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**YEAR TO DATE
PERFORMANCE (JAN 1)**

Dow Jones Industrials: -33.8%
S&P 1500 Composite: -36.7%
S&P 500 (Large Cap): -37.0%
S&P 400 (Mid Cap): -37.3%
S&P 600 (Small Cap): -32.0%
Int'l Developed Mkts: -45.1%
Int'l Emerging Mkts: -57.7%

YIELDS & RATES

2-Yr T-Bond Yield: 0.77%
5-Yr T-Bond Yield: 1.55%
10-Yr T-Bond Yield: 2.21%
30-Yr T-Bond Yield: 2.68%
30-Yr Mortgage Rate: 5.26%
15-Yr Mortgage Rate: 5.07%

Financial Markets a Work in Progress for 2009

Thank goodness 2008 is in the rearview mirror! As we enter 2009, however, there are more than just a few positive things in the financial markets we have to look forward to: 1) The current \$8.9 trillion in cash sitting on the sidelines should provide momentum for a higher market as institutional money managers and mutual funds put money to work in the new year. This cash balance matches the relative level achieved at the bottom of the market in 1990, although it falls somewhat short of balances at the bottom in 1974. 2) The equity market has consistently moved higher in the midst of horrible economic and geopolitical news. The huge jump in unemployment insurance claims in November, the small decline in 3rd quarter GDP, the continuing announcement of more layoffs in the first quarter, and rising tensions in Gaza between Israel and Hamas have all been, at the worst, “non-events” for the market. 3) President Elect Obama’s stimulus package should provide more belief that help is on the way to our economy, businesses and individuals who need it. This may provide the markets with further optimism and a reason to stage a rally. 4) Recent Federal Reserve and Treasury actions have greatly improved credit conditions (yield differentials between high grade bonds and junk bonds have narrowed significantly) and have taken a depression-type scenario off the table—at least for now. 5) World Central Banks have joined the US Federal Reserve in a coordinated effort to lower rates in order to promote more economic activity as well as provide support to financial markets. **IF** we can get through January’s earnings season without any major issues, these things will all aid upside momentum in the market. However, that’s a big IF and the likelihood of that is probably a little less than 50%.

Although 2008 will go down as one of the worst stock market years ever, the S&P 500 has rebounded 19% and the DOW 16% since the November lows. Every day we move forward, the Federal Reserve and Treasury’s policies should gain further traction in order to help us out of our economic mess. Additional help will most likely be needed, but the Government has taken a stance that it will do anything to avoid a scenario similar to the depression-era 1930’s. That doesn’t mean that the market can’t or won’t move lower. We expect a very volatile first half of the year, especially the first few months and during earnings reporting season. But these declines will bring about longer term buying opportunities in companies with large dividend yields!

Improving conditions in the credit sector remain the key to a bigger rally. After the government’s announcement that it would be purchasing mortgage backed bonds, corporate bonds and other troubled assets, interest rates have plummeted and credit markets are on their way to normalcy. Rates for ultra safe bonds (Treasuries especially) are so low that we believe this market is nearing a bubble itself. Lower rates should help provide more relief and needed assistance to weakened companies and SHOULD push investors out of less risky assets and into more risky assets (such as corporate bonds or equities). This shift has already begun as the spread between junk bonds and Treasuries has narrowed and bargain hunters have stepped in to buy. Corporate bonds, municipals and the equity market now represent a TREMENDOUS bargain over straight treasuries and CD’s. Lower interest rates will also afford borrowers in adjustable rate mortgages and hybrid loans the opportunity to refinance to a significantly lower

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fixed rate. Call your mortgager and ask about a refinance if you haven't already. It makes significant sense to refinance for the long term.

The global recession has also forced major economic powers such as China and Japan to join the U.S. in undertaking unprecedented aggressive monetary and fiscal policies. Benchmark interest rates in the U.S. and Japan are now down to effectively zero after cuts in the last couple of weeks. The U.S. and China have committed about \$1.3 trillion on fiscal spending and rescue packages while many other governments have made it very clear that they will do whatever is necessary to get their economies back on target meaning that further stimulus could very well be on the way. And don't forget the European Central Bank, which is stubbornly holding its benchmark interest rate at 2.5%. If Europe's economies deteriorate further, the ECB has more room to lower its rates. All of these steps and the coordinated efforts on behalf of the Central Banks lead us to believe that the absolute worst may be behind us.

As we've commented previously, the economic news will continue to be poor for some time, but recent action in the equity market portends to the fact that most of the bad news has already been accounted for. Although the market has moved through its 50-day moving average, which is a huge technical positive, we are concerned about recent news events with regard to more necessary capital raises by the major banks as well as very poor earnings reports in January. We are hopeful that the 8150 level on the DOW will hold if retested and the trading range of 8150-9100 will remain intact. We believe this type of trading volatility/trading range will be commonplace through at least the first two quarters of the year, if not the entire year of 2009. Therefore, our portfolio management actions may resemble more of a trading philosophy rather than a committed buy and hold philosophy. The volatility we have seen has been unprecedented and gains must be taken when made available.

Happy New Year!

A happy New Year to each of you and a "good riddance" to the year 2008! We want to thank you for your continuing confidence and support throughout this difficult time. The year end report that is included in this package is hopefully the final reminder that last year produced the worst calendar year stock performance since the Great Depression. The New Year has not started in a positive direction, but the consensus opinion is that the worst is behind us.

In this edition of Financial Insight, Gail points out a silver lining to the dark clouds that have surrounded us, and Kevin forecasts better times ahead. After a winter of heavy snows and temperatures rising and falling there are normally many potholes to maneuver. So it is in the investment arena. How completely and quickly we repair those potholes will determine how soon we'll have a smoother ride. There will always be winter and there will always be potholes, we just never know when or where they're going to appear or how long it will take to repair them.

We begin the New Year with cautious optimism, yet we also enter the year with a defensive investment strategy. Being prepared for the unexpected is what allows us to survive the downturns positioned to enjoy the good times. Throughout the United States' economic history there have been downturns and good times, with the years of good times outnumbering the downturns three to one.

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Gail Gardner MBA, CFP, ChFC
Director of Financial Planning

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We would like to meet with each and every one of you during 2009 to review where you are, determine whether your goals have stayed the same or changed, and to plan a course of action for this year and beyond. We would like to formalize an investment policy statement for your portfolio and create or update your financial plan so as to meet your goals and directives. We extend this offer to you as a continuance of our commitment to communicate with you and also as an additional thank you for putting your trust in us. Barbara will be calling you to schedule your first appointment in this process with us. You certainly can call anytime with questions, and you do not need to wait for a call to schedule an appointment to speak with us.

All of our team members, Barbara, Michelle, Brian, Gail, Kevin and I wish you a healthy and prosperous New Year and we all look forward to seeing you as the year progresses.

Low Inflation the Silver Lining to a Cloudy Stock Market

This is the time when economists weigh in on their predictions for the coming year. Many pundits see the stock market returning 6-8% by year end, but only after seeing more pain in the first half of the year. They claim the market begins to recover 6-8 months before the economy, since equity investors tend to factor anticipated future earnings into their pricing models. The experts also seem to believe that inflation is going to be less of a worry than deflation in the immediate future, and they even go so far as to say that it may not be a significant factor for the foreseeable future. With equity account values down 40% or more in 2008, we’ve had many clients asking to reevaluate their financial plans to determine what they can expect going forward.

Consider that our planning assumptions typically include an average annual return assumption of 7% and average annual inflation of 3.5%. That equates to an average return assumption of 3.5% net of inflation, or a 3.5% real average annual return on investments. If the S&P 500 returns 8% going forward and inflation is low or 0% then that’s an 8% real return. If you lost 40% of your value, at that rate it would take 7 years to get back to even. At a 6% annual rate of return it would take 9 years to be back on track. In addition, if your plan included annual savings, which you still intend to do, THAT money will be earning the same real rate of return, which is better than the projected real rate of return (3.5%) even at 6%.

So why the low inflation expectations? Because the almighty consumer is strapped from years of overextending and now has to pay the piper. It took a long time to accumulate all that debt, and it will take some time to pay it off. And those debt service payments mean less spending capacity. So our consumer driven economy is unlikely to gain any momentum from consumers for awhile, and businesses can’t raise prices when they can’t sell what they’re making at the current price. That’s why I believe that long term predictions of inflation rates near zero may be the silver lining for investors who are planning for retirement.

If you’re concerned about your own planning assumptions and you’d like to review your plan, or if you’ve never done one and want to find out where you stand, please feel free to call and schedule an appointment!

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Fund Focus List Managers Still Sound

Rest assured, we are mindful that many of the funds on our fund focus list underperformed during 2008. We continue to monitor, track and research these mutual funds and fund managers in order to make an informed decision with regard to adding new funds or replacing funds that already exist in portfolios or on our list. Many of these managers were outperforming by 5-6% through July, but witnessed a precipitous decline from August through November as all equity sectors, commodities and bonds alike collapsed. The long term track record of these managers provides us comfort that they will outperform once again when the market returns to some form of normalcy. Evidence of this arises from the fact that these funds are up 3-4% when the market is up 2% during a particular day.

Prior to the decline, many of these managers were in the top 10% of their respective asset classes over the past five and ten years. The fact is that they are still good, sound managers, but the rules of the game were changed on them in mid stream. The market has gone from rational to irrational thinking with a sell first and think second mindset. When lucid and reasonable investment philosophies return to the marketplace, the assets controlled by these managers will be rewarded once again.

If you have specific questions about the mutual funds or fund managers in your portfolio, please don't hesitate to call. We are here to answer your questions and concerns about the market, your portfolio and overall investments as well.

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