THE COMPASS

A QUARTERLY NEWSLETTER FROM MARTIN CAPITAL ADVISORS, LLP
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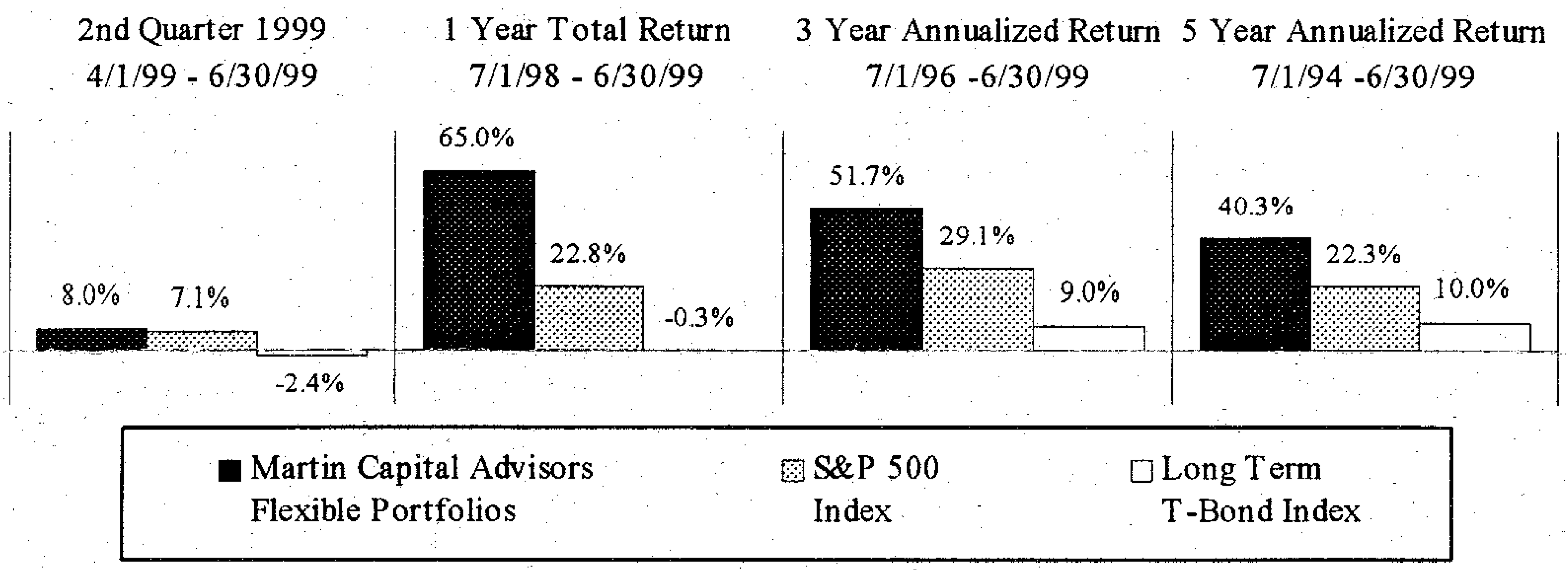
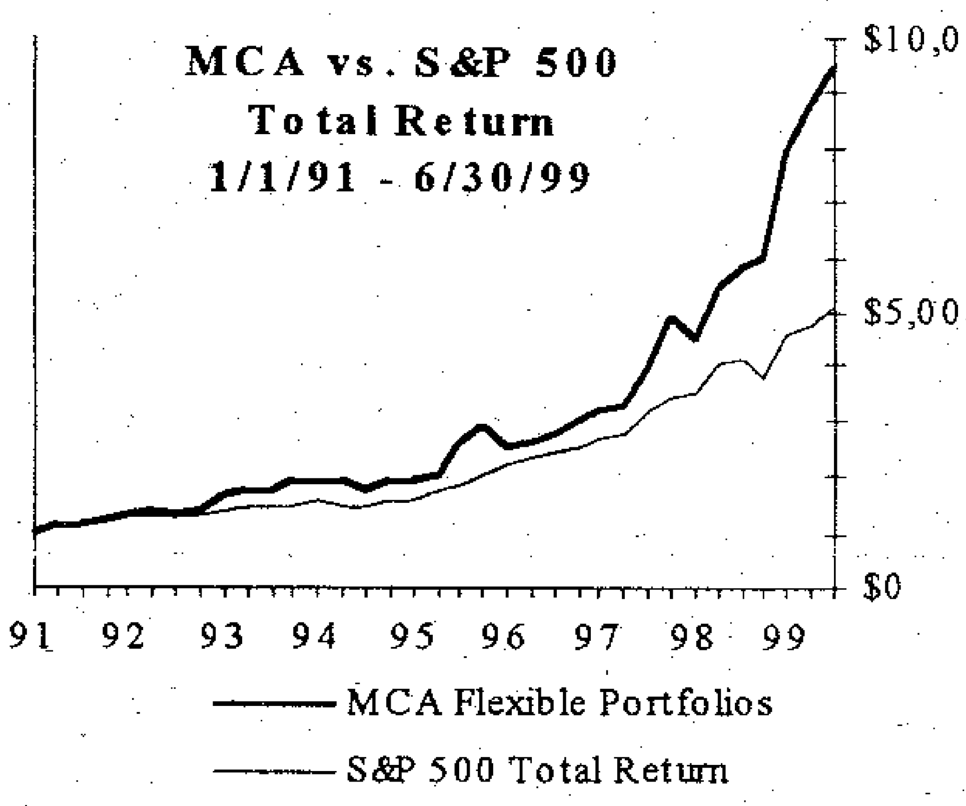
July 1, 1999

Investment Results





MCA Flexible Portfolio 12 Month Tax Efficiency: 97.2% (After Tax Return divided by Before Tax Return)

Investment Perspective

Stock market returns for the second quarter were slightly higher than anticipated in the April newsletter. In line with expectations, however, stocks moved higher during the first part of the quarter, then gave back some of the gains as the quarter progressed. A strong rally at the end of the quarter pushed prices back up to previous highs. This surge at the end of the quarter came earlier than forecast, but was in line with our belief that the bull market will continue to surprise more to the upside than the downside. Interest rates finished the quarter significantly above our April estimate. Higher oil prices were the primary cause of what we believe to be a temporary rebound in inflation statistics, but the bond market continues to over-react to short-term inflation concerns, despite long-term deflationary economic trends.

The third quarter should see a continuation of the stock market rally that began at the end of the second quarter. We plan to remain almost fully invested, but may hold on to some cash to deploy in the event of a stock market correction later in the quarter. At current stock market prices, we are neutral short-term and bullish long-term. Consequently, we will continue to maintain a high level of stock market exposure even as the risk of a short-term correction increases. As inflation statistics return to their long-term disinflationary trend, long interest rates should fall back to around 5.5%, which is about the middle of their recent range.

As reported in the last newsletter, the Martin Capital U.S. Opportunity Fund began operations at the end of March. The fund is managed the same as our Flexible Portfolios. The minimum investment is one thousand dollars. A prospectus is available on request. The Austin Opportunity Fund will be available for purchase on the first of September. The Texas Opportunity Fund should be available for purchase later this fall.

Nelson's *World's Best Money Managers* (http://www.nelnet.com) is now rating our Flexible Portfolios in their U.S. Equity (all styles) and U.S. Equity Growth categories instead of their U.S. Tactical Asset Allocation and U.S. Balanced/Multi-Asset categories. Although our Flexible Portfolios continue to be tactically allocated, this change was necessitated by the Securities and Exchange Commission's concern that our high equity allocation has resulted in much higher returns than would normally be expected in a tactical asset allocation portfolio. Despite the fact that our Flexible Portfolios have a lower-return bond component, Nelson's ranks our Flexible Portfolios near the top of their U.S. Equity (all styles) returns for all time periods up to and including five years. **For example, our three-year Flexible Portfolios' return is ranked number 3 out of 1347 equity portfolios.** An independent performance review for 1991 through 1998 by the certified public accounting firm Jeff D. Heard, Jr., P.C. is available on request.

Market Timing Viewpoint

Recommended Tactical Asset Allocation

Stocks 90% (Δ UNCH) Bonds 10% (Δ UNCH) Cash 0% (Δ UNCH)

Performance Expectation

	September 30, 1999		December 31, 1999		December 31, 2003	
	Target	% Change	Target	% Change	Target	% Change
DJIA/S&P 500	11520/1440	+ 05.0%	12070/1510	+ 10.0%	21950/2750	+ 100.0%
Nasdaq Comp.	2820	+ 05.0%	2955	+ 10.0%	6000	+ 120.0%
30 Year T-Bond	5.70%	+ 05.0%	5.40%	+ 10.0%	4.00%	+ 35.0%

20 Largest Common Stock Positions

(Prices as of June 30, 1999)

1 Dell Computer	37.00	6 Applied Materials	73.88	11 Whole Foods Mkt	48.06	16 Enzon	20.69
2 Charles Schwab	109.00	7 Intel	59.50	12 Sun Microsystems	68.88	17 Motorola	94.75
3 Cisco Systems	64.44	8 Hewlett-Packard	100.50	13 Tiffany	96.50	18 Citigroup	47.50
4 Microsoft	90.19	9 Home Depot	64.44	14 Oracle	37.13	19 Starbuck's	37.56
5 Texas Instruments	144.00	10 Southwest Airlines	31.13	15 Williams-Sonoma	34.81	20 Sprint	53.00

Investment Philosophy

Our investment approach focuses on the reality that in order to achieve long-term superior performance there must be an acceptance of some amount of short-term risk. With this in mind, we pursue an investment allocation strategy emphasizing a diversified mix of stocks and bonds - structuring our clients' portfolios according to their ability to withstand short-term volatility in the pursuit of long-term investment returns.

Both fundamental and technical factors are taken into account in determining a prospective investment's risk-reward ratio. Socially responsible issues, such as environmental policies and employee relations, are evaluated as part of our investment risk assessment.

Overall market risk is considered in the timing of investment decisions and the implementation of hedging strategies. The reduction of investment exposure during periods of high market risk, and the complementary increase of investment commitment during periods of low risk, should normally reduce volatility and enhance portfolio performance.

Our general goal, which will vary depending on market conditions and individual client risk tolerance, is a 15% to 20% average annual return over the course of a five year period or market cycle. We expect this goal can be achieved with minimized volatility through our combination of risk-reward analysis and market timing strategies.

Comparison of Investment Results

		Performance of Relevant Indexes					
	Martin Capital Advisors*	Dow Jones Industrial Average	S&P 500 Index	Wilshire 5000 Index	Long-Term T-Bond Index	Money Market Avg. Yld.	Consumer Price Index
1991	+ 33.9%	+ 24.5%	+ 30.6%	+ 34.2%	+ 18.5%	+ 5.2%	+ 3.1%
1992	+ 26.8%	+ 8.0%	+ 7.7%	+ 9.0%	+ 8.0%	+ 3.3%	+ 2.9%
1993	+ 14.5%	+ 18.1%	+ 10.0%	+ 11.3%	+ 17.3%	+ 2.7%	+ 2.7%
1994	- 2.1%	+ 5.9%	+ 1.3%	- 0.1%	- 6.9%	+ 3.8%	+ 2.7%
1995	+ 27.5%	+ 36.9%	+ 37.6%	+ 36.5%	+ 30.7%	+ 5.5%	+ 2.5%
1996	+ 29.4%	+ 29.1%	+ 23.0%	+ 21.2%	- 0.8%	+ 5.0%	+ 3.3%
1997	+ 41.4%	+ 24.9%	+ 33.4%	+ 31.3%	+ 15.1%	+ 5.1%	+ 1.7%
1998	+ 78.8%	+ 18.1%	+ 28.7%	+ 23.4%	+ 13.5%	+ 5.0%	+ 1.5%
1999 YTD	+ 19.6%	+ 20.4%	+ 12.2%	+ 11.9%	- 6.6%	+ 2.2%	+ 1.1%
Total**	+848.8%	+428.5%	+410.4%	+387.6%	+120.8%	+ 44.6%	+ 23.6%
Avg.***	+ 30.3%	+ 21.7%	+ 21.2%	+ 20.1%	+ 9.8%	+ 4.4%	+ 2.5%

* Total Annual Performance, net of commissions, fees, and expenses, of all Martin Capital Management flexible investment portfolios. Audited 1991 through 1998 by Jeff D. Heard, Jr., P.C., Certified Public Accountants.

** Total compounded return, including reinvestment of dividends and interest.

*** 1991 – 1999 annualized return.

(Independent CPA performance review available on request. / Past performance does not guarantee future results.)

Martin Capital Advisors, LLP is a registered investment advisor, managing discretionary investment portfolios for individuals, trusts, and pension plans.

MARTIN CAPITAL ADVISORS
QUARTERLY ECONOMIC REVIEW

by Alston Boyd, Economic Director

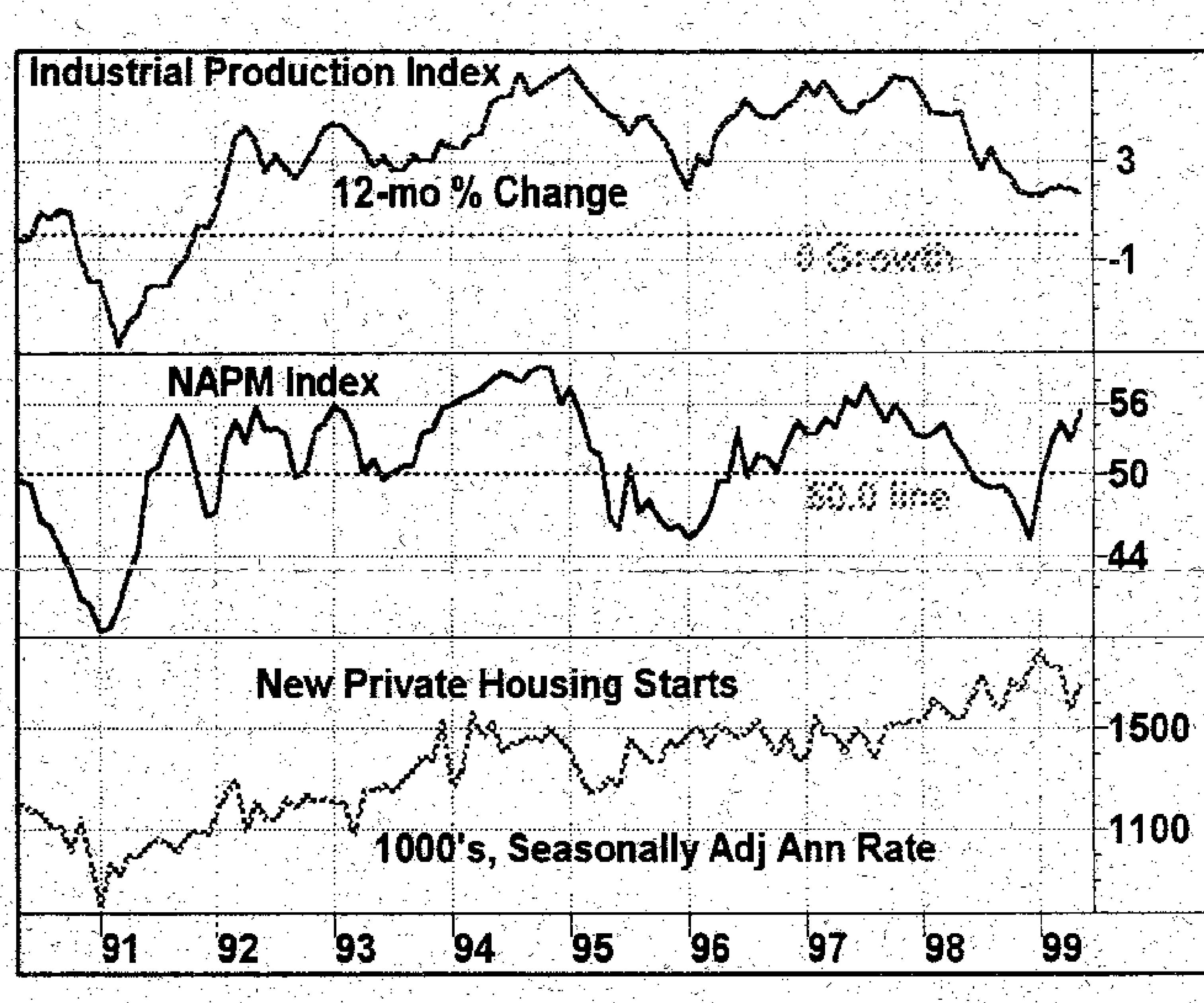
Stock Indices*		3 mo	12 mo	Interest Rates		3 mo	12 mo	Prices, Inflation		3 mo	12 mo
Dow Industrials	10971	12.1%	22.6%	91-day T-Bill DR	4.66%	7.1%	-6.0%	CPI, May	166.2	4.1% apr	2.1%
S&P 500	1373	6.7%	21.1%	30-yr T-Bond Yld	5.97%	6.2%	6.0%	PPI, May	132.4	4.6% apr	1.4%
NASDAQ Comp	2686	9.1%	41.8%	FNMA 30yr mortg	7.59%	8.4%	8.4%	Gold, cash - H&H	261.0	-6.7%	-11.9%
NASDAQ 100	2297	9.1%	71.7%	Prime Rate	8.00%	3.2%	-5.9%	W Tx Int Cr Oil	18.57	10.6%	30.8%
NYSE Comp	648	7.4%	12.0%	Fed Funds Trgt	5.00%	5.3%	-9.1%	Copper. cash	0.76	22.6%	4.1%
Wilshire 5000	12584	7.5%	18.0%	Fed Disc Rate	4.50%	0.0%	-10.0%	CRB Futures Ind	191.5	0.1%	-10.8%
Russell 2000	458	15.1%	0.1%	S/L Long T-Bnd Ind	8103	-2.4%	-0.3%	CRB Raw Indust	259.7	1.1%	-11.9%

* excluding dividends

Money				Industry				Economy			
M2, Bil Curr$, May	4507	1.4%	8.0%	Indust Prod Ind, May	134.1	1.2%	1.7%	GDP-Bil$, 1st Qtr	7760	4.3% apr	4.0%
Free Reserves	1070	-4.6%	-20.9%	NAPM Index, Jun	57.0	2.7	7.3	Unemplmnt %, Jun	4.3%	0.1%	-0.2%
Money Mkts - Bil$	1455	-0.3%	22.1%	Cap Utiliz, May	80.5%	0.3%	-2.1%	Empl Cst Ind, 1st Qtr	140.2	1.4% apr	3.0%
US $$$ Index	102.7	2.6%	1.5%	Bldg Permits - May	1586	-8.7%	2.8%	Leading Indic, May	107.4	0.7% apr	1.9%

Market and Economic Statistics as of Market Close on June 30, 1999, with 3-month & 12-month Changes

Stock indices shown in the table above have all gained respectable percentages over the last quarter, with the Russell 2000 Small Cap Index setting the pace. Note that this same index lags the group over 12 months, coming out ahead only a tenth of a percent, while the NASDAQ 100 is up 71.7% for the same period. Obviously, we've had a year of very uneven performance in stocks. Short interest rates have risen in the past quarter, but are still lower than they were a year ago, while long rates are higher now than three and 12 months ago. The Consumer and Producer Price Indices show pretty shocking annual rates of change over the last quarter in the table above. Normally, seasonal adjustments are applied to monthly changes. These rapid rates of increase are simply the changes over three months multiplied by four, and may be distorted by the lack of those seasonal adjustments. In any case, the 12-month changes are higher than for the proceeding months of this year, but low by historical standards. The wide variation between the 12-month changes in prices of different commodities and commodity price indices shows that inflation has been very uneven.



MANUFACTURING The manufacturing sector of our economy shows clear signs of recovery after the slump caused by the Asian economic crisis. A curious divergence exists between the two indicators most followed in manufacturing. Historically, the North American Purchasing Managers Index and the 12-month change in the Industrial Production Index have shown very similar patterns; this is not so for the past six months. The NAPM report shows a pretty strong body of evidence that a recovery in manufacturing is under way. Some 16 of 20 industries polled show growth rather than contraction; pricing power hit the highest level since October 1997; a larger backlog of orders exists and deliveries are generally slower because of that higher demand. Comments from individual companies to the NAPM indicate that inventories are already being built up in advance of Y2K. Orders for exports have continued to strengthen, showing that a tentative Asian recovery is also under way. The Bureau of the Census reported that new orders for manufactured goods grew 1.1% in May, with increases in both durable and non-durable goods. Transportation equipment showed the biggest increase. Capacity utilization of manufacturing and of industry as a whole appear to have bottomed out, although they remain at low levels: 79.7% and 80.5%, respectively for May.

The construction industry has been a mainstay of our economy, as manufacturing was in a slump until early this year. Very low interest rates and consumers that felt secure enough to buy big-ticket items were a potent combination. They combined to raise the level of activity in the housing industry and commercial construction to new highs. The bottom chart shows the number of housing starts reaching a peak near the beginning of 1999, and then falling back slightly. The fallback has been due to higher interest rates, which will probably show an even more pronounced negative effect on housing and construction in general over the coming months.

SALES Our continued low unemployment rate means that most consumers have jobs with good pay. Bolstered with the confidence provided by job security and with plenty of disposable income, they have been the principal force behind the U.S. economy over the past year. Their free spending has warded off an economic slump coming from Asia that otherwise might have washed over us and pulled us down into a recession or worse. Total retail sales were up 7.5% in May, close to the highs of the past 10 years, but slightly lower than the previous three months. Auto and light truck sales in May were 17.2 million units, a figure not exceeded for the past months ending in March, the second consecutive quarterly decline in this index. Hourly wages of production workers reached a peak rate of increase of 4.4% a year in April of 1998, then the rate of increase started to fall. The latest figure was an increase of 3.6% over 12 months, up slightly from May, but still on a downtrend. These increases in labor costs have been offset by equally strong increases in productivity, negating the inflationary impact. So far, no widespread evidence exists of the Fed's fears of wage inflation.

SUMMARY AND OUTLOOK The second quarter has been one of incipient recovery in manufacturing and a turnaround in raw industrial materials prices. There is every reason to expect these trends to continue into the next quarter and beyond, helped by the beginnings of an economic recovery in Asia. Higher long interest rates will inevitably have some negative effects on the overall economy, particularly on construction and housing. This will to some extent counteract the positive factors of stronger manufacturing and raw materials producers, resulting in economic growth at an annualized rate of 2.5% to 3.5% over the next two quarters. The single move by the Fed in raising short rates will have more of a psychological effect than a real one. Although it seems unlikely now, if we do see an acceleration in wages resulting from a stronger manufacturing sector and economy as a whole, the Fed is certain to raise rates again in order to counteract such inflationary tendencies.