

The Advantage Advisor

Volume 12, Issue 3

March, 2008

Market Commentary:

From its peak on October 9, 2007 through the first week of March, 2008, the Dow Jones Industrial Average fell by just over 16%. Over that same timeframe the S&P-500 fell by 17.4% and the NASDAQ Composite Index fell by 21.1%. There remains little doubt now that we are in a bear market.

Normally, a bear market is the result of a normal economic cycle that has moved through expansion to overheating, and then corrects through a recessionary phase. In this case, however, the major impetus for the decline in prices is a direct result of a sudden stoppage in the flow of credit.

Banks have become suddenly unwilling to lend to each other for fear that the borrower, known as the counterparty, might default on the transaction. This fear over counterparty risk has caused a virtual shutdown in many areas of the lending markets, and has rippled through the remaining financial markets in a sort of domino effect. Even the marketplace for government backed municipal securities has ground to a halt.

The US Federal Reserve is working furiously to try and relieve the strain in the credit markets and get things moving again. They are providing a coordinated effort through direct low rate lending to financial

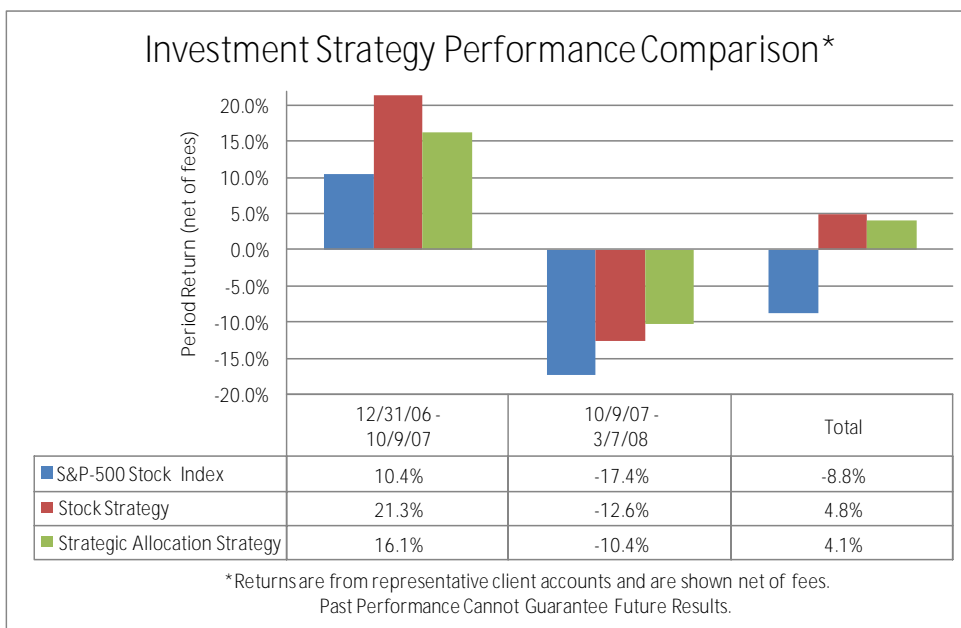
institutions, aggressively lowering the Fed Funds rate, and pumping liquidity into the financial system through open market operations.

Market Index	Closing Price	% Change
Dow Jones Industrial Average	12,266	-3.0%
S&P-500 Stock Index	1,331	-3.5%
Russell 2000 Stock Index	686	-3.8%
Shearson Treasury Bond Index	15,720	0.5%
Dow Jones World Stock Index	277	0.2%
Nasdaq Composite Index	2,271	-5.0%

These measures should provide the liquidity required to keep us out of an all-out crisis. However, it does take time for them to take effect, generally 6 to 9 months. In the mean time, our best course of action is to maintain defensive investment positions and be prepared to move swiftly once the markets do regain their footing.

So how are our stock based strategies weathering this bear market? The chart below compares our Stock and Strategic Allocation strategies with their market benchmark, the S&P-500 Stock Index. As you can see, from the end of 2006 up until the peak of the bull market on 10/6/07, the our strategies significantly outperformed their benchmark on the upside. In addition, from the

market peak until the end of the first week of March both strategies have lost significantly less than the benchmark. The net effect is that since the end of 2006, the Stock Strategy has outperformed the market benchmark by a stunning 13.6%.



The outperformance of the Strategic Allocation Strategy is equally amazing at 12.9%. That clearly demonstrates the benefits of an actively managed investment strategy.

The Economic Picture

Because of the continued slowdown in various measures of the US economy, we have moved our position fully into Stage 5 - Contraction. While the likelihood of two consecutive negative GDP quarters is still low, there can be little doubt that things have slowed considerably.

The US Fed is now fully focused on supporting economic growth and trying to minimize the impact of the credit crunch. As of this writing, the marketplace is predicting at least a 3/4% cut in interest rates at month-end, and is looking for a Fed Funds rate of less than 1.75% by late summer. That will create a situation where interest rates drop below the level of inflation, known as a negative Fed Funds Rate.

The last time we saw this was back in mid 2003, when Mr. Greenspan cut the Fed Funds rate to a mere 1%. The effects of that kind of stimulus on the economy were generally positive, but the beneficial effects in the financial markets were far more dramatic, pulling us out of the worst bear market since the depression.

The main concern with such low rates is, of course, a rise in inflationary pressures. Currently, most inflationary pressures are coming in the form of rising commodity prices such as oil, gas, and food. Core measures of inflation, which strip out the impact of food and energy prices, have held fairly steady.

Commodity prices have by and large become disconnected from supply and demand fundamentals. For example, on March 12, the report on Oil and Gas Inventories was released and showed a dramatic and unexpected increase in inventories. And we are not talking about small differences here - the increase in crude oil inventories was more than 3 1/2 times what was ex-

Current Economic Position:
Stage 5 - Contraction

Economic Indicators

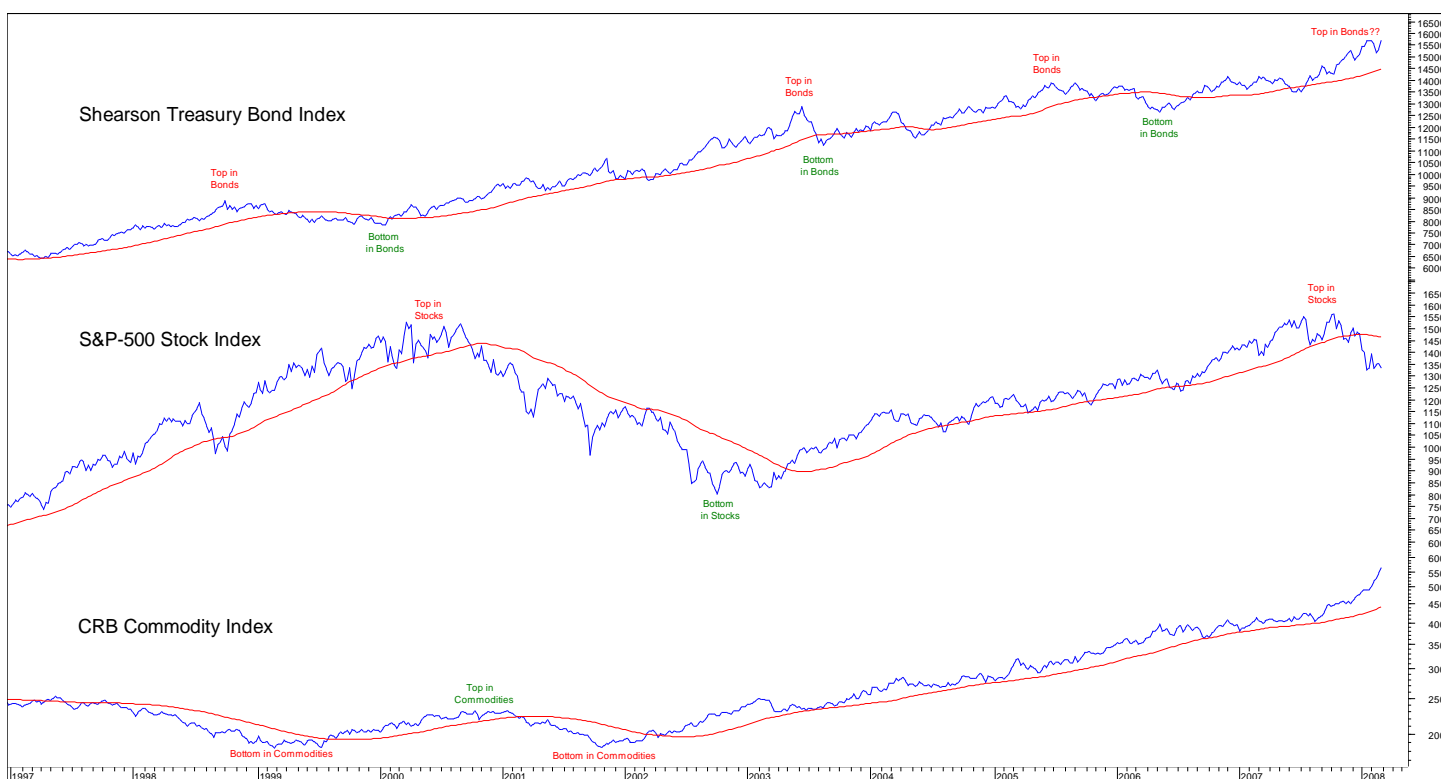
	<u>Latest</u>	<u>Prior</u>
Growth		
GDP	+0.6%	+4.9%
Productivity	+1.9%	+1.8%
Employment Cost Index	+0.8%	+0.8%
Capacity Utilization	81.5%	81.5%
Inflation		
Consumer Price Index	+0.0%	+0.4%
Core PCE Deflator	+0.3%	+0.2%
Implicit Price Deflator (GDP)	+2.7%	+2.6%
Sentiment		
Consumer Confidence Index	75.0	87.9
Unemployment Rate	+4.8%	+4.9%
Personal Income	+0.3%	+0.5%

↑=revised up, ↓=revised down

Source: Moody's Economy.com

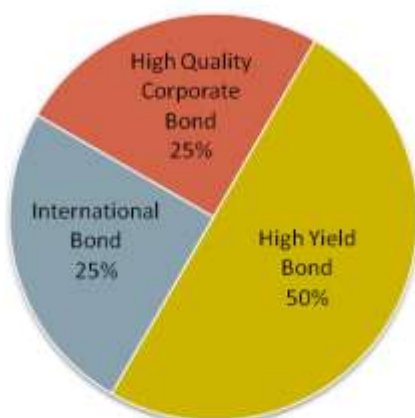
pected and the increase in gasoline inventories was almost 6 times higher than expectations. In normal markets, that kind of surprise would have driven oil and gas prices sharply lower, but we are not in a normal market. Instead, crude oil prices actually rose almost 1% following the report.

As a result of climbing energy prices, inflation expectations are starting to rise. This bears close watching because rising inflation expectations are the precursor to actual rising inflation. However, the CPI report released on March 14th posted a 0% change in consumer prices for the month of February. While one month does not make a trend, it is a welcome sign that consumer prices are holding steady and may cause inflation expectations to moderate as well.

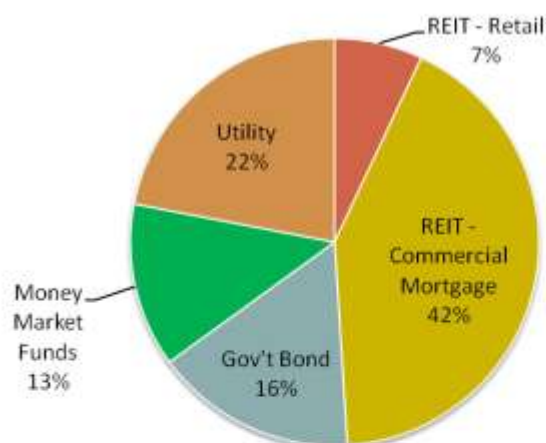


Current Investment Management Strategy Allocations

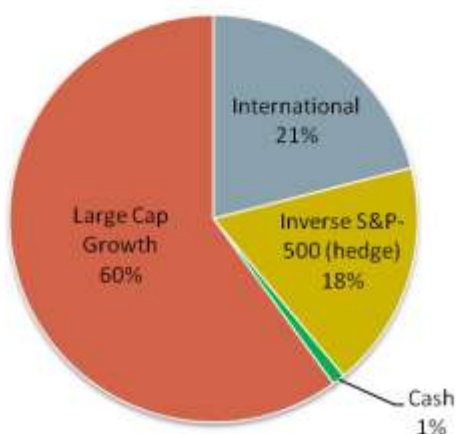
Bond Strategy



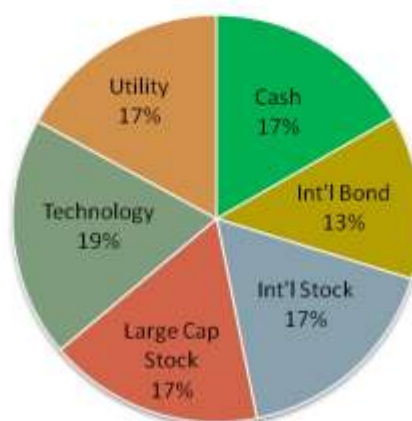
Current Income Strategy



Stock Strategy



Strategic Allocation Strategy



Investment Strategy Review

There has been no change in our investment strategy allocations over the past month. The current investment environment certainly calls for the defensive posture we hold across all of our portfolios. The Bond strategy continues to hold defensive positions in both international and high quality corporate bonds. The Current Income Strategy holds an overweight position in cash and we are monitoring events in the Utilities sector very closely for the need to employ any additional hedging there. The inverse (hedge) position in the Stock Strategy has seen some good appreciation as has the exposure to commodity producing companies. Those two positions

have actually risen in value even as the broad market has declined. Finally, the Strategic Allocation Strategy holds an overweight position in cash that we are ready to deploy just as soon as the markets show signs that they have indeed found their bottom.

Bear markets are tough to weather, but our defensive posturing has certainly allowed us to avoid the worst of the storms. For now, patience is the most important piece of our strategy. When the markets do find their bottom we are ready to act to take advantage of all the bargains that will be available.

Please note: A current copy of Advantage Investing's form ADV (registration statement) is available at no cost upon request. Please contact us at the address or phone number below if you would like to request a copy for your own records.