

October 14, 2009

As I write this letter, the third quarter has just come to a close in what continues to be a most eventful year for financial markets and the economy.

It has also been one year since the weekend that shook the foundations of Wall Street and the global financial system—when Lehman Brothers collapsed, Merrill Lynch vanished as an independent entity and AIG was taken over by the government.

In light of that, I thought it might be worthwhile to briefly summarize where we have been this year, where we are today and the prospects for the period ahead—and also to highlight some lessons from last year's financial collapse.

Where we've been

For many investors, in early March of 2009, it truly did feel like the world might be coming to an end. Talk of a return to a Great Depression-like economy dominated radio, television and print. Understandably, fear was rampant and stocks responded to these nightmarish scenarios by hitting their lowest levels in years, with the financial sector especially hard hit.

Although no one knew it at the time, that turned out to be the bottom. Since then, we have seen the economy move back from the precipice; there is a growing consensus that we will return to economic growth in the second half of this year. *The Economist* recently ran a cover story discussing the extent to which the economic recovery was led by Asia.

As a result, we have had a strong recovery in the financial markets. From the bottom in the beginning of March, stocks are up 50%, retracing a good portion of the losses since last fall.

In the meantime, here are five lessons from the past 12 months:

1. Investors were reminded of just how volatile stocks can be.
2. Investors realized the great importance of true diversification.
3. Many investors discovered that they were less comfortable with risk and volatility in their portfolio than they had believed.
4. Investors were also reminded of the need to focus on what they can control, understanding cash flow needs and thinking through how much risk they can live with to fund those needs.
5. Finally, we were reminded that in today's world, we need to expect the unexpected.

Where we are today

Two years ago, the market was characterized by rampant optimism. The market was hitting a new high and any concerns were set aside as minor annoyances.

By contrast, eight months ago the market was overwhelmed by absolute pessimism—there was no sign of hope anywhere.

Today, the market is somewhere between those two extremes and many investors can be characterized as extremely nervous.

As a general rule, I think a certain level of healthy anxiety is positive—what gets investors in trouble is an excess of either optimism or pessimism. While today's mood may be erring on the side of being a bit too pessimistic, I think being cautious in the current market makes sense, provided that prudent caution does not cross the line into panicked inertia.

The good news is that there are still excellent opportunities for investors who are prepared for short-term volatility. At Doyle Wealth Management, we have 100 years of combined market experience. We have seen bull markets and bear markets and all of the multiple cycles in between. I am reassured that daily we are still finding very good value—not to the extent that we did earlier this year, but still well ahead of what we saw two years ago.

The outlook going forward

In August, *BusinessWeek* ran a cover story called "The Case for Optimism." The premise was simple: beyond the issues facing the global economy, there are many underlying positives that give cause for optimism if we look out two or three years and beyond.

There are things happening under the surface that will drive economic growth and with that economic growth will come growth in stock prices. Examples include the positive impact of technology, the recovering housing market, the revitalization of the American economy currently taking place and the incredible energy from the developing world's educated youth and emerging middle class.

Let me close by talking about market volatility. In 1907, financier J. Pierpont Morgan single-handedly averted a banking panic. Later in life, someone asked him his best guess on the direction of markets. His answer: "They will go up and they will go down."

One hundred years later, that is still the best answer to someone looking for a short-term market forecast. No one can predict market movements in the immediate period ahead—all we can do is understand clearly how much short-term volatility we can live with, adjust our portfolios accordingly, and stay focused on the horizon as we deal with the

rough waters. No one likes volatility, but for most of us, it is the necessary price for arriving at our ultimate destination.

In the meantime, my team and I are constantly looking for opportunities to realign portfolios and give our clients the best trade-off between risk and return. Given the current uncertainty and volatility, we are continuing to focus on higher-quality companies in both stock and bond portfolios.

Over the past few months, I have spoken with many clients about their portfolios. If I missed you for some reason, or if you would like to discuss your portfolio in more detail, I am always delighted to have that conversation.

Thank you for the continued opportunity to work together. Remember, my team and I are always here should you have any questions or wish to talk about anything related to your portfolio or your finances.

Sincerely,

Robert K. Doyle, CPA, PFS