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Points of Interest:

- Selling your stock investments in a bear market turns a temporary decline into a permanent loss.
- The U.S. stock market goes up by an average of 24% in the six months following a recession.
- Competing investments such as Treasury securities and bank deposits are offering uncompetitive yields.

HAVE THE BEAR MARKET JITTERS? HERE IS HOW TO SURVIVE AND THRIVE

Recession fears, rising unemployment, and stock markets plunging worldwide: What's a poor investor to do?

Not only are the headlines scary and unsettling but so are the monthly statements from your broker showing a drop in your portfolio value.

It can be very hard to maintain your focus and long-term commitment to the stock market when investors all about you are losing their heads. Seasoned investors know that times like these demand calm and patience, rather than panic and action. In fact, it is usually better to sit it out and do nothing until the dust settles.

Here is a guide to help you avoid mistakes, maintain focus, and eventually prosper.

Don't make mistakes

The number one worst mistake panicked investors make is turning a temporary portfolio decline into a permanent loss by selling out in an effort to avoid further declines.

Any investor whose portfolio is diversified throughout U.S. and international stock markets will eventually recover as the markets begin rising at the end of a bear market.

In 10 of the last 11 recessions, the U.S. stock market rallied by an average of 24% during the six months after a recession ended. The sole exception was 2001,



Bear markets are meant to scare investors away and cause losses. Patience and persistence can help you chase the bear away.

when stocks were still overvalued at the recession's end and had further to fall.

How to stay calm

The astute investor carries around a mental checklist of reminders that help him counter the daily drumbeat of bad news that accompanies a bear market.

First on the list: the horse is already out of the gate. By the time you think a bear market is in progress, there have already been sharp declines and the market is closer to the bottom. It is simply too late to take cover.

Second: are competing investments the best place

for money in the long term?

During market panics investors flee to U.S. Treasuries. The heavy buying interest pushes down yields, meaning that new investors will get lower returns over time.

Last month yields on Treasuries fell sharply and new investors had the choice of locking in 10-year notes with yields as low as 3.5%. After inflation and taxes the chance of keeping up with inflation over the next 10 years is very low.

Meanwhile, rates on bank deposits and money

(Continued on page 2)

RISK FALLS AS A BEAR PROGRESSES, AND NEW BUYING OPPORTUNITIES ABOUND

(Continued from page 1)

market funds were falling due to rate cuts by the Federal Reserve.

Third, as scary as the market seems right now, it is actually less risky than it was last year. Yes, a recession will slow corporate profits, but stock prices fall so precipitously in a bear market that they become more of a bargain in relation to future corporate earnings.

Fourth, a diversified portfolio will offer decent returns over the long term. Although

losses come at the beginning of the bear market, eventual recoveries boost your long term return so that, looking back a few years after a bear, returns look much better.

Your next move

You can help your portfolio recover faster by keeping it balanced. Set a target percentage of stocks to bonds and stick with it. When your stock investments fall by some predetermined amount (say, five percentage points below target), it is time to take some



Bears present buying opportunities.

money out of fixed income investments and buy stocks. This forces you to buy bargains.

TURNABOUT FOR CRAMER: USE INDEX FUNDS

This may be one of the strangest investment stories of the year: Jim Cramer, the cable television madman who rants about buying stocks, now says most investors should use index funds.

Wait a minute, this isn't the same Jim Cramer who ran a hedge fund and whose Mad Money show on CNBC nightly touts individual stock plays, is it?

You bet. Cramer's newest book, "Jim Cramer's Stay Mad for Life," warns that individual investors almost never beat the stock market.

In the book, subtitled "Get Rich, Stay Rich (Make Your Kids Even Richer)" and written with Cliff Mason, Cramer advises that most investors will be better off using low-cost index stock funds.

How to lose money

Cramer says investors who want to buy individual stocks better do a lot of research or "you'll probably lose money."

It is worth noting that

Cramer was a typical hedge fund manager, rapidly trading into and out of securities in hopes of capitalizing on the latest information.

He now says that new rules on release of information by corporate executives makes "trying to game short-term movements in stocks almost impossible."

In an interview with Business Week, Cramer said that he doesn't advise investors to do short-term trading because that is as misleading as telling them "you too can play in the NBA."

Cramer's epiphany is backed by plenty of research on real world investors showing that those who trade more

frequently have worse results on average than those who trade less frequently.

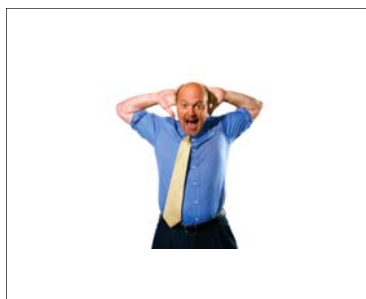
Good advice

Although he isn't too enthusiastic about diversifying a portfolio with bonds ("necessary and boring," he says) Cramer's book ends up giving the same sound financial advice that many financial advisors offer.

He tells readers to make sure they have adequate insurance, to pay off credit cards to avoid unnecessary interest charges, and to contribute to 401k plans and individual retirement accounts whenever

possible.

He criticizes 401k plans that are filled with mediocre mutual funds and an employer's stock, which he calls "the most dangerous investment you could ever make."



Jim Cramer, CNBC's resident investment madman, says investors are better off buying index funds than trading individual stocks.

"Trying to game short-term movements in stocks (is) almost impossible."

THE RICH GET RICHER, BUT OTHERS HAVE A CHANCE TO MOVE UP TOO

Despite growing income inequality in the United States between the rich and poor, Americans still have a good opportunity to move up the income ladder, found a new study by the U.S. Treasury.

In fact, over half of all households moved to a different income group during the period 1996 through 2005, while half of those who were at the bottom of the economic ladder in 1996 had moved up by 2005.

The Treasury admitted that income inequality has increased. Back in 1980 the richest fifth of American households controlled 44% of the nation's income; by 2005 they accounted for 50% of income.

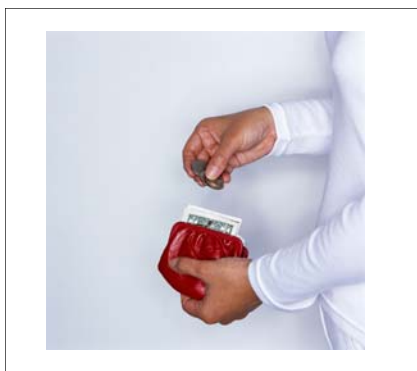
Meanwhile, those in the poorest fifth of households saw their share of the national income drop to 3% from 4% in 1980.

The income hotel
Such statistics obscure the dynamic nature of the U.S. economy, the Treasury argues. No one has to stay in

a particular wealth group and the evidence suggests that there is plenty of movement among income groups over time.

The Treasury's study, "Income Mobility in the U.S. From 1996 to 2005," uses the metaphor offered by the famous economic historian Joseph Schumpeter. He said income distribution is like a hotel with luxurious rooms and rooms that are small and shabby. This is not unfair as long as those in the small rooms have a chance to move into the big rooms, and the luxury rooms are not always occupied by the same people.

The Treasury study seems to confirm this. It found that only a quarter of those who were in the very highest income group in 1996—defined as those in the top 0.01% of all households—remained in the top group by 2005. Their places had been taken by others who had



The average household income grew faster than inflation from 1996 to 2005.

moved up from lower income groups.

All groups gained
Even those who didn't change income groups gained over the period: the median income of all households increased by 24% after adjusting for inflation. Those in the lower income groups increased their income at a faster rate than those in the upper income groups.

This "income escalator" allowed everyone to participate in a growing economy, the Treasury said.

"The evidence suggests that there is plenty of movement among income groups over time."

LUCKY KIDS, THE BOOMER EFFECT, & MORE

Grandchildren in the United States have it made: their grandparents are spending \$50 billion per year on them, according to a study done for Grandparents.com.

About half of that amount is being contributed to investments for grandchildren.

The study found that the average grandparent spends \$1,691 during the child's first year, while a first-time grandparent spends \$3,150.

Some 71% of grandparents in the study said they

wanted to contribute to their grandchild's education.

No baby boom effect
Fears that baby boomers will depress the financial markets by dumping their stocks and homes at retirement are overblown, found a study by Capitol Analysts Network Inc., a Washington, DC research firm.

Baby boomer retirements will be tempered by the 21 million younger immigrants who came here between 1980 and 2000.

"There will be many more

Americans than ever who will want to buy your stocks and your bonds and your houses," said firm president Stuart Sweet.

An adage for investors
Investors shocked by the big declines in stocks in January may feel that getting out of the market now and getting back in later will help.

They would do well to remember a time-tested Wall Street saying about investment patience: It is time in the market, not market timing, that counts.

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HOW HEAVILY SHOULD A RETIREE INVEST IN THE STOCK MARKET?

Common sense seems to tell those who are in or approaching retirement that they should cut back on their investment risk.

After all, they will have to rely on it for income and feel they can't afford to lose it. One rule of thumb says that you should subtract your age from 100 and the remainder is the percentage that should be invested in stocks.

By that measure a 70-year-old should invest only 30% of a portfolio in stocks.

Research into retirement income generation in recent years has turned these common sense ideas on their heads.

Although the stock market can be risky in the short term, the studies say that a retiree's biggest worry is



A retirement nest egg should be weighted more heavily toward stocks.

keeping up with inflation. Over the long term, supposedly "safe" fixed income investments do not tend to keep up with inflation, especially after taxes are paid on interest. The stock market does keep up.

A new study by Consumer Reports magazine and the investment research firm Ibbotson Associates looked at the performance of a wide

range of stock and fixed income portfolios over the past 66 years.

The study adjusted returns and annual withdrawals for inflation.

It found that an all-stock portfolio handily beat an all bond portfolio, providing an average of over \$750,000 in extra retirement income on a portfolio that begins retirement at \$500,000.

This result held up no matter which 20- and 35-year market cycle was chosen, meaning that it did better even in periods that included severe bear markets.

An all-stock portfolio may be impractical for many retirees, both because they may feel terrible during market declines and also won't have a source for withdrawals.

Consumer Reports suggests an 80/20 or 70/30 stock to bond mix instead.

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