



# THE PILLAR

Second Quarter 2009

Issue 18

In the last quarter, the stock market had one of its biggest declines and biggest upticks. Not since the 1930s has the market experienced such a jump. The question on many peoples' minds is, "Is this the 'the big fix'?" Investors, politicians and reporters are all hopeful that the increases we've seen over the last six weeks mean the recession is behind us. At Beacon, while we appreciate the reminder that there is hope, we do not believe this is the big fix.

It's just too easy for this to be the big fix. The situation we are in was precipitated by years of massive leveraging and a greedy Wall Street that believed there was no limit to how many securities it could market to the same people. We should have learned our lesson during the market fiascos of 2000 - 2002 or during the 1989 real estate debacle, but we didn't. And yes, even the greed of small investors contributed to our current market conditions; it was our exuberance and inability to realize we were in an overbought market with interest rate spreads too small to be real. Therefore, in our opinion, what took years to build up will take years to unwind.

It has been our belief that we are experiencing a bear market rally and that it will end with a true bottom as overbuying is corrected. This has not been proven at this point in time, but bear market rallies can last for months. Unfortunately, we will only get confirmation of our suspicions once the rally ends.

We are not the only ones who suspect a bear market rally. In an interview with Bloomberg on April 21, Nouriel Roubini, a professor at New York University's Stern School of Business and chairman of the independent economic research firm RGE Monitor, said stock markets may not have reached bottom. "I'm still cautious and bearish," he said. "I believe we are closer to a bottom in the stock market than a year ago but this is a bear-market rally."<sup>1</sup> And then on May 1, he stated, "We are still in a severe and deep and protracted U-shaped recession that – unlike the forecast of the current consensus economists – will not be over in Q3 but will last until the beginning of 2010."<sup>2</sup>

But it's not all bad news. Credit markets in the US and overseas appear to be improving. This improvement is reflected in the reduction in the spread (or the difference in the yield) between "risk free" bonds (treasury bonds) and top quality corporate bonds. Spreads have been at record highs in recent times. In addition, the junk or high yield bond market seems to be improving despite a high rate of default.

Huge declines. Big upticks. Improved credit market. What does all this mean for the average investor? What should our strategy be to withstand big swings and market volatility? 2008 taught us that typical asset allocation based on historical standards may not be the best approach in these times. Buying, selling and systematically rebalancing may not work when markets get turned inside out.

Beacon took to a defensive position in the fall and is still defensive today. Our defense includes strong cash and bond positions. Bonds, in our opinion, provide a cash flow that results in a floor for the overall portfolio. Bonds were hurt in the fall massacre and have been selling at a discount because of the higher than normal spreads, which makes them a good value today.

Holding a cash position is important for two reasons. First, for clients with required cash flows, we are not forced to liquidate positions at depressed prices in order to meet their cash flow requirements. Second, having cash allows us to move back into equities gradually as the market improves. As we all know, there are no guarantees, and our strategy is intended to help preserve capital and to position to re-enter the equity market when the time is right.

1. [www.bloomberg.com](http://www.bloomberg.com). 21 April 2009. Bloomberg News. 3 May 2009.

<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=alBO5ep3pkx0>

2. [www.rgemonitor.com](http://www.rgemonitor.com). 1 May 2009. The RGE Monitor. 1 May 2009. [http://www.rgemonitor.com/roubini-monitor/256589/the\\_thinkers\\_who\\_predicted\\_early\\_on\\_many\\_aspects\\_of\\_this\\_financial\\_crisis](http://www.rgemonitor.com/roubini-monitor/256589/the_thinkers_who_predicted_early_on_many_aspects_of_this_financial_crisis)

What indicators are we looking at to verify signs of real market improvement? Banks will increase lending, unemployment additions will abate and then begin to decrease, and real estate prices will level or cease to decline. These major indicators will definitely add up to an economy that is fundamentally on the mend. Government stimulus has helped ease the pain, however, it begs the question does the small investor always need to bail out the big money making enterprises? But that is a political discussion and not one for The Pillar.

Moving everything to cash is not a strategy! Some Beacon clients want to go to and sit in cash. History has proven that this is absolutely the wrong strategy; it comes from fear and indecision. Interest rates on cash are near zero and the hope for big yields when holding cash is not realistic. The purpose of holding cash right now is to have it available to buy back into the market. All investors would like to be in the market as it runs up and then instantly get out as it turns down. That is an unrealistic game to play and does not match the idea of investing for the long term.

As part of Beacon's communication process we have a regular conference call each month. Recently, a major theme of our calls has been patience. We all need to have more patience and our patience will be tested as we try to avoid kneejerk reactions to rapid changes in the market. The process of trying to predict the market's changes and buying and selling is only for a trader that can sit and watch the moment by moment changes and be in a position to move quickly. Our recommendation is to set a strategy and then implement it. This process is what we refer to as drawing a line in the sand.

One specific change in our allocation approach is we are limiting the number of positions or funds in client portfolios. We believe using fewer managers allows us to be more nimble.

Beacon is a wealth manager and as such, we need to continue to look at the planning components of each client. In the next few months you will hear from your client service manager to set planning times in order to determine action steps over the coming year. If you would like to initiate a meeting before then please call our office at 201.447.9500.

#### **New Managing Director of Operations**

We've made a huge improvement in operations this month by adding Eric Frankel to our team as Managing Director of Operations. Eric is a twenty-year veteran of Wall Street operations at Morgan Stanley, Prudential and JP Morgan. This experience has equipped him with the skills to improve the flow of information, enhance reporting and streamline procedures here at Beacon. Eric is an expert at financial analysis and at making sure all things get done in a timely fashion. Although he has only been with us for the last few weeks, we are already reaping the benefits of having him here. Mark will now be able to spend more time on planning and managing portfolios and less time on day to day operations.

#### **Client Surveys**

Early in 2009, we sent out a survey to all Beacon clients. Approximately 20% of Beacon clients returned a completed survey, and although the data was not statistically relevant, it did give us a lot of good feedback. None of you felt your investment objectives were being met (3.5 out of 5) but, given the current market conditions, this was no surprise. The reviews regarding client statements were mixed with some clients rating the statements a 5 out of 5 and others wishing to see more frequent reports with increased detail. Eric will be assessing different reporting alternatives in the coming months. And lastly, while overall our responsiveness to your calls, the quality of our support staff and our level of communications were good (4.3 out of 5), we see plenty of room for improvement.

We hope our January 2010 survey results will be much improved! If you didn't complete the survey and would like to do so, please call us to request another copy. We are open to any feedback – good or bad – so please keep the lines of communication open!

Thank you for your continued support of Beacon Wealth Management.



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