

MARKET UPDATE – FEBRUARY 29, 2008

In 2007, we experienced the fifth year in a row of world stock markets going up in value. However, we also saw signs of the equity markets struggling during the year, with significant declines in February, August, and November. Since 2008 began, the stock markets around the world declined in value, with the S&P 500 Index dropping 9.0%. Looking back to the market high in October, 2007, the S&P 500 has decreased 14%.

Clearly investors have concerns about why the market is behaving like it is and what to do about it.

Why is the Market Down?

In January and February, we've seen many companies report disappointing earnings (mostly from financial companies), causing stock prices to drop. In addition, investor concerns have been sparked by a financial crisis resulting from the combination of defaults on subprime mortgage loans and the decline in values in the housing market. This immediately impacted bank and other lending institutions, as they saw the value of their assets dramatically decline. They were either unable or unwilling to continue to make loans to both individuals and corporations. This shortage of accessible money means less spending and, therefore, a slowdown in the economy. This has led to predictions of a U.S. recession, with the potential that it might spread worldwide.

We may be in a recession, may be entering a recession, or maybe we will miss a recession, for the time being. But, as far as the mood of the stock market is concerned, a U.S. recession is a reality and *the market has already reacted to this*. If companies and consumers continue to curtail their spending, it could lead to further declines in corporate earnings and a continued gloomy outlook for stocks. However, all is not bad news, when compared to previous recessions and market downturns:

- ✓ Short-term interest rates are declining, allowing consumers to repay debt easier, and in select cases refinance homes at more reasonable rates
- ✓ Unemployment is relatively low by long-term historic measures
- ✓ Stock valuations are attractive compared to other investment alternatives (e.g., bonds)
- ✓ Companies are making adjustments to improve future earnings and have ample capital
- ✓ Both Federal Reserve and Congress are acting to ease economic strains through monetary and legislative policy

Note that in 10 out of the last 11 Federal Reserve rate reductions, regardless of whether there was an economic recession, the stock market using the S&P 500 Index as proxy returned an average of 17% in the 12 months after the first rate cut. This current round of short-term interest rate reductions began September 18, 2007, just over five months ago.

What Should Investors Do Now?

It's important to recognize that recessions happen and sometimes, but not all the time, the stock market's react negatively. In addition, we must recognize the stock market will always go up and down, and that as investors we will be challenged emotionally when this happens. But as a general statement, stock markets have always recovered, and over the long-term, investing in the stock market is a critical factor in meeting your retirement goals. So, the best course of action is to stay with the strategy that you've already put in place. If you feel you do not currently have a long term investment strategy, please call our Client Services team for help at 248-620-8100.

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