

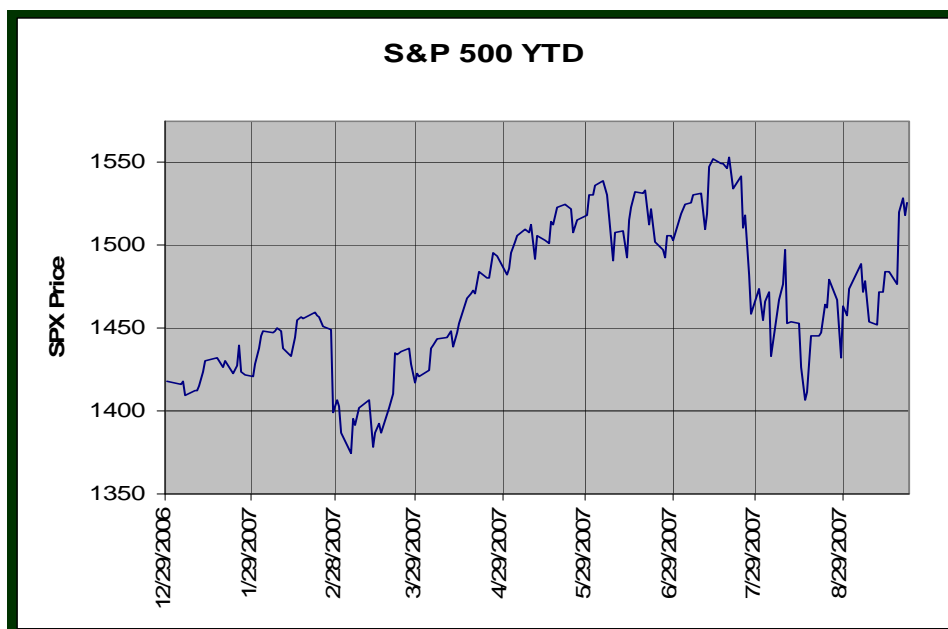


Third Quarter 2007 Market Commentary and Outlook

A confluence of events transpired in the third quarter culminating with the Federal Reserve cutting US interest rates by 50 basis points. This rate cut will most likely be a reputation making or breaking decision for its Chairman, Ben Bernanke, coming very early in his appointment. In addition, the rate cut will likely be a significant milestone in the current US economic cycle. We are 70 months into the current economic expansion, 13 months longer than the 57 month historic average expansion going back to the early 1940's. This decision may have been an even more significant milestone for the US dollar. While a bit nerve racking, the events (and volatility) experienced during the quarter should play right into the investment themes and asset allocations that we have established for our clients.

The Year Was Off to a Solid Start...

The market ended the 2nd quarter on solid footing. Any slowing in the US economy resulting from the growing glut of unsold homes was offset by continued demand from economies outside of the US. In our last letter, we discussed the continued global growth story and reviewed how Beaumont clients were positioned to benefit from this investment thesis. We also talked about the risks inherent in the fixed income segment of the market and the fear that this time the "sure thing" that would unwind would probably be found in that sector. While we were well positioned we did not see things falling apart as quickly and broadly as they did.



What Happened?

In mid July, panic struck the fixed income markets and a global credit crunch appeared almost over night. According to Morgan Stanley's Chief Investment Strategist David Darst, this time the proverbial "butterfly flapping its wing's over the African savannah was the City of Oakland, CA". Oakland decided to reduce its exposure to BNP Paribas Bank's asset backed commercial paper offering. These asset backed products were collateralized by mortgages and other structured fixed income products whose value were suddenly called into question with the growing number of sub-prime mortgage defaults. Unlike the US housing slow down, a credit crunch of this magnitude was a much larger threat to the global economy. Essentially banks refused to lend to each other, as no one wanted to end up holding the bad mortgages. With credit markets frozen, European banks like Sachsen in Germany and Northern Rock in the UK experienced "runs on the bank" as depositors lost faith in the soundness of the value of the assets on their books. To halt the credit crisis, Central Banks globally injected billions of dollars into the banking system to prevent commercial lending from coming to a screeching halt.

The longer term implication of these events is that we have hurt some of our best trading partners by selling them high risk investments. BMO Financial Group Global Portfolio Strategist Don Coxe described it this way:

"Once again, the great marketing skills of Wall Street have been demonstrated...they've been able to peddle off this toxic waste. If you actually looked at the US balance of trade in this sense, the US has been running a balance of trade deficit on BMW's and Mercedes but giving the Germans bad mortgages...Anytime you can get somebody to take this stuff off your hands and you can get high quality German engineering on the other side-that's a great trade".

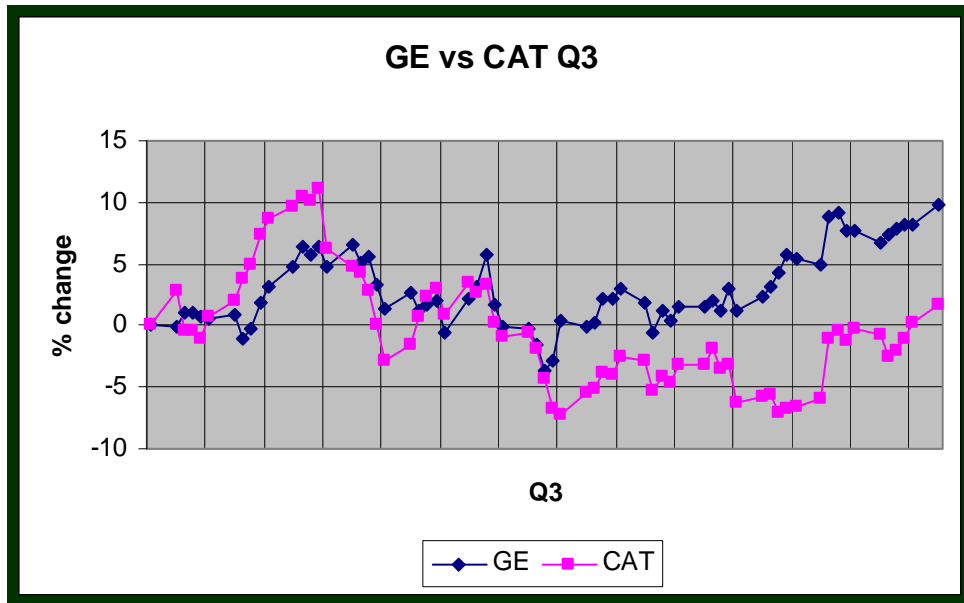
August Payroll Numbers Go Negative!

On top of this global lending crisis, the near term outlook for the US economy was called into question in September when the August payroll numbers came out with a significant disappointment. Consensus had been looking for a job creation figure of 100k, and instead there was an actual decline of 4k jobs. Up until this point there had been some debate about the need for the Federal Reserve to cut rates, this news removed any questions. With the September 18th rate cut the Fed essentially was sending three messages. First "we stand ready to do what we need to do"; second "perceptions count and we understand the importance of psychology"; and, lastly "the Fed is driving the Bus".

Initially, the Fed had taken a back seat to the massive (150 billion Euro) liquidity injection by the European Central bank. When I first read about this move I thought to myself, Bernanke must have read Tom Sawyer. He is letting the "new kid" paint the fence so to speak. I felt that Bernanke's handling of the situation showed tremendous composure and provided some badly needed political credits in the bank, especially with his European counterparts. However, the employment number "forced" Bernanke's hand.

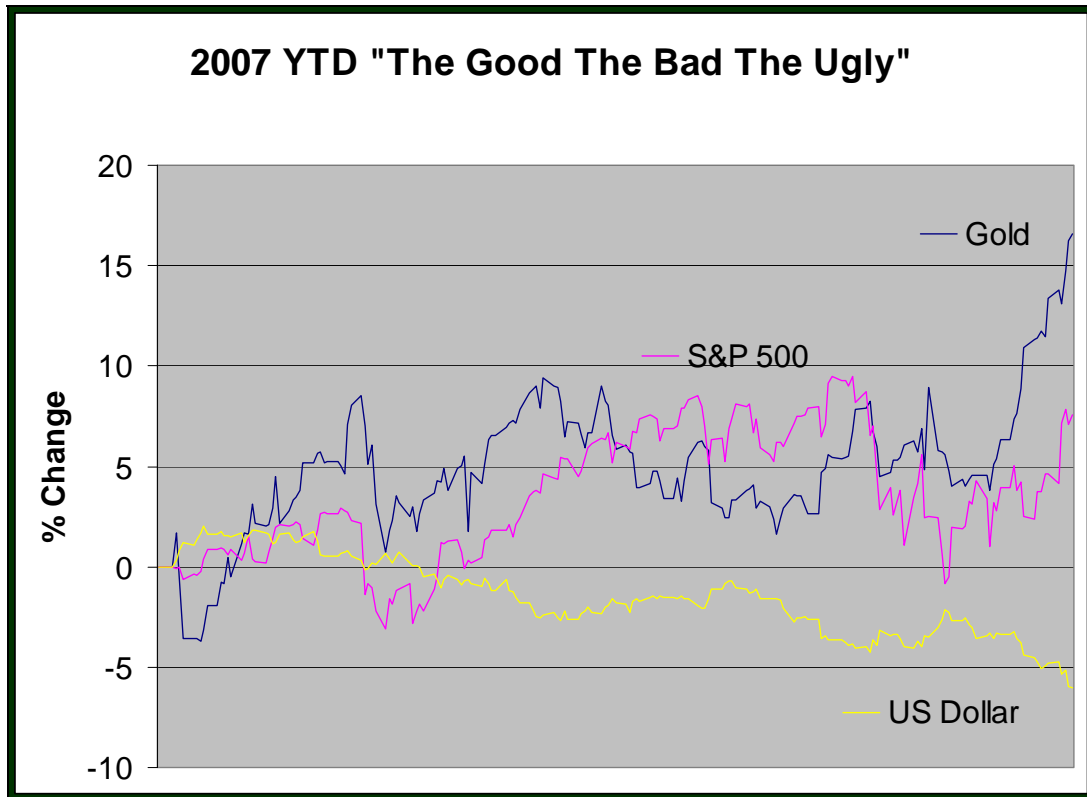
Rebound and Recovery for Many But Not All Asset Classes

As the third quarter came to an end, the credit markets have largely stabilized and the global equity markets have staged an impressive rally off of their mid August lows. We have made no changes to our asset allocation or investment approach. We continue to look for high quality, unexploited ways to participate in the global growth thesis. See below an update on our GE - (unexploited global growth name) vs Caterpillar - (fully exploited global growth name) trade. With the market shifting to companies with superior management, GE outperformed CAT by 8% during the third quarter.



Longer Term Implications for the Dollar

One asset class that has not recovered its luster during the quarter is the US dollar. The most recent spike in the price of gold is a very telling indicator. Gold has traditionally been the proverbial “Canary in the coal mine” anticipating inflation and global unrest. Wealth has and continues to exit the US dollar (traditionally the largest and most important fiat currency) favoring real assets. On a year-to-date basis Gold is up 17%, the S&P 500 is up 9% and the US dollar is down 6% relative to a trade weighted basket of currencies. What is this diverging picture telling us? We believe investors are saying that “the emperor has no clothes”.



Learn From the Fall of Rome, US Warned

David Walker, Comptroller General of the US, issued these comments: the US government is on a “burning platform of unsustainable policies and practices with fiscal deficits, chronic healthcare under funding, immigration and overseas military commitments.” Drawing parallels with the end of the Roman empire, Walker warned there were striking similarities, including declining moral values, an over-confident and over-extended military and fiscal irresponsibility by the central government.

How Are We Positioned to Deal with These Inconvenient Truths?

We feel it is important to communicate to you how we have positioned your accounts to capitalize on these trends. Risk and return objectives permitting, some examples include the following:

Non-Dollar Exposure

Franklin Templeton Hard Currency Fund – this is a predominantly non-U.S. denominated short-term government bond fund which provides shareholders exposure to high quality foreign government bonds while collecting a 3%-5% yield and experiencing the relative appreciation of the local currencies as they move up against the dollar. We remain confident that the U.S. dollar will continue to struggle over the next 12-24 months.

Energy

Energy exposure is provided in Arc Energy Trust, Enerplus Resources Trust, Peyto Energy Trust, Canadian Oil Sands and Suncor. These are all energy companies with long reserve lives ranging from 15-40 years that are domiciled in Canada. We have also recently added a Global Clean Energy ETF to many portfolios.

Gold & Precious Metals

In the aggressive equities segment of your portfolios you may see holdings in names including Aquila Resources, Petaquilla Minerals, Northern Star, Gammon Gold and the Central Fund of Canada. Compelling arguments made by Phil Dubuque (current portfolio manager of the Walnut Street Absolute Return Fund), suggest there will be continued strong demand for commodities from emerging markets. Chronic underinvestment has made and will continue to make these “consumable assets” more and more valuable. As Phil explains, with respect to precious metal stocks, the “store of wealth from in the ground reserves” will likely add significant value to these companies over time as many of these holdings are valued at significant discounts to the value of their reserves. In addition, during high inflationary period, gold typically appreciates in value as investors flee depreciating fiat currencies in search of wealth sustaining “real assets”.

Summary

Investing is driven by both near term and the long term factors. In the near term, it looks like the rollercoaster ride of the 3rd quarter has smoothed out as a result of the excellent hand holding done by the central banks globally. The longer term issue, specifically the direction of the US dollar, will now need to play out. How much damage has been done to the reputation and hence status of the dollar as a result of the third quarter events? Our opinion is that it has been significant and we have your portfolio positioned to benefit and take advantage of these developments.

If you have any questions or comments please contact us at 781-237-7170 or e-mail me at mstack@bfpartners.com.

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