MOK CAPITAL MANAGEMENT
A Registered Investment Advisor

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Dear Client,
As we expected, the strong global economy in the prior quarter outweighed domestic weakness relating to housing. With help from the federal reserve, which belatedly recognized the credit crisis arising from the sub-prime loan debacle, the market boomed at both the beginning and end of the quarter, with a sizable retreat in the middle. As a result of this help from the Fed, we were vindicated in our guess that for once the summer doldrums in the market, always a concern, were not going to have the same effect as in most recent years.

Inflation continues to be a worry globally. With materials and energy costs high and capacity constrained, the drop in US interest rates is a real concern. The federal reserve decision to lower the discount rate by half a percent was not matched by similar moves from foreign central banks. As a result, investment will move to foreign countries with higher rates, putting further downward pressure on the dollar. This is a matter of real concern for Americans. As the dollar drops, foreign goods will become more expensive. Since a large part of the goods we buy come from China and other foreign suppliers, we can expect a good deal of what we buy to get more expensive in the near future. That should in turn cause an increase in domestic spending, and in the price of American goods. That will also make American exporters more competitive, as their prices will be comparatively cheaper.

We see several attractive investment opportunities from this scenario. First, we will continue to invest in foreign companies, and in U.S. companies that export the majority of their production. Second, we will look for attractive takeover candidates. As the dollar declines, the relative price of U.S. real estate, principally in prime commercial facilities, will look particularly attractive to foreign buyers. At the same time, U.S. businesses, particularly those with excess capacity, will look very attractive to foreign business. Finally, we expect raw materials to continue to rise, both due to their shortage for actual use, and also as a repository for value in times of inflation. Its interesting to note that Europe and Japan are unlikely to raise their rates at the beginning of a global inflation because this will result in the transfer of large amounts of global business to U.S. companies. Eventually however, these countries will begin to raise rates, which could send the dollar into a fairly steep decline, unless U.S. exporters have so increased their business that U.S. interest rates begin to climb. [Japanese companies may prove particularly attractive, as their currency has not had much inflationary pressure, and they have a fair bit of unused manufacturing capacity for further growth.]

Geopolitical risks remain high, with particular instability in Iran and Pakistan. Recent intelligence also shows Syria buying nuclear materials from North Korea. We will look this quarter for signs of escalating inflation in China, India, Brazil and Russia, in order to determine the attractiveness of holding assets denominated in those currencies. In general, those of you with equity portfolios are doing well. We will keep an eye on our income portfolios to protect against the effect of inflation, but see some opportunities in special instruments that are indexed to inflation.

Regards,

Stanley Q. Mok
Principal