

Volume 3, Issue 8



The (not so) Almighty Dollar

August 17, 2009

Monthly Newsletter and Update

Greetings,

July was a terrific month in the stock market in spite of my expectation that the summer would be flat to negative. As I write this the market is diving on a global basis so I still may be correct although I hope I am not.

I am not done flagellating myself about missing the stock crash of 2008/2009. This is discussed in detail in the article on the next page.

A few clients left me in the first half of 2009. They expressed disappointment that I hadn't been more respectful of their aversion to loss or that I hadn't been more aggressive in getting "out" in the face of impending disaster. My numbers for 2009 year to date have been terrific because of my emphasis on international and alternate energy stocks. Those clients who departed missed that significant recovery.

Back to the flagellation. As noted on the next page I have come to some broad conclusions because of what happened in the last year. The positive news is that making strong fundamental calls is the way to go with equities. I am more than ever convinced that it is right to avoid "risk" in the fixed income allocation. Finally, I am abandoning attempts to time the market systemically on a short term basis. The problem remains, when to get back in. If we limit stock exposure to long term money, we are less likely to make a mistake.

Sincerely,

Jeff Sprowles, CFP®



Mid Quarter Update

- S&P 500 – domestic large cap
 - 6/30 to 8/14 9.5%
 - Trailing 1 year (20.2%)
- BarCap Intermediate Gov Bonds
 - 6/30 to 8/14 0.5%
 - Trailing 1 year 6.4%
- 90 Day U.S. Treasury Bills
 - 6/30 to 8/14 0.0%
 - Trailing 1 year 0.6%
- MSCI Emerging Markets
 - 6/30 to 8/14 11.9%
 - Trailing 1 year (11.3%)
- Jeff's Current Stock Outlook
100% of target

Market comments

Money market rates are almost zero. To obtain more than 2% return using insured CDs on the national desk one has to tie up money for three years. To obtain more than 2% return using U.S. treasuries one had to go five years. AA corporate bonds yield 2% at the one year mark but one is buying unsecured notes of a real estate company. Corporates that inspire confidence require a three year commitment to reach the 2% threshold. There are municipal bonds that are attractive with a tax equivalent yield over 2% at the 2 year mark. This works for clients in the 35% marginal tax bracket and is helpful for those in the uncomfortable alternate minimum tax zone. It doesn't work for retirement fund money.

My summer intern spent a significant amount of time trying to find a silver bullet for fixed income in the last few weeks. My clients are sitting on a lot of cash that is allocated to fixed income. Many analysts, including Paul Krugman, aren't overly concerned about inflation for the short term. The Federal Reserve Board declined to raise short term rates last week sending a signal that interest rates aren't likely to explode in the immediate future. On the other hand, if the "green shoots" that one reads about concerning the economy start to grow aggressively the Fed is going to have a twin task of soaking up the TARP and other stimulus money and controlling inflation if they want to avoid a serious devaluation of our currency.

My best effort is to bite my lip and keep things short. For clients in taxable situations I am buying some municipals. For clients with access to local banks offering teaser rates with CDs I am suggesting they buy some of them. Give me a call if you would like to discuss these options further.

Breaking News

According to news reports Charles Schwab is being sued for improper activity concerning auction notes.

Clients of Jeff Sprowles and Associates, LLC have accounts at Charles Schwab. Jeff trades almost everything through Schwab.

None of Jeff's clients purchased auction notes directly at Schwab.

[Breaking news in a monthly newsletter?]



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After the bear market of 2000 to 2002 I did analysis to figure out what happened and what I should do about it. It didn't take a genius in 1999 to know that stocks in general and tech stocks in particular were unrealistically priced. In 2000 I started an asset management firm for an accounting firm in Princeton. I was a "by the book" modern portfolio theory manager. I believed that it was impossible to time the market consistently. To avoid missing the "up" days that are necessary to achieve proper equity returns, I believed that once one determined the amount of stocks a portfolio needed, one dumped that amount in the market and let it ride.

We started taking money late in 2000 and lost a lot of money in equities. By early 2004 when I left there had been a recovery to some extent after 2 years of excellent stock performance but I decided not to make the same mistake again.

I installed a system that would indicate large market movements. It survived a rigorous back test. I was of the opinion that when the market was oversold my clients would not suffer as they had in 2001 and 2002.

In 2007 it didn't take a genius to know that real estate prices were overheated and that unsound mortgages were being made. My system sent me a signal to reduce from 100% stocks to 75% stocks on 12/31/2007. On January 2nd, 2008 the market opened sharply down. I don't like to sell into a declining market and decided I should wait for an up day. While I was waiting we had the worst January in decades. After the market was down over 10% I figured I missed the sell signal and it was better to wait it out. Unfortunately, I didn't understand that the real estate bubble was going to have the ramifications it did. My clients and I rode the stock market all the way down.

Standing firm in the face of a declining market is the "proper" advice if one is not trying to time the market. It took a lot of intestinal fortitude to stick it out through the 4th quarter of last year and the first quarter of 2009. I lost a few of my clients who felt that I hadn't listened when they said they didn't want to lose a lot of money in stocks or felt that I should have dumped out of the market at some point.

Subsequently, my long term call on international stocks in general and emerging markets in particular as well as my 10% allocation to alternate energy has generated a terrific result in the last four months. See the box for year to date and 3 year numbers by issue.



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Morningstar 8/14/2009

So what conclusions have I made? The experience of the past 18 months has made me more conservative. My long held prejudice against large American companies has been irritated to the point that I am systematically reducing exposure to them. I will probably continue to do so until it is apparent that compensation of executives has returned to the kind of ratios typical prior to the greed explosion that started in the early 1980s.

1. Long term fundamental decisions are the basis for allocation.
2. International is likely to be more profitable than domestic.
3. The dollar is likely to continue to weaken over time unless we can change our fiscal and trade policies.
4. So called "emerging" economies are misnamed. China is the third largest economy and has enormous potential.
5. Note in the chart that the YTD and 3 year numbers have a strong correlation to the amount in international securities. There are no 3 year numbers for the alternate energy ETFs because they have been in existence for less than that time.

<u>ETF/Fund</u>	<u>YTD</u>	<u>%Int</u>	<u>3 Year</u>	<u>Category</u>
India Fund	69.95%	100%	19.39	Emerging
Brazil	65.82%	100%	17.00	Emerging
Matthews India	59.14%	100%	10.28	Emerging
Matthews China	56.83%	100%	22.77	Emerging
Hong Kond	49.79%	100%	7.25	Emerging
Latin Am 40	49.21%	100%	13.13	Emerging
China Xinhua/25	45.12%	100%	19.00	Emerging
Emerging Markets	44.39%	100%	5.84	Emerging
First Trust Wind	22.42%	83%		Alternate Energy
Russell Mid-Cap	19.89%	1%	(6.04)	Mid Cap Domestic
Claymore Water	15.79%	61%		Alternate Energy
EAFE	14.67%	100%	(5.51)	International
Russell 2000	13.66%	0%	(6.04)	Small Domestic
Claymore Solar	12.66%	68%		Alternate Energy
Russell 3000	12.28%	0%	(6.10)	Broad Domestic
Market Vectors Global	6.64%	60%		Alternate Energy
Russell 1000 Value	4.71%	0%	(9.56)	Large Domestic



At Jeff Sprowles and Associates, we are striving to be more environmentally friendly, which is why we are now offering the option of receiving our monthly newsletters via email. If you would like to be added to the list, please email ntran@sproyles.com with the subject line of "Newsletter Mailing List"