

High Desert Investment Advisors

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Serving Your Personal Investment Needs Since 2003

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HIGH DESERT ADVISOR - FINANCIAL MODEL ADVISORY

Understanding money flows that have occurred during the past 12-14 months, is an important step in understanding the recent fall in stock market value, and for predicting future economic growth.

There has been a very sharp decrease in the monetary aggregates during this period - including money supply - that was not visible in the Federal Reserve weekly data. I have had to reconstruct that data in order to reflect what has been an off-books deleveraging process taking place during this period.

Underlying our recommendations as to when to change your portfolio's volatility - buy or sell equities - is the assumption that the market will follow the economy. If we can predict economic growth (positive or negative), then we can predict how the market will act - in a very "macro" picture.

After making these adjustments to the Financial Model data input, the Model should once again properly reflect domestic economic changes.

As of the time of is writing, The Model indicates that the economy has stabilized.

Based upon what we know is happening to (a) the financial markets and to (b) bank lending to the real estate and commercial lending markets, there is considerable reason to be concerned about future economic growth.

For now, I am not recommending taking more money out of equities. This analysis is very dependent upon current data showing that the Fed is successful in growing our money supply. It is a week by week analytical process.

I will provide an update when the Financial Model recommendation changes.

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FNMA AND FHLMC MORTGAGE BACKED SECURITIES

There is still a lot of confusion about Fannie Mae and Freddie Mac mortgage backed bonds. These mortgage backed bonds are securities backed by individual home mortgages. FNMA and FHLMC provide a guarantee for the payment of principal and interest on the mortgages included in the securities they issue.

As a liquidity backstop, The U.S. Treasury Department is making credit available to both GSEs (FNMA and FHLMC), so that the GSEs may operate in a strengthened financial condition.

FNMA and FHLMC mortgage backed bonds are rated AAA.

That being said, in addition to the guarantees provided by FNMA and FHLMC to make principal and interest payments on their sponsored home mortgages, the mortgages themselves are underwritten to what are called “conforming standards”, typically requiring 20% down payment by the borrower.

There are no “Sub Prime” loans included in these bond securities.

During a very difficult 12 month period in the credit markets, Fannie Mae and Freddie Mac bonds have not lost value, and in many cases, have actually increased in value.

The mortgage backed securities, though not backed by the direct faith and credit of the U.S. Government, are presumed to have that government guarantee and backing and are therefore among the highest rated securities that are available in the marketplace