Oakwood Outlook

& Quarterly Review

Volume 10, Number 3 July 2007

A Word

From the Advisor

Our Purpose

Our mission at Oakwood Capital Management LLC is to provide our clients with outstanding investment and wealth management services, and we take this responsibility seriously. **The time-tested investment process we use to tailor portfolios to our clients' specific needs is based on quantitative and qualitative techniques and sound research.** We all know that anyone can go to the store to buy flour, eggs, sugar and butter. The "magic" occurs in how those ingredients are put together to create a culinary masterpiece. The same is true of stocks, bonds, or mutual funds. **The "magic" occurs when these investment vehicles are properly structured to create a portfolio that matches a client's risk tolerance and return objectives.**

Since its inception, Oakwood has been respected for its expertise in managing large capitalization US equities and fixed income products. A strict and continuous adherence to our investment process has been the key to success in providing clients with portfolios that build wealth and enable them to reach their investment goals. An extension of that same process came into play in our effort to find

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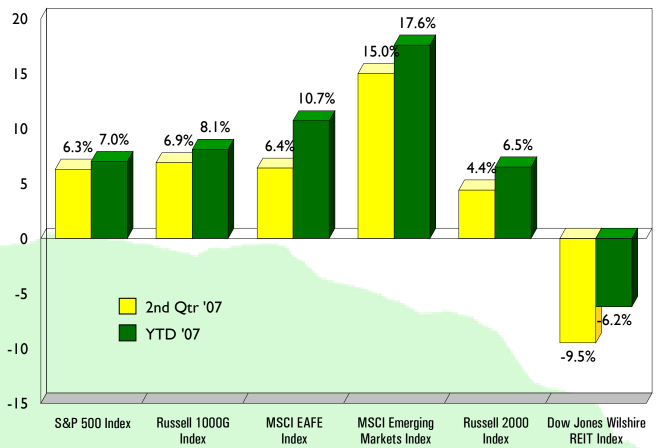
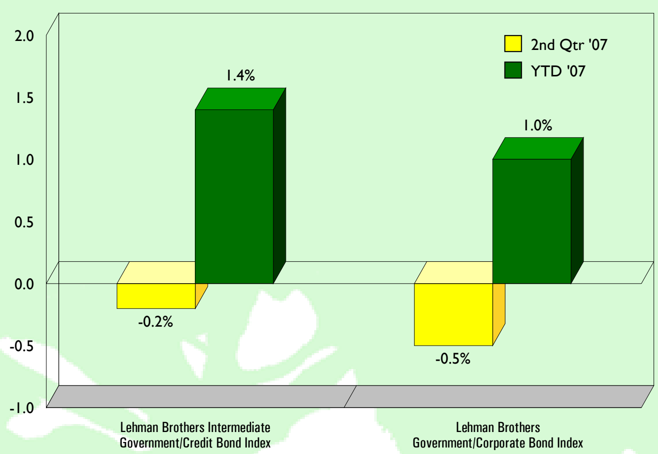
Global Economic Outlook

The resurgence in US economic growth, following the first-quarter slowdown, and continued strong global growth abroad (with the exception of Japan) has driven handsome returns in the global equity markets, as seen below.



Source: Frank Russell Company, Standard & Poor's Index Service Group, MSCI data copyright MSCI 2005, Dow Jones Indexes, Oakwood Capital Management LLC

The US bond market experienced a more difficult quarter, as seen by the representative indices below.



Source: Lehman Brothers, Oakwood Capital Management LLC

Several themes that were important in the first half of 2007 will become even more important in the second half. First, broad expectations for resilience in the US

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ways to improve the risk/return profile of client portfolios, and expand our abilities to other asset classes. We conducted research on various solutions to expand our investment universe the same way we would on an individual stock or bond. These intensive research efforts resulted in Oakwood's alliance with the institutional firm, Dimensional Fund Advisors (DFA)[1], and increased our ability to offer clients very cost effective portfolio diversification throughout all markets, with a comprehensive allocation throughout all asset classes. We have listed below the answers to some Frequently Asked Questions regarding this topic.

Frequently Asked Questions

- When you mention DFA Funds, you use the word "institutional". What does that mean?

In the purest sense, an institutional fund is available only to an institutional investor, such as a large corporate or public pension plan. The firms that manage these funds rely upon their ability to deliver superior and consistent investment results at a low cost, and word of mouth among plan sponsors and professional consultants to build their asset base. Their financial resources are used for research and technology versus expensive advertising campaigns and costly distribution strategies, which are common characteristics of retail name-brand funds.

- I have been a client at Oakwood for many years, and have been a believer in the benefits of Oakwood's management. I need to understand if your process has changed as a result of your alliance with DFA. Can you explain this?

Oakwood's management process has not changed. What has changed is the expansion of both our investment universe and our research department. Prior to our alliance with DFA, our investment universe and equity research focus was on high quality, large capitalization US equities, multinationals and ADRs. We realized, over time, both from our own knowledge of how the world is changing and from feedback from our clients, that we needed to offer more investment options. Research shows that over the past 25 years, the broad US market, which is 1 of 17 countries represented by the MSCI Developed Market Index, never topped the list in terms of annual returns.

We wanted the ability to offer strategy options that could span across asset classes, from small-cap to large-cap, from value to growth, from emerging markets to developed international markets, to real estate, and we wanted to do it in **a cost effective manner**.

Year	Best	Annual Return	Worst	Annual Return
1982	Sweden	22.73	Hong Kong	-44.43
1983	Norway	80.41	Spain	-7.12
1984	Hong Kong	46.99	Denmark	-35.82
1985	Austria	176.27	Singapore	-22.18
1986	Spain	121.22	Norway	-2.52
1987	Japan	43.00	Italy	-21.31
1988	Belgium	53.61	Austria	0.58
1989	Austria	103.91	Japan	1.72
1990	United Kingdom	10.29	Japan	-36.11
1991	Hong Kong	49.51	Norway	-15.50
1992	Hong Kong	32.29	Denmark	-28.25
1993	Hong Kong	116.67	US	9.15
1994	Norway	23.57	Hong Kong	-28.91
1995	Switzerland	44.11	Austria	-4.73
1996	Spain	40.05	Japan	-15.50
1997	Switzerland	44.25	Singapore	-30.05
1998	Belgium	67.76	Norway	-30.06
1999	Singapore	99.42	Belgium	-14.27
2000	Switzerland	5.83	Japan	-28.16
2001	Australia	1.68	Japan	-29.41
2002	Austria	16.56	Sweden	-30.49
2003	Austria	58.03	Netherlands	22.80
2004	Austria	71.52	US	10.14
2005	Canada	28.31	Italy	1.90
2006	Spain	49.36	Japan	6.24

- I would like to have a greater understanding about how Oakwood is adding value through its managed Global Equity, Balanced and Fixed Income Strategies. Can you help me with this?

Oakwood's managed Global Strategies are based on extensive proprietary research and quantitative models that combine various underlying funds to create an overall portfolio that provides diversification with distinctly different risk profiles.

All Oakwood Managed Global Equity Strategies invest in US, non-US developed and emerging markets, and real estate securities.*

Conservative Equity Strategy	Moderate Equity Strategy	Aggressive Equity Strategy	Tax Managed Equity Strategy
• Balance of value and growth • Small, medium and large cap	• Bias towards value • More emphasis on smaller cap	• Higher non-US component • Tilted more towards value and smallcap	• Bias towards value • More emphasis on smaller cap

← Risk/Reward →

* Certain strategies can be managed to minimize the impact of federal taxes on returns by deferring the realization of net capital gains, particularly short-term gains, in order to minimize the taxable distributions to investors. In addition, certain portfolio segments can be managed to meet the social investing needs of investors.

Let's take a closer look at the management of Oakwood's Moderate Global Equity Strategy, which is comprised of 100% global equities. This diversified strategy has an increased bias towards value, invests in multiple asset classes with an emphasis on smaller capitalization stocks, and is suitable for

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investors seeking above average returns through long term capital appreciation.

Oakwood's management in this Moderate Global Equity Strategy consists of US Equities, Domestic and International Real Estate, Developed International Markets Equities, and Emerging Markets Equities. In structuring the US Equities portion of this Moderate Equity Strategy, Oakwood has researched and modeled five funds from the vast array of Dimensional Funds, based upon their risk and return characteristics. This is the **identical process Oakwood employs to create any traditional equity portfolio except we increase diversification by using DFA funds instead of individual stocks.** To break it down further**,** the US Equities portion of the Moderate portfolio consists of:

- **Micro Cap**
- **Small Cap**
- **Small Cap Value**
- **Large Cap**
- **Vector Equity** – A Core Portfolio seeking to purchase a broad and diverse range of small, medium, and large capitalization US securities that are considered value stocks to the market universe.

Oakwood has undergone a similar structuring process for each of the other segments (Real Estate - Real Estate Investment Trusts, Developed International Markets Equities and Emerging Markets Equities) to create a one-of-a-kind structure that, when backtested, outperforms both the S&P 500 Index and the MSCI EAFE Index[2] over a 10-year time period, and does so with lower overall portfolio volatility. Each of Oakwood's other managed Global Strategies, the Conservative Equity Strategy and the Aggressive Equity Strategy, have undergone the same extensive structuring process.

- ## What are the primary advantages of investing in a managed Oakwood Global Structured Strategy?

  - **Research and Risk-Factor-Based Management**
    In its alliance with DFA, Oakwood's clients benefit from many years of pioneering investment research, now taken for granted in the industry. DFA was founded 27 years ago to provide institutional investors access to US small cap stocks, underrepresented at the time in most portfolios. DFA later introduced its first value strategies based on the Three-Factor Model[1]. Oakwood incorporates this research into its managed Global Strategies to efficiently target risk factors across the global financial markets.

  - **Smart Trading Increases Returns**
    Careful trading can reduce or even reverse the costs borne by traditional managers. Because Oakwood's managed Global Strategies focus on capturing the systematic performance of broad markets rather than the random fluctuations of individual securities, we can keep costs low. We can also patiently and expertly concentrate on favorable price execution that neutralizes the effects of momentum and index rebalancing. And, finally, we can maintain portfolio-specific hold ranges that reduce turnover and trading costs.

  - **Exceptional Investment Portfolios and Client Service**
    We are eager to continue building trusted investment relationships with high net worth individuals, and to manage assets for retirement plans, including IRAs and 401(k) plans, foundations, endowments, financial institutions, and consultants. And, as always, we support these customized investment portfolios with exceptional client service.

One of the most significant decisions you can make is choosing the right investment advisor. The right advisor can appropriately allocate your assets for a more secure future. Trying to do it yourself, or choosing the wrong advisor can lead you down a path of both second guessing and owning investments that may not be consistent with your investment goals. The course to risk-appropriate and optimized returns is one that we carefully analyze and design. By doing so, we increase your ability to generate returns commensurate with the risk you are willing to take. We add value by matching investors with carefully researched and structured portfolios, by defining their risk capacity and their return objectives, and then continuously monitoring and managing their portfolios.

We encourage you to freely communicate to us any questions, comments or concerns that you may have regarding the stock or bond markets, the economy, or any other investment questions as frequently as they come up. We invite you to send your questions to questions@oakwoodcap.com, *where a member of our team will be available to respond to your inquiries.* ■

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[1]The investment strategy of Oakwood and DFA is based on the principles of Modern Portfolio Theory (MPT) and the Fama and French Three Factor Model for Equities. An important part of MPT is the Efficient Market Hypothesis, which says that market prices are fair; that they fully reflect all available information. This does not mean that prices are perfect; some prices may be too high and some too low, but there is no reliable way to tell. In an efficient market, investors cannot expect to earn above-average profits without assuming above-average risks.

Fama and French's Three-Factor Model is an extension of another important part of MPT, the Capital Asset Pricing Model (CAPM). Put simply, the CAPM says that an investor's expected return is proportional to a single factor, the stock's risk relative to the entire stock universe. The expansionary Three-Factor Model is based on the following:

- **Market:** Stocks have higher expected returns than bonds.
- **Size:** Small company stocks have higher expected returns than large company stocks.
- **Price:** Lower-priced "value" stocks have higher expected returns than higher-priced "growth" stocks.

[2]The MSCI EAFE Index is recognized as the pre-eminent benchmark in the United States to measure international equity performance. It comprises 21 MSCI country indices, representing the developed markets outside of North America: Europe, Australasia and the Far East.

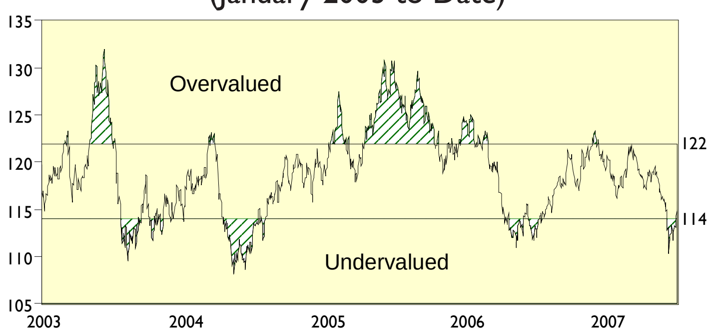
TAXABLE FIXED INCOME

Strategy

On June 28, the Federal Reserve (Fed) kept its key Federal Funds rate at 5.25%, for the eighth straight meeting. They stated that core inflation (absent food and energy) is showing signs of improvement. Supporting this claim is the Fed's preferred Personal Consumption Expenditures (PCE) Index. Excluding food and energy, the PCE Index rose 2.1% during the past year, down from 2.4% and is now closing in on their 1% to 2% desired target range.

It continues to be our view that persistence on the part of the Fed is setting the stage for a favorable bond market. This seems to be the most plausible forecast, even if the economy rebounds modestly from the very weak 0.7% annualized GDP economic reading in the first quarter. However, it is also important to observe the behavior of long Treasury prices over a four year time frame. The following graph shows a period of time when monetary policy was both restrictive and easy. This provides us with insight as to the effectiveness of monetary policy and can be used to time structural changes in portfolios, as part of Oakwood's management.

30 Year Treasury Historic Price Volatility
(January 2003 to Date)



Source: Bloomberg L.P., Oakwood Capital Management LLC

During periods when Treasury prices reached unsustainable levels, investors were wise to take gains and shorten bond positions. Conversely, during periods when prices fell to low levels, there were opportunities to lengthen portfolio structures. These technical market gyrations are indicative of shifts in market psychology, being triggered by fears of either too much economic growth and rising inflation, or anticipations of a slowdown and a calming in inflation expectations. We feel these are normal market reactions to unpredictable day to day economic data. Unfortunately, even though the price volatility may be somewhat technical in nature, for investors who have exercised poor market timing or structured portfolios too aggressively, losses can be significant. To avoid this,

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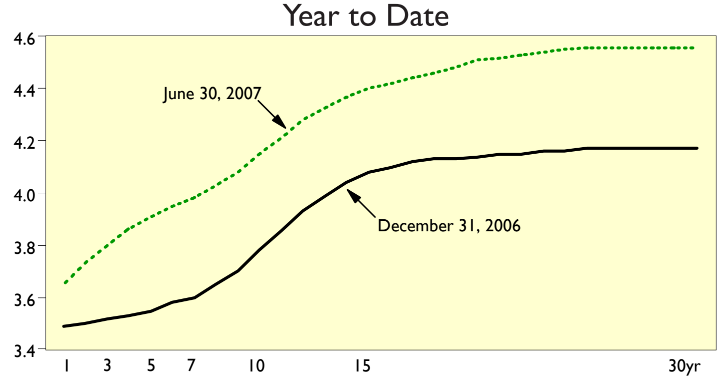
TAX EXEMPT FIXED INCOME

Strategy

The municipal bond market enters the second half of 2007 with signs of encouragement. The Fed has acknowledged that inflation is improving while most municipalities benefited from a long period of economic expansion. In addition, as shown, the increase in tax-free bond yields this year provides an opportunity to lock in good coupon income, especially for clients who rely on cash flow from tax-free income payments.

Municipal Bond Yield Comparison
Year to Date



Source: Bloomberg L.P., Oakwood Capital Management LLC

During the past several years and as interest rates moved higher, we invested heavily in above market coupon securities for several reasons. As you are aware, the total return from municipal investments is a combination of coupon payments, the reinvesting of those flows and security price adjustments. During this period of rising interest rates, Oakwood stressed the importance of the cash flow component of return to offset any security price erosion. This above market cash generation was then reinvested into the marketplace, if available, as yields moved higher. This process further enhanced portfolio values. Furthermore, as we experienced in April and May, the price levels on many lower coupon "market discount" bonds fell below the "de minimis" threshold (a cutoff point that changes the tax-exempt status of a municipal bond's accretion to a partial taxable status) and, as a result, we have seen values drop more quickly. We were able to avoid this by holding only above market premium securities.

Now that we are forecasting a decline in yields, albeit unevenly, we see an opportunity to both lengthen the overall maturity and lower the coupon structure in client portfolios. This will shift our focus away from high income generation to a combination of income and market appreciation.

There are many issues facing investors. One of them is the US Supreme Court case of Davis versus Kentucky. The basis of the argument in the case rests on a State's right to tax

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GLOBAL EQUITY MARKET

Strategy

The first half of 2007 saw its share of tumult in global markets. Rising interest rates and the US subprime loan crisis roiled international markets, and an exciting presidential election in France gained the world's attention. Stock markets around the world fell sharply in late February and early March. After dropping 3.5% on February 27, the largest loss in one day since the 9/11 tragedy, the S&P 500 Index roared back to life and now sits 7.0% above where we started the year. The markets appeared to be sputtering in June, but unlike in late February, another tumble in Chinese stocks at the end of May caused barely a ripple on other global exchanges.

Emerging markets continued to lead the way for the first half of 2007. Latin American stock markets, which to a large extent means Brazil and Mexico, have had powerful returns, and so have many countries in emerging Asia. Even China's market continues to soar, despite government actions specifically designed to rein it in. Most of Western Europe's markets remained strong, and a slight gain in the euro versus the US dollar added a further boost to returns from all those US-based foreign holdings that don't hedge much or any of their currency exposure.

By contrast, Japan's market has lagged. Although the Japanese economy is showing encouraging signs, some investors still aren't fully convinced. A more specific problem is that takeovers are much more difficult to accomplish in Japan, so the "takeover premium" that has pushed up so many stock prices in Europe and the US is much less common in the Japanese market.

Interest-sensitive sectors of the market have been experiencing volatility, and as such, US REIT prices are down for the first half of the year, after seven strong years of performance. **REIT returns have variations through time that are unexplained by equity factors. They don't behave like other stocks and they don't fully behave like stock-bond hybrids.** Another important factor to keep in mind is that US REITs have a negative correlation to non-US REITs (which means that when one variable increases, the other can decrease). For these reasons, and for their excellent potential to add return over time, REITS as an asset class are an essential component of a well-diversified Oakwood managed global strategy.

On the domestic side, a continuing housing slowdown, and high energy prices haven't spooked the rest of the economy, which is still solid, though slowing. **From an historical standpoint, a spate of US market valuation metrics, ranging from price-to-next twelve months estimated earnings (P/E), to price-to-cash flow (P/CF), among others, show the market as currently fairly valued.**

We feel there is remaining strength in the US market and encourage a US bias in global investing, due to the following factors:

- Corporate capital spending discipline in recent years implies that "pent-up" demand will support business investment outlays.
- Financial conditions are still supportive of growth.
- Corporate earnings growth will continue, but at a slower pace.

As with other international markets, the US stock market continues to benefit from strong merger and acquisition activity, as both corporations and private equity firms remain active participants in this ongoing trend. US corporate takeover activity is likely to remain high in order to take advantage of a Justice Department that has shown very little interest in getting in the way of corporate marriages. The one caveat to this positive environment is a proposed change in the US tax law which may slow the pace of acquisitions by venture capitalists. However, the United Kingdom has no interest in changing their tax structure for these firms, and has created a business environment that welcomes them with open arms. The result is that many these US-based firms have moved their headquarters to London, circumventing any tax roadblocks to the flow of deals.

We continue to be cautiously optimistic towards the US equity market, although we feel volatility may increase from its current level. Therefore, we remain well diversified, favoring the following sectors: energy, telecom, industrials, healthcare, and consumer staples.

We have increased our technology weighting, adding two companies, both household names, which dominate their respective industries. The first is a company whose sales have grown from $6 billion a short decade ago to nearly $40 billion in its most recent fiscal year, and returns on invested capital have averaged a staggering 77%. This company's operating margins hover in the high 30% range, and the firm generates more than $1 billion in cash per month. The next addition in the technology sector is the leading payroll and human-resources

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Taxable Fixed Income Strategy

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Oakwood uses these types of studies to increase the probability of success.

In fact, during this difficult interest rate period, Oakwood preserved capital and even generated modest positive returns. This is a testament to our controlled investment process and resistance to high-risk derivative type investments or newly developed products designed to promote above market yields. Instead, changes in our portfolios involved the systematic reduction of corporate bond exposure, in favor of higher quality, more price sensitive government bond positions. This decision is based on our belief that earnings momentum within corporations will slow, causing risk premiums (the yield advantage over Treasuries) to widen further, making investments in corporate bonds less attractive.

Another concern involves companies like Amgen Inc. that, through the bond markets, are taking advantage of cheap sources of money to raise large amounts of capital. In fact, new issue volume in May exceeded $128 billion, making it the third largest ever. The pattern of widening corporate bond spreads should continue until the Fed shifts its policy in favor of economic growth. **Absent a marked slowdown in current economic fundamentals or an unexpected financial shock, we do not expect the Fed to lower interest rates until early in 2008.**

Nonetheless, we still expect bond yields to fall modestly. This means that we will continue to shift short bond holdings to the 3 to 5 year maturity areas. This action will move portfolio durations neutral to their respective benchmarks and we intend to further lengthen portfolio durations soon. For now, there continues to be a delicate balance between the negative effects of defaulting sub-prime mortgage loans on the consumer and the economy overall versus the Fed's mandate to squelch inflation. In fact, in their latest statement, the Fed has stated that "lower inflation needs to be convincingly demonstrated." We believe that they will be successful and we see current yield levels as attractive. ■

Tax Exempt Fixed Income Strategy

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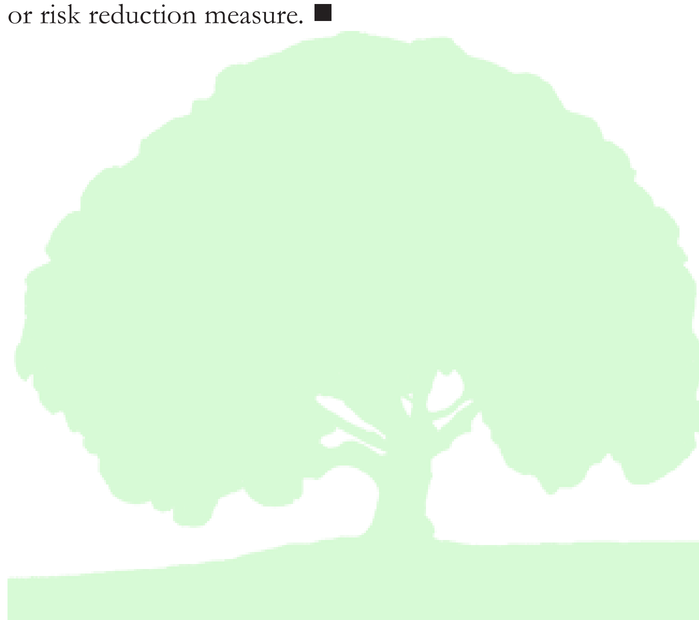
out-of-state income on municipal bonds. Simply stated, currently, if a state resident purchases a tax-free bond from any other state, it is taxed at the state of residence tax rate. If this is disallowed, we would expect those states that do not have a state income tax to benefit. We are constantly monitoring the status of this case, and feel it will not prevail, as precedent has given states their autonomy on decisions such as these. However, we hold a vigilant eye to the opportunity to introduce non-California bonds in client portfolios, pending the ruling. We believe that as this case approaches its hearing date, highly taxed states, such as California, may underperform more tax-friendly states. Our strategy is based upon our ability to capture enough yield to pay California taxes.

Similar to our taxable portfolios, we are pleased that we are able to preserve capital during this very difficult interest rate environment. As outlined in the most previous edition of the Oakwood Outlook, we embarked on a program to extend shorter municipal holdings in favor of 10+ year maturities. However, recently we halted that effort as municipal versus taxable yield ratios tightened to unattractive levels. Now that long maturity yields have readjusted, we have returned to this program. It is now our goal to extend average portfolio durations to 5.25, up from less than 4.5. We are paying particular attention to the current weakness in housing throughout the country. A drop in home values and defaults can easily alter expected tax revenues and spending plans of local municipalities. Most investors view municipal bonds as a safe haven. It is true that municipal bonds are among the safest of all investment classes; however, it is vital to scrutinize all investment choices on their ability to preserve capital, meet future interest obligations and provide liquidity, if needed. As an active bond manager, we view each factor as a potential investment opportunity or risk reduction measure. ■



Global Economic Outlook
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economy have led the market to push back expectations for a Federal Reserve (Fed) rate cut in 2007. Despite its gloomy outlook, the US housing correction will not cripple the broader economy. It will, however, limit acceleration for growth in the second half of the year. Second, investors will be on the watch for signs of further fallout from subprime lending. News that two Bear Stearns hedge funds that had invested heavily in these mortgages were nearing collapse reminded markets about the fundamental meaning of risk. In the second half of 2007, there could be more equity risk aversion, which could prop up demand for high quality large cap stocks, a significant asset class in all of Oakwood's managed portfolios; and also prop up demand for bonds, keeping the yield curve positively sloped.

The outlook for economic growth in Europe, long the laggard of major economic powers, is running at the highest level in years. Despite the prospect of higher interest rates, high oil prices and the euro's current strength, we note that confidence in the European economy was the strongest in six years, according to a May 2007 European Commission survey.

The Chinese economy continues to surge ahead, and there has been little slowing in the pace of credit growth, thanks in large part to the still-undervalued currency. The valuation of the Chinese yuan remains a key issue in global financial markets. The US Treasury's semi-annual report on currencies failed to identify China as a currency manipulator. Instead, the Treasury noted that the yuan remains "undervalued and market sentiment clearly favors appreciation." **China may turn out to be one of the larger markets in our diversified emerging markets strategies. As of March 2007, it was the third-largest country in the MSCI Emerging Markets Index, after South Korea and Taiwan.**

Through the first five months of 2007, the US dollar's correction has accelerated in pace. While on a trade-weighted basis the greenback has only dropped 1%, its adjustment against the major currencies has been much more obvious. The combination of shifting interest-rate differentials, imbalances in global current accounts, volatility in commodity prices, and potential corrections in global markets such as China will influence currency trends.

Gasoline stockpiles remain well below their average levels for this time of year and refinery utilization is weaker than it should be. Moreover, gasoline demand is holding steady despite elevated gasoline prices. With these factors in mind, the oil bull story is still intact and we feel oil will continue to trade above $70 in the near term. ■

Global Equity Market Strategy
Continued from page 5

services firm for small businesses. Its services include 401(k) plan recordkeeping and a newly announced tax credit service, a product that provides small and medium-sized US businesses with an easy and cost-effective tool to help them identify and apply for wage-based tax credits they may be eligible to receive. This company is extremely profitable, and operating margins have been increasing as the firm takes advantage of scale economies. Lower interest rates over the past few years slowed this improvement, although operating margins were still north of 30%.

In the energy sector, we have sold a smaller capitalization company in the oil and gas services industry and bought a larger capitalization company that is the world's largest land-drilling contractor. With a balance sheet that is in excellent shape, this company's rig-expansion program will probably be financed with cash from operations. The management team has administered the balance sheet wisely, and its commitment to a strong financial position serves the firm well in industry downturns.

We have begun to increase both our emerging and developed international markets exposure through increased allocations to DFA Funds or Ishares in Oakwood managed Global Strategies to take advantage of diversification benefits and growth prospects. ■

Oakwood clients will receive redesigned statements this quarter. We hope you find them easier to read and more intuitive. We invite you to send your questions or comments to:

questions@oakwoodcap.com