ADVISER INVESTMENTS

ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments

August 6, 2009

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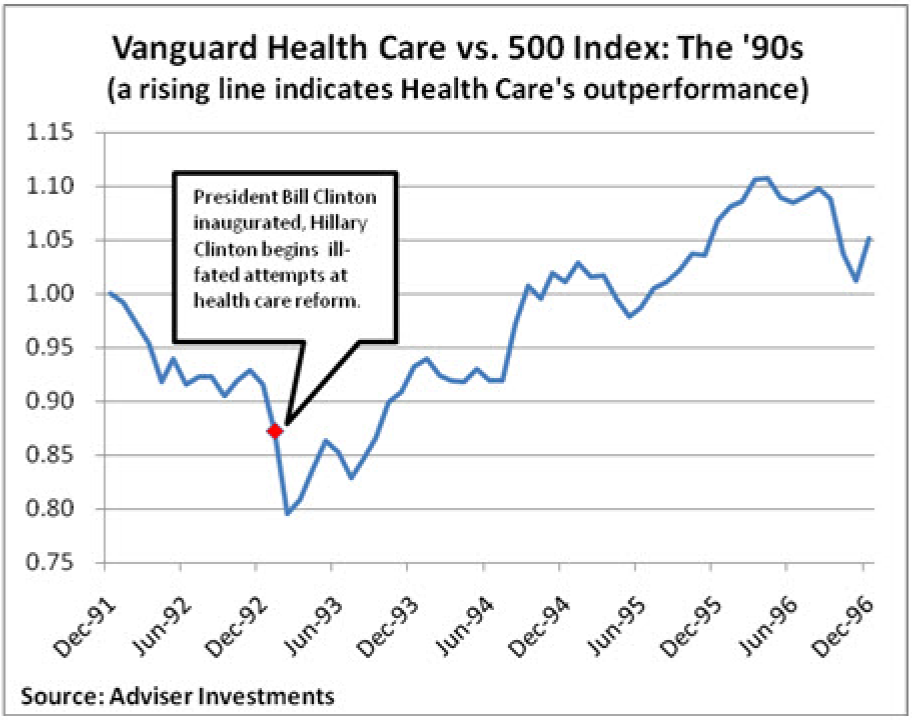
A Healthy Investment?

With all of the ink, bandwidth and news media minutes dedicated to health care reform lately, in combination with investors' concern over the long-term health of the sector, we thought this would be a good time to give our exposure to it a checkup.

In past *Adviser Fund Updates*, we've discussed our fondness for several health care funds, namely Vanguard Health Care and Hartford Global Health (a decent, no-load, lower-minimum substitute for either of these funds is ICON Healthcare), one or the other of which is a vital component of many of our clients' portfolios. But a number of the managers we rely on to make sector bets across their broader funds also have a predilection for health care stocks, specifically the PRIMECAP portfolios such as Vanguard Capital Opportunity, PRIMECAP Core and the independently-run PRIMECAP Odyssey Aggressive Growth and Odyssey Growth. The two funds PRIMECAP runs for Vanguard have approximately 25% of their portfolios in health care, while the two Odyssey funds have nearly a third of assets invested in health care stocks. Also worthy of note is Fidelity's Contrafund, which has over 15% of assets in health care. In comparison, health care stocks represent a bit more than 13% of the overall U.S. stock market and less than 10% of foreign markets.

As you may have surmised, all of these percentages add up to an oxymoronic healthy overweight in the sector in many of our clients' portfolios. In broad numbers, the portfolios we manage have about one-and-a-half to twice the exposure to health care that an investor in a broad U.S. market index has.

But we view that as a good thing, as we feel the sector is poised for outperformance in the coming months.



Note: This chart shows relative performance between Vanguard Health Care and 500 Index, with each 0.10 rise representing 10% of outperformance over the index fund for Health Care.

Let's examine Vanguard Health Care, since it's obviously a pure play on the sector, and has been around long enough to take a look back at relevant historical returns. Almost from the minute the Obama administration came into office, Health Care has been lagging. In the chart above, the line represents the performance of Health Care compared to 500 Index. When the line is rising, as it did through much of 2008, Health Care is outperforming the market. But it lagged in the early part of this year, as the falling line shows.

This being said, every time the market has some down days, the health stocks hold up much, much better. One reason: They continue to offer impressive dividend yields and are seen as safe havens when markets get rocky. From the beginning of 2009 through the March 9 market low, for instance, Health Care lost 18.2% while 500 Index and Total Stock Market Index both dropped 24.6%. Since then, however, Health Care has gained 30.9% (through the end of July) while 500 Index and Total Stock Market are up 47.2% and 49.4%, respectively.

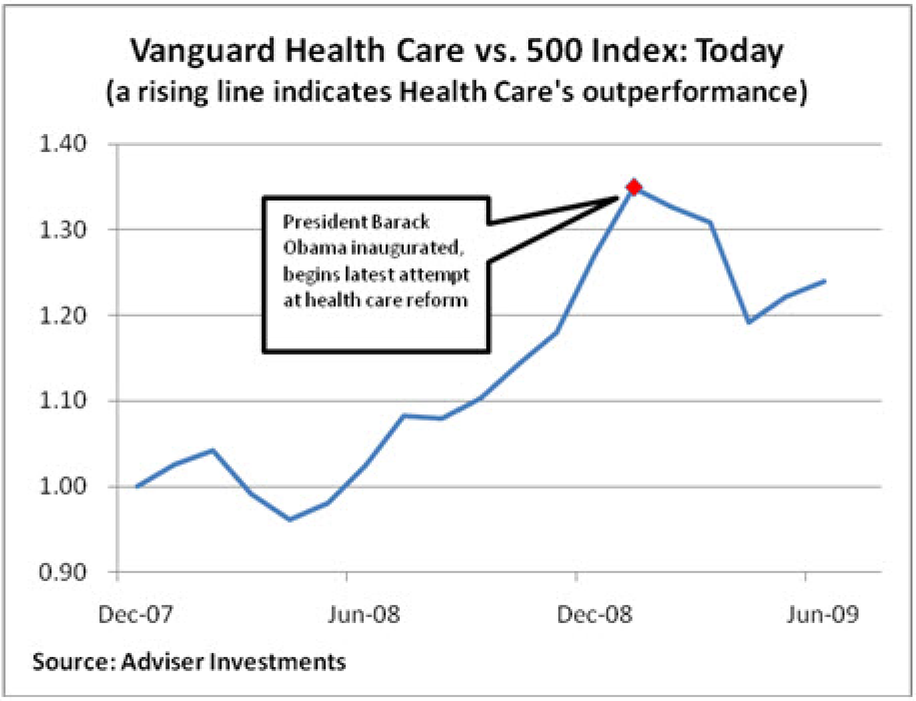
The lag, and the fear, of course, is health reform. And Wall Street has been voting with its feet—running from the sector without considering the historical precedent of past attempts at reform. We can't tell you what form the next reform will take. But whatever Congress and the

President ultimately come up with in terms of health care reform is not going to be as dire as so many critics seem to think—there's just no way we are going to see this country move to a form of socialized medicine. It may be called that by the critics, but we believe there'll be plenty of profits left for the drug and managed care companies after all is said and done.

One should also consider that if reform means more health care for more people, this will result in a corresponding increase in drug demand and more service demand. The managers we're invested with who have large holdings in the area know more about this than we could after years of study (and probably could design a better health care system than any government committee, for sure).

One certainty we can operate off of is that, at some point, everyone will need health care. And no matter what is said, the drug companies are not going to conduct research and development for free, so they have to be able to make a profit, or they will simply close up their labs and sell what they've got until it goes off-patent, then shut down. The government just won't let this happen. For one thing, if U.S. drug companies shut down, who's left? Japanese and British drug companies. And you can be sure the U.S. government is not going to be able to control them the way they think they'll control U.S. companies.

However the health care debate shakes out, it is our assertion that there is money to be made in our health care holdings. Take a look at the chart below to see just how well Health Care did in the aftermath of the last attempt at reform. We remain hopeful that the sector will get a similar shot in the arm this time around as well.



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About Adviser Investments

Adviser Investments is an independent, professional money management firm specializing in Fidelity and Vanguard mutual funds. With 1,500 clients and $900 million dollars under management, Adviser is one of the nation's largest mutual fund research and money management firms. Our staff of 35 investment professionals focuses on helping individual investors, trusts, foundations, and institutions meet their investment goals. Our minimum account size is $350,000.

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