INVESTMENT OUTLOOK

Year End 2007

2007 was the year of the biggest Ponzi scheme ever concocted. Starting at the lowest level of the food chain were the home buyers who couldn't afford or were duped into their mortgage obligations. Complicit with them were the greedy mortgage brokers, the Washington Mutuals and the Countrywides. Then came Wall Street with their quantitative geniuses who sliced and diced the sub prime mortgages into bonds only Svengali could recognize. But wait…tiptoeing in from backstage came the monoline insurers whose staid, sober business of insuring municipal bonds wasn't lucrative enough. So…why not insure these Collateralized Debt Obligations (CDOs) and partake of the booty? Get the greedy rating agencies, Moody's and Standard & Poors, to rate the CDOs AAA. Voila, a pig magically turns into a silk purse! Never mind the rating agencies had little or no knowledge about the various CDOs or data points for their performance. Never mind stress testing future performance using unfriendly assumptions—that's only for the elderly with heart problems.

With stupidity that cannot be under estimated, Wall Street brokerages and banks sold the CDOs world wide. They leveraged their special hedge fund clients even more. Mr. Ponzi rests in peace as Wall Street and the insurers' balance sheets lie in ruins.

As for the insurers; they are paralyzed until they can raise additional capital. They haven't the reserves to cover all the CDOs they insured. Write downs, red ink, lost jobs—there's more to come to all these deserving souls.

Oh yes! The cavalry, known as the Federal Reserve, has come to the rescue. This time, lower rates don't work. This gigantic Ponzi scheme conceived of and consummated by the greediest of the egregious, created the worst credit crunch of this decade. As the Church Lady on Saturday Night Live would say, "Isn't that special".

The equity, bond and municipal markets have all felt the after-shocks of these obscene events. If you ask me, tar and feathering the scoundrels would be a good start; followed by something really painful. Am I bitter? Am I angry? You bet. The quagmire will take time to resolve.

In past Investment Outlooks we usually only spend a paragraph or two discussing tax-free municipal bonds. These bonds have always been safe havens to preserve and maintain your principal. Now, the largest municipal bond insurers have gotten themselves into a financial mess. You can understand why you saw more muni bond sales and swaps in your portfolios than ever.

In the fourth quarter it was clear to me that trouble was brewing in muni-land. I began selling insured munis that had no underlying credit rating unless it was an essential service bond like water, sewer, prisons etc or a tax based issue.

Many of you called asking what was happening to the usually serene municipal market. After all, some thought, munis were not part of the sub prime meltdown. As the muni insurers—AMBAC, MBIA, FGIC, XL Capital, Radian, ACA—shares sank, it was clear that financial calamity was unfolding. Almost all of our munis held up well. But additional good, old fashioned General Obligation bonds are better to own in this environment. Give someone else the non-rated bonds with potentially worthless insurance slapped on them. Oh what a tangled web they weave…

I do believe over time the dominos that fell due to the sub prime scheme will stand tall once more. But not all the players will survive. This is how credit cycles usually end. There will be mega law suits and counter charges, Congress will throw in its non-inflation adjusted 2 cents. In the end, only the lawyers will benefit. We've seen this movie before.

So in 2008 we will continue to side-step the mine fields. Both individual and institutional balance sheets will be restored…it's all part of the next cycle. Clean out the old and bring in the new.

With that, I wish you a wonderful 2008 loaded with good health and happiness. The worst of this credit crunch is over…let the New Year begin!

Marilyn

Here's What Made 2007 Worthwhile

There are some things that money alone cannot buy. One of them is the satisfaction of helping someone whom you've never met; who never asked for your help and from whom no amount of thank you's could ever repay what you did for them. 2007 was a year I experienced this elation. Chris and I have been volunteer puppy raisers for Canine Companions for Independence (CCI) for five years now. After raising three puppies, our latest one—Susie—finally made it. She is now a working CCI Service Dog with all the training and licenses to prove it. Her lucky partner, Lin Prideaux, lives in Oceanside, CA. She's been in a wheelchair for 22 years following a chemical accident. Susie fills in many of the things Lin cannot do for herself. Most are simple tasks—such as picking up a sock that fell out of the laundry basket. With the tug *command, Susie grabs and drags the entire basket out of the laundry room and into the folding area for Lin. That simple* tug *is just one of over 50 commands Susie joyfully performs for her partner for nothing more than a pat on the head and a warm bed to sleep in beside Lin at the end of their work day.*

Reunion before graduation

Two happy partners after graduation