January 15th, 2010

2009 Year End Letter

To Our Clients and Friends:

2009 has ended very nicely, from an investment perspective anyway. We are surrounded by political conflicts, economic uncertainties, vast numbers of unemployed, terrorist threats caught only by alert and aggressive civilians, increasing casualties among or service member's abroad and investment frauds. **Through it all the S&P500 Index is up 26.46% for the year and the majority of you, our clients, experienced returns that met or beat your portfolio's benchmark returns.** I have had many reflect that this does not make sense to them. Market recoveries from lows reached during deep recessions or from a depression precede the economy's recovery and therefore, precede any of the DATA, or evidence, that improving economic activity can produce. Human beings, particularly capitalist ones are by nature largely optimistic, or they fear falling behind, in either case bad times cause many to react aggressively, and that is good for economies and markets.

Of course the market didn't just earn a couple percent per month to go up 26%. **The S&P 500 was actually up 67% from its low point for the year to the finish!** While reaching the low from January first it was down some 24%! Many have asked what I think about markets for 2010. Actually what I think won't tell you much that is useful, the investment manager/economists that I tend to find useful seem to feel that 2010 is going to be a good year, but not as good as 2009. That sounds ok when you look at the end of the year results, but don't forget what you had to survive to enjoy them!

Just prior to the end of the year **we changed our web site host and** completely changed **our online reporting and document management system** for you. You should notice much **faster and easier access** to your adobe acrobat formatted reports and to your dynamic or HTML Monthly Performance Reports online. **Please be sure to log in and review them.** You will receive an email from us each time we post a report to your page, with a link right to it on the "Unread items" page. Our new site makes it much easier for us to see if you have looked at your reports or not. We will be bugging you to do so.

2009 provided some startling examples of the value of consistently applied investment strategy versus rapidly changing strategies.

"The story you are about to see (read) *is true; the names have been changed to protect the innocent," **Sgt Joe Friday, Dragnet 1952-1959**.*

This story serves well as an illustration of the consequences of changing investment strategies in the midst of crisis. Following it I'll review a couple of the pragmatic lessons learned, both for us as the advisor and those for you as the client.

We have two nice families as clients, they are different in age and occupations, but both are busy families. Both were invested in our Moderate Portfolio prior to the market's collapse and at the end of the year, although one cashed out and was not yet entirely back in to the Moderate Portfolio at year end.

- Continued –

Family A, the younger family, enjoyed a stable earned income throughout the market collapse. They started and finished the period in the Moderate Portfolio with no changes throughout besides a couple of modest deposits. **Family A's Moderate Portfolios were up more than 19.5% for the year, 1.7% more than their benchmark.**

Family B, older, with more at stake, and with a small business of their own. During the market collapse their earned income declined substantially and it appeared for awhile that it could dry up completely. Their business overhead remained high and their collateral in the form of business assets shrunk in value at the same time. Being busy with business they did not review their portfolio's reports that came through each month until February of this year! You can imagine their shock, having not looked at statements from prior to the collapse until the point that turned out to be about the low of this market. Family B at this point had to sell some of their invested assets with us at this time to make ends meet, but due to the business stress as well as the shock of seeing all the downturn's bad news all at once they had us sell all their investments as they couldn't stand to lose anymore. Getting a feel for their actual cash needs took some time, and by June we were able to craft with them a plan to get re-invested in the Moderate Portfolio, just where they had started. We did still need to leave 20% or so of the portfolio in cash, in an IRA in case they needed another withdrawal. **Family B's Moderate Portfolios were down 0.3% percent for the year!** Nowhere near the Moderate Benchmark, in which they started and ended the year, but didn't use consistently throughout the period.

The obvious first lesson is to stay with your strategy, especially in times of crisis. But what does that take? **The second lesson is to be in the right strategy to begin with, one appropriate for investment capital requirements and your risk profile** would help. Notice I didn't say risk tolerance. Risk tolerance, which is often tested, provides only a modest benefit, as it is notoriously fickle. It tends to increase substantially as you experience profits in your portfolio or business and drop even more quickly as you experience losses. Both of these families are in the appropriate strategy from a strictly investment risk/reward/your personality standpoint. Which are the pieces of the puzzle that we can keep up with reasonably.

What are some of the things that impact your investment profile? Family B for example would not tolerate well, trailing good markets as much as they would have been required to do to be in sufficiently conservative portfolio during the downturn. But I knew that they had (in previous 2 years), increased the fixed costs of their business substantially in an effort to increase their rate of growth. I should have had the discussion with them about reducing their portfolio risk, to offset the increased business risk that that overhead represented, and ensured that they understood the likely performance reduction in the portfolio they could expect in a rising market. **The same kind of change in your risk profile could occur if you didn't have a business but simply lost your job, or experienced a dramatic change in health, or had your savings or emergency funds wiped out by an accident, theft or a new roof.** Expect your risk profile and to change equally dramatically in the face of exceptionally good economic news. It wouldn't seem like it but experiencing **"Sudden Money" can be equally destabilizing to your risk profile.**

- Continued –

So lesson three for you is to let us know when things happen, send a note, call and speak to me or to Paul, use email or a text message. I will also want to know how you are feeling about things, as that impacts how you think about things. **Our lesson on this point is to ensure that we adjust your strategy and/or help you adjust savings/emergency fund amounts appropriately when things change.** We can't change your strategy without you and your input, that part of the job is team effort between us. The really important things don't happen regularly or on a schedule, so know how to contact us and how to do so when things are hairy, scary or awesome, and please do so right away!

We have much to discuss with you this year and our resolution is to be in touch with you more throughout the year. Welcome to 2010! I wish you a healthy, a happy and a prosperous new year. May your Wealth and Well-Being soar from its beginning to its end!

Sincerely,

Benjamin G. Baldwin III CFP® ChFC
President