychological threat to the consumer. The employment report for December showed that only 18,000 jobs were created in the month and the unemployment rate jumped to a two-year high of 5%. While this is still below the 5.4% average of the last 20 years, the trend is negative.

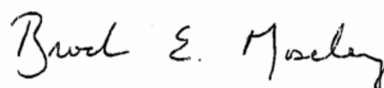
- The global economy has broadened and matured. According to the World Bank, 104 countries grew at a rate greater than 5% in 2006, which is a modern record. While it appears that most of them grew at a similar pace in 2007, the global economy is by no means immune to weakness in the U.S. It's inevitable that Asia's export-dependent economies will feel the slow down in U.S. consumption, but regional strength should help mitigate the impact. If these economies can successfully sustain growth without the U.S. as its main engine, this could signal a major shift in the global economic landscape.

☑ Whether or not we technically fall into a recession, we know that the U.S. is slowing. The goal is to identify the areas in the markets that are growing, and will not be dragged down by blanket weakness in the U.S. We believe that domestic growth in emerging countries will help maintain strength and those regions of the world other than the U.S. and Europe will absorb slack in demand. Non-dollar denominated assets are attractive for U.S. based investors, real assets should provide protection against the falling dollar and the possibility of inflation gaining traction. The housing market in the U.S. has more room to unwind, and we believe that real estate-related investments in western economies will languish for awhile longer.

Conclusions

Our major, long-term investment themes are strength in the emerging markets, capitalizing on weakness in the U.S. dollar, and preserving the value of capital against inflation in the U.S. Regardless of how and when these themes manifest, we believe that maintaining a broadly diversified, global portfolio of ETFs is the best way for individuals to achieve superior after-tax returns. Our monthly thematic research reports will continue to expand on our views, and provide a roadmap to navigate the opportunities we believe will make money for our clients.

January 15, 2008



Katherine Krantz
Chief Economic Strategist

Brock E. Moseley
Chief Investment Officer

Copyright © 2008 Miracle Mile Advisors

Disclosures

The views of Miracle Mile Advisors, Inc. ("MMA") may change depending on market conditions, the assets presented to us, and your objectives. This research is based on market conditions as of the printing date. The materials contained above are solely informational, based upon publicly available information believed to be reliable, and may change without notice. MMA makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in this report change.

MMA shall not in any way be liable for claims relating to these materials, and makes no express or implied representations or warranties as to their accuracy or completeness or for statements or errors contained in, or omissions from, them.

This report does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The securities discussed in this report may not be suitable for all investors. MMA recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives.

This report is not an offer to buy or sell any security or to participate in any trading strategy. In addition to any holdings that may be disclosed above, owners of MMA may have investments in securities or derivatives of securities mentioned in this report, and may trade them in ways different from those discussed in this report.

The value of and income from your investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in your securities transactions. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data.

The information and analyses contained herein are not intended as tax, legal or investment advice and may not be suitable for your specific circumstances; accordingly, you should consult your own tax, legal, investment or other advisors, at both the outset of any transaction and on an ongoing basis, to determine such suitability. Legal, accounting and tax restrictions, transaction costs and changes to any assumptions may significantly affect the economics of any transaction. MMA does not render advice on tax and tax accounting matters to clients. This material was not intended or written to be used, and it cannot be used by any taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer under U.S. federal tax laws.

The projections or other information shown in the report regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results and are not guarantees of future results.

Other Important Disclosures

Physical precious metals are non-regulated products. Precious metals are speculative investments and, as such, their value can be subject to declining market conditions.

Real estate investments are subject to special risks, including interest rate and property value fluctuations as well as risks related to general and local economic conditions.

Foreign/Emerging Markets: Foreign investing involves certain risks, such as currency fluctuations and controls, restrictions on foreign investments, less governmental supervision and regulation, and the potential for political instability. In addition, the securities markets of many of the emerging markets are substantially smaller, less developed, less liquid and more volatile than the securities of the U.S. and other more developed countries.

This report or any portion hereof may not be reprinted, sold or redistributed without the written consent of MMA.

Additional information on recommended securities is available on request.

Copyright © 2008 Miracle Mile Advisors