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Serving Your Personal Investment Needs Since 2003

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HIGH DESERT ADVISOR

It almost goes with out saying; this has been an investor's nightmare year! Even though almost all of our managed portfolios have shown losses so far this year, typically, those losses are about half of what the market has lost during this period. In years past, we have provided 2-4 advisories each year. For 2008, thus far, there have been 14 advisory letters! I think that this statistic alone speaks volumes about your concerns, as well as mine.

On October 11, 2008, I suggested that it was a time to begin making a plan to reinvest the money we have sitting in cash – which came out of equities at higher levels. Several of you have decided to begin averaging into the market with that money - at around the 850 level, basis the S&P 500 Index price.

I am a more cautious.

ADVISORY SUMMARY:

Portfolio Management Considerations:

A. **I am suggesting that it is appropriate to consider increasing the portfolio investment percentage level of fixed income investments, during the coming 2-4 years. For Example: If your target is 30% Fixed Income, increase that to 40% Fixed Income; If your target is 50% Fixed Income, increase that to 65% Fixed Income**
    - **This recommendation assumes that we can obtain a 6+% interest income yield for very high quality fixed income assets.**

B. **During the coming 6 months, restructure asset allocations for every portfolio, rebalancing and reevaluating each investment and each investment manager.**

The reasons to be cautious:

1. Consumer spending is a problem; this spending has been funded by mortgage equity withdrawals (MEW) for the past several years. This year, there is no mortgage equity to draw on. MEW is responsible for perhaps 2-3% of our annual GNP growth, for the last three years.
2. The Adjusted Monetary Base is expanding at heretofore unimaginable rates…..**but M-1 is not growing.** Until M-1 grows steadily each week for several bi-weekly data reports (from the St. Louis Federal Reserve) - and this growth must continue - the domestic U.S. economy cannot grow.
3. The stock market cannot grow without growth in the American economy. Perhaps, it can grow without growth in global market economies.

The Plan:

1. Once M-1 is on a consistent growth path, begin to dollar-cost-average the available reinvestment cash back into the equities market, over 10 weeks – 10% per week. Buy on down days once each week for 10 weeks. An Advisory will be sent to you making this recommendation at the appropriate time.
2. There is a rather high probability that (#1, above) will not happen, and that the opposite occurs.
3. Should M-1 not show consistent growth, I will write another Advisory recommending that more money be taken out of equities.

The Changing Long Term Outlook:

1. The longer term domestic economic growth rate (2-4 years) is likely to be less than what has been generally considered normal – perhaps less than half of that level (think 1% ±).
2. Interest and dividend income will have to make up a greater percentage of the annual investment portfolio potential growth, because stock values will not grow much under this scenario.
3. During this period, a reasonable investment strategy is to increase the percentage of interest bearing investments as compared to the past. This might well include convertible bonds.
4. If real GDP grows at a rate of 1% annually for the next three years, and inflation is 2% during this period, the projected growth rate for the S&P 500 Index is about 6% annually.
5. We can get a 6% + yield on mortgage backed government guaranteed securities today.

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