WealthHealth
Personal Wealth Management

April 2009

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Stocks saw their best one-month gain in March in more than six years, but while it was a welcome respite from the battering in January and February, the first quarter still ended with a double-digit loss for equities. The large-cap S&P 500 surged by almost 9% in March, yet finished the first quarter with an 11% loss. REITs were beaten sharply lower as investors reacted negatively to deteriorating fundamentals and fears about debt rollovers, and after a weak rebound in March finished the quarter down 32.1%. High-yield bonds, on the other hand, had the best showing of any of the broad asset classes we track, with a gain of 5.3% for the opening quarter. Abroad, the results for developed-market equities were similar to what we saw at home. The MSCI EAFE Index gained over 9% in March, but their 14% loss for the quarter was a bit worse than that of domestic equities. In contrast, emerging-market equities had a great March and finished the first quarter slightly in the black, based on Vanguard Emerging Markets Stock Index Fund. Turning to bonds, the Barclay Capital US Aggregate Bond Index Fund was up 1.4% for the month, bringing their year-to-date results slightly into the black.

Index Returns *Through 03/31/2009*

			Annualized Returns		
Index	**Quarter-To-Date**	**1-Year**	**2-Year**	**3-Year**	**5-Year**
S&P 500	-11.01%	-38.09%	-23.24%	-13.06%	-4.76%
Russell 1000	-10.45%	-38.27%	-23.58%	-13.24%	-4.54%
Russell 2000	-14.95%	-37.50%	-26.26%	-16.80%	-5.24%
MSCI EAFE	-13.94%	-46.51%	-27.85%	-14.47%	-2.18%
Barclay Capital US Aggregate Bond	0.12%	3.13%	5.37%	5.77%	4.13%
Barclay Capital Municipals	4.22%	2.28%	2.09%	3.20%	3.21%
Dow Jones AIG Commodity	-6.31%	-44.99%	-18.15%	-9.84%	-3.25%
CSFB/Tremont Hedge Fund	0.85%	-16.71%	-5.71%	-0.27%	3.60%

Recap of the Current Economic Situation

The list of issues affecting today's investment landscape is dizzying; at the top is the dismal state of the global economy. The fundamental problem is that over the past several economic cycles U.S. households and financial services businesses took on increasing amounts of debt in order to fund consumption and investments. This trend was self-reinforcing as purchases with borrowed money drove up asset prices (such as homes and financial stocks) and profits, which supported even more borrowing. Ultimately this upward spiral was unsustainable, and its unwinding has created an adverse feedback loop of falling asset prices and lower spending and profits. As the economy deteriorates, contributing factors (such as rising unemployment, mortgage defaults, loan write-offs, reduced lending, and overall fear) all fuel one another.

In such a situation, most experts agree that the government needs to step in as a consumer and lender of last resort to try to stop or mitigate the effects of this adverse feedback loop. In effect, the public sector (the government) must take on more leverage and spend more in

The broad economic environment remains highly stressed, and there is a great deal of uncertainty as to what the impact of the recently enacted government policies and programs will be.

Broadly speaking, the near-term imperative is to prevent a debt-deflation spiral from taking hold and that is the basis for policy actions. But longer-term these actions are likely to come at the cost of lower growth, higher inflation, and dollar weakness.

We consider four broad economic scenarios that we believe are reasonably possible in assessing valuations and potential returns for equities and other asset classes. We believe the likelihood of one of our more negative scenarios playing out is high enough to justify weighting those scenarios more heavily in our portfolio allocation decisions.

Short-term risk remains, and investors should consider now how they would react to another significant decline in the stock market.

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order to try to plug the gap created by the deleveraging in the private sector. The $800 billion fiscal stimulus package and the monetary and credit policy actions undertaken by the Federal Reserve and the Treasury to support the financial and credit markets are the result so far.

We agree that stopping a debt-deflation spiral from taking hold is very important, but there remains a lot of uncertainty as to how the government's efforts will play out. Generally speaking, we think that the policies and programs recently announced are likely to help move the economy towards recovery, but they may not alone solve the serious problems we are facing and we expect more government action in the months ahead. In our opinion, no matter what policies are introduced, the impact of consumer and financial system deleveraging will almost certainly be a significant drag on economic growth over the next several years, as saving and paying down debt replaces borrowing and spending. We also believe that there will likely be a price to pay down the road for the current policy actions in the form of a weaker U.S. dollar, higher inflation, higher interest rates and tax rates and, consequently, subpar economic growth and corporate profits, with lower-than-normal stock market valuations (P/E multiples).

Today, we are giving considerable weight to our more negative scenarios when making investment decisions, but even in those scenarios, returns from current asset price levels are likely to be positive over our five-year horizon. As we extend our investment time horizon out towards 10 years, our expectations for equity returns move toward the more optimistic end of our range, in the upper-single-digit to lower-double-digit return range. This is because earnings and P/E multiples are more likely to revert to their long-term trend averages as the global economy improves. However, the path from here to there is likely to be bumpy and there could still be some big dips along the way. It's important that investors try to make an honest assessment now about how they would react to another painful shorter-term downturn.

When stocks do become sufficiently undervalued in the short term, we will look to opportunistically add to our equity exposure in order to generate higher long-term returns for our clients' portfolios. Moreover, while we don't expect big gains from the overall stock market in the years ahead, we continue to hear from many of our equity managers that they are finding once-in-a-generation opportunities that they believe will prove highly rewarding over coming years as the true value of those businesses are eventually recognized.

Though uncertainty is high, we want to emphasize that we are focused on meeting the challenges of navigating this environment and taking advantage of the opportunities that it presents. We appreciate your confidence. Please contact me to discuss any questions or your individual situation.

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