LFM&P

LINNARD FINANCIAL MANAGEMENT & PLANNING, INC.

Registered Investment Advisor, Wealth Management & Financial Planning

January 1, 2009

Outlook & Trends

Conditions continued to worsen during the last quarter of 2008. The S&P 500 average lost 22.4% since our last letter. How should you protect your financial future? To reach your financial goals, it is important to place economic events in the proper context and maintain a sound financial strategy. Our goal is to provide you with independent thinking that will challenge the conventional wisdom when necessary. In this issue, we hope to help you understand the current financial and economic conditions and provide an answer to the often asked question, "What should I do now?"

The Economy

A recession was officially pronounced retroactive to last December 2007. Although many areas were weakening progressively during the year, the GDP growth did not turn negative until the third quarter. Unfortunately, all the forces causing the initial weakness are still in effect. The National Association of Realtors reports that it would take 11.2 months to sell all of the homes that are currently offered for sale, the longest time seen to date. Employment is dropping along with corporate profits. Retailers are reporting a poor Christmas season as consumers tighten their budgets.

In times of stress, the weakest areas feel the effects first. The growth of the mortgage industry was built on a flimsy foundation, and it was the first to fail. Likewise, banks that relied on too much borrowed money were the next to go. Recently a Ponzi scheme run by Bernie Madoff to look like a hedge fund also came crashing down. As the economy weakens additional organizations, like General Motors, that can survive in good times, have their weaknesses exposed, some to the point of failure. The government has been pouring huge amounts of money into the economy to keep the precarious institutions afloat. The money has reduced the rates of short-term Treasury bills essentially to zero. It has also begun to bring mortgage rates down to the low 5% area. There is no telling how long it will take until the crashing sound of economically sensitive organizations is no longer heard.

Economist Joseph Schumpeter suggested that our capitalistic system is one of creative destruction, with new evolution destroying the old, weak and inefficient. Although we are currently in a destructive phase now, surviving organizations will emerge the stronger for it, and individuals who have learned, adapted and taken advantage of the conditions will have a stronger financial foundation. Eventually lower mortgage rates will make housing more affordable again. People will see their house prices stabilize and will refinance mortgages at lower rates. Feelings of greater personal financial stability will improve confidence and engender a willingness to buy. Low rates will also make corporate investment in new equipment attractive, creating jobs in those sectors. Investors will recognize that investment values have reached a once or twice in a lifetime level and begin to pursue equity investments again.

The Financial Markets

The stock market has dropped 43% from its peak in 2007. At one point in October it was off 51%. At the low, the decline exceeded the 2001-2003 bear market as well as 1974. The drop in the price of oil has been even greater, showing a 75% decline. Treasury bonds are the only asset class that has bucked the deflationary tide, but their interest rates have become so low that even Treasuries can now be considered a risky holding. The stock market decline has been very fast and severe. We have reached a level that has produced bottoms in prior severe markets, but there is not a conclusive change visible in the trend yet. A rapid advance retracing much of the prior fall often follows this type of a waterfall decline, powered primarily by investor psychology and the wish to grab bargains. Whether this type of advance evolves into a new bull market depends on improving real economic conditions.

For Everything There Is A Season

In this financial season of falling housing and investment values, in an economy littered with failing companies, the most common question people ask is "What should I do now?" Most financial experts advise sticking to your strategy during tough times. This can be good advice, but there are several pre-requisites:

- First, you must *have* a strategy
- Second, the strategy should have a reasonable expectation of producing the results that you want. A strategy that is not designed for you and your individual objectives is of little value to you.
- Third, you must have confidence in the strategy. If you have no confidence, you are likely to abandon your strategy, often at just the wrong time when emotions become strongest. When it comes to financial issues, emotional decisions are often the wrong ones.

If any of these conditions are not true for you, you risk making decisions based on emotion rather than careful consideration. The key is to develop a strategy objectively, away from emotional influences, and then stick with it as long as it remains viable for you and your situation. A good plan helps provide a straight course to navigate through the fog of uncertain times and the excesses of over-optimism.

Paradoxically, hard economic times are filled with more opportunity than the easy times. Seeds sown in the cool, rainy spring grow and are harvested in the warm summer. Gardeners know that planning and tending gardens is a year-around activity. Sports teams plan and select their players guided by a coherent strategy during the off-season, knowing that the results will be seen on the field months later, a time when only minor adjustments can be made.

Before reacting to events emotionally, make sure your actions are consistent with your strategy. If you have not developed a financial strategy, if you aren't sure your strategy will work, or if you haven't reviewed and updated your strategy recently, this is the season to do it, *and* the answer to the question, "What should I do now?"

Use this season to "learn, adapt, and take advantage of conditions" to develop "a stronger financial foundation". Make the effort to develop a workable, comprehensive financial plan and strategy if you have none. If you have a strategy, but it is not up-to-date, this is a good time to review and assure yourself that it is still targeted toward achieving your goals. If you have found that your strategy is not producing the results you want or is producing too much anxiety, a thorough review is in order, so that you may rebuild your confidence. If you have recently reviewed and confirmed your strategy, enjoy the confidence, comfort and clarity that it brings, and follow your plan.

LFM&P may be able add an important element to your financial strategy. In addition to helping you to review your strategy with comprehensive financial planning, we concentrate on risk-management to reduce the effect of difficult market conditions like we have today. The attached sheet explains the MarketAware℠ approach we developed over thirty years of study, and the actual results that it has provided since the last challenging period in 2002.

We believe that planning for a strong financial future must consider individual clients' needs and changing economic conditions. We are concerned that pre-packaged financial advice may be less than helpful, especially in stressful economic conditions. To learn more about our risk-managed investment approach and client goal-centered financial planning services, we encourage you to contact us or look at our website, www.linnardfinancial.com.

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