

January 5, 2009

Dear clients,

Greetings. Happy New Year!! Where to start? Global stock markets drop like a rock in 2008. Bernard Madoff steals tens of billions from unsuspecting trusting clients both large and not quite so large. A new administration is about to take the reins in Washington. The “Big Three” U.S. automakers are fighting for their lives... No shortage of topics to start this year. That’s for sure.

Let’s start with stocks – what to make of 2008’s precipitous drop in markets all over the world? Sure, there are those who say they saw this calamitous financial train wreck coming and fled stocks at just the right time. To these people I extend congratulations for a forecasting job exceptionally well done. May their future prognostication skills be equally adept. For me, I figure it is likely, but far from certain, that stocks will rise **or** fall somewhere between 0 and 40 percent each year. How’s that for going out on a limb? That is about as truthful a forecast as you should ever rely upon.

Probably the best way to reinforce my philosophy here is through an anecdote. I told a client the other day (actually several over the last couple months) that even if I had known in January of 2008 of the impending carnage in financial markets I would not have altered her equity exposure. I’m certainly aware that she would see me as a hero today if I had steered her life savings ship to calm waters just before the tsunami struck. But the stark reality is that if this were the case, her financial future would actually never be in greater peril. For if we are to be intellectually honest, this hypothetical presents a financial future for us that is dependent on the prescient timing skills associated with precisely knowing when to be in and out of ever changing markets. This is a **skill** that not you, me, her, or anyone else possesses no matter how vehemently some might purport otherwise. Luck may produce these cherished results for a while. Skill alone can’t. What should we do? Stick to our all weather investment mixes through horrible as well as spectacular markets. This approach will maximize our odds of having a long-term successful investment experience.

Bernard Madoff. In a word the lesson learned here is that investing and investments must be forever transparent. **TRANSPARENT!!** Madoff was especially conniving in that he didn’t promise ridiculously high returns to prospective investors. Most would have been too skeptical. No. He pitched, and seemingly delivered, solid, yet unspectacular, returns through all kinds of markets year after year after year. His strategy was believed to be fruitful whether markets were going north, south, or gyrating. Who of us wouldn’t want solid year to year returns regardless of current financial conditions? Madoff knew this and leveraged these every investor wants to astonishingly unbelievable and unprecedented levels of thievery. The rub here is that when others tried to mimic the trading strategies that Madoff claimed to deploy, they could never come anywhere close to his results. This is when Madoff claimed many of his techniques were proprietary. If others weren’t bright enough to come up with similarly effective strategies that was their problem. Transparent? Not hardly. Opaque? Without a doubt.

Your portfolios are created and maintained in about as transparent a fashion as possible. When it comes to stocks, we own, through a handful of hugely diversified mutual funds, shares of thousands of different companies all over the globe (never professing to know which is any “better” or “worse” than the other). We want to own so many stocks that we will ensure ourselves the appropriate amount of return for the given “asset class” risk level we choose to accept (less a modest reduction for the necessary expenses of the process). Like it or not, during difficult stock markets our portfolio values will fall. Just take a look at your enclosed report. This is a reality that is as sure today as it will be for as long as capitalism is practiced. Our long-term success will ultimately be determined not by the uncontrollable and unknowable short-term behavior of fickle financial markets, but by the very predictable (if I have any say) behavior of ourselves.

Be well all,

