

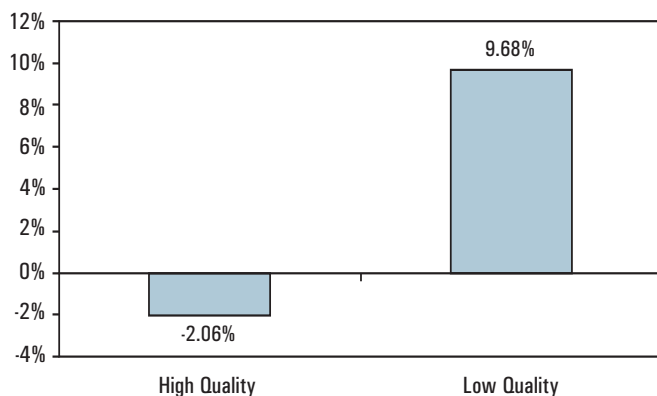
**Market Overview**

After rallying during April and May to erase much of the markets' first-quarter declines, the markets experienced one of the worst (if not the worst for certain indexes) monthly returns in history for the month of June. The markets continue to be affected by the slowing economy, persisting credit problems, and rising inflation. For the quarter, the Russell Midcap Index rose 2.67%, outperforming both the Russell 2000 Index (+0.58%) and the S&P 500 Index (-2.73%). Growth significantly outperformed value during the quarter, with the Russell 2000 Growth Index up 4.47% versus the Russell 2000 Value Index down 3.55%. Year to date through the second quarter, all equity indexes, regardless of asset class, were down in the high single-digit to low double-digit range.

Reflecting record high oil prices, energy was the strongest performing sector by a wide margin, increasing more than 30% in every small and mid-cap Russell index. Financial services was among the worst performers, continuing the trend experienced for several quarters, along with transportation and consumer staples, which were both impacted by higher commodity prices.

Low-quality stocks, as measured by S&P Credit Ratings, held up substantially better than high-quality stocks during the quarter (See chart: *Performance by S&P Credit Ratings*). Although high-quality should intuitively outperform in this type of market environment, high quality underperformed due to the large weighting of banks in the high-quality segment of the benchmarks, which were down considerably during the quarter. Excluding financials, the performance between high and low quality appeared more balanced. However, in the sectors where low quality outperformed, it was by a greater magnitude than in the sectors where high quality outperformed.

**Performance by S&P Credit Ratings**  
 Russell 2000® Growth Index



*Data is obtained from FactSet Research Systems and is assumed to be reliable. Past performance is no guarantee of future results. Data is for the second quarter 2008. High Quality - Stocks in the Russell 2000® Growth Index with an investment grade S&P credit rating. Low Quality - Stocks in the Russell 2000® Growth Index with a below investment grade S&P credit rating.*

**“At this point in the cycle, we believe owning a diversified portfolio of companies with a high return on equity, strong balance sheets, and above market earnings growth is a prudent strategy.”**

– Robert Schwarzkopf, CFA      – Sandi Gleason, CFA      – Todd Beiley, CFA  
*Chief Investment Officer & Portfolio Manager*      *Portfolio Manager*      *Portfolio Manager*

**Portfolio Overview**

The Small Cap Sustainable Growth Portfolio underperformed the Russell 2000 Growth Index for the quarter. The underperformance was driven primarily by the aforementioned performance of low quality during the quarter.

The companies that contributed the most to performance during the quarter included CARBO Ceramics and Tesco. CARBO Ceramics is the world's leading producer of ceramic proppants, which are high strength, spherical pellets used in hydraulic fracturing of natural gas and oil wells to accelerate rates of production. The company achieved a new quarterly record in revenue and proppant volumes due, in large part, to its new product, HYDROPROP, that is effectively capturing share away from resin-coated sand that is used with slick water fracturing in drilling in sandstone formations. As the company's volume increases, the company is able to leverage its excess capacity. Additionally, the company is benefiting from the strong energy prices that are increasing drilling activity and well completions. Tesco is a global leader in the design and delivery of technology-based solutions for the drilling industry through its Top Drives and Casing Services offerings. The company announced strong performance after several quarters of disappointing results due to missteps and high costs. However, Tesco mended those issues and now is back on track for strong growth. High energy prices spurring additional drilling prospects and the tight labor market in the energy industry are playing right into the company's business model of providing technology solutions to the industry.

Companies contributing the least to performance during the quarter included ScanSource and K-V Pharmaceutical. ScanSource, a leading two-tier distributor of specialty technology products, continues to produce healthy profitability, driven by the application of its unique distribution model to additional product categories and geographies. However, the stock suffered during the quarter when one of its partners mismanaged a product launch, while another mismanaged pricing in Europe. We view the issues as temporary in nature and not reflective of a change in the quality of the underlying business. Additionally, the company expanded its opportunities in telecommunications and security with the acquisition of MTV Telecom in Europe and the new vendor relationship with GE Security. Shares of K-V

*Continued on Page 2*

Pharmaceutical, a specialty pharmaceutical company with unique drug-delivery capabilities, suffered from a competitor's patent challenge to one of its key branded products. While the pharmaceutical industry is inherently litigious, we believe K-V's portfolio of differentiated delivery technologies and relationships with specialist doctors in its niche markets remain intact and provide long-term competitive protections.

### Purchases and Sales

In the Small Cap Sustainable Growth Portfolio, we increased our position in Quality Systems during the quarter. Quality Systems operates NextGen Healthcare Information Systems, a wholly-owned subsidiary that provides practice management computer systems and electronic medical records software to mid and large-sized medical practices. The shares weakened after the company reported sluggish fiscal Q4 2008 system sales growth of 2% in its core NextGen division. However, these growth rates can be volatile as customers grapple with the high up-front expenditure required for a new software platform. Importantly, NextGen's intermediate-term sales pipeline remains robust and the long-term outlook is healthy. We took advantage of the weakness to increase our position given the business' exceptional financial character, its durable competitive position, high customer switching costs, and positive organic growth outlook as governmental and industry efforts to increase the efficiency of the health-care system intensify.

### Outlook

Inflationary concerns, driven by the cost of oil rising to over \$140 per barrel, are limiting the Federal Reserve's ability to further lower interest rates to stimulate the economy. Globally, higher inflation is leading policy makers to implement policies to slow growth. This should lead to a decrease in demand for commodities over time and, if past cycles repeat, lower prices. At this point in the cycle, we believe owning a diversified portfolio of companies with a high return on equity, strong balance sheets, and above market earnings growth is a prudent strategy.

### Portfolio Characteristics

	KAR Small Cap Sustainable Growth	Russell 2000® Growth Index
<b>Quality</b>		
Return on Equity—Past 5 Years	19.9%	13.6%
Interest Expense Coverage	10.1 x	7.4 x
Earnings Variance—Past 10 Years	48.8%	92.1%
S&P Stock Ranking (A+, A, A-)	11.0%	3.0%
<b>Growth</b>		
Earnings Per Share Growth—Past 10 Years	14.0%	13.1%
Capital Generation—(ROE x {1-Payout})	18.1%	12.6%
<b>Value</b>		
P/E Ratio—Trailing 12 Months	19.3 x	32.3 x

*Data is obtained from Bloomberg, FactSet Research Systems, and a major consulting firm, and is assumed to be reliable. Other principal consultant firms may use different algorithms to calculate selected statistics. Data is as of June 30, 2008.*

As always, we endeavor to manage your portfolio with the highest quality businesses, outgrowing their markets, purchased at discount values.

*The Russell 2000® Growth Index consists of those Russell 2000® Index companies with higher price-to-book ratios and higher forecasted growth values. The S&P 500® Index is a free-float market capitalization-weighted index of 500 of the largest U.S. companies. The Russell Midcap® Index consists of the smallest 800 securities in the Russell 1000® Index, as ranked by total market capitalization. The Russell 2000® Index measures small-company stocks. Performance is calculated on a total-return basis with dividends reinvested. These indexes are unmanaged and not available for direct investment.*

*This report is based on the assumptions and analysis made and believed to be reasonable by Adviser. However, no assurance can be given that Adviser's opinions or expectations will be correct. This report is intended for informational purposes only and should not be considered a recommendation or solicitation to purchase securities. A complete list of holdings and specific securities transactions for the preceding 12 months is available upon request. Holdings are subject to change. Past performance is no guarantee of future results.*