



VIEW FROM VISTA

October 9, 2006

Dear Valued Client,

Enclosed is your Quarterly Report from Vista Capital Partners for the third quarter of 2006. The stock market provided plenty of drama during the period. Major U.S. stock indicators were at or near lows for the year in mid-July, but then staged an impressive comeback. The rally was aided by a pause in the Federal Reserve's campaign of interest rate hikes as well as price declines for oil and other commodities. The Dow Jones Industrial Average gained 4.7%, its best third quarter result in 11 years. This left the Dow up 9% for the year and just 44 points shy of its January 2000 peak. International equities joined the party too with the MSCI EAFE index advancing 3.4% (+12.2% so far in 2006). Real Estate Investment Trusts (REITs) continued their incredible run. The Wilshire REIT Index enjoyed a 9% surge that pushed its year-to-date return above 24%. Even bonds got in on the action, despite gloomy expectations. The Lehman Aggregate Bond Index rose 4.1%, pulling its 2006 return out of negative territory to 3.4%.

Some of our observations on the financial markets:

- The National Association of Realtors reported that August sales of existing homes dropped for the fifth straight month and the median price of all homes sold was 1.7% lower than a year earlier, the first year-over-year decline in more than 11 years. *The cooling home market has helped ease inflationary fears, lowering interest rates and boosting the bond market.*
- There are now 48 mutual funds that invest in commodities with assets totaling \$56 billion, up from 34 funds with less than \$10 billion three years ago, according to fund tracker Morningstar Inc. *Much as they did with tech-oriented investments in the late nineties, investors have rushed into commodities, lured by recent outsized returns. The exuberance has risen to the point where short-term speculators are driving some prices more than the industrial customers who buy the materials to make things.*
- A few mutual fund companies are finally addressing investors' propensity to buy high and sell low. There is less promotion of hot funds, fewer launches of funds in high flying corners of the market, and more education about the benefits of diversification. Morningstar Inc. has begun adjusting funds' stated returns for the timing of purchases and sales to provide an estimate of the returns earned by a typical investor. These adjusted returns are usually quite a bit lower. *Positive steps in the fight against the destructive habit of performance chasing and Wall Street's shameless efforts to profit from it.*

Investment Focus

Rebalancing—the process of realigning the relative weight of each asset in a portfolio back to its target weight—is primarily used to maintain a desired level of portfolio risk, but it does have another equally important benefit. Disciplined rebalancing forces investors to sell a relatively appreciated asset (sell high) and to reinvest the proceeds in a relatively depreciated asset (buy low).

Unfortunately, human nature compels investors to act irrationally. Investors believe what has worked well in the past will continue to work well in the future. For this reason, most investors pour money into a bull market (buy high, as they did in 1999) and sell in a bear market (sell low, as they did in 2002). Emotionally-driven, ad-hoc moves such as these can have a devastating impact on long-term wealth accumulation.

An alternative to rebalancing which can help mitigate poor investment decision-making is to simply buy-and-hold. While the cheapest strategy (no transaction costs are incurred) and also the most tax-efficient (nothing is sold), a buy-and-hold strategy can expose the investor to dramatic shifts in the risk profile of the portfolio. Research by Weinstein, Tsai, and Laurie, showed that a rebalanced portfolio composed of 60% stocks and 40% bonds from 1980 to 2002 yielded *after-tax* annual returns that were 0.20% higher than a buy-and-hold portfolio. And it did so with significantly less volatility. A \$1 million portfolio grew by an additional \$325,000 when rebalanced versus buy-and-hold.

Regardless of market direction, disciplined rebalancing removes emotion from the investment decision-making process, empowering investors to make prudent, rational decisions consistent with their stated investment policy. The reward for such discipline: lower risk and higher returns over the long-term.

Private Wealth Management

Estate planning involves the transfer of wealth during life and at death. Not only can effective estate planning help ensure wealth passes according to one's wishes and in a tax-efficient manner, it can also help prevent discord among heirs. While we recommend clients utilize the services of an expert, such as an attorney specializing in estate planning, these few simple steps can help prepare you for the inevitable:

1. Prepare a will. This legal document governs how assets will be distributed upon your death and can be used to designate legal guardians for children. Without a will, assets will be distributed according to state laws without regard to your wishes. It is a good rule of thumb to update your will every five years or whenever a life altering event occurs.
2. Designate beneficiaries. Regardless of what your will stipulates, assets such as retirement accounts and life insurance policies will pass to the designated beneficiaries.
3. Appoint a general power of attorney for finances. This document names another person to make financial decisions for you. A durable general power of attorney is effective immediately, and can be used in the event of incapacity. When invoked, a power of attorney allows your appointee to pay bills, access accounts and handle your financial affairs without going to the court for approval.
4. Make health care directives. A health care advance directive gives another person the ability to make medical decisions if you are unable to do so. It also tells family and medical personnel how you want to be treated under various scenarios.

Estate tax laws are complex and will change over time. While these four steps cover “the basics,” using a qualified attorney for estate planning may insure your plan is carried out and tax considerations are properly addressed. We have developed a network of highly competent estate-planning attorneys over the years and encourage you to contact us for a referral.

Other

We are pleased to introduce a new addition to our investment team, Adam Cornwell. Adam joined us in August as a portfolio manager and research analyst. He brings a diverse background and high intellect to Vista. Prior to joining Vista, Adam spent five years in the web technology field providing business development solutions to small business owners and four years as a designer/engineer for a local manufacturing company. Adam returned to school to pursue what had long been a passion of his, a career in investing and personal finance. He recently graduated summa cum laude from Washington State University with a Bachelor of Arts degree in Finance. Adam is already a Level III candidate in the Chartered Financial Analyst (CFA) program. Adam and his wife, Kristi, live in Vancouver with their two great danes. He enjoys playing golf and spending time with friends.

We would like to thank all of you who returned our client questionnaire/survey. We were grateful to receive such high marks and appreciative of your suggestions for improvement. The results will help make us a better firm. As promised, Vista donated \$5 to charity for every completed survey, sending \$260/each to CASA and March of Dimes.

Below you will see a table of year-to-date 2006 returns for most of the major asset classes. We welcome your calls and e-mails and look forward to our next account review or conversation. Thank you for your referrals and for being a client.

Sincerely,

Vista Capital Partners

Comparative Returns:

Index	2006 Returns	Description
S&P 500	+8.1%	<i>Large Cap Stocks.</i> 500 of the largest U.S. companies in all sectors of the economy.
Russell 2000	+8.7%	<i>Small Cap Stocks.</i> A broadly diversified index consisting of about 2000 small companies.
MSCI EAFE	+12.2%	<i>International Stocks.</i> An aggregate of 21 major country indexes, excluding the U.S.
Wilshire REIT	+24.9%	<i>Real Estate.</i> Measures the performance of publicly traded real estate equity.
Lehman Bros. Aggregate Bond	+3.4%	<i>Bonds.</i> Represents the performance of the entire US bond market.