



THE FOXHALL GLOBAL OUTLOOK



MAY 16, 2008

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Dear Paul,

My clients keep asking me when oil prices will stop going up. What do I tell them?

OIL PRICES WILL KEEP GOING UP!

As I have mentioned before in the FOXHALL GLOBAL OUTLOOK there are many factors causing oil to go up.

First is supply and demand. While we Americans continue to complain about prices, we still consumed more gasoline last year than we did the previous year. China and India are now the second and third largest auto markets in the world and they are consuming record amounts of new gasoline.

Another factor is oil is priced worldwide in “barrels per dollar” and the dollar continues to drop, which means it takes more dollars to buy the same barrel of oil.

THE “PEAK OIL THEORY” SAYS WE WILL EVENTUALLY RUN OUT OF OIL!

Almost every oil executive and analyst agrees that the world is consuming oil at a faster rate than the oil companies can find new oil reserves. That means that at some point we will reach a “peak” where the world will be consuming ever greater amounts of a decreasing supply of oil reserves.

EVENTUALLY WE WILL COMPLETELY RUN OUT OF OIL!

The oil experts can’t agree when this will happen. Some say we have already reached “peak oil,” while others say we won’t reach the “peak” for another 30 years. The point is—it will eventually happen.

The laws of supply and demand are such that whenever you HAVE INCREASING USE OF A DEPLETING SUPPLY OF SOMETHING—usually the price goes through the roof.

We often forget that Europeans have been paying \$5 to \$6 a gallon for gasoline for years. Of course most of that in the past was for taxes.

When speaking with your clients, it often helps to have all the

facts. Recently, CNN asked a number of experts what they thought were the key questions regarding oil and oil prices.

Given all the political rhetoric and misinformation about oil issues, I thought I would share with you some of their questions and answers.

HOW MUCH OIL DO WE CURRENTLY CONSUME?

In short, a lot. We consume around 30 billion barrels a year currently, which amounts to around 82 million barrels every day.

Consumption varies enormously around the world, but no prizes for guessing who uses the most. The United States guzzles a quarter of all oil produced, China, at the moment, comes a distant second with around 9 percent and Japan third with 6.5 percent.

WHO ARE THE WORLD’S BIGGEST PRODUCERS?

In 2006, the U.S. ENERGY INFORMATION ADMINISTRATION figures for production reveal that Saudi Arabia is the world’s biggest oil producer, with 10.6 million barrels being filled every day, Russia produces 9.6 million and the U.S. 8.3 million.

According to an OECD INTERNATIONAL TRANSPORT FORUM discussion paper published in 2007 there are around 47,000 oil fields in the world. But only a fraction of these—around 500—are considered “giant”—harboring upwards of 500 million barrels.

WHY HAS OIL BECOME SO EXPENSIVE?

In January 2008, oil prices reached, the not so magic, \$100 figure. Five months on and a barrel of light sweet crude oil is pushing oil towards \$130 a barrel. Some, like GOLDMAN SACHS and the ORGANIZATION OF THE PETROLEUM EXPORTING COUNTRIES (OPEC), think oil might soon cost upwards of \$200 a barrel. Good for the oil companies who are posting record profits—but bad for industry and consumers.

The reason for the rise in prices is, on the face of it, a simple tale of supply and demand. The last big oil crisis during the 1970s was more to do with supply when an Arab oil embargo made oil scarce and sent prices skyward.

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In recent years though, the exponential growth of the economies in China and India has meant the story is one of demand. Couple this with a rise in car ownership—500 million in 1990 to around 750 million in 2008. If predictions are correct then expect that figure to almost double by 2030.

If you throw in planes and trains to go with all the automobiles along with shipping, it is not difficult to understand why oil demand is rising so much.

According to THE INTERNATIONAL ENERGY AGENCY'S 2007 KEY WORLD ENERGY STATISTICS report, just over 60 percent of all the oil produced in 2005 found its way into a petrol tank of one description or another.

WHERE DOES THE OTHER 40% GO?

Booming economies, like China's, also need oil to make their goods. Not just to power the production lines, but to make a range of products we all consume every day.

All this demand has put a strain on oil refineries whose costs and workload have risen in recent years. New environmental regulations requiring 'cleaner' grades of petrol have added to their burden.

AREN'T THERE PROBLEMS WITH SUPPLY AS WELL?

Yes. Tension over supplies has never really gone away either, especially in the Middle East where decades of disagreements and conflict have continued to feed uncertainty into global stock markets. Terrorist activities and the consequent disruption to oil supplies in other parts of the world—notably in Nigeria—still provoke a collective fit of the jitters amongst economists.

WILL WE EVER RUN OUT OF OIL?

All of the world's resources are finite so we will run out at some point. The big debate at the moment is about when oil production will peak—i.e. when half of oil stocks have been used and production begins to slow.

Texan born geophysicist Dr. M. King Hubbert first came up with the “peak oil theory”—known as “Hubbert's peak”—in the 1950s, arguing that U.S. oil production would peak in the early 1970s. He was right. And since 1981, the world has been using more oil than it has been finding.

SO HOW MUCH OIL IS LEFT?

OPEC states that there were oil reserves of 1.1 trillion barrels in 2006, of which they control over three quarters. They predict that current stocks will last 81 years if consumption remained at 2006 levels—76 million barrels per day (mb/d).

But according to Professor Kjell Aleklett of ASSOCIATION FOR THE STUDY OF PEAK OIL & GAS (ASPO INTERNATIONAL) peak oil is going to happen a lot sooner.

"We have a decline in production at today's oil fields of roughly 4 percent a year. At current production levels [82mb/d] that means we are going to lose 30 million barrels a day over the next ten years," Aleklett told CNN.





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Aleklett, a Professor of Physics at Uppsala University, Sweden is concerned about the production problem allied to growing consumption.

He highlights the current situation in China. The Chinese economy is growing at around 10 percent each year and oil production in the country is at full capacity. This means that China will have to import much more oil than the current figure of 3.5 mb/d. "This will push the demand for oil to a completely different scale," Aleklett said.

He believes that the worst-case scenario for peak oil is a plateau from 2007—2012 before oil production starts to decline. The best case will be that production will go up to 93 mb/d. But he thinks that this would require the 10 giant oil fields in Iraq to go into production now.

But a report by the influential energy advisor CAMBRIDGE ENERGY RESEARCH ASSOCIATES (CERA) published in January 2008 takes a different view. Oil is not running out they say, predicting supply will top 100 mb/d by 2017.

BUT SURELY WE'LL KEEP ON FINDING OIL TO REPLACE DEPLETED STOCKS?

Well, Brazil and Mexico have found big oil fields in recent years and oil companies are investing heavily in Canadian oil sands in Alberta where it's thought to be plentiful. But like the tar sands of the Orinoco Belt in Venezuela this oil is difficult and expensive to extract, as well as being environmentally controversial.

Professor Aleklett remains pessimistic about increased rates of discovery in the coming years. "If you look at the discovery trends over the past 40 years, we will find 150 billion barrels in the next 30 years. **If you are consuming 30 billion barrels every year it means that that stock will last five years,**" he said.

WHERE ARE THE INVESTMENT OPPORTUNITIES IN ALL THIS FOR FOXHALL CAPITAL CLIENTS?

Energy is so important at FOXHALL CAPITAL that we follow both the energy markets and the alternative energy markets every day. We read almost every important study and analyst report on the subject.

As you can see from the questions and answers above, while there is some disagreement on timing, almost every energy expert knows that we will eventually run out of oil.

THE WORLD MUST BEGIN A SERIOUS EFFORT TO DEVELOP AND FIND ALTERNATIVE SOURCES OF ENERGY!

There is not one answer! There will be many answers. We will eventually be forced to build more nuclear power plants.

95% of all the electricity in France comes from nuclear power and so far, no one in France is glowing green. No matter how you feel politically, eventually nuclear power has to be part of the new energy mix.

Biofuels are another must. Ethanol has been criticized in the U.S. recently because we use a percentage of our corn crop to produce ethanol. That has driven corn prices up over 100% in the last 18 months.





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Corn is one of the worst crops to use to produce ethanol because it produces far less energy per acre than other crops like sugar cane or switch grass. The only reason farmers use it is because of U.S. Government subsidies. That make no sense whatsoever, when corn is selling at a 65-year high.

We must get rid of the U.S. corn subsidies. Then we can let the free market decide that there are far better crops to produce ethanol and that will not drive up the worldwide price of food and will produce far more energy per renewable acres of land than corn.

THE INVESTMENT OPPORTUNITIES ARE ALMOST ENDLESS!

At FOXHALL CAPITAL, we still maintain a significant investment in global energy and energy related investments. We believe, based on everything discussed in this article, that oil drilling and alternative energy investments are part of an “investment super-cycle” that will remain in a long-term uptrend for the foreseeable future.

We hope that the money we make for our clients in their energy investments will help make up for their higher prices at the pump!

UNTIL NEXT WEEK...

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PORTFOLIO COMMENTARY AND ALLOCATIONS

THE FOXHALL WAY: SOUND PROCESS + DISCIPLINE = SOMETHING FOR EVERY INVESTOR

As regular readers of the FOXHALL GLOBAL OUTLOOK know, we continue to hold a bearish view of the global developed stock markets, including the broad US and European market indexes, consistent with our January 10th long term trend following ‘sell signal’ for these markets.

FOXHALL portfolios reflect this by avoiding investment in broadly diversified domestic index funds and those of the developed international markets, such as Europe.

That portion of our portfolios that invests in these stock markets during persistent up-trending ‘bull’ markets is currently invested in what we refer to as ‘defensive’ positions.

At FOXHALL CAPITAL, we employ different approaches in ‘bull’ and ‘bear’ markets.

- In persistently up-trending markets, we go on ‘offense’, investing globally in the strongest stock markets identified by our quantitative research process, seeking growth of capital for our clients.
- In persistently declining markets, we go on ‘defense’, avoiding the higher risk of the equity markets, and instead seek to preserve capital by identifying up-trending, but lower risk, ‘defensive’ asset classes such as domestic and international bonds, including inflation-protected bonds (TIPS), as well as strong foreign currencies.





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- A unique element of our investment process is that we also seek to identify 'global hard assets', such as gold, oil, alternative energy, basic materials, other physical commodities, and the stocks of related industries (such as mining, steel, and agribusiness), that are experiencing strong investor demand. We have observed that these assets are not normally highly correlated with the global developed stock markets, and often rise when those stock markets are falling. Much academic research has pointed out that portfolio diversification is enhanced with the addition of low and non-correlated asset classes.

FOXHALL's disciplined research and execution process has positioned client portfolios as follows:

- Emerging Markets equities are at approximately two-thirds of maximum allocation within each of the FOXHALL Global ETF Series portfolios. High yielding currencies make up the balance of this allocation.
- Global Hard Assets are at maximum allocation levels within each of the FOXHALL Global ETF Series portfolios.
- Consistent with our long-term 'bearish' view of global developed stock markets, defensive positions in fixed income and foreign currencies are held instead of stocks in this allocation.

At FOXHALL, we serve a wide range of clients with money management services that are appropriate for their risk profile and time horizon. By allocating differing amounts to higher and lower risk asset classes, we vary both the income produced and the volatility of the portfolio's returns to seek to meet the current income needs of those in retirement, or the wealth creation goals of those with many years left in the workforce.

FOXHALL offers four diversified ETF based strategies within the FOXHALL Global ETF Series: Growth, Growth & Income, Balanced, and Conservative. We also offer three targeted ETF based strategies: Global Hard Assets, Pacific Rim & Emerging Markets, and Strategic 50-50.

Whether you are a conservative, income seeking investor, or focused on growth of capital, FOXHALL has a strategy designed to fit you!

As always, we are watchful for emerging trends, prepared to take action as global economic and market conditions unfold, using our sound, repeatable investment process combined with disciplined action for the benefit of our clients.

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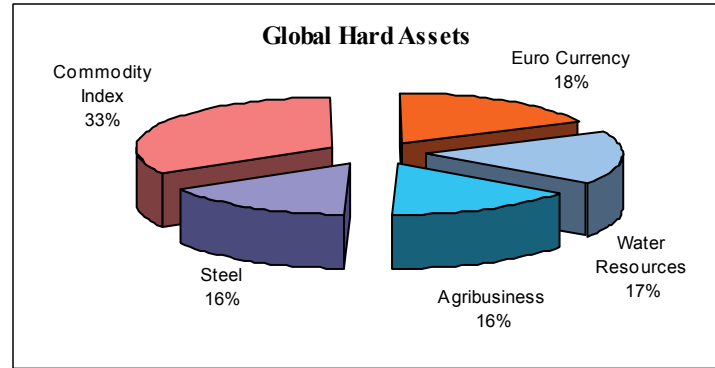
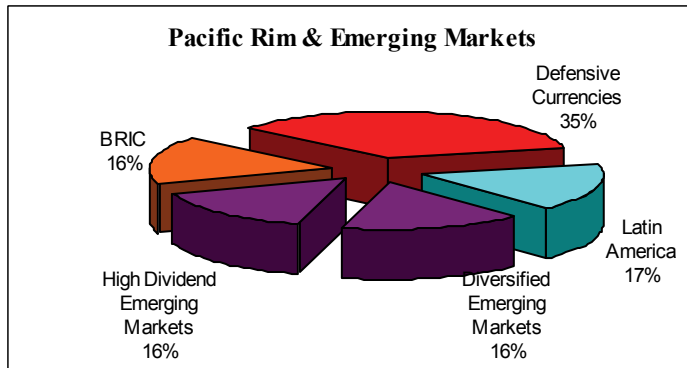
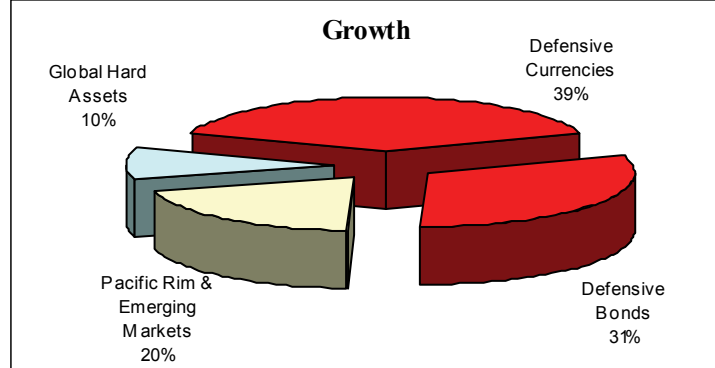
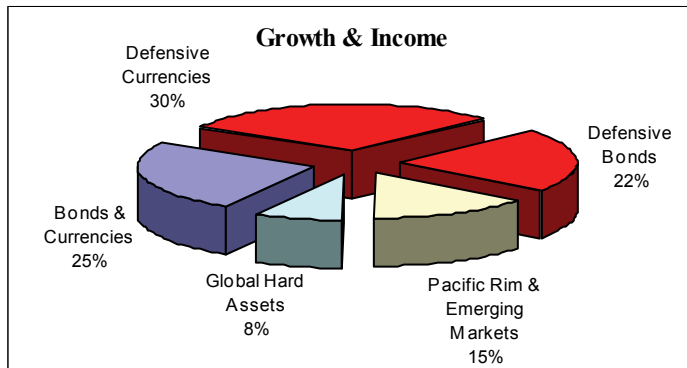
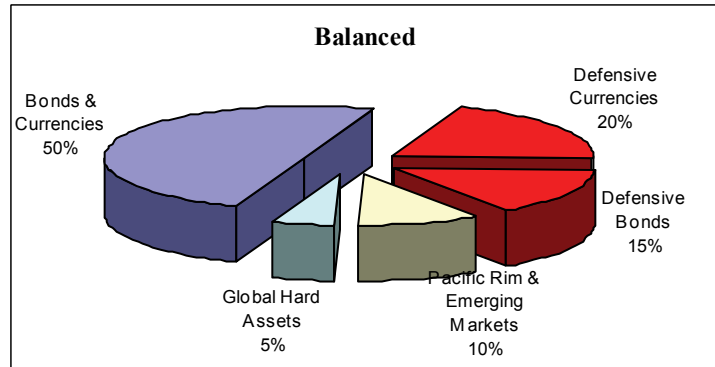
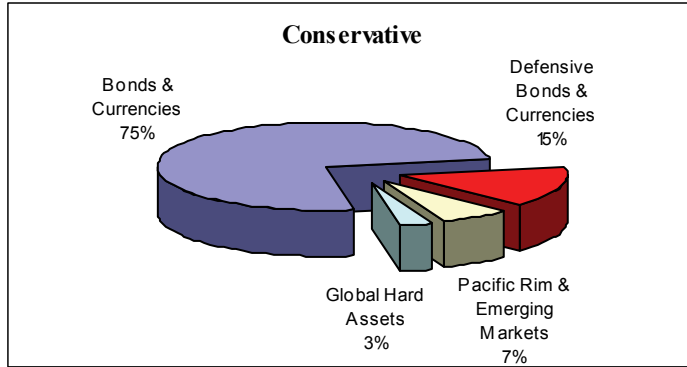
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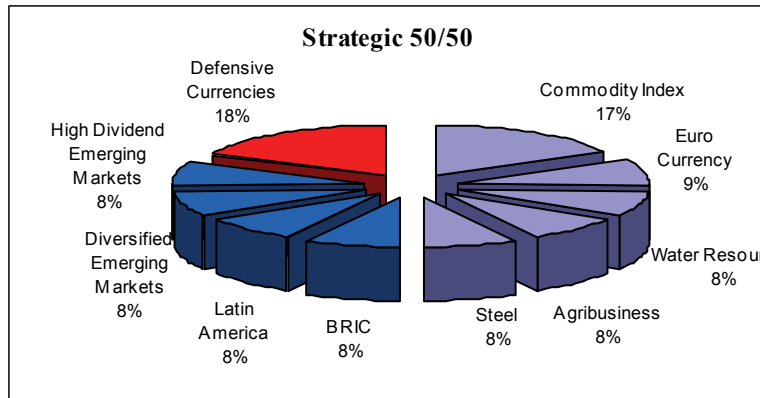
THE FOXHALL GLOBAL OUTLOOK GLOBAL MARKET ROTATION PORTFOLIOS

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- Emerging Markets ■
- Hard Assets ■
- Defensive Position ■



The allocations illustrated are model allocations, actual client accounts could vary due to many factors. Variable annuity/variable life accounts will vary significantly due to the availability of investment options in each contract. All allocations may change without notice.