



Krosnowski & Scott LLC

Investment & Retirement Planning Specialists

K&S Spring Financial Market Perspective Update (May 2009)

Dear Clients and Friends,

We are hopeful that the rise in the Dow Jones Industrial Average (DJIA) over the past few months may have signaled a market bottom at 6500 in February. At the beginning of the year we forecasted a bumpy uninspiring ride in the stock market in 2009 after the steep decline we experienced in 2008. Little did we know that the market would exceed our expectations on the downside during the first quarter. Even though we may not be out of the woods yet, it appears that we are starting to see some signs of life in the financial markets.

Stock investment analysts typically reduce their corporate earnings estimates during times of economic recession. If you lower the bar far enough, companies will begin to exceed the analysts earnings expectations and stock prices will begin to recover. We are beginning to see some positive earnings [reports](#) starting to give the stock market a boost. As we approached the beginning of 2009, FED Chairman Bernanke warned that he felt that the economic recession would probably last until sometime during the second half of this year. We agree with this observation and so far it appears that we are heading in that direction. It would not surprise us if the stock market recovers to somewhere between 9000 and 10,000 on the DJIA by February 2010. This would be consistent with the historic bear market recovery over the twelve months from the market bottom that we discussed in our Winter Newsletter in March.

As a result of the massive Federal Government spending, many investors have voiced concerns about the threat of rapidly growing inflation over the next few years. Currently, we are experiencing deflation and interest rates are at fifty year low levels. In a recent conversation with an economist from Lord Abbett, the following viewpoints were communicated to us:

Ø Over the next three to five years inflation is expected to increase but not out of line with economic growth. If the Federal government executes fiscal policy which reduces debt, fears of hyperinflation may be avoided.

Ø Based on historic returns it may take the real estate market approximately seven to eight years and the stock market close to six years to return their previous high levels.

During the week of May 8, the U.S. Treasury announced that the results of the financial stress tests that they have conducted will require several large national banking

institutions to increase their capital reserves by \$75 Billion. On the surface this may appear as bad news which it is. However, the financial markets do not like uncertainty. The fact that the amount of capital that these companies need to meet their reserve requirements has been defined can be viewed as good news because it provides certainty. This is not to say that these banks are not going to continue to be facing head winds in the form of ongoing bad loan write-offs but it is a step in the right direction.

Kiplinger's Personal Finance- Here is some investment commentary from money manager's Jean-Marie Eveillard of First Eagle and Pimco's Mohamed El-Erian: Eveillard believes that the American and British consumer is "tapped out" and foresees mediocre consumption growth over the next three to five years. Partly for this reason he sees more opportunity by investing in the emerging markets- particularly in Asia, where consumer debt levels are relatively low and governments realize that they need to stimulate domestic consumption. El-Erian sees a tectonic shift occurring as merging economies in Asia and elsewhere join the established powerhouses, especially the U.S. No longer will the world simply march to our beat; the U.S. will have to share leadership with emerging giants, such as China and India. The good news is that this change in the global power structure is not altogether bad for America. He predicts that the new economic giants and other developing nations will buy more U.S. goods, easing our trade deficit and stimulating growth and jobs over time. Because of all these changes, Mohamed suggest that investors spread their assets over a wide array of assets.

The Bottom Line: We believe that the worst may be behind us regarding the devastating bear market that we have been experiencing in the financial markets since January 2008. If you moved assets out of the stock market or if you have cash you that have been holding off investing, we believe that now may be a good time to invest depending on your specific financial situation. There is arguably eight to nine trillion dollars in cash waiting on the sidelines until greater optimism returns to the psyche of investors. If you put your assets back to work now you may be ahead of the wave. **We continue to encourage our clients to balance their portfolios, globally diversify their assets, emphasize income and focus on the long term.** Reminder: In the Fall of 2002, after the stock market declined for 30 months by nearly 50%, many investors sold at the bottom of the market. In 2003, the stock market advanced 36%. Not until the first quarter of 2004 did many investors move their assets back into the stock market. We do not want any of you to repeat this mistake (i.e. selling when the stock market is low and then investing back in after it moves back to higher levels).

Please do not hesitate to contact us to review investment strategies.

We look forward to talking to you soon.

Sincerely,

Andrew J. Krosnowski & Melissa Scott Paine