



This week's catastrophic events have touched us all; as individuals, as communities, and as a nation. Ordinary priorities in our life, like financial markets, were jolted into new perspective as we shared in this horrible loss.

Yet, quickly trying to regain equilibrium and specifically supporting the economy and system that were deliberately targeted by these acts of terror seems almost obligatory. The markets are set to reopen on Monday and this is a very brief outline of our view and current thoughts.

Most likely, the U.S. financial markets will open significantly down. But the delay in reopening the markets may somewhat temper the duration and depth of the immediate downturn. Additionally, the Federal Reserve has already unleashed significant liquidity to support the system and may issue another interest rate reduction sooner than expected in an attempt to refuel the economy and help mitigate some equity market selloff caused by this event.

However, like the country as a whole, the U.S. stock market has repeatedly demonstrated remarkable resiliency. Though the market may decline near-term, there is little reason to suspect any direct market movement caused by the terrorist attack will endure.

Historically, markets often bounce back rather quickly from national disasters. For example, Ned Davis Research examined the response of the Dow Jones Industrial Average to 28 relatively recent crises; ranging from Pearl Harbor (1941), to the Kennedy assassination (1963), to the previous World Trade Center bombing (1993). On average, the Dow dropped 7.1% immediately following the event, but subsequently rebounded and finished up 3.8% after one month, up 6.8% after three months, and up 12.5% after six months.

The Standard & Poor's 500 has often reacted in similar fashion. The chart below shows the immediate, short, and longer-term movements of the S&P in response to recent crises:

<b>EVENT</b>	<b>1 day</b>	<b>10 days</b>	<b>30 days</b>	<b>1 year</b>
Cuban Missile Crisis, 1962	-1.1%	3.9%	12.7%	33.5%
Kennedy assassination, 1963	-2.8%	3.3%	6.1%	23.6%
Reagan shooting, 1981	-0.3%	-0.1%	-3.7%	-16.6%
World Trade Center bombing 1993	0.2%	2.6%	-0.1%	6.2%
Oklahoma City bombing, 1995	-0.1%	1.9%	5.6%	27.7%

Source: Lockwood Advisors, USA Today 9/13/01

Of greater concern is the general health of the overall economy. With the U.S. economy already sputtering, these events cast additional uncertainty as to how quickly an economic rebound can occur. Certain industries (airlines, travel, and commercial insurers) will tend to suffer due to the week's tragedy, while others could possibly see an increased demand for their goods and services (defense, aerospace and security). Even overlooking the impact of recent events, a very selective equity market will most likely remain the norm near-term; with some industries doing okay, while others will languish until a broader economic turnaround ensues.

Additional slowness of both corporate and consumer spending will move the economy closer to the classical definition of a recession, i.e. two consecutive quarters of negative growth, with some observers already tooting a 'here comes the recession' tune.

While this very well may be true, recall that economic slowdowns/contractions *and* economic growth/expansions are *both* part of a business cycle. We continually cautioned investors not to lose perspective and overreact when the bull market was raging. The same applies here. Once, and if, a recession occurs, remember that by definition the term reflects economic measures that have already been accounted for. It does not foretell what will come. Care needs to be taken that a ‘recessionary’ mindset does not feed on itself and cloud potential opportunities moving forward.

Outlined below are a few tactics currently being used to help build and preserve assets in these challenging times. Each client situation is unique and addressed accordingly but certain guiding themes apply throughout.

- For the majority of our clientele, we have been at or below minimum equity, as defined by their personal investment policy, since earlier this year when we recommended that such a tactic might be prudent. We remain there today. Typically, our approach would have us rebalancing overall portfolio allocations to the minimum equity level but we’ve chosen to err on the side of having greater liquidity at the present time.
- One of our core beliefs is that a client’s disciplined long-term investment strategy should not be dramatically altered by short-term market events. Tactical shifts within a defined range, absolutely. But attempting to time the market by jumping in and out is not effective. For this reason, as well as the market precedence outlined above and the fact that we are already at or below our minimum equity range per investment policy, we will not attempt to liquidate equity holdings at fire sale prices should the market sharply decline on Monday.
- As normal, we continue to phase into desired investment exposure percentage when presented with large initial cash positions. This provides the benefit of averaging purchase prices as core stock and bond positions are being built. This phase in has continued to occur during the past few months, albeit slower and more selectively. If stock prices decline, phase in for cash heavy clients looking to build to minimum equity levels will be accelerated.
- Equity diversification; by management style, industry group, and market sector remains a priority in our management approach. We currently shade toward a *value* versus *growth* investment style and try to maintain a close to benchmark level weighting in industry and sector diversification. Moving forward, new purchases of individual equities may tend to favor companies with strong fundamentals in favorably positioned sectors but a portfolio’s overall diversification will still be maintained.
- Our normal bias towards larger cap stocks is even stronger. Mid/small cap “growth” stocks/funds were the first holdings reduced when the markets began deteriorating last year. Mid cap “value” exposure was increased but most clients remain toward the lower end of their overall policy range for this category.
- For large fixed income positions, we use individual bonds to control both maturity and quality. We typically emphasize short to mid term maturity investment-grade bonds, though reduced yields have pushed maturity timeframes slightly longer and increased the selective use of prudently chosen, just below investment grade bonds for certain accounts. Currently, the maximum maturity considered is approximately ten years.

I hope this brief overview was helpful. I also hope your family, friends, and loved ones remained safe through this ordeal. We truly value your business and our ongoing relationship. As always, please don’t hesitate to call with any questions or if we can be of additional service.

**E. Jeffrey Roof**