



WINTER 2008



trust & investment perspectives

Hey, Let's Be Careful Out There **by Nils L. Berglund**



A generation ago one of the "must watch" dramas on television was *Hill Street Blues*, a show about the lives and work of an inner-city police precinct. Each episode began with a squad meeting during which officers got their assignments for the day. Each meeting ended with Sergeant Phil Esterhaus reminding everyone, "Hey, let's be careful out there." Off they went, to face challenges known and unknown.

As we set out on 2008, we are inclined to follow his advice – it is a time to be careful out there. There are challenges for investors, known and unknown, that will test us over the upcoming year, and we must begin to prepare for those challenges today. At the same time, we must remind ourselves that challenges often beget opportunities and it is our job to seek out these opportunities, as well as evaluate existing positions.

Newspaper and internet headlines, television and radio news readers, and pundits of all stripes remind us daily of the challenges, with tales of economic woe and concern. These sources point out that the dollar is in critical condition. China and our other trading partners control our

economic fate by holding so much of our debt. Crude oil is headed through \$100 per barrel and is on its way to being re-priced in Euros; gold is looking at the same dynamic, but with \$1,000 per ounce being the target. The U.S. economy is in or is teetering on the brink of a recession caused by the collapse of the home construction market, and the Fed is either powerless or unwilling to do enough to keep recession at bay. U.S. credit market participants "gamed" the system and are now being forced to pay the piper in massive writedowns of bad loans/investments. Include as well the

rhetoric of the upcoming Presidential election, the soon-to-expire income- and estate-tax cuts put in place earlier this decade, and the looming Social Security and Medicare funding shortfalls, and each dip in the stock market is said to herald a much larger decline.

Despite these and other concerns that have caused the market to retreat from its October highs, we remain confident in the long-term resiliency of the U.S. economy and, in turn, the stock market. The fourth quarter of 2007 and the first half of 2008 should be a time of testing and sorting out **continued on page 4**



Pennsylvania Trust Welcomes New Board Member

Richardson T. Merriman, President and Chief Executive Officer of Pennsylvania Trust, is pleased to announce that Peter J. Vogt, FSA, MAAA, has joined Pennsylvania Trust's Board of Directors. Mr. Vogt serves as Executive Vice President and Chief Financial

Officer of Penn Mutual and has over 20 years of experience in the financial services industry. He joined Penn Mutual in June of 2005 from CIGNA Group Insurance, where he served as Senior Vice President and Chief Financial Officer.

Mr. Vogt holds a bachelor's business administration degree in actuarial science and economics from Temple University. In addition, he attended the ITT Executive Development Program at Duke Fuqua School of Business.



President's Message

It's January – time to take stock, make new plans, and move forward.

While taking my mental inventory of 2007, I see the past year as having been very productive for Pennsylvania Trust. We welcomed new clients and I thank them, as well as those who have been long-time supporters of Pennsylvania Trust. We added talented new staff and officers. They have bolstered our capabilities and areas of specialized expertise while helping us maintain a client-to-staff ratio that is among the most favorable in our industry. To further enhance our ability to provide personal high quality attention, we continued to invest in technology solutions geared to reduce time-consuming paperwork and put more – and more useful – information at our fingertips.

In that same information-sharing vein, we invited former Secretary of Defense William Cohen to present his views on the global geopolitical and business environment at our annual Investor

Seminar. Moving from the macro to the micro, we held our first jointly sponsored client seminar, at which a panel of experts in the valuation and protection of collectibles and other tangible assets provided very useful insights.

As an update on our investment solutions, we continue to add to our suite of offerings, most recently with the introduction of a quantitatively driven investment strategy. The investment professionals at Pennsylvania Trust guided it and our other investment strategies to strong results in a market that, for at least half the year, was less than cooperative.

Entering 2008, we are actively searching for more ways to provide information you can use, and outside resources that can address specific wealth-management challenges. Meanwhile, the investment team is working to keep the portfolios advantageously positioned. Because the stock market still seems reluctant to let go of 2007's problems and move ahead, our team is

exercising a measure of caution amidst the chaos while looking for the stocks that could lead the next move forward (see Nils Berglund's article page 1).

One area where things will definitely advance in 2008 is assisted living services for residents of Pennsylvania. On page 3, Jean Hunt discusses a newly enacted law that will give Pennsylvanians greater flexibility and more rights in health care decisions and in the receipt of supplemental health care services, without the need to enter a traditional nursing home.

All things considered, I am optimistic about 2008 for our clients. We are better positioned than ever before to actively respond to this new year's challenges and opportunities. As always, we look forward to helping you and your families.

With many thanks for your support of Pennsylvania Trust,

Richardson T. Merriman

President and Chief Executive Officer

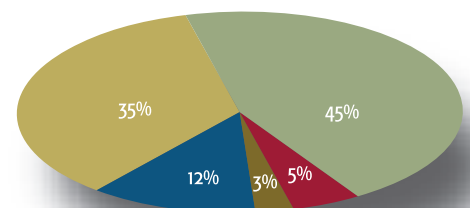


2007 Investor Seminar

In October, over 200 clients and guests of Pennsylvania Trust attended our fourth annual Investor Seminar which featured a presentation by the Honorable William S. Cohen, former U.S. Secretary of Defense and three-term United States Senator, pictured here with Pennsylvania Trust

CEO Richardson T. Merriman. His illuminating presentation on the promises and perils of the new world put into perspective the responsibilities we face in a global economy.

Balanced Asset Allocation



- Large Cap
- International
- Mid Cap
- Fixed Income
- Small Cap

TRUST TALK

Pennsylvania's New Assisted Living Legislation by Jean E. Hunt, Esq., CPA



On October 23, 2007, Pennsylvania's law regulating assisted living residences became effective. Prior to that date, Pennsylvania was one of 11 states that did not have such a law. The new law was modeled on those of Vermont, Oregon, and New Jersey, all early leaders in regulating assisted living residences. The General Assembly's findings envision assisted living residences as "a combination of housing and supportive services that allow people to age in place, maintain their independence, and exercise decision-making and personal choice." The law provides for the licensing and regulation of facilities that call themselves assisted living residences. Once the regulations are in place (1/09), such residences must comply with the law or stop calling themselves assisted living facilities.

Prior to this new legislation, there were two types of residential facilities in Pennsylvania: nursing homes and personal care residences (PCR). Nursing homes are regulated by the federal government and the Pennsylvania Department of Health. PCRs are regulated by the Pennsylvania Department of Welfare. In 2005 new PCR regulations were implemented, resulting in stricter inspections and enforcement. As a result, many PCRs closed. Such residences are appropriate for those who need help with the basic aspects of daily living such as dressing, bathing and eating; they provide no nursing or medical care. Therefore, individuals

who need more than custodial care are forced into the institutional setting of a nursing home. They cannot stay in a PCR.

Today there are many facilities in our area which call themselves assisted living centers. However, these facilities are really PCRs in terms of the licensing that they have received from the state.

With the passage of the new law and the development of regulations to implement it, Pennsylvania will establish a procedure for inspecting and licensing assisted living residences. These facilities must obtain such a license from the state. If they do not obtain a license they will continue as PCRs. The impetus behind the new legislation was to allow individuals to obtain supplemental health care services so that they would not have to move to a nursing home when their health declined. In addition, the new law permits the residents to participate in their care plans and negotiate the terms of their residency in an atmosphere of "informed consent."

The law also provides for the licensure of home health care services and establishes (through the regulations) procedures for investigation of aides. There will be specific staffing and educational requirements for employees of licensed assisted living facilities. Also the minimum square footage of the residences' living suites will be specified.

An assisted living residence that advertises a special unit for the cognitive impaired must meet specific criteria to

use the "special care" designation. This designation means the facility must be "capable of providing cognitive support services to residents with severe impairment in the least restrictive manner to insure safety." Such services will require a higher level of education and training for staff.

Additionally, all supplemental care above the basic personal care level must be priced separately. A resident can then utilize whatever service and care level is appropriate to allow him or her to continue to live in the assisted living residence. The regulations will require that the assisted living facility undertake an initial standardized screening of the resident to determine the potential services that will be required. While licensed assisted living facilities will be able to offer significantly more medical care than is currently offered in PCRs, there are some medical conditions for which nursing home placement is required. These include ventilator dependency, continuous intravenous fluids, and medical conditions that require continuous skilled nursing care 24 hours a day.

The goal of this legislation is to allow seniors to remain in a residential setting, actively involved in their health care decisions, and receiving supplemental health care services, without transferring to an institutional nursing care setting.

Ms. Hunt is Senior Vice President in the Trust Department at Pennsylvania Trust.

continued from page 1 as the economy displays more weakness than we have seen in a number of years. Yet recent strength in information technology and industrial stocks suggests that the economy will generally hold together. Given our underlying bullishness, we will be looking at the behavior of many of the stocks that fell most dramatically late in 2007, especially the financial stocks, for signs of improvement and some market opportunities. At the same time, we are not abandoning those stocks that have continued to perform well, especially if their progress has benefitted from consistent above-consensus earnings growth.

For nearly five years, the stock market has not seen a decline of greater than 10%. We believe this is a sign of both economic progress and reasonable

valuation. Helped by a weaker dollar, U.S. exports of all types have grown, corporate earnings have increased as overseas profits were translated into dollars, and returns on foreign investments have been similarly enhanced. Stocks have ridden this earnings recovery back from the 2002 bottom, with the S&P 500 nearly doubling in that time period. Despite these gains, we still see U.S. stocks as attractively valued. Today, the market is valued at only 14 times forward earnings, well below the peak ratio of 25 set in 1998-99 and 18 times the figure at the end of 2003.

Barring a sustained hit to corporate earnings as a result of some expected economic weakness or more fallout from the mortgage/credit debacle, we believe the market's valuation will eventually provide the necessary support to pull the

market higher. However, we do wonder if this is the right time to be aggressive. It may be that only time is needed to sort out the impact of the weaker economy, but we could also encounter a softer market early in 2008.

Reflecting our caution, we are allowing our cash position to increase by 5% of the portfolio. We are raising our fixed income/cash position in long-term oriented balanced accounts to 35%, keeping any cash raised from stock sales in short-term investments. Our new stock allocation is 65% (67% large cap, 20% international, 8% mid cap and 5% small cap stocks). The risks are real and, for now, we want to be more careful out there.

Mr. Berglund is Senior Vice President of Portfolio Management at Pennsylvania Trust and a member of the Investment Committee.

Painting Profile



Pennsylvania Trust is proud to feature the work of artists such as Ann Lofquist (b. 1964). A native of Washington, D.C., Lofquist earned a B.F.A. from Washington University School of Fine Arts in St. Louis, Missouri, and an M.F.A. from Indiana University, Bloomington. Ms. Lofquist is known for her exquisite New England landscapes. She describes her large landscapes as depicting "the immediacy and poignancy of the moment of discovery." Shown above is 'Foundry Hill, Morning.'



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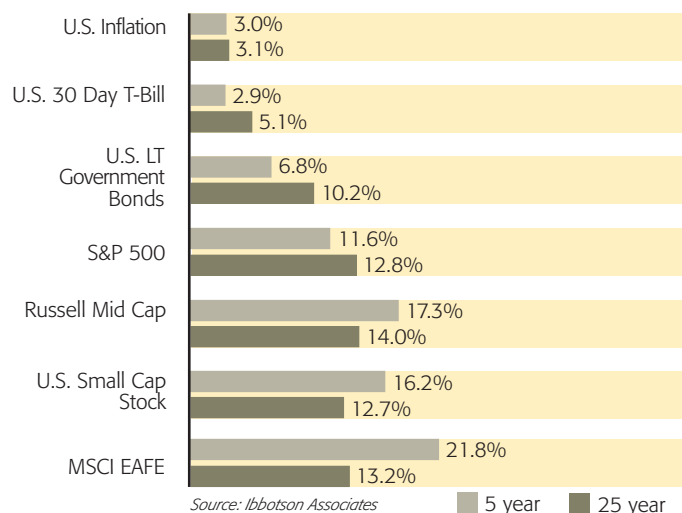
Pennsylvania Trust is committed to conduct all our relationships with integrity and to maintain the highest ethical standards; provide outstanding professional and personalized services; produce superior investment results consistent with client objectives; and retain exceptionally skilled individuals, empowering them with state-of-the-art technology.

Market Indicators

	Current	Three Months Ago	One Year Ago
Stock Indices	12/31/07	9/30/07	12/31/06
Dow Jones Industrial Average	13,265	13,896	12,463
Standard & Poor's	1,468	1,527	1,418
U.S. Treasury Yields			
2 Year	3.0%	4.0%	4.8%
5 Year	3.4%	4.2%	4.7%
10 Year	4.0%	4.6%	4.7%
30 Year	4.5%	4.8%	4.8%

ANNUALIZED RETURNS OF SELECT ASSET CLASSES

Over the past 25 years, equity returns have outpaced bonds, cash and inflation.



CORE LARGE CAP DIVERSIFICATION

In order to maintain a well diversified large cap common stock portfolio, we recommend the following relative sector weightings within the Standard & Poor's 500:

S&P 500 Sector Weightings	Pennsylvania Trust	
Consumer Discretionary	8.5%	—
Consumer Staples	10.2%	—
Energy	12.9%	=
Financials	17.6%	—
Health Care	12.0%	=
Industrials	11.5%	+
Information Technology	16.7%	+
Materials	3.3%	+
Telecommunication Services	3.6%	=
Utilities	3.6%	=

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