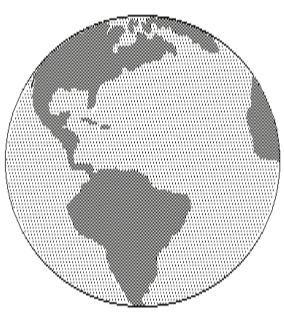
MOSAIC
FINANCIAL PARTNERS, INC.
a Wealth Advisory firm

Market Watch
4th Quarter 2007

Summary

- The S&P 500 closed at a record high early in the quarter before retreating, ending with a loss of 3.3% for the quarter and a gain 5.5% for the year.
- International investments were relatively flat this quarter compared to their full year returns; developed international markets lost 1.7% for quarter while gaining 11.6% for the year.
- Investors emphasized safety as inflation protected treasury bills (TIPS) had the best returns of the 4th quarter.
- Inflation worries negatively influenced the market as 2007 saw the highest inflation numbers since 1990.
- The Federal Reserve cut its Federal Funds rate ½ a point this quarter.
- Large financial companies suffered a difficult fourth quarter as several CEOs were replaced and billions of dollars were written down.



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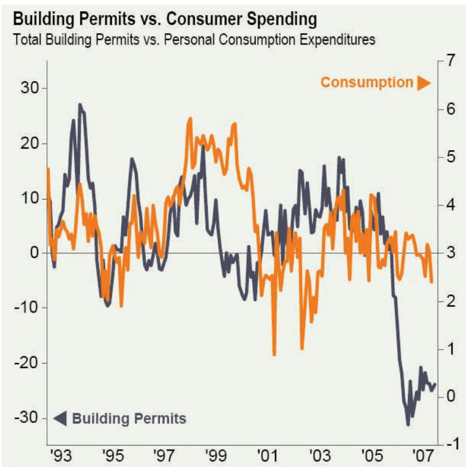
2007 was a volatile year. Despite widespread 4th quarter declines, the major U.S. market indices ended the year in positive territory. The S&P 500, the primary indicator for the U.S. stock market, had a total gain of 5.5% for the year despite losing 3.3% in the fourth quarter. The Dow Jones Industrial Average initially continued its 3rd quarter momentum and moved to a record high of 14,164 on October 9th. It then fell backward, with stock prices declining 4.5% over the full fourth quarter, closing at 13,264. Even with this retreat, the Dow still finished the year with an 8.9% total gain. The NASDAQ, made up mostly of U.S. technology companies, declined 1.8% in the 4th quarter but completed the year with a 9.8% gain.

The S&P 500 benchmark is made up of ten business sectors, making it an effective gauge of the market and the economy. All but two of those sectors (financials and consumer discretionary) increased in value in 2007. Energy and materials were the two biggest gainers, with yearly increases of 34.4% and 22.5% respectively. The consumer discretionary sector, which reflects the demand for and spending on consumer goods, fell 13.2% for the year with almost all of that decline coming in the final quarter.

The 4th quarter's market declines were driven by two primary influences: 1) recessionary worries as the economy slowed and 2) write offs banks were forced to take as a result of their sub-prime mortgage exposure. While sub-prime mortgages make up only about 5% of the bond market, they still are a large enough proportion to cause significant worries. As a result of sub-prime losses, the financial sector was particularly hard hit, losing 14.3% of its value in the fourth quarter alone.

Sub-prime Impact: The story of 2007 was the sub-prime mortgage debacle and its associated impact on the credit markets. Bear Stearns, one of the biggest and best known financial firms, recorded its first quarterly loss ever as it wrote down some of its riskier debt in the fourth quarter. Merrill Lynch and Citicorp, two other financial giants, replaced their CEOs because of similar problems.

As a rule, the more uncertainty, the more volatile the market is likely to be. That rule certainly applied this quarter to the financial sector. Stock prices of financial companies ended the year decidedly lower as investors continued to worry about the possibility of more write downs in 2008. Accordingly, both institutional and individual investors have found it difficult to value the companies holding these assets.



Building Permits are total permits in the U.S. as a percent change over 1-year. Consumption is shown using Personal Consumption Expenditures at an annual rate. Data reflects most recently available as of 12/31/07.

To replace losses caused by failing sub-prime loans, many financial firms began to look abroad for capital. The Chinese, Singaporeans and Saudis all invested several billion dollars in major financial firms (Morgan Stanley, Merrill Lynch, UBS and Citibank). While more sub-prime problems are still ahead, it is our belief that the investments being made in these temporarily weakened firms actually reaffirms the strength and long-term attractiveness of our major financial institutions.

The Credit Markets: As banks have had to cope with the difficulty of pricing sub-prime loans, the Federal Reserve has tried to buoy the financial sector by increasing liquidity into the credit market. In response to the market's concerns over the banks' losses, central banks worldwide have tried to innovatively inject money into the market. Reduced liquidity leads banks to restrict their lending practices. This, in turn, slows the economy by making it harder for many businesses to arrange short term credit to expand or meet financial obligations. To reassure financial markets the Fed's chairman, Ben Bernanke, has said he will continue supporting the credit markets "for as long as necessary" in order to mitigate the typical credit tightening reactions.

To alleviate pressure on the economy, the Fed cut the Federal Funds rate twice in the fourth quarter—once on October 31st and again on December 11th. The Fed funds rate ended the year at 4.25%, its lowest rate since January of 2006. The Fed also lowered its discount rate (the interbank lending rate). There are strong expectations that the Fed will lower interest rates again at the end of January, 2008 to further ease any economic slowdown.

Declining interest rates cause the relative attractiveness of the U.S. dollar to fall for international investors. This, in conjunction with the continuing trade and budget deficits the U.S. has been running, has caused a significant drop in the value of the dollar. If you have traveled abroad recently, you've felt it in higher prices. Similarly when we buy imported products, they are likely to be more expensive. At the same time, a weaker dollar makes it easier for American companies to sell their products overseas. Exports shot up approximately 9% in 2007 as foreigners snatched up American bargains. As a result, our trade deficit has declined somewhat — but our thirst for ever more expensive oil has kept that deficit from falling very far.

U.S. exports rose about 9% in 2007 thanks to the weakening dollar

Recession: Recession concerns have been raised by the continuing problems in the credit markets, declining home sales, slowing employment growth, the acceleration in foreclosure activity and increased energy costs. New home sales in 2007 are projected to have fallen by about 25% from 2006. Existing home sales were about 20% below their 2006 levels (although in November, the National Realtors Association reported a 0.4% increase in sales after nine consecutively negative months). Home sales have slowed as a result of tighter financing and the slowing economy. Potential home buyers have become increasingly skeptical and cautious as they wait for the market to bottom and the economy to strengthen.

Reflecting the caution in the home market, U.S. consumer confidence fell to 87.8 in November —100 and above generally signifies consumer optimism. While employment has been a strength throughout most of the year, by December the numbers started to weaken with the estimated unemployment rate rising to a two year high of 5%. Concurrently, U.S. job growth in December saw the lowest number of new jobs created in a month since August 2003 (when the economy was still struggling from the 2001 recession). Particularly troubling was that private sector job growth actually fell (government payrolls increased). That said, 2007 still saw an average growth of about 111,000 jobs per month and average hourly earnings increased to $17.71 to close out the year 3.7% higher than in 2006.

The Consumer Price Index shot up by 4.1% in 2007. With wages rising 3.7% during the year and inflation increasing by 4.1%, wage earners actually lost 0.4% in real purchasing power, potentially slowing discretionary consumption further. However, core inflation (which excludes food and gas price changes from the inflation measure) rose a more modest 2.4% for the year.

U.S. Stocks: As the price of oil has risen, it should not be surprising that investments in that sector have done well. Among domestic funds, natural resource funds had the best 2007, gaining an average of 37%. Utilities also enjoyed 20% returns for the year. (It's worth noting here, that our client portfolios almost universally have exposure to these sectors as part of a diversified portfolio, and if your portfolio also contains commodity holdings, you further benefited from the rise in the price of oil.)

Returns by Category

4Q	2007
Large Growth -0.8%	Large Growth 11.8%
Mid Growth -1.7%	Mid Growth 11.4%
Small Growth -2.1%	Small Growth 7.0%
Large Value -5.8%	Large Value -0.2%
Mid Value -6.0%	Mid Value -1.4%
Small Value -7.3%	Small Value -9.8%

After many years of exceptional performance, real estate stocks were hard hit this last year as funds lost an average of 14.6%. . The decline in 2007 was triggered by concerns that 1) the drop in residential values would infect the commercial side, 2) the economic slowdown would lower demand for space, and thus cause rental rates and occupancy to fall, and 3) the liquidity problems of banks would cause financing to become less available or more expensive and thus lead to a slow down in real estate development.

For the past several years, value stocks have outperformed growth stocks. Similarly small company stocks have outperformed larger companies. During both the quarter and the year, these trends reversed. Because the falling financial sector is more heavily weighted in value sector, the value group was especially damaged. But there was also generally a flight away from "risk" in 2007. This drove many investors to larger, "safer" companies. Technology companies, which are typically characterized as growth stocks, turned in a particularly good year in 2007 (up 16%). Much of the strong 2007 growth among technology stocks was driven by companies such as Google, Apple, and Research in Motion, all of which saw their share prices increase by at least 50%. The Russell 1000, an index of the 1000 largest companies when sorted by market value, returned 5.7% for the year (though declining 3.2% in the 4th quarter). The Russell 2000, an index of small companies, fell 1.5% for the year and 4.5% for the quarter.

2007 was the first year in the last seven in which small growth has outperformed small value or that large growth has outperformed large value. In fact, the worst performing category of growth outperformed the best performing category of value this year. The large company growth sector had the best returns for the quarter and year with returns of -0.8% and 11.8%, respectively. Small value companies fell by 7.3% for the quarter and 9.8% for the year — the worst performing sector for both the year and quarter. Because your portfolio holds both large caps and small caps with a slight overweighting to the typically steadier value stocks, our domestic stock holdings generally under-performed the broader indices.

World Markets: Non-U.S. stocks slowed in the fourth quarter, but still enjoyed a spectacular year gaining 3.7% in the quarter and 39.8% for the year. The gains were fueled by the declining dollar as the U.S. currency fell against 14 of the 16 most actively traded currencies — including declines of 9.5% and 17% against the Euro and Brazilian Real, respectively.

For several years, "value stocks" have consistently outperformed "growth stocks." Small stocks have also beaten larger stocks. In 2007, both trends were reversed.

Strong returns continued to be found in Asia. India was up 23.3% in the fourth quarter. China lost some of its luster for investors as it had a flat quarter but still returned an impressive 66.2% for the year. Other noteworthy countries include Brazil and Russia which gained an impressive quarterly return of 13.4% and 17.4%, respectively.

The Emerging Markets, as measured by the MSCI Emerging Markets Index, once again had a stellar year. Returns rose 3.7% in the quarter and 39.8% for the year. Although returns were flat in the 4th quarter, the MSCI Pacific Index (which excludes Japan) generated a 31.7% return for the year. The MSCI Europe Index (excluding the UK) was also flat in the last quarter of 2007 but still posted an impressive 17.5% yearly gain as it was helped by the Euro's strength. The MSCI UK Index lagged most international

Exchange Rates

Country	10/1/2007	12/31/2007
Australian Dollar	0.8884	0.8767
Brazilian Real	0.5449	0.5654
Canadian Dollar	1.0082	1.0194
Swiss Franc	0.8596	0.8884
Euro	1.4272	1.4729
British Pound	2.0477	1.9973
Indian Rupee	0.02513	0.02536
Japanese Yen	0.00871	0.00891
Mexican Peso	0.09161	0.09188
Russian Ruble	0.04024	0.04081

indices but still outperformed S&P 500 by nearly 3 full points as it posted an annual gain of 8.4%. Of the major international indices, only Japan fell — the MSCI Japan Index declined 4.1% in 2007.

Investments by American investors in overseas stocks were bolstered by the weakened dollar. Profits in foreign currencies are listed in US dollars, so American investors not only enjoyed the healthy profits, but also the favorable change in currency values. For example, the MSCI Europe (excluding the UK) Index lost 2.1% in the fourth quarter in local currency (the Euro), but U.S. investors still managed a gain of 0.5% after accounting for differences in currency values.

Like the U.S. markets, foreign growth investing outpaced foreign value investing. The EAFE (Europe, Australia, Far East) Growth Index lost 0.3% for the quarter while gaining 16.8% for the year. EAFE value lost 3.2% for the quarter and gained 6.5% for the year (as with all international investments, aided by the relative strength of international currencies relative to the dollar).

Bonds: Bonds had an interesting quarter as the Fed lowered interest rates twice, but at the same time the risk premiums on non-government debt rose. The first would generally cause bond values to increase, while the second acts like an interest rate increase and pushes bond yields lower. At close of the year corporate bonds carried a "spread" of almost three percentage points above the yield on US Treasury debt. Reflecting the flight toward safety, the yield on 2 year US Treasuries ended the year at 3.1%, down from 4.8% from the end of 2006.

Investors once again began to worry about inflation, causing TIPS (inflation protected treasury bonds) to come back into favor with investors. After returning just .4% in 2006 TIPS had a strong year, returning 11.6% for the year and 5.0% in the 4th quarter.

Alternative Investments: Commodities saw increased returns as worries about inflation and increased demand for goods (particularly oil) drove up prices. Gold had its largest gain (30%) since 1979, closing the year with a record price of $834.50 (for perspective, even with gold's rise in 2007, over the last 20 years, the annual return on gold has been 2.8% — a negative return after accounting for inflation). The demand for many commodities (and many derivative products, like ethanol) has grown significantly as China, India and other emerging market economies have grown. Global warming concerns have also created a premium for certain agricultural commodity futures.

After sub-prime mortgage concerns, oil was the second biggest story in the fourth quarter of 2007. Oil prices neared $100 (and briefly crossed that limit for the first time ever in early 2008). Political turmoil and foreign demand helped push barrel prices higher, as did the continuing decline of the dollar. Since oil is traded in dollars, the decline in the value of the dollar has led to higher oil prices to compensate for our weaker currency. For the year, the price of oil rose 52.3%, cutting into the discretionary spending of the American consumer.

While oil and gold saw significant increases in price, some other commodities, notably timber, slowed. Demand for timber fell with the housing market. Even with the downturn in the timber industry, Plum Creek Timber (a stock most Mosaic investors hold) returned 18.3% during 2007.

Overview: For some of our clients, the continuing volatility may be a concern. For our part, we see this as a natural part of the economic cycle. The economy will always alternate between periods of strength and weakness. Today, there is a growing sentiment on the part of many economists that we are entering, or have already entered a recessionary period. Most hold that this economic downturn will be relatively modest and is unlikely to persist beyond 2008. In either case, we anticipate that the markets will remain unsettled for at least the next few months and allow for the possibility that further market decline is possible.

It has been our successful practice to not overreact to the markets' short term moves. Markets may indeed decline in 2008 but we can't be certain of this ahead of time. Should the market fall in 2008, we are confident that it will come back as the economic cycle follows its natural progression. In the meantime, we seek to maintain our investment discipline and look to the broad diversification of our portfolios to reduce the impact of any downturn. Consistent discipline may sometimes seem like inaction, but buying on weakness and benefiting from the often sudden and steep market recoveries that occur have each proven to be critical building blocks for successful long-term investing.

Thank you for allowing us to be of service to you.

Sources: JP Morgan Quarterly Review, The Federal Reserve, Reuters, Forbes, Bloomberg, Morningstar, Google Finance