



Mid-Quarter Newsletter

August 15, 2008

From My Corner

Jeff Mengis – President

It's hard to believe that another beautiful Pacific Northwest summer is coming to a close and making way for fall. I hope you have been able to enjoy the summer with your family and friends. Sunriver seemed to be the vacation spot of choice for the Mengis office this year. Cindy made her trip with the family to Sunriver in July, while I visited with my family in August. Both of us had a great time with our families playing tennis, riding bikes and exploring. It's hard to believe that it's already time to send the kids back to school.

The end of summer also means that traders on Wall Street are returning to work and reevaluating their investments. As you may know, the continued financial turmoil has resulted in a flight to quality which has caused investors to buy treasuries, sending the 10-year bond yield lower to 3.9% and the 2-year note down to 2.4%. Declining treasury yields have led to lower yields in money market funds (MMF). For example, the Schwab Prime Reserves MMF, is yielding approximately 2.1%.

Fortunately, there are options available for those seeking more cash flow from their assets and are willing to take some additional risk. Select corporate bond yields are looking more attractive when compared to MMF yields. We recently bought investment grade corporate bonds without financial sector exposure in the 2012-2013 maturity range that are yielding around 5.25-5.75%. This area of the yield curve offers attractive returns while providing less volatility when compared to long-term bonds. In addition, as part of a diversified fixed income portfolio, we have been adding to positions of the Goldman Sachs Hi Yield Bond Fund yielding about 9%. If you have a CD maturing soon, or money earning a lower interest rate, you may want to contact us to discuss these fixed-income options.

In the meantime, I hope you have had a good summer to date and are able to enjoy the warm weather while it lasts.

Investment Focus:



AT&T (T) is one of the largest telecom providers in the world and the largest in the U.S. Its sales in 2007 were split between landline voice (34%), data (20%) and wireless, etc. (46%).

During the last quarter, wired revenue fell 2.1% year-over-year while wireless segment revenue rose by 15.8%, fueled largely by a 52% increase in wireless data revenue. That revenue growth illustrates why customers that use 'smartphone' mobile devices with the ability to surf the web are the most desirable users among telecom companies. We think AT&T has a considerable competitive advantage because it has the exclusive rights to the hottest smartphone around: Apple's iPhone.

We feel the iPhone will be a long-term success and that AT&T is one of the best ways to benefit from iPhone sales. The iPhone is essentially a phone, computer, video device and music player in one that has exclusive access to Apple's iTunes music and video library. AT&T did not benefit as much as hoped from sales of the original iPhone, because many phones sold were never connected to AT&T's network. In order to ensure that iPhones are used with the AT&T network, AT&T has subsidized the initial price of the new 3G iPhone from \$399 to \$199 for customers signing a 2 year contract. The 3G iPhone sold over 1M units in its first weekend and some analysts predict worldwide iPhone sales of 45M through 2009. The initial subsidy cost to AT&T will be high, but we feel AT&T will be rewarded over the long-term with high-margin, loyal customers.

The stock is trading at 9.5X forward earnings, toward the bottom of their 5 year valuation range. This lower price is due to fears that AT&T's wired phone business is shrinking and higher marketing costs have reduced margins for their wired bundle service "U-Verse". We feel those concerns are adequately priced into the stock. With consensus earnings growing at around 10% for the next few years and a 5% yield, we believe AT&T is a good buy.





Investment Strategy and Goal

The *Focused Taxable Composite* seeks long term capital appreciation by investing in companies which, in MCM's judgment, offer value relative to their long term potential and the market as a whole. Using a multi-cap approach, the composite is able to invest in companies of all sizes, although most companies have market capitalization in excess of \$500 million. Our overall goal is to consistently outperform the S&P 500 index.

This information is presented as supplemental and complements the Annual Disclosure Presentation located at the bottom of this page

Top 10 Holdings (as of 06/30/08)

Intel	6.3%
Qualcomm	5.9%
Costco	5.6%
National Oil Well Varco	5.4%
Genentech	5.0%
Amgen	4.5%
Cisco	4.5%
General Electric	4.4%
Precision Castparts	3.9%
Du Pont	3.7%

Data presented represents a percent of the total market value of the Focused Taxable Equity Composite, including cash. As of June 30, 2008, cash represented 8.7% of the total composite. This information is presented as supplemental and complements the Annual Disclosure Presentation located at the bottom of this page.

Performance

	1 Year**	3 Year**	5 Year**	Since Inception** 10/1/98
Focused Taxable Composite	-10.97%	5.66%	9.54%	9.41%
S&P 500 Index	-13.12%	4.41%	7.58%	4.07%

* Past performance does not guarantee future results. Numbers are net of fees.

** Annualized performance figures

Mengis Capital Management, Inc., has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®). Mengis Capital Management, Inc. is a registered investment advisor. The firm maintains a complete list and description of composites, which is available upon request. Performance prior to November 28, 2001 occurred while the portfolio manager was employed at a prior firm and was the only individual responsible for selecting the securities to buy and sell. Compliance with the Association for Investment Management and Research Performance Presentation Standards (AIMR-PPS®, the predecessor to GIPS) was verified at the prior firm, beginning February 1, 1998. As represented by management, the performance from the predecessor firm conforms to the GIPS guidelines with regard to portability of investment results. Focused Taxable Equity Composite contains fully discretionary taxable equity accounts and for comparison purposes is measured against the S&P 500 Index. Sector weightings observed in the Focused Taxable accounts vary significantly from those in the S&P 500 Index. In addition, from time to time, the Focused Taxable accounts will generally have 20-30 holdings as compared to the S&P 500 Index (composed of 500 different stocks). Due to the limited number of holdings relative to this index, the investment risks associated with concentration are significantly greater for the Focused Taxable accounts than it is for the index used for comparison. For periods shown prior to January 1, 2006, the minimum account size for this composite is \$50 thousand. Effective January 1, 2006, the minimum account size has been changed to \$150 thousand. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. At present, there are 14 accounts being managed consistent with the discipline referred to as "Focused Taxable." Mengis Capital Management, Inc. currently manages over 200 other portfolios on a discretionary basis. These portfolios are not managed according to the Focused Taxable methodology and the results in these accounts will vary, both positively and negatively, from those experienced by the Focused Taxable accounts. Information regarding the performance achieved in these accounts is available upon request. The U. S. dollar is the currency used to express performance. Returns are presented gross and net of management fees and include the reinvestment of all income. Net of fee performance was calculated using actual management fees. Beginning January 1, 2002, gross returns are reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Prior to January 1, 2002, accounts in the composite were charged an all inclusive wrap fee. Gross returns for this period are shown as supplemental information and are stated gross of all fees and transaction costs; net returns are reduced by all actual fees incurred. The standard management fee is a maximum of 2.00% on all assets. Additional information regarding policies for calculating and reporting returns is available upon request. There has been no material change in personnel responsible for the investment management of this composite. The Focused Taxable Equity Composite was created October 1, 1998. Past performance is not indicative of future results. Investments are subject to market fluctuations and investors could lose some or all funds invested.

	Total Firm Assets (thousands)	Composite Assets		Accounts at Year End	Asset-Weighted Annual Return		S&P 500	Annual Composite Dispersion
		US Dollars (thousands)	% of Firm Assets		Gross	Net		
2007	121,952	17,970	15%	14	8.29%	7.20%	5.49%	2.5%
2006	97,596	15,637	16%	16	14.66%	13.50%	15.80%	1.1%
2005	89,242	15,206	17%	12	9.55%	8.49%	4.88%	1.1%
2004	85,368	11,016	13%	9	17.70%	16.51%	10.88%	1.2%
2003	86,803	8,414	10%	13	30.04%	28.79%	28.69%	1.1%
2002	61,896	4,072	7%	10	(24.82%)	(25.44%)	(22.10%)	2.2%
2001*	45,728	1,848	4%	8	(9.74%)	(11.16%)	(11.88%)	4.4%
2000*		1,404	2%	6	35.90%	33.49%	(9.11%)	N.A.
1999*		481	1%	5 or fewer	25.13%	22.35%	21.04%	N.A.
1998*		137	<1%	5 or fewer				

- N.A. - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year.

- *Information presented pertains to portfolios managed by the portfolio manager while affiliated with a prior firm. Their presentation conforms to AIMR-PPS guidelines (the predecessor to GIPS) regarding the portability of investment results.

- S&P 500 Index performance returns reflect gross dividends reinvested into index. S&P Index performance returns through September 30, 2001, were obtained from Bloomberg; index performance returns for periods after September 30, 2001, were calculated using data from FT Interactive Data.