

Market Meltdown

Market Commentary by Randy McGill, Branch Manager/Owner – October 11th, 2008

Recently, you received a letter from Tom James, Chairman and CEO of Raymond James Financial, Inc., regarding the financial strength of Raymond James and its subsidiaries as well as his take on the current status of the credit crisis affecting America and the world. Over the past several weeks, we have addressed these same subjects at several well-attended client meetings in our conference center, and we have spoken with many, if not all of you on the telephone. In our meetings and conversations, we have also reiterated our investment philosophy and detailed our beliefs as to the appropriate course of action for our clients. Now, I would like to take a few minutes to review those views.

Before I begin, let me acknowledge that the stock market experienced a horrific sell-off this past week, e.g., the S&P 500 declined 18 percent in just five trading days. The Dow Jones Industrial Average and the NASDAQ index of over-the-counter stocks experienced similar declines. These types of declines are indeed frightful and give pause to even rational, long-term investors. We have heard from many of you as you express your concerns and seek advice from us. Let me say that we greatly appreciate the fact that you seek our counsel and that you trust our advice. Let me also say that we have been very impressed with our clients' collective calm, courage and patience through this difficult period. As for your advisors, please know that we have leaned heavily on our now significant number of years of experience. We have also made every effort to consult with and consider the views of industry experts whose expertise we have respected for years. As professionals, we have met with each other and even consulted managers from other branches of Raymond James. We find that generally speaking, we are in agreement on the following observations.

First, the decline in stock prices is largely, if not entirely, based on conditions in the credit market, rather than the stock market. The problem in the credit market has dissolved into a crisis of confidence wherein banking institutions are simply afraid to loan money to one another. We find that banks have the resources, i.e., cash, and the wherewithal to loan, they simply do not have the confidence to do so. In its worst form, this causes business activity to slow down and in some cases, whole industries to grind to a halt. The stock market, in turn, devalues securities of the companies deemed most vulnerable, and it devalues the securities of even healthy companies as well. With its decline, the stock market is demanding an end to this "lending strike" and is demanding that confidence and sanity be restored to the credit markets.

Thus far, the actions of the Federal Reserve Board Chairman, the Secretary of the Treasury, President Bush and members of Congress have been met with skepticism as the financial markets seek more direct and immediate action. Beginning this past Friday, members of the G7, the seven largest industrialized nations in the world, met in Washington with talks continuing in Paris over the weekend. Many now believe that some type of global cooperation is necessary to solve this financial crisis. And while it is true that last week saw five central banks coordinate an interest rate cut, the market is suggesting that global liquidity is not the problem; rather, concerns continue to surround the balance sheet strength (or weakness) of global financial institutions, as knowledge of individual institution's exposure to toxic mortgage-backed assets is not yet known. As I write this, there is talk of governments (Great Britain and the United States) stepping in and actually injecting capital (taking equity positions) in troubled institutions in order to shore up balance sheets and restore confidence at both the institutional and public levels. At some point, confidence must be restored so that institutions are willing to resume lending money once again, since it is the flow of money (in the form of credit) that provides the fuel for economic activity/growth at almost every level of the local and global economy.

So, what are intelligent, long-term investors to do in the meantime? To put it simply, confirm that your portfolio is properly diversified, have faith in your money managers, and stay the course. Now, as your advisors, we realize that this is easier said than done; it is hard to sit back and watch your investments decline in value. Frankly, it is

hard for us as well. The fact is that we could have advised you to sell your equity investments to cash any number of times the past few weeks - and many have wondered why we have not done so. Well, over the years, we have spelled out our philosophy many times: we simply do not believe that it's possible to "time the market" successfully. In other words, we believe that at any point during this decline, we may have put ourselves in the position of "selling the bottom" and locking in losses. Many investors express the opinion that they'd rather be out of the market and be prepared to re-enter when the market settles down. This viewpoint is typically offered in *hindsight* and ignores the lessons of history.

The reality is that knowing when to "get back in" is next to impossible with the fear of being "suckered" into a short-lived rally ever-present. Imagine if you will, moving to cash following the Dow's 812-point decline from Monday September 15 to Wednesday September 17. On the morning of the 18th, stocks fell precipitously until the administration announced a comprehensive "rescue package" that caused the DJIA to rally 778 points the next two days. Had you been tempted to repurchase your positions at the close of business on Friday the 19th, you would have *compounded your losses* early the next week. Of course, you may have waited and been pretty happy that you did, but that is not the typical course of action for an investor trying to time the market. Not to mention that most investors who time the market wait far too long before reentering – sacrificing the often substantial gains that result off a market bottom. And, so, we have chosen not to advise our clients to sell their equity investments, but rather to be patient.

And holding on has been painful; nonetheless, ultimately we believe this is the correct course of action. We must be patient and remain confident that stock prices will rebound. Unfortunately, this may take some time, and although I believe that the depth of this sell-off may ultimately lead to a significant rally in the near-term, recovering the entire decline will likely take much longer.

And that's why we have to ask you to take a slightly different view of your portfolio at this time. Historically, we have asked you to take a "holistic" view of your portfolio, i.e., to view it on a "total return" basis, taking both income (from interest and dividends) and capital appreciation (accomplished over time) into consideration when evaluating your returns. Now, we must ask you to draw a line between the two – focusing for now on the relative and in some cases absolute stability of the fixed income portions of your portfolio, while taking a much longer-term view of the equities in your portfolio. Ideally, the fixed income portion should be large enough to provide for your cash needs for a number of years. As for the equity portion, we must take a longer-term view, expecting prices to bottom-out and grow back to reflect realistic values once economic and market conditions stabilize.

As I said at the outset of this letter, we have spoken with most of you over the past several weeks – paying particular attention to those who are dependent on their investments for current income. In many cases, we have reviewed your portfolios and the above-outlined philosophy with you. Most importantly, if you have not attended one of our meetings or if we have not yet spoken with you, please realize that we are here for you. If you believe that your portfolio has been too volatile or you simply cannot sleep at night, it is important that you contact us. Under these circumstances, our advice will likely be that we use *rallies*, not declines, to raise cash or to rebalance your portfolio to a more conservative allocation. In any event, our goal is to assist you in making reasoned decisions that consider your individual financial circumstances, time frame and risk tolerance.

On behalf of my colleagues, again, I thank you for your continued confidence through this difficult period.

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