



Capital Ideas

2009

You might have noticed (or, perhaps not) that we discontinued *Capital Ideas* with the September edition. This is not to herald the return of the monthly newsletter. We are going to use the format for our quarterly notes to you.

Last year was certainly the most trying of my 29 years in this business. I started out in the 1980–81 recession when we had double-digit inflation. I went through the crash of '87. I worked through the S&L and then the bank collapses of the early 90's. I saw the Asian Contagion first-hand. LTCM was actually terrifying in the way those Nobel laureates came so close to bringing the financial system to its knees. The tech bubble and collapse early this decade seemed frightening at the time. Everyone knew that the real estate bubble that followed would burst. But no one knew how deep the financial alphabet soup of CDOs, SIVs, CDSs, and the others would send the market.

On March 9, 2009, the Dow closed at 6547.05. That was the Dow's lowest point since April 15, 1997. It was 54% below the all-time high of 14,164.53 set on October 9, 2007. It may not have been the end of the world, but it sure seemed like it.

Since March the Dow has risen 61%. Who would have thought in March that such a gain would have been possible? We believed that the market was oversold, but we did not think it would rise as far and as fast as it did.

Still, the world did not end and the capitalist system has survived. Yes, the Dow is still down 25% from the 2007 high. But the rally has brightened spirits.

We lost a couple clients (that is all) during the market decline in the first quarter. They wanted to put their money in cash so they would not lose any more. In hindsight, that was the absolute worst decision they could have made. Not only did they lock in the loss, they moved their money to money market accounts earning 0.01%. Double whammy. They missed out on the 60+% gain after March 9.

Some people get emotional about their investments. That leads to bad decisions. That is why we always hear that individual investors (as opposed to institutions) sell low and buy high. They forget that stocks are indicia of ownership in corporations and that bonds are loans to governments and corporations. Investing should be treated as a business, not as a game or as a lottery.

No one is able to call the direction of the market. If anyone could do so, they would be the only investment advisor in business and we would all live happily ever after. That could never happen because the market is, well, a market. There are two sides to every transaction, a buyer and a seller. The market falls when buyers think the price is too high. The market rises when the sellers think the price is too low. What a simple concept. However, the market does not go from peak to trough imme-

diately. It is a process as information is revealed and digested.

That is why we stick to our discipline. It has worked for many years. It has been tweaked along the way, but the basic process has stayed the same.

So, what will 2010 bring? I have no idea.

I can give valid arguments for a strong rise in the market. There is still a lot of money to be invested. After missing out on the rally last year, many fear missing out on more. As those investors put their money in the market, the owners of the shares (you) will be reluctant to sell unless they believe they are getting the best price. Supply and demand will dictate that the prices will rise.

Then, there is the flip side of the coin. Eastern Europe is a mess. Greece may be bankrupt. And, the banks have not written down their non-performing commercial loans. Yes, I know the banks have been paying back the TARP money, but they are not out of the woods just yet.

That is just the way the market works. As long as people are capable of independent thought, they will draw different conclusions from the same set of facts. That is why there were still folks buying all the way down and people selling all the way up. There

are two sides to every transaction.

We cannot make any guarantees. Seriously, the SEC will not allow it. The market will not always act the way we think it should. Fear and greed rule the day.

That is why you have to take emotion out of managing money. That is why you must have a discipline and stick to it.

All in all, I believe that 2010 will be a good but not great year. That could change in a heartbeat if we have some calamitous event. But you can't worry about lightning strikes.

We will continue to do our best to earn your confidence. As always, we appreciate your business.

Happy New Year!



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