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For investors this year will be a hard one to forget as stock and bond markets around the world have plummeted in unison and the credit and lending markets have come to a virtual standstill. A number of major financial institutions, both here and abroad, have failed, while many others are surviving only with the help of unprecedented government intervention. The fear and uncertainty that pervades the investment landscape has never been greater, as nearly every investment asset class has fallen with rare breadth and magnitude. U.S. stock prices fell more than 33% in just over a month from late August to their recent lows, and the S&P 500 Index has now fallen 40% since the beginning of the year. Foreign stocks, as measured by the MSCI EAFE Index have fallen about 45% this year. Emerging markets are down 58%. Bond prices fell in similar fashion, but given their lower risk profile, declines were smaller than for stocks. Intermediate investment grade corporate bonds fell more than 10% in just over a month's time, and high grade municipal debt fell more than 8%. Commodity prices, meanwhile, have fallen more than 40% just in the past three months, with the price of crude oil falling more than 50%. This was a year in which diversification did little to mitigate losses.

As you know, we expressed our concerns about the investment landscape going back at least two years. Last year, we predicted that the economy was headed for a recession as the bursting of the residential housing bubble worked its way through the economy. As such, we began to reduce our equity exposure beginning in June of 2007 just before the stock market began to show signs of weakness. We continued lowering our equity exposure on rallies over the past year as we believed that the economy had indeed fallen into a recession that would be deeper and last longer than previous recessions. We focused our reduced equity exposure on large, high quality stocks, and invested in high quality taxable and municipal bonds as a safe harbor. Even so, we did not foresee the extent to which the housing downturn would ultimately affect the entire credit market (even the higher quality segments) and the global financial panic that would ensue.

As such, our portfolios were not immune to loss in this financial maelstrom, but our conservative stance did limit the overall damage. Our portfolios have been at a maximum underweighted allocation to stocks (relative to each investor's Investment Policy) since May of this year. Our high quality taxable and municipal bond holdings have served as a cushion to the large stock market declines, even though they suffered moderate losses.

While the events of the past months are unprecedented in many respects, they are not wholly unique. The market has suffered many panic sell-offs in its storied history. The lesson of these panics is that they should be viewed as an opportunity, particularly for those who anticipated the declines. Stock prices, generally, are now at attractive levels. In fact relative to interest rates, stock valuations are the lowest they have been since the early 1980's. Because our portfolios have weathered the storm better than most, we are in a position, both financially and emotionally, to take advantage of the values. On October 10 we took advantage of the panic selling and, for the first time in a long time, added to our equity allocations. We expect that over the next twelve to eighteen months, we will return our portfolios back to their target equity allocations. The process will be very gradual as many uncertainties in the investment landscape remain and the possibility of greater losses cannot be dismissed. We tend to believe, however, that much of the damage is behind us. We will seek to add exposure to the managers of large, high quality growth stocks, which remains the most attractive style-sector of the equity markets. In fixed income, we believe that high quality municipal bonds are very attractive for taxable accounts. In our retirement accounts, we expect to eventually allocate a larger percentage of our portfolios to high quality corporate bonds. Outside of the two core asset classes, we will be evaluating the risk-reward opportunities in those investments that we believe will provide us with a hedge against rising inflation over the long-term. While it may seem odd to worry about inflation at a time when it seems like the price of everything is falling like a rock, we believe that many of the remedies being used to ease the current panic will ultimately fan the inflationary fire.

Sincerely,

A handwritten signature in black ink, appearing to read "David B. Ackerman". The signature is fluid and cursive, with a long horizontal stroke at the end.

David B. Ackerman, CFA, CFP