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FUN FACTS TO KNOW AND TELL

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What should we do now? The stock market has plummeted, the economy is precarious and government intervention is questionable. The S&P 500 index of large U.S. companies is down over 25% from its peak on October 9, 2007 to a low on September 29, 2008. We will leave the news reporting to the media, but what does it all mean to us?

Here are our choices.
"Plan #1" calls for selling all of our investments and parking the money in the bank or money market fund. This will stop any further losses and make us feel better now. But we will lock in our paper losses. In the long run the investment return from the bank account or money market fund at 2% to 4% will get eroded by inflation and taxes and not be enough to live on for many years.

"Plan #2" calls for selling all or most of our investments and waiting for the market to recover or stabilize and then re-invest our money. This, again, will stop or reduce any further losses and make us feel better now. But when will the market recover or stabilize? How will we know if a recovery is permanent or just temporary before the next downturn? What if we get back in and it goes down again? What if the market surprisingly takes off and we miss the growth? How will we know? With this plan we have to be right twice (when to get out and when to get in) and be right consistently with every fall and rise of the stock market over many years.

"Plan #3" calls for a broadly diversified investment strategy that balances our need for higher than bank or money market fund investment returns over a long time frame with our tolerance for volatility. If we are withdrawing from our investments, it includes adequate cash reserves to meet our short-term spending needs without having to sell any investments at a loss. If we are adding to our investments we now have an opportunity to invest at lower prices and a higher expected future return. This plan requires discipline and patience and it is contrarian to popular thinking.

As cited above, U.S. Large Company stocks are down over 25% from their peak. That is very painful. But since 1960 this is only the 10^{th} decline of over 15% during that nearly 50 years. Painful but rare. September dealt a triple whammy: US Stocks and Bonds and International Stocks. Bonds actually had large negative returns in September, indicating investors were selling bonds due to credit risk concerns. International stocks fared poorly in September, down 14% for the month after having enhanced our returns in recent years.

So what should we do now? Is it different this time? Are any historical arguments or examples irrelevant? Are we on the brink of a recession? Are we on the brink of a depression? Believe it or not, we've been through many a financial crisis before, each of which seemed to be the end of the world. We lived through them and we've just forgotten them. We recommend an excellent website video entitled "Is it different this time?" by Weston Wellington of Dimensional Fund Advisors, which is available at http://www.dfaus.com/library/videos/different/. It is about 20 minutes long and well worth viewing. The first few slides about market premiums may not excite you, but the balance of the video on multiple past financial events provides a valuable lesson.

What should we do now? We vote for Plan #3. Are you surprised? But if you would feel more comfortable if we raised a little cash in your portfolio, please let us know or call or email us to discuss further.

What do we plan to do in the near future? We will be strategically looking for opportunities in the following areas as the year comes to a close: rebalancing bonds to stocks to "buy low" since the stock market is down, taking tax losses to reduce taxable income in 2008 and create tax loss carry forwards for future years, taking long-term capital gains for investors in the 15% or less tax bracket since a 0% long term capital gains tax bracket is available in 2008 for investors in the 15% or less tax bracket and evaluating opportunities to convert IRA's to Roth IRA's to enable tax-free withdrawals in the future. We will continue to exercise the discipline and patience of successful long-term investors.

In closing, contrary to popular belief or expectation, our phones and email have been remarkably quiet during this challenging time. We hope that is because we have educated you well and you are indeed disciplined, long-term investors. We absolutely, positively recognize that this may be a painful and difficult period for you so please do not think that we are too busy to talk to you about your personal situation. Please call or email us.

As always, your trust and confidence are important to us and we appreciate the opportunity to serve you!

A monthly publication for our firm's clients, prospective clients and friends.