

# Weekly Commentary

## June 30, 2008

### The Markets

The stock market and life seem to have at least one thing in common. Both go through transitions over time.

As we age, we move from one stage of life to another such as from infancy, to childhood, to adolescence, to young adulthood, to middle age, and then to senior adulthood. How well we manage these life transitions goes a long way toward our success and fulfillment in life. The stock market is no different as it is in the midst of a wrenching transition. How we deal with this transition—both proactively and reactively—will help determine your ultimate financial results.

It's always dangerous to say "this time is different," but, the reality is, each time the market experiences difficulty, there's a unique set of circumstances that leads to the difficulties. In our present situation, unusually low interest rates and easy credit terms in the early to mid-2000s led to an unsustainable speculative housing boom that is now painfully unwinding. The low interest rates also drove down the value of the dollar and that helped cause commodity prices to soar and inflation to rise. The net result is consumers are hurting, corporate earnings growth is slowing, and the stock market is correcting.

To deal with this transition, here's the process we're following:

- First, we're analyzing the root causes of the problem.
- Second, based on our understanding of the causes, we're developing a working thesis for who we believe will be the winners and losers in this environment.
- Third, we're adjusting our clients' portfolios to try to take advantage of asset classes that may benefit from the current environment and to avoid the asset classes that may be hurt.
- Fourth, we remain ever vigilant in incorporating new data into our working thesis and making adjustments that we deem appropriate.

Despite our best efforts, there will likely be bumps along the way. As of last week, the decline in the Dow Jones Industrial Average brought it within a whisker of the traditional definition of a bear market, according to Barron's. In markets like this, there are few places to hide.

Over time, we expect the economy and the financial markets to find some stability. Once that happens, the stock market may turn up again and we'll do our best to take full advantage of it.

Returns through 6/27/08	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Dow Jones Industrials	-4.2	-14.5	-15.4	3.3	4.8	2.3
NASDAQ Composite	-3.8	-12.7	-11.1	4.2	7.3	2.0
Standard & Poor's 500	-3.0	-12.9	-15.0	2.4	5.5	1.2

Sources: Yahoo! Finance, Barron's. Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. Three-, Five-, and 10-year returns are annualized. Assumes dividends are not reinvested.

**SINCE WE'RE NEARING BEAR MARKET TERRITORY**, it makes sense to review what a bear market is and to discuss what has been done from an historical perspective. While there's no standard definition of a bear market, The Vanguard Group says one common definition is a decline of 20% or more over at least a two-month period. Using that definition, Vanguard says we've had 10 bear markets in the U.S. over the past 50 years.

Here are some statistics on what the last 10 looked like (all data is based on the S&P 500 Index):

- Shortest duration – 2.9 months from July 1990 to October 1990
- Longest duration – 30.5 months from March 2000 to October 2002
- Average duration – 14.1 months
- Smallest decline – 19.9% from July 1990 to October 1990 (while this is less than 20%, Vanguard included it in the list)
- Largest decline – 49.1% from March 2000 to October 2002
- Average decline – 30.4%

If the current correction should turn into an “official” bear market, the above figures may help us keep perspective on the decline. Since the S&P 500 hit its all-time record high back in October 2007, we would already be eight months into the new bear market should the S&P 500 cross that 20% threshold in the next few days. Of course, we have to let you know that past performance is no guarantee of future results. Markets will do what they want and they don't necessarily have to follow a script from the past.

With that said, it's important to understand the past. From the above data, here are several key points we'd like you to keep in mind:

- First, bear markets are normal. Over the past 50 years, we've had 10 of them – that's an average of one every five years.
- Second, the last bear market ended in October 2002, which is more than five years ago. If we enter a new bear market now, that would be in line with the historical average.
- Third, every bear market in the past eventually gave way to new record highs in the S&P 500, according to data from Vanguard and Yahoo! Finance. We have no reason to think this time will be different.
- Fourth, bear markets can be ugly. As equity investors, we may have to endure the pain of the occasional bear market in order to reap the potential long-term attractive returns offered by equity investing.

As always, we're available if you have any questions.

## **Weekly Focus – Think About It**

“I can't change the direction of the wind, but I can adjust my sails to always reach my destination.”  
-- *Jimmy Dean*

Best regards,

## **The Advocate Group**

P.S. Please feel free to forward this commentary to family, friends, or colleagues. If you would like us to add them to the list, please reply to this e-mail with their e-mail address and we will ask for their permission to be added.

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\* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

\* The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks.

\* The NASDAQ Composite Index is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System.

\* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.

\* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

\* Consult your financial professional before making any investment decision.

\* You cannot invest directly in an index.

\* Past performance does not guarantee future results.

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