

Market Update

**STEVE VAN HOUTEN,
CFP®**

LOU OBERMAN, RFC



**Lifetime Financial
Advisors, Inc.**

227 N. El Camino Real
Suite 201
Encinitas, CA 92024
www.lfa-inc.com

760.943.0430
760.943.0950 fax

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www.lfa-inc.com

1st Quarter Update

In over 25 years of closely following world economic and market developments, it has never been more challenging and frankly, perplexing, to get a sense of how the current economic downturn will unfold and how the inevitable recovery will transpire. Opinions vary. The number of government initiatives is mind boggling: bank bailouts, new regulatory frameworks, national health care, real estate mortgage lending reform, cap and trade energy, education, and new tax laws. Time will tell how well all of these efforts will succeed and how their impacts will ripple through the economy. There will no doubt be unintended consequences from many of the hurried incentive programs as well.

We are in the seventeenth month of the Great Recession (the longest economic downturn since the Great Depression); unemployment is rising around the world, yet stock markets have rallied. Is a global economic recovery in sight?

While it is too soon to say for sure, it does seem clear that the fear that had gripped the investment world and the credit markets since last September has subsided and that optimism is growing that efforts begun under George W. Bush and continued in the Obama administration, the European Central Bank, and the Group of 20 nations will eventually be sufficient to shore up the global banking system and stimulate the world economy.

There are also signs ("green shoots", as market pundits call them) that the economy may in fact be nearing an inflection point. Improvements in housing starts, industrial production, manufacturing, and retail sales suggest that at least some parts of the economy may be bottoming. They don't suggest that the economy is going to recover any time soon but that a degree of stabilization has occurred, that the rates of decline will lessen, and that the trough of the recession might have been reached.

As is often noted, capital markets anticipate what they think is about to happen in the real economy. The volatility of the past quarter indicates the vast difference of expectations for corporate profits. While the stock market has seen the most aggressive four week rally in more than seventy years, much wariness remains.

In the past, early indicators that the stock market is at or near a bottom have been moves up in the prices of copper, corporate bonds, and inflation-adjusted U.S. Treasuries (TIPS). Prices for all are higher than they have been in a while (copper is up more than 30% year to date). Moreover, there is now a record amount of money sitting in cash instruments—often an indicator that markets have reached bottom.

However, there is also greater uncertainty than usual. The erratic actions of the government over the past several months have left corporations and investors feeling that the rules of the game keep changing. And it is difficult to judge what "normalized earnings" of corporations will be in the future, since they had been boosted over the past few years by the housing bubble and financial leverage, and whether stocks are cheap or expensive.

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So where does that leave money managers and their investors? Caught, as ever, between the fear of losing (more) money and the fear of missing out on potential upswings in securities prices.

Portfolio managers focus on the value of underlying businesses, whereas investors see only their prices. The managers to whom we have entrusted your money believe that the business values of their portfolio companies by and large have not changed nearly as much as recent stock declines would indicate. Where they see greater value in the fixed income securities of their companies than in the stock, they are buying them. All feel that the securities they hold have the potential for appreciation.

While it might sound hollow and repetitious after such a long bear market, the argument that low securities prices provide the potential for long-term capital appreciation remains appealing. Bear markets present the opportunity to benefit from earnings growth, dividend yield, and multiple (price to earnings) expansion. In fact, great records have developed from the depths of past bear markets as steady-handed investors purchased stalwart companies with decent dividends at low P/E multiples and simply hold on, letting compounding and gradually improving confidence take care of the rest.

Once a sustained rebound begins, it will be much easier to distinguish those managers who have incurred permanent impairments to your capital (and should be replaced) from those whose holdings have suffered only temporary declines. Poor results may not reflect a flawed discipline but rather the fact that prices and value can irrationally diverge for relatively long periods of time. A decrease in volatility will signal an increase in certainty about the intrinsic values of the securities in your portfolio. Once that occurs, we can begin to make the changes to your portfolio that we have recommended in the past.

It is worth keeping in mind a sentiment that is often quoted these days: *markets hit bottom not when you see light at the end of the tunnel but when today looks less dark than yesterday.* Let's hope that we have reached that point.

Lifetime Staff News

Brian and his wife Daniella have a new baby boy! James Field was born April 3, 2009 and was welcomed by his older brother Owen, almost 2 years old, a seasoned veteran in the Field household. Mom and baby James are doing well. We have noticed Brian is drinking more coffee during the day! Best wishes to a great family.

Ken Conway and his fiancé Jen Pesavento will be married this June in Chicago. Congratulations to a sharp couple. We wish them well.

Thank you for your trust

We do appreciate your confidence and patience in these challenging times. Times like this illustrate the value of self examination and the value of keeping our priorities in perspective during good times and bad. We have had many conversations with our clients on this subject.

Please let us know immediately if your financial situation has changed in any way so that we can make changes to your portfolio to reflect and accommodate your revised financial goals. It is important that you communicate with us in this ever changing economic environment.

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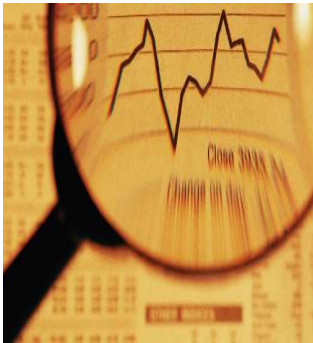
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We recognize that this bear market has been long, steep and severe. Like many clients, you may feel battle weary. We will continue to closely monitor the economic and market environment, as well as your portfolio. While the general outlook in the near future is anything but certain, we do see increasing clarity and focus around the issues at hand. We look forward to discussing your portfolio, financial plans and objectives in our next update meeting. We thank you for the trust you have placed in us during this difficult time and we look forward to continuing to help you work toward your financial goals. We are here to assist you in any way we can. Don't hesitate to call with any questions or concerns about your account(s).

Best Wishes,

Steve Van Houten, CFP®

LPL Registered Principal
CA Insurance Lic#0613686

Lou Oberman, RFC

LPL Financial Consultant
CA Insurance Lic#0393733

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