COMPASS WATCH

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OCTOBER 2008 - - A FEW WORDS OF PERSPECTIVE AND ENCOURAGEMENT

As this newsletter is being written (October 27, 2008), the Standard & Poor's 500 stock index is down in price about 40% so far this year. The waterfall decline in October has been particularly jarring, as innumerable hedge funds, 401(k) participants and other investors have rushed for the exits. Yet, seasoned investors know that serious bear markets are neither new nor unexpected. In fact, they seem to be necessary. As Forbes reminded its readers in the October 13, 2008 issue, there have been at least six major bear markets in the U.S. in the last eighty years. Some have been very serious, such as the Great Depression (1929-1939), in which the Dow Jones industrial average fell 89% and remained under stress for many years. Others were far less damaging and lasted much shorter periods of time. On average, however, these major bears declined about 43% - - similar to the decline we have endured so far this year. Forbes went on to remind its readers that U.S. stock markets have always recovered after these bear markets - - at least so far (Forbes, "Perspective," October 13, 2008, pp. 52-53.)

There have been a variety of specific causes for these severe downturns - - hedge fund debacles, poor business practices by banks, housing speculation, etc. What they have in common, however, is significant human error. Nevertheless, over time, we seem to figure it out - - as long as we are allowed the freedom to address the problems and take the consequences. Correcting excesses (and shortages) created by human mistakes seems to be what bear markets are about.

So, what can be done to minimize the damage from a serious bear market? Here are a few thoughts.

1. Adopt a longer-term time horizon. Short-term thinkers suffer in bear markets. Long-term investors see them as buying opportunities.

2. Recognize that not all investments are suffering equally. Quality bonds, for example, have delivered strongly positive returns during this stock bear market. Moreover, many stocks have come through this downturn in fine shape. (Wal Mart stock, for instance, is actually up this year, while the S&P is down over 40%).

3. If you can, add cash to your investment account. Some quality stocks are at their lowest valuations in twenty years! Cash = buying power!

4. If possible, reduce withdrawals (spending) from your portfolio. Taking out too much money when an account's value is down sharply can do significant harm to the long-term health of a portfolio. (This will be discussed in detail in a future Compass Watch).

5. If you are still working, consider delaying retirement, until the market has recovered. The combination of early retirement and a significant bear market can be a challenging investment problem.

6. Most important, talk to your advisor - - it's your money and you should feel free to share your thoughts as well as hear those of your advisor. This goes well beyond "hand holding." It's just smart to stay in touch to make sure you understand each other and that you, your advisor and your portfolio are headed in the same direction.

At Compass, talking with existing and prospective clients is one of the best aspects of the business. Another is helping them meet their investment goals appropriately - - with portfolios of quality stocks and/or bonds. We have been doing this successfully for over twenty years, in all kinds of market conditions. May we help you?

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