



INVESTMENT NEWSLETTER

CEP FINANCIAL, LLC

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NATIONAL ECONOMY
SHRINKS BY 6.2%, THE
LARGEST CONTRACTION
IN 26 YEARS.

STOCK MARKET FALLS
MORE THAN 50% IN LESS
THAN SIX MONTHS

FEDERAL GOVERNMENT
CONTINUES TO BORROW
TRILLIONS OF DOLLARS
WITH NO END IN SIGHT.

INDIVIDUALS CANNOT
CONTROL THE SHORT
TERM MEANDERINGS OF
THE STOCK MARKET, THE
ECONOMY OR THE
FEDERAL GOVERNMENT.

STAY THE COURSE OR
NOT?

The Investment Letter is mailed periodically to our clients and friends. It is compiled primarily from reports in the Wall Street Journal, Houston Chronicle, Morningstar, advisors Littman Gregory, columnist Bob Veres, the Patriot Post newsletter, and Warren Buffett's annual report to shareholders of Berkshire Hathaway.

STAY THE COURSE OR NOT?

As we approach the Ides of March, the economy is in a deep recession, the stock market is in free fall and the federal government's solution is to borrow money (surprise, surprise) that our children will have to pay back, and increase taxes / regulation on businesses and individuals.

The nation's GDP (gross domestic product of all the goods and services produced in this country) decreased by 6.2% in the 4th quarter of 2008 and unemployment has reached 8.1%.

In the last 9 months, the S&P 500 has fallen 52%. 401Ks really have become 201Ks.

The federal government has committed \$9 trillion to bail out the financial institutions that caused this mess. They've committed another \$3.3 trillion, more or less, to stimulate the economy, and are ready to implement a budget with 9,000 earmarks.

These are the times that try men's souls. In times like these it is important to focus on what you can and cannot control.

WHAT YOU CANNOT CONTROL

You cannot control or predict the **short term meanderings** of the equity markets, the economy, or our political system. Luckily for us, the

long term is more dependable and has proven over the years to be self-correcting.

The Stock Market. In his annual report Warren Buffet notes that the S&P 500 has had positive returns in 33 of the last 44 years. He guesses that the next 44 years will see about that same percentage of positive and negative years. But no one, not even Mr. Buffett can predict which years will be positive or which will be negative. Over the long term, the market has returned about 10% per year. Something close to that average will most likely persist.

The Economy. Although our economy is in shambles now and may be for a couple of years, it will come back. The economy can shrink or expand dramatically in the short run, but over the last 47 years, our economy has grown. Every contraction in the economy has the seeds of future expansion built into it. After each contraction we have an expansion. These expansions and contractions occur in a sort of predictable manner without the help of government.

Now, here's the good part, the economy gets larger. Sometimes a lot, some-times a little, but the long term growth is about 3% per year.

The Political System. Luckily for us, we live in nation of free men and women who vote in our own self interest. When we stop trusting our elected officials to act in our best interest, we throw the bums out and start with new folks, even if some of their ideas seem wacky. (Just ask the Republicans.) This self-correction mechanism is one of the earmarks (pun intended) of our system and it makes the long term more dependable.

Basic arithmetic also keeps our elected officials from spending too much on their favorite projects. The government takes as much money as they can from us, but not so much that the

economy suffers and the federal government revenues go down. That number works out to be about 20% of GDP. In the 1950s and early 1960s marginal tax rates were 90%, and the government revenues were about 20% of GDP.

In the 1980s and early 90s when the rates were 30%, the government revenues were about 20% of GDP. This administration's projection of how much the federal government will take out of the economy is 19%. I know you will believe it when you see it, but if they take too much from us, we can always throw the bums out.

WHAT YOU CAN CONTROL

So if you cannot control the market or the economy or the government in the short run, what do you control? You can control your own actions by arranging your financial affairs to take advantage of opportunities and avoid problems presented by the stock market, the economy and the political system. Things to do include:

1. Maintain sufficient emergency funds
2. Don't sell your investment assets at the current fire sale prices. Contribute to your 401k at least to the point of getting the maximum company contribution. Review your asset allocation strategy. Some assets have become very attractive.
3. Be prudent in the use of debt. Only incur debt on terms that you can live with and only if the debt improves your financial position.
4. Live within your means. The threat of unemployment is here. Now is not the time to take on debt that you make not be able to repay due to a job loss, or make risky investments with cash you may need in the near future.

5. Avoid taxes as much as legally possible. Changes in the tax laws have provided new opportunities and pitfalls for tax savings.

6. Maintain adequate health, disability, life, long term care, property and liability insurance coverage.

STAY THE COURSE OR NOT

NOT. The world has changed dramatically in the last six months. If you have a dependable source of income and low expenses, these are the best of times. You can purchase autos and homes, stocks and consumer goods at fire sale prices. If on the other hand you have lost your job, have few emergency funds, and high fixed expenses (e.g. debt repayment), these are the worst of times. You may have to sell assets at current prices and drastically cut back on lifestyle expenses. A Dave Ramsey (beans and rice, rice and beans) approach to life may be necessary.

STAY. If neither of the above describes your situation, your best course of action is probably to stay the course and continue to focus on strengthening your financial position by following the six action steps noted above.

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