

INVESTING WITH DISCIPLINE

NEWSLETTER

SEPTEMBER 30, 2008

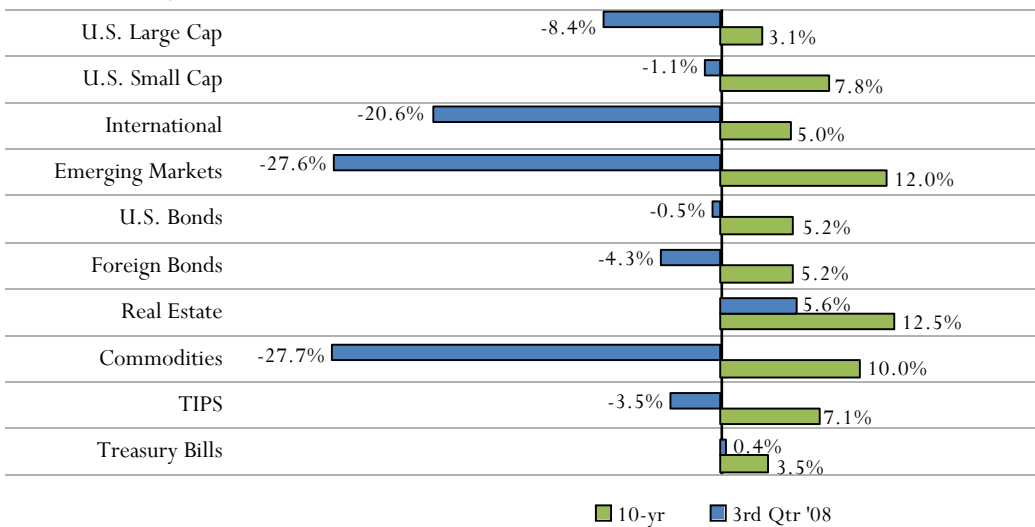
MARKET UP-DATE

The third quarter of 2008, and into October, saw a dramatic reversal of fortune for nearly all investment categories. U.S. Large Cap stocks lost nearly 20% while their international counterparts declined almost 30% through the end of September. Commodity prices plummeted as the world economy slowed. Gains made by REITs have been erased. Foreign bonds declined as investors fled to the only safe corner of the market, Treasuries, and as a result the U.S. dollar rallied.

The current environment was difficult for anyone to make money, from the smallest investor to the largest pension or hedge fund. Rather than become disheartened, we are sticking to our philosophy and investment plans.

Please visit the Archive section of our website to see additional charts and information about the previous quarter in our Quarterly Review & Outlook. Also, please read our quarterly article and other pieces of correspondence for greater perspective on the state of our investing world.

Performance by Asset Class



INDEX SCORE-CARD

QUARTERLY RETURNS

US Large Cap:	-8.4%
US Small Cap:	-1.1%
International Stocks:	-20.6%
Emerging Markets:	-27.6%
US Bonds:	-0.5%
Foreign Bonds:	-4.3%
REITs:	5.6%
Commodities:	-27.7%
TIPS:	-3.5%
Treasury Bills:	0.4%

All data as of the period ending
09/30/08

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WIT & WISDOM

"Look at market fluctuations as your friend rather than your enemy; profit from folly rather than participate in it."

- Warren Buffett,
a legendary long-term investor

QUARTERLY TOPIC: BACK TO BASICS

Winston Churchill once said, "If you are going through Hell, keep going." Right now our financial markets are making a heated and uncertain journey through unknown territory. As they struggle to function normally, we are faced each morning with dire headlines and predictions. Perspective is very difficult to have in the midst of a crisis. But that is exactly what is needed – perspective. This, along with a healthy dose of patience and a return to basic investing principals, will help investors "keep going."

First, how did we get here? At the most basic level, financial companies and individuals borrowed too much and had too little in reserve for a rainy day. When air began to leak out of the housing market bubble and unrealistic expectations that home prices always go up rapidly proved false, all parties were caught off guard. There are many nuances to this story. However, the bottom line is this – prosperity bred complacency.

Complacency has been washed away and replaced by austerity and extreme conservatism. Banks are in the process of reducing their leverage (debt) and rebuilding that boring rainy day fund (capital reserves). Consumers nationally are starting to reduce their spending and refocus on paying down debt and saving more. This shift occurs in every downturn, but the process is painful and is causing the financial system to freeze. The Feds are attacking the problem on various fronts to ensure basic lending, the lifeblood of our economy, keeps flowing while a more solid foundation is laid for our economy's future.

In the meantime, investors in all markets (stocks, bonds, foreign, and domestic) are participating in an unpleasant journey through bear market territory. The danger of veering off course could not be greater, nor the

consequences more severe. Let's revisit some investment basics to help stay focused:

First of all, trying to time the markets is a losing proposition. There are reams of data to demonstrate that even seasoned pros have great difficulty buying & selling frequently to outperform a simple buy & hold approach. In fact, more fail at the task than mere chance suggests. To avoid market timing and the emotions prevalent during market declines, it is crucial to have (and follow) a written investment plan. We have one for each client. The discipline it imposes means we are buying stocks in market troughs, not at market tops.

Second, cost still matters. Low mutual fund expenses keep more money in your portfolio. Those savings are crucial when returns are scarce, and when the market recovers the savings compound in your favor.

Next, diversification reduces risk and helps capture return. The collapse of Lehman, Bear Stearns, and Enron lead to complete loss for their shareholders. Yet mutual funds who owned those stocks were hardly affected. At the portfolio level, diversifying across many asset types allows us to capture returns without the need to forecast which market will be the next top performer.

Finally, everything has a cycle. Our economy and the markets will eventually find equilibrium and then recover. For long-term investors, potential returns today are much better than they were just a year ago. Bond yields are higher, stock valuations are lower.

We are quite likely in for more of a tumultuous journey. Time is needed to heal the wounds to our global economy. However, patient and calm investors who "keep going" will be rewarded.

Regards,
Brian J Lawrence, CFA

Index Definitions

US Large Cap: A U.S. large company stock index measured by the S&P 500. A group of 500 of the most widely traded stocks in the U.S., as chosen by Standard & Poor's.

US Small Cap: Measured by the Russell 2000. The index is comprised of the smallest 2000 stocks in the Russell 3000 Market Index.

International Stock: An international stock index measured by the MSCI EAFE. It is comprised of stocks from developed markets in Europe, Australia, Asia, and the Far East.

Emerging Markets: An international stock index that tracks non-developed markets throughout the world. It is measured by the MSCI Emerging Markets Index.

US Bonds: A measure of the Total U.S. Bond Market by the Lehman Aggregate Bond Index. It takes into account corporate, government, mortgage and asset backed securities.

Foreign Bonds: Measured by the Citi World Gov't Bond Index. The fund is comprised of primarily investment grade bonds from around the world.

REITs: Measured by the FTSE NAREIT Index which is a composite of Real Estate Investment Trusts traded on U.S. exchanges.

Commodities: Performance is represented by the PIMCO Commodity Real Return Strategy Fund, which uses the DJ AIG Commodity Index as a benchmark.

TIPS: Performance is represented by the Lehman Brothers US Treasury Inflation Protected Securities Index. TIPS are government bonds that have adjustable coupon payments based on the rate of inflation (as measured by the CPI).

Treasury Bills: Short-term government issued securities with maturities less than 90 days. Because they are government issued, T-Bills are free from default risk.

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