Campbell Capital Management

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Dear Money Management Client:

Another good year for portfolios with Campbell Capital Management. In spite of crashing real estate values, imploding sub-prime loans, systemic credit crises, a falling U.S. dollar, rising oil prices, and mounting U.S. recession fears, our investment themes proved rewarding in 2007. Many of the companies in which we invested benefited greatly from the growth in emerging markets. Demand for resources and commodities remained strong all year and will likely be this decade's best investment bets.

At the end of 2006, we knew the housing bubble was going to cause much pain, but we had no idea just how much. A year later and we still don't know when the bleeding will stop. The inventory of unsold homes and number of mortgages falling delinquent grows each month. Delinquencies are often preceded by burdensome interest rate "resets" from adjustable rate mortgages (ARM's), and the resets only started this past October. Financial institutions already making headline announcements of billions in dollar losses won't know their total foreclosure exposure until these "resets" work their magic in quarters to come. It's therefore impossible to predict how much pain there will be or when the pain will stop. Concerns that the U.S. economy will slow abruptly are now serious because all types of loans are being dragged into the fire. Commercial loans and credit cards are the most recent victims, all indicating that a contraction in credit could cause a recession. Credit markets are the source of liquidity to fund operations and if they are not functioning, the economy is threatened.

Nearly all recessions result from restrictive monetary policy. In the typical cycle, robust economic activity leading to inflation requires the Federal Reserve to embark on a series of interest rate hikes that restrict credit and slow the economy. When the economy is weak or falling into recession, the Fed typically reverses course and reduces interest rates to stimulate business activity. With fears of a recession now looming, Chairman Bernanke stated this week that the Fed would act aggressively to support a weakening economy. The problem is that if we do have a recession, it won't be the result of restrictive monetary policy and therefore lowering interest rates may have little immediate effect. This recession will be a result of lenders lacking confidence in borrowers ability to repay, which has nothing to do with the rate of interest charged. Abundant liquidity and low interest rates will certainly help, but much time is required to sort through the sub-prime mess. And the sub-prime mess won't see any "light at the end of the tunnel" until the housing market stabilizes.

The next six months will be challenging. Stock values are historically cheap but investors will remain cautious and defensive until corporate earnings stabilize. Later this year we think Fed rate cuts and a Government sponsored stimulus plan will gain traction and get the economy moving again. Until then, we favor a cautious and defensive strategy.

We remain committed to a conservative investment philosophy, which emphasizes the preservation of capital. If you have any questions or would like to discuss your portfolio, please do not hesitate to call.

Very truly yours,

Clay Campbell

SEC Disclosure

As you know, Campbell Capital Management is registered as an investment adviser under the Investment Advisors Act of 1940. We are required to update the information in our Form ADV periodically, to ensure that it contains up-to-date information about our company. If you would like to receive a free copy of our most recent amendment to Part II of our Form ADV, please call or write us at the address below.

Please send your request to:

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