

Investment Pool Allocations

For more than a year now, the NCF investment management team has been acting to reduce the risk characteristics of the investment pools while still honoring the targeted allocations of 80%, 60% and 40% equities in the Growth, Balanced and Conservative pools, respectively. As a result of those modifications, the year to date, one-year and three-year numbers of all the pools are better than their benchmarks and, in some cases, dramatically better. We have effectively limited our losses despite a punishing 3rd quarter.

Of equal importance, we were even more defensively positioned at the end of the quarter. We did not add capital back to equity managers as the markets declined, but instead held our cash. After the close of the quarter, we then rebalanced to targets by making additional investments with our defensive hedge fund managers. Overall, therefore, we are confident that our pools will continue to perform well relative to targets should the markets decline further in the future.

Global Markets Overview*

The ongoing credit crisis reached extraordinary intensity in the third quarter 2008, resulting in historic changes to the financial industry, a virtual freeze in the credit markets, and the most far-reaching government intervention in the financial markets in US history. Some of the more notable events in this startling quarter included the bankruptcy of Lehman Brothers, the takeover of Fannie Mae, Freddie Mac and AIG by the US Government and, just after the quarter, the passage of a massive \$700 billion package of Federal aid to the financial system. By the end of the quarter, most commentators believed the US was in or near a recession.

Throughout this startling time, credit markets temporarily stopped functioning and yields on 90-day US Treasury bills actually turned negative as a result of investor fear and a flight to safety. Nonetheless, the markets did ultimately continue working and NCF emerged from this volatile period relatively unscathed. All of our cash and money market funds were secure and are now largely government insured. Our pools with equity investments, while lower, have not suffered catastrophic losses, nor do we expect them to do so in the future. Overall, we are grateful to be weathering this storm as well as we are.

Additional Information

This Market Overview is part of a more complete performance report that is available on-line in the "Forms & Reports" section of the NCF website: www.nationalchristianfoundation.com.

Equities

US equity markets in the quarter came under pressure due to the credit crisis and evidence that the US was in or near a consumer-led recession. US consumer spending growth faced challenges due to tightening access to credit, declining home values, and rising unemployment. The S&P 500 declined 8.4% in the quarter and 19.3% year to date.

Among stock market sectors, only Consumer Staples—traditionally considered a safe harbor for investors—was positive, up 4.1%. Healthcare and Financials were flat. Declining commodities prices caused the Energy sector—a lead performer over the last several years—to fall sharply by 25.0%.

Small Cap stocks outperformed Large Cap stocks in the 3rd quarter, with the Russell 2000 declining a mere 1.1% as small cap stocks appear to have benefitted from their lack of exposure to large financial firms. US Small Cap companies also had a relative benefit in the slowdown of global growth and the strengthening of the US dollar.

International Markets

International equity markets underperformed the S&P 500 because of growing evidence that both the credit crisis and a dramatic economic slowdown were global phenomenon and not just a US problem. Losses were magnified for US-based investors by the strengthening US dollar, which benefited from the flight to quality and the retreat of US investors from global markets. The Morgan Stanley EAFE (Europe Asia Far East) index declined 20.6% in the third quarter and 29.3% year to date.

Fixed Income

The dominant theme of fixed income performance in the third quarter was investor fear. The inexorable spread of the credit crisis caused investors to lose confidence and led to a virtual freeze in the credit markets, including the Municipal bond market.

Fixed income returns mainly reflected investors seeking safety by purchasing Treasuries, which led performance with a rise of 2.3% in the ML US Treasury Master Index. In general throughout this period, the riskier the bonds, the more those bonds underperformed short term treasuries. The ML US Corporate and Government 1-5 Yrs Index, which is closest to the bonds held by NCF, declined a mere 0.2% in 3rd quarter and was up 1.56% year to date. As you will see in the following pages, our bond investments did considerably better than the index.