LFM&P

LINNARD FINANCIAL MANAGEMENT & PLANNING, INC.
REGISTERED INVESTMENT ADVISOR

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Outlook & Trends

As we look forward to the arrival of spring weather here in the Northeast, we find that we are in a bit of an unusual period, not because there is anything of great importance happening, but precisely because there is little news. Neither the business nor the mainstream media is hyperventilating over any real or potential catastrophe. The closest known threat is the bird flu arriving in North America, and that is predicted to be six to twelve months away. The effects of bear markets, wars, over-valuation, housing bubbles, and hurricanes all seemed to have passed by without forcing the national economy into submission. There are, however, real long-term demographic and geographic forces at work that will slowly change the world, our national economy, and our own lives. Perhaps this otherwise uneventful spring is a good time to take a moment to think clearly about the future, and to build and execute a plan to help it turn out the way you would like. The planning segment of this *Outlook & Trends* discusses the necessity to prepare for the demographic change that has already begun.

Economy

There are some signs that the twin pressures of higher energy prices and higher interest rates are keeping excess economic growth in check. The economy grew at an inflation-adjusted annual rate of 1.7% during the fourth quarter, or 5.2%, if inflation is added back in. Growth is expected to have picked up again in the first quarter of 2006. The Federal Reserve's "Beige Book" reports that the economy continued to expand during the first two months of the year. Inflation is still being driven by higher energy prices. The so-called "core" rate of inflation, which excludes energy and food, is up only 2.1%. As one might expect in a growing economy, employment continues to increase, as does industrial capacity use. Corporate profits, a key driver of stock prices, rose a whopping 21.3%, and consumer confidence hit its highest level since April 2002.

The Federal Reserve is continuing their policy of raising short-term interest rates. Higher short-term rates are a boon to savers, but are beginning to squeeze borrowers. The higher rates have begun to bring the real estate market back to earth, especially in the Northeast and Midwest. The average national home price increase was 6.2% over the last 12 months, but most of this increase occurred in the first half of 2005. Prices for homes have actually been declining in the Midwest, South and West since posting highs last summer. (That was about the time that *Outlook & Trends* cautioned you that the market had gotten too hot.) In addition, there continues to be a higher inventory of houses for sale, which should also help to keep a lid on further price increases.

Financial Markets

The stock market extended its rally that began in October. The S&P 500 turned in a respectable gain of 11% from its low during last autumn, and other market segments have performed even better, with gains approaching 20%. Bonds have labored under the more restrictive Fed rate policy, and longer maturities showed a negative overall return. The widely followed Dow Industrial Average climbed back to about four hundred points of its all-time high, a mark that was set in 2000. In contrast, the NASDAQ market value remains less than half of its 2000 level. If this quick synopsis seems to contain inconsistencies, you are reading correctly. Different parts of the financial markets are performing differently. This is not an unusual occurrence and is especially true when the markets do not have a strong trend. The run-up during the late 1990s, where "buy-and-hold large-cap stocks" was the winning strategy, was a more unusual period. In today's market, the value of diversification becomes clear, and a strategy based on tactical asset allocation may outperform others.

The Times They Are A-Changin'

In 1964, Bob Dylan recorded "The Times, They Are A-Changin", which announced the coming of age of the "Baby-Boom" generation. As this generation nears retirement age, it is safe to say that the times will again be a-changin'.

Today we have a generation of workers whose size and productivity has kept the economic growth engine humming for years. As a society, we have taken advantage of good economic times and extended the benefits through excess consumption, credit card debt, stretched mortgages and government deficit spending. The debt liability has always been bailed out by a growing economy. It is tempting to believe that the magic of this prosperity will continue. It will be nice if it does, but as the number of retirees grows, and the proportion of productive workers shrinks, there is a good chance that it will not. These trends, plus the many effects of continued globalization, may contribute to significant lifestyle changes that affect all of us.

In addition to these forces, longer lives, vanishing pension plans and a questionable Social Security system are changing the retirement outlook. Some people are preparing for retirement. Others are not. A survey by ING showed that while 50% of people are comfortable with their retirement preparations, 62% spend less than 1 hour per month checking their investments or speaking with an advisor -- activities than can at best be rather loosely construed as preparing for retirement. The likely outcome of this lack of attention today will be a longer working life or a lower standard of living in retirement tomorrow.

Whether you are actively saving for your retirement, are already retired, or are part of the 62%, there is a straightforward method you can use to improve your position:

1) Develop *and maintain* a financial plan, so you can most effectively use the resources you have and avoid financial mistakes. Take a broader and longer-term view, rather than making ad hoc decisions. Make sure you know how much you need for your goals and whether you are saving enough.

2) Appropriately balance your expected risk and return. Putting your money in a mattress or relying on winning the lottery are approaches that are not likely to be effective. Consider working on a continuing basis with a financial advisor, who can help you evaluate your position and stay on track.

If you are already retired, or are in the group who is actively preparing for retirement:

3) Consider engaging a personal investment manager to optimize the effectiveness of your plans and investment approach, and execute them effectively. An investment advisor can help you manage risk and adapt your strategy for changing personal and economic conditions.

Whatever your age or financial situation, today is not too early to begin --- "for the times, they are a-changin'."

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