

MISERY (THE FEELING), UNENDING

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It seems all news is bad, investment horizons are increasingly short, and the appetite for risk grows smaller each day. Both economic and financial news is bleak. The credit crisis and its dampening effects on the economy rage on globally. The result: many market indexes are making new lows (from November 20, 2008) despite a new financial stimulus plan, TARP, and even TALF. Part of investors' challenge centers around a vague communication about how these plans are evolving under the new Washington administration.

Stock vigilantes are voting "No" on Washington's budget/tax plans and policy response which do not appear helpful for capital formation. Domestic stock funds sold off over 9% in February, on top of a 7% loss in January. The Dow plunged 11.7% and the S&P 500 dived 10.7% during February. Both have undercut their 1997 lows and have fallen over 50% from their highs established in October 2007. Cash on the sidelines is at an all time high. Investors, consumers, and businesses are caught in a mood of misery that is unending.

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Style	February		Client Objectives		
	February	YTD	(Stocks/Bonds)	February	YTD
Large growth	-6.9%	-11.2%	20/80	-1.43%	-1.95%
Mid growth	-7.2%	-11.6%	35/65	-2.57%	-3.66%
Foreign	-8.2%	-16.7%	50/50	-3.43%	-5.83%
Small growth	-8.7%	-15.1%	65/35	-4.12%	-7.50%
Mid value	-10.5%	-17.7%	80/20	-5.13%	-9.24%
S&P 500	-10.7%	-18.2%	95/5	-6.44%	-10.88%
Large value	-11.4%	-19.8%	S&P 500	-10.66%	-18.17%
Small value	-12.2%	-17.9%			

Growth funds sold off by less than value funds in all size categories, and by pretty wide margins during February. US Treasury securities also sold off as bond investors worried about all the new debt to be sold in order to finance the ballooning federal deficits from big spending. Municipal bonds were the only fixed income category to report positive returns in February, as many muni-bonds (tax-exempt) offer higher yields than Treasuries (taxable).

Fear of the unknown is widespread, and the unknowns today appear too numerous to count. Words once considered too inappropriate to utter, like nationalization and depression, seem to now be part of our language. Have we arrived at the point of maximum fear (misery)? If so, are we not therefore, at the point of maximum opportunity?

It is easy to forget during the difficult days of a bear market and recession, that while very unpleasant, it is finite; both will come to an end. Fed Chairman Ben Bernake, in his recent Senate Banking Committee testimony reminds us, "There is a reasonable prospect that the current recession will end in 2009, and 2010 will be a year of recovery."

The recent stock market lows, leading the economy by 6 months, would similarly suggest a recessionary economy might conclude late this fall (2009). We are watching the credit markets for further unthawing and the economy for its pace of deterioration to become less negative. Thus, the stock market should start to rally before all news turns positive; it should move upward on less bad news. Given the maximum fear, could it be that the advance will be a generational opportunity?

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MISERY (THE FEELING), UNENDING -CONTINUED-

We are cautious near-term, but given the high level of negative investor sentiment, we would expect another “head-fake” rally to start very soon. The first “head-fake” rally, I call it the “Holiday Rally (started November 20 and fully evaporated on March 2), rose 24% to its peak on January 6. “Head-fake” rallies are normal during a bear market bottoming process. The challenge is, no one knows how many “head-fakes” there will be before the final one keeps on going. We hold a lot of cash in client accounts and need to determine when to reinvest it. It is very difficult to determine “head-fakes” from the start of the next new bull market.

If you feel miserable, and it feels unending, we need to review your situation and portfolio together. Give us a call so we can provide helpful counsel. Maximum Fear = Maximum Opportunity.

BEARS HAVING TOO MUCH FUN...



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