

Weekly Commentary

August 11, 2008

Please Note:

The Advocate Group is making a substantial new investment in technology and communication infrastructure. We have long desired to utilize our website as a communication, education, and client service access point. We will be launching a completely rejuvenated new website in early October. It will launch with basic functionality and then blossom over time. Stay tuned for further developments....

We are also pleased to announce that we now have access to the powerful investment management and asset allocation prowess of the private wealth management divisions of JPMorgan, one of the world's leading private wealth managers, and State Street Global Advisors who is the developer of the "SPDR" series of Exchange Traded Funds, not to mention being one of the largest investment banks in the world with 2.1 trillion dollars of assets under advisement. These new additions are highly complementary to our existing access to Goldman Sachs, UBS, New Frontier Advisors, and AssetMark RAFI Fundamental Indexes. Within the Zip file attached is JP Morgan's third quarter Guide to the Markets which is published one day after each quarter close. It is full of great investment and economic information and the format is about the same from quarter to quarter. This will be a regular feature of our new website but in the meantime, enjoy this sample.

The Markets

A big drop in oil prices helped fuel a significant rise in stock prices last week. However, is there normally a neat and tidy inverse relationship between oil prices and stock prices?

Crude oil prices dropped 7.9% last week while the Dow Jones Industrial Average popped 3.6%, according to *The Wall Street Journal*. The Dow's rise included two days of more than 300-point gains. Since its July 3 high, crude oil prices have now dropped 21% as of last Friday, according to the *Journal*. Believe it or not, that suggests oil prices are now in a "bear market," as measured by the traditional definition of that usually dreaded condition.

Interestingly, since crude oil's July 3 high, and subsequent 21% drop, the Dow has risen just 3.9%. Going back a little further, oil prices have risen about 66% for the 12 months ending August 8, while the Dow has dropped only 11.4%, according to the *Journal*. Clearly, there are other factors at play in the market. We still have credit issues to deal with; we have concerns about corporate earnings; and inflation is still a concern, although the recent drop in oil prices may help ease some of the pressure.

At various times, the stock market may become fixated on a certain indicator and then trade off that indicator for a period. For example, back in the late 1970s and early 1980s, the money supply figure was widely watched by analysts. At other times, corporate earnings, the value of the dollar, the consumer price index, weekly jobless claims, and a myriad of other

numbers took center stage. Currently, oil prices are grabbing headlines, but the inverse relationship between oil prices and stock prices does not appear to be strong – except perhaps on certain days.

When all is said and done, the stock market tries to take into consideration just about everything that could possibly affect prices. The difficulty of staying on top of all these potential factors is one reason why it's so hard to outsmart the market. However, that doesn't stop us from trying!

Returns through 8/8/08	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Dow Jones Industrials	3.6	-11.5	-11.4	3.5	5.0	3.2
NASDAQ Composite	4.5	-9.0	-5.1	3.7	8.0	2.8
Standard & Poor's 500	2.9	-11.7	-10.8	2.0	5.8	1.8

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.

THE CHINESE STOCK MARKET IS A GREAT EXAMPLE of why it is so important to preserve capital in times of market difficulty. If we go back to December 29, 2006, the benchmark Shanghai Composite Index (SCI), which tracks both the yuan-denominated A shares, as well as B shares priced in foreign currency, closed at 2,674, according to data from Yahoo! Finance. By the end of 2007, the SCI had nearly doubled to close the year at 5,261. So far, so good. However, as 2008 dawned, the Chinese stock market began a dramatic slump. As of last Friday, the SCI closed at 2,605, which represents a year-to-date loss of just over 50%, according to MarketWatch.

Notice the symmetry here. The SCI rose nearly 100% in 2007, then dropped about 50% in 2008, which left the index at almost the same price as it began in 2007. On the surface, it doesn't make sense. If the market rose 100% in one year, then dropped 50% the next, shouldn't it still be up on a cumulative basis? No, and that's why capital preservation is critical.

Here's how the math works. Let's pick a starting number, in this case we'll use 200. Now, if we double it, i.e., a 100% increase, the ending value is 400. In year two, let's say we cut that number by 50%. Now we're right back to 200 – right where we started. This is essentially what happened to the Chinese market since the end of 2006. The near doubling in 2007 was wiped out by the subsequent 50% drop in 2008.

This mathematical structure also helps explain why the NASDAQ Composite Index is still far below its all-time closing high of 5,048 set way back on March 10, 2000. The brutal bear market that followed took the NASDAQ down to 1,114 on October 9, 2002, which represents about a 78% decline, according to data from Yahoo! Finance. Doing the math, the NASDAQ would have to rise more than 350% in order to recoup that 78% decline – a tall order to say the least. As of last Friday, it had added back about 116% of the 350%.

Stock market gains are hard fought so we try to do everything we can to help ensure we maintain those gains and not get into the mathematical hole of trying to dig out of a big loss.

Weekly Focus – Unity and the Opening Ceremony

The opening ceremony at the Summer Olympics was simply spectacular. It's comforting to know that there's at least one time and one place where 204 countries can gather and put aside their differences. Let's hope the good feelings continue during the games and long after the Olympic torch is extinguished.

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.
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