

QUARTERLY REPORT

VOLUME 8, ISSUE 4 OCTOBER 2009

AFTER THE FLOOD - ONE YEAR LATER

What a difference a year makes. Only a year ago this September the venerable investment bank, Lehman Brothers, was forced into bankruptcy, while its former rival, Merrill Lynch, entered into a shotgun marriage with Bank of America. At the same time, AIG, one of the world's largest insurers, required hundreds of billions of dollars of government support in order to prevent a global financial meltdown. Through Herculean efforts by the Federal Reserve, the F.D.I.C., U.S. Treasury and reluctant financial support from Congress and ultimately an outraged U.S. public, an economic disaster was thwarted. As a result, we are now seeing a rebound in global stock markets. Moreover, after a year and a half of economic recession, the U.S. now appears to have returned to a modest level of economic growth as measured by Gross Domestic Product. As further evidence of a return from the abyss of last September, the following extraordinary measures have ceased: (1) the U.S. Treasury has withdrawn its year old guarantee of money market funds, (2) the FDIC no longer guarantees the senior debt of banking institutions and (3) the Federal Reserve has terminated its extraordinary purchase program of U.S. Treasury debt.

We feel that the worst of the "Great Recession" is behind us but are cautious as to the strength of the recovery. With national unemployment at 9.8% and

rising, we remain concerned about the housing market's prospects as debt-strapped borrowers continue to walk away from mortgages and more job losses are leading to debt delinquencies in the prime mortgage market. As recently as a year ago, the U.S. consumer accounted for 70% of the U.S. economy. Today, the U.S. consumer is retrenching, having paid down more than \$110 billion in outstanding debt over the past seven months. It is clearly encouraging to see the consumer get his house in financial order but it also means that there is little appetite for consumer discretionary spending. The combination of a weak Consumer, limited lending from the banking sector and high unemployment will likely result in an anemic economic recovery, which could put a damper on further appreciation of U.S. stock prices. We expect the Federal Reserve to keep interest rates low for several more months as a continuing means of strengthening "too big to fail" banks while at the same time providing low rates for the refinancing of outstanding mortgages.

As the recovery improves, we expect to see improved corporate profitability and higher interest rates. We are cautiously optimistic for the economy and project a long, slow, rocky recovery.

Cordially,
Kathy Wimmer, CFA, CIC
President

KEY FACTS FOR 2009

- *Annual gift exclusion*
\$13,000
- *Estate tax exemption*
\$3.5 million
- *Highest marginal estate tax rate*
45% in 2009
- *IRA contribution limits*
\$5,000, plus another
\$1,000 for those over fifty
- *SIMPLE IRA and 401(k)*
contribution limits
\$11,500, plus another
\$2,500 for those over fifty
- *401(k) contribution limits*
\$16,500, plus another
\$5,500 for those over fifty
- *SEP IRA contribution limits*
25% of compensation, max. of
\$49,000
- *Top Federal tax rate is 35% on*
income over \$372,950

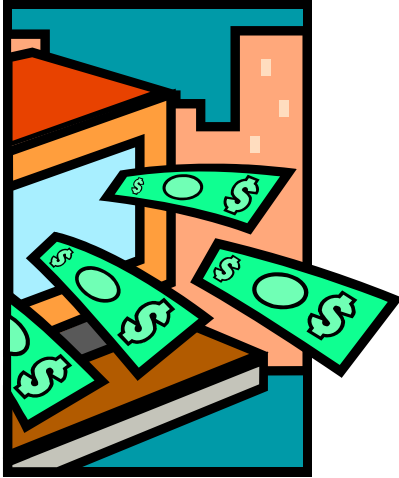
INSIDE THIS ISSUE:

AFTER THE FLOOD 1
- ONE YEAR LATER

THIRD QUARTER 2009 2

FOURTH QUARTER 2009 3

THIRD QUARTER 2009



“Without the benefit of the Federal Reserve printing money in the billions of dollars, it’s hard to imagine that consumers would be in a position to refinance mortgages or even buy a new car!”



While the U.S. gross domestic product (GDP) declined by less than one percent in the second quarter, the third quarter has moved into positive territory, with preliminary growth estimates of 2.5% to 3.5%. This is a marked improvement after a year and a half of declining production in the States. The uptick in GDP is a potent signal that the U.S. economy is emerging from recession. Another bright note for the economy is that the latest Case-Shiller home price data showed a third month of consecutive price increases with August topping out at a +1.6% gain. We have held the premise that U.S. home prices must stabilize or improve before the economy can move forward and grow. We are heartened by the Case-Shiller data but remain concerned that there are still millions of delinquent home mortgages that have not yet been forced into foreclosure. This expected acceleration in foreclosures, coupled with a high unemployment rate, foreshadows an invariably downward pressure on home prices. So although recent GDP and home prices have been on an upward trajectory, we are sobered by the knowledge that all is not well for workers, homeowners and banks.

On the international front, Europe is seeing a similar but weaker recovery to that of the United States, with GDP growth hitting +0.9% in August after a miserly lift of +0.2% in July. Asia has recently picked up growth by undertaking large government stimulus programs to make up for slack demand for their exports from the U.S. and Europe. China is currently growing its GDP at a +8% clip while India enjoys a +6% rate of growth. The U.S. dollar has lost about fourteen percent of its value

versus the Euro over the past year (-4.1% this quarter), which makes commodities such as oil a better deal for Europeans. The Chinese Yuan has been pegged to the dollar as the Chinese government subsidizes the export of its goods to the States with its undervalued currency. We believe the weakness of the U.S. dollar reflects foreigners’ skepticism over whether Congress will get deficit spending under control and whether the Federal Reserve will withdraw its massive liquidity programs in time to stave off incipient inflation concerns. On a more positive note, the dollar, despite its recent weakness, remains the world’s reserve currency. This means whenever there is a global crisis, investors worldwide flee to the relative safety of the U.S. dollar. In the past six months, concerns have abated over the global economic and financial situation, so investors have left the safety of holding dollars in risk-free U.S. Treasuries, opting instead for riskier assets such as equities or corporate bonds.

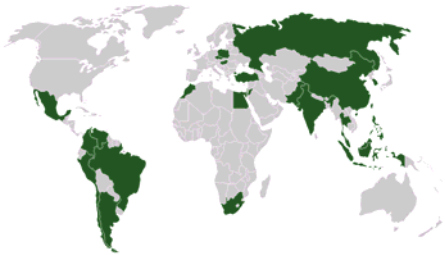
The broad-based S&P 500 index rose +15% in the third quarter, which is the best quarterly performance since 1998. Surprisingly, financial stocks led the broad market higher with a 25% increase during the third quarter. Following close behind, consumer discretionary stocks climbed 19% at quarter end with a major boost coming from the multi-billion dollar “Cash for Clunkers” incentive program. Without the benefit of the Federal Reserve printing money in the billions of dollars, it is hard to imagine that bank stocks could do so well or that consumers would be in a position to refinance mortgages or even buy a new car!

THIRD QUARTER 2009

Continued from page 2

Global equity indices also climbed back strongly in the third quarter as France, the U.K., and Germany rose +21%, +21% and +18%, respectively. The European strength is primarily attributable to hopes for a strong economic recovery. Europe is benefiting from its own stimulus programs, low interest rates and a weak U.S. dollar, which should translate into strong earnings from the overseas operations of U.S. based subsidiaries. The flip side is that a strong Euro versus the dollar will make it pricier to export European goods to the United States.

After climbing +34.7% in the second quarter, the MSCI Emerging Markets index rose +20.9% in the third



“The emerging markets have outperformed the developed nations’ stock markets year-to-date.”

quarter of 2009. The emerging markets have outperformed the developed nations’ stock markets year-to-date, reflecting the lack of subprime lending, a limited use of derivatives and collateralized debt securities and an aversion or exclusion from leveraged financings. In other words, emerging markets saved at a higher rate than rich nations, borrowed within their means using conventional debt financing and shunned or were shut out of leveraged financing. This is a remarkable turnaround over the past twelve years as the debacle of the Asia Contagion crisis of 1998 recedes from memory only to be replaced with the developed countries’ “Great Recession” of 2008-09.

FOURTH QUARTER 2009

The U.S. Commerce Department now reports a preliminary estimate of +3.50% domestic growth and we expect more of the same through year end. The fourth quarter will not have the benefit of the “cash for clunkers” program or the \$8,000 first-time homeowner tax credit to stimulate economic growth. However, we do expect to see inventories restocked after draw downs to minimal levels during the recession. One can question the efficacy of the \$900 billion stimulus program and its purported job creation, rather than job preservation, but we do see the expenditures as having a beneficial effect on economic growth in the short run. Federal profligacy, however, is only a temporary antidote to debt-strapped consumers who are retrenching their spending habits and

discovering the necessity of personal savings. Maintaining a policy of low interest rates, federal bailouts for insurance, automotive and banking companies, coupled with incentives to buy homes and cars, are stopgap measures which limit the economic pain and restructuring that are prerequisites for a healthy recovery. Even with the extraordinary measures undertaken by the U.S. and its global trading partners, we project a rather anemic recovery from the recession and do not foresee economic growth in the U.S. to surpass 2-3% per annum on a sustainable basis. We are more favorably inclined for growth prospects in the emerging markets of China, India and Brazil. Of course, future growth will be compared to the “bubble” or halcyon periods of growth



“The U.S. Commerce Department now reports a preliminary estimate of +3.50% domestic growth and we expect more of the same through year end.”

Please turn to page 4

WIMMER ASSOCIATES

Investment Counsel

350 West Colorado Blvd, Suite 200
Pasadena, California 91105
626-683-3150

We're on the web
www.wimmerassociates.com

We strive to optimize our clients' financial well being by coordinating investment decisions with other professionals in the fields of taxation and estate planning.

FOURTH QUARTER 2009

Continued from page 3

which included the dot-com, tech, commercial and residential real estate, commodity (oil, copper, fertilizer, etc.) and subprime bubbles! We will remain vigilant as to "emerging bubbles" and try to avoid "boom and bust" investment rides.

Although the U.S. and global economies are now clearly on the mend, our cautious optimism is loaded with caveats. First, we view the current interest rate environment with short-term rates near zero to be unsustainable. We do believe that it is unlikely for the Fed and other central banks to raise interest rates in the next six months as the recovery is in its nascent stage and monetary

authorities will not want to choke off economic "green shoots" prematurely. Second, large-scale budget deficits can be used to stimulate the economy and make up for a drop in consumer demand over the short-run but long-term deficits will lead to the

debasement of one's currency, inflation, high interest rates and ultimately, recession redux!

We take the Federal Reserve at its word and believe the central bank will remove its loose monetary policy and quantitative easing (printing money) as soon as the economy can withstand the withdrawal of this extraordinary support. We are not as sanguine about Congress' willingness to turn off the fiscal faucet in a timely manner, but that could change with the upcoming mid-term elections should the electorate choose to impose its newfound spending discipline on the federal budget.



Disclosure: "Be careful about reading health books, you may die of a misprint." Mark Twain Keep that in mind as you read these articles. We obtain data from sources we believe are reliable but they should not be relied upon for making life-changing decisions.