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MONTHLY

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EQUITY STRATEGY UPDATE

Introduction

Recently, in light of the volatile investment environment, we have received a considerable number of questions regarding our views on the equity market. Figure 1 shows how much the global equity markets have sold off over the last year. In this *Monthly,* we will review the recent past and look at how the decline in equity prices has affected our outlook and strategy.

Background

Many investors extrapolate near-term trends. A recent example of this behavior was seen in mid 2007. Investors expected the strong earnings growth experienced from 2003 through mid 2007 to continue well into the future. As we have written in the past, earnings growth can exceed economic growth for a period of time, but not forever. Consequently, our earnings expectations were much lower.

Extrapolation of near-term positive trends can cause investors to allocate capital into markets that have already priced in the good times. The reverse can also be true when fundamentals deteriorate and investors anticipate the environment will stay bad or get worse. This often leads to selling when prices have already fallen.

To avoid these pitfalls, we look through the cyclicality of the near-term trends and examine market prices against a longer-term, more stable backdrop. We do not view our investment process as one that provides trading or timing information, but instead as a process that provides an anchor in evaluating risk and reward. We feel our approach can be especially important in times such as these.

Recent Past

As most of our readers know, our portfolio strategy

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CURRENT TOPIC

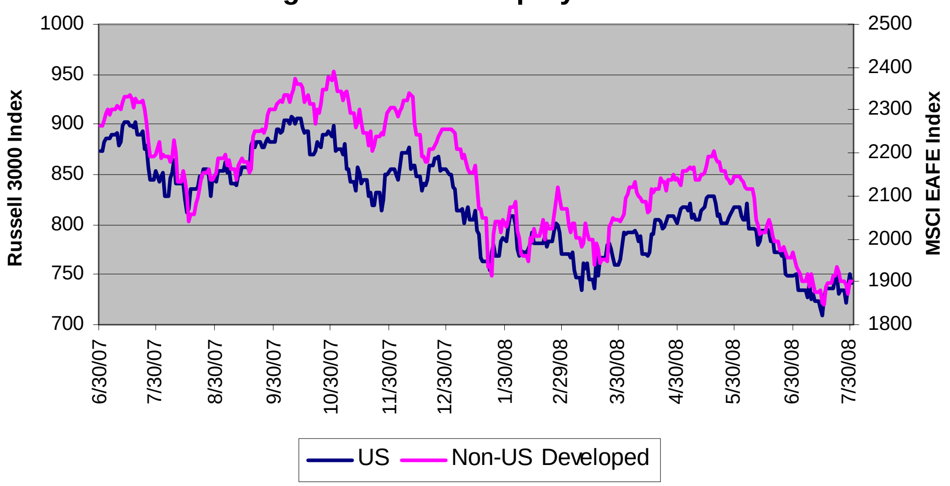
Equity Strategy Update

- *Introduction*
- *Background*
- *Recent Past*
- *Current Strategy*
- *Conclusion*

Strategy

- *We made no changes to strategy during the month of July*
- *Equity indices remain near the levels of our last purchase/strategy change in March*

Figure 1: Global Equity Markets



Sources: Russell, MSCI

"WE FEEL OUR APPROACH CAN BE ESPECIALLY IMPORTANT IN TIMES SUCH AS THESE"

Equity strategy update- cont'd

(Continued from page 1)

in mid 2007 was significantly underweight higher-risk asset classes - equities, high yield and emerging market debt. This posture was quite different than what many were recommending at the time. We believed that equity markets, which had posted solid returns since 2003, had become somewhat overvalued. As described earlier, the primary driver of the overvaluation was the extrapolation of double-digit earnings growth. Our view was that this assumption was flawed.

Figure 2 compares our assessment of fair value in US equities versus the actual market price as of June 30, 2007. We felt that the US and non-US equity markets were sufficiently overvalued to warrant a strategy of significantly underweighting equity risk across portfolios. To illustrate this point, Figure 3 shows how this assessment translated into a typical balanced portfolio with a benchmark of 60% equities and 40% bonds. The portfolio had significantly lower risk than the benchmark primarily by having an equity allocation of 48% versus a normal allocation of 60% and a 17% allocation to cash.

Current Strategy

As time passed, investors were faced with bad news on multiple fronts. The economy was weakening, commodity prices were up dramatically and significant problems were emerging in the financial sector. This all led to a darkening outlook for corporate earnings.

As a result, equity markets, which began their sustained downtrend during the 4th quarter of 2007, continued to sell off into 2008 (Figure 1). The consensus view, which had been overweight equities mid-year 2007, shifted to an underweight, after prices went down. This change in the consensus view once again was in sharp contrast to our strategy shifts.

As equities moved lower, driven by near-term developments, we believed they started to look more attractive - or in some cases less unattractive - on a longer-term basis. Figure 4 - as compared to Figure 2 - shows just how much the drop in equities changed our assessment. In the non-US developed equity markets, valuations also improved by a simi-

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Figure 2: US Equity Market Valuation - 6/30/2007

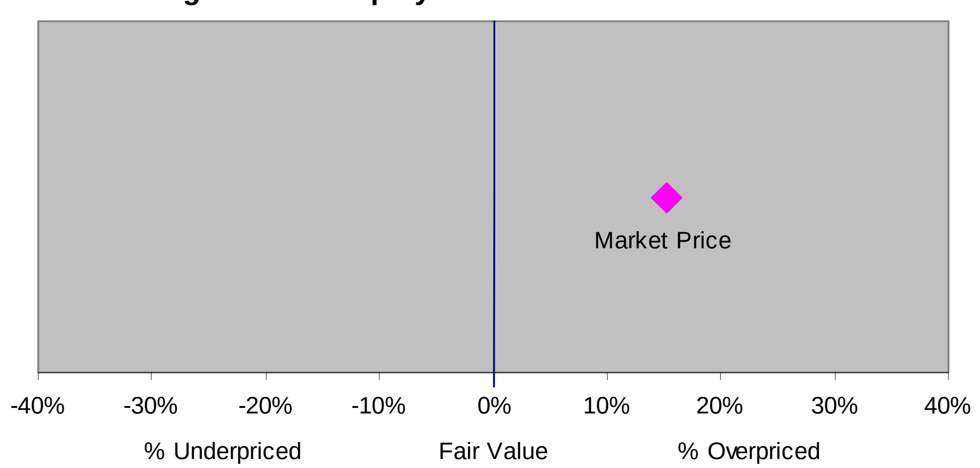

Figure 3: Strategy - 6/30/2007

Asset Class	Benchmark	Strategy	Deviation
US Equity	30%	27%	-3%
Non-US Developed Equity	25%	21%	-4%
Emerging Equity	5%	0%	-5%
Investment Grade Bonds	35%	35%	0%
High Yield	3%	0%	-3%
Emerging Debt	2%	0%	-2%
Cash	0%	17%	17%
Equities	60%	48%	-12%
Bonds & Cash	40%	52%	12%

Note: Figures are in market value %

"Our portfolio strategy in mid 2007 was significantly underweight higher risk asset classes"

About Stairway Partners, LLC

Stairway Partners was formed to provide our clients (starting with ourselves) with an effective and comprehensive solution for managing their wealth. Our disciplined and rigorous approach comes from our collective knowledge in serving large institutional clients over many years.

Our core investment belief is that asset allocation is the single most important determinant of success in any investment plan. The dominant amount of risk and return comes not from your choice of individual investments but from your asset class mix. Stairway Partners focuses our resources on risk management and asset allocation. This includes building your custom blueprint (investment policy and benchmark) and aligning your portfolio with our investment strategy utilizing the global capital markets.

lar amount. Emerging equity valuations have also improved but have yet to reach a level that we find attractive.

Figure 5 - as compared to the same portfolio in Figure 3 - shows our current strategy which we implemented on March 17, 2008. As prices moved down, we increased our allocation to equities, leaving this typical portfolio with an overall equity exposure of 57% versus a normal exposure of 60%. Note that the portfolio is still slightly underweight equities by 3% and has a small 5% allocation to cash. If the equity markets were to move substantially lower, we would continue to add to equities on an incremental basis.

Conclusion

Equity markets have been difficult and volatile. We believe that, as equity markets go down in price, driven by a poor near-term outlook, they actually become more attractive. Our investment process shows that equities, after declining significantly since last summer, are more attractive now than they were a year ago. As a result, we have moved equity strategy closer to neutral from underweight across the portfolios that we manage.

Figure 4: US Equity Market Valuation - 7/31/2008

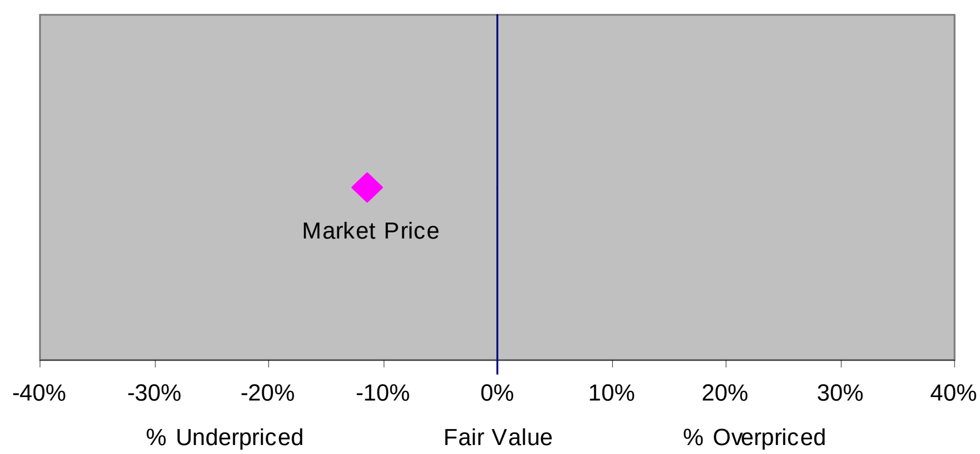

Figure 5: Strategy - 7/31/2008

Asset Class	Benchmark	Strategy	Deviation
US Equity	30%	34%	4%
Non-US Developed Equity	25%	23%	-2%
Emerging Equity	5%	0%	-5%
Investment Grade Bonds	35%	35%	0%
High Yield	3%	3%	0%
Emerging Debt	2%	0%	-2%
Cash	0%	5%	5%
Equities	60%	57%	-3%
Bonds & Cash	40%	43%	3%

Note: Figures are in market value %

"As prices moved down, we increased our allocation to equities, leaving this typical portfolio with an overall equity exposure of 57% versus a normal exposure of 60%"

Strategy

Asset Class	Expected Return	Hurdle Return	Strategy Exposure	Comment
Equities				
US	11.8%	7.0%	small over	Exposure slightly above benchmark weight
Non-US Developed			small under	Asset class has become more attractive as markets have fallen
Eurozone	14.2%	7.9%		
Japan	1.9%	4.6%		
UK	15.7%	8.6%		
Emerging	0.1%	11.7%	under	Asset class remains expensive
Fixed Income				
US Treasury Bonds			neutral	Non-Treasury sectors more attractively priced
2-Year	2.3%	3.5%		
5-Year	2.3%	4.1%		
10-Year	2.5%	4.6%		
30-Year	2.6%	5.0%		
US Municipal Bonds			neutral	Sector overall is near fair value
2-Year	2.4%	2.8%		
5-Year	2.9%	3.3%		
10-Year	4.1%	3.8%		
30-Year	8.0%	4.4%		
US High Yield	10.2%	5.4%	neutral	Sector is pricing for deteriorating fundamentals
Non-US Government Bonds			under	Yields have been rising toward fair levels
Euro 10-Year	3.8%	4.7%		
Japan 10-Year	0.3%	2.0%		
UK 10-Year	4.1%	5.2%		
Emerging Markets Debt	3.7%	5.7%	under	Spreads over US Treasuries remain too tight
Cash	3.5%	---	over	Allocation comes from overpriced asset classes

Currencies	Expected FX Change	Equity Return with Currency	10-Year Bond Return with Currency	
Euro	-9.5%	4.7%	-5.7%	Euro is expensive
Japanese yen	2.9%	4.8%	3.2%	Yen is close to fair value
UK pound	-6.0%	9.7%	-1.9%	Pound is expensive

Notes: **As of: July 31, 2008**

The expected return is our estimate of the annualized return likely to be generated over a 3-year horizon.
The expected returns are expressed in local currencies (e.g., Japanese equity return is stated in yen terms).
The hurdle rate represents the annualized return that an asset needs to generate in order to cover its risk.
Equity Return with Currency (in Currencies section) is the annual return we would expect a US dollar investor to earn from holding foreign equity markets.