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[Letter to Clients Regarding Present Market Volatility - October 8, 2008]

The remarkable events that have recently occurred in the financial markets have caused many individuals to grow concerned about the future of the U.S. economy and the effect on their investments. In this letter we hope to address many of the questions being raised.

What is happening in the markets?
What began in 2007 as a localized subprime mortgage concern has escalated into a major global financial crisis. Disruptions in the financial markets caused banks to begin peeling back layers of their complex operations to reveal a startling exposure to distressed mortgages. One by one, financial institutions began to crumble as their exposure to bad mortgage-related assets proved disastrous. Many banks labeled "too big to fail" began to collapse - none bigger than Lehman Brothers, which filed for bankruptcy on September 15th. As efforts by the government to address the crisis on a case-by-case basis became ineffective the credit markets tightened up. Global banks, hobbled by wrong-way bets on mortgage securities, remain starved for cash as credit has dried up. These events have stalled economic growth, threatening to push the U.S. into a deep recession. Equity markets have fallen sharply this year in response to the crisis with the S&P 500 index falling 27% through October 6th, 2008.

What is being done to address the problems?
While the long-term goal is to improve economic growth, the short-term challenge has been to unlock the frozen credit markets. Corporations in the U.S. and abroad rely on short-term borrowing to help run their businesses. When banks are unwilling to lend to even the most credit-worthy companies it creates a very challenging business environment.

The Emergency Economic Stabilization Act, which was signed into law on October 3, 2008, gives sweeping powers to the U.S. Treasury Department to purchase up to $700 billion of mortgage-backed assets from banks. With the creation of a market where banks can sell these unmarketable securities, they should be able to improve their books and use the much-needed cash proceeds to fund their normal operations. The initial benefits of such activity may not be felt for months. However, as banks see the prospect of selling mortgage-backed assets, they may become more willing to lend to other companies, thus loosening up the credit markets. This legislation also temporarily increases the FDIC coverage for bank deposits to $250,000 in an attempt to reassure account holders.

In addition to the sweeping legislation of Congress, the Treasury has taken steps to protect money market funds, purchase short-term corporate notes (called commercial paper), and the Federal Reserve lowered the Fed Funds rate by 0.5%. All of these actions are designed to help restore confidence within the credit markets and increase liquidity to financial institutions.

What is going to happen?
It is difficult to predict how soon the recent efforts of Congress and the Treasury Department will work to unfreeze credit markets. Some economists have suggested that even if credit markets quickly become unclogged the U.S. economy will likely see a recession lasting 2 or more quarters. One thing remains certain, it is critical that the credit markets loosen up and banks begin lending to one another so that the stalled U.S. economic engine can start moving again and pull us through these tough economic times. When the economy begins to show signs of increased growth the U.S. equity markets will likely respond favorably. However, the financial markets are likely to face many more challenges before that time comes.

We remain vigilant in monitoring the economic trends that are occurring across the globe. We realize that our clients are facing challenging times and it is our intent to oversee each investment account with the client's long-term interests in mind. During volatile times such as these we are reminded of the importance of diversification, asset allocation, and maintaining an objective perspective.

If you have questions about this letter or about your account please feel free to call us anytime.

Sincerely,

Steven O. Wykoff, CFP®