



# The THOUGHTFUL INVESTOR

Warren Wall, CFP®, MBA

Third Quarter

July-September 2007

## Market & Investment Update

The third quarter was a roller coaster for stocks and bonds, starting with mid-summer highs followed by swift drops through mid-August when credit woes drove major indices down. Oil prices hit a high and the dollar hit a low against the Euro. The Federal Reserve helped in September with a half point cut in short-term interest rates. By quarter end, the Dow recovered to close up 3.60% and the S&P 500 finished just 1.50% ahead.

An action-packed quarter like the one just past clearly demonstrates the value of a disciplined approach like Wall & Company's tactical asset allocation. At the worst of the quarter's decline, most of Wall & Company's tactically managed accounts had been moved to the safety of money market funds. Equally important, we were quick to move back into the market once our market trend signals were positive, allowing us to participate in the market's recovery.

Historically, the fourth-quarter is the best quarter of the year. The Dow climbed in the fourth quarter in each of the last

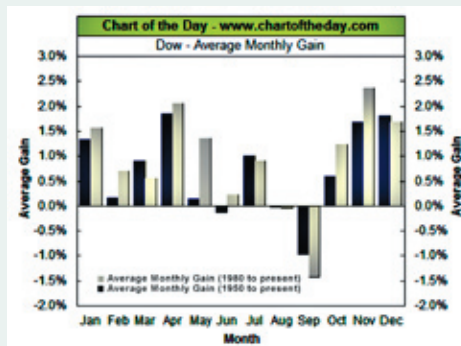
nine years, and in 24 of the past 27 years. The S&P has produced fourth quarter rallies in 13 of the past 15 years. In fact, according to the NOLOAD FundX Sept 2007 newsletter, these last three months of the year generated 63% of the total return achieved by the S&P 500 stock index from 1990 through 2006.

Wall & Company managed programs "net after fee" model results ending September 28, 2007 are shown below:

Performance Chart		
Program	3rd Qtr	YTD
GGPVA	-1.96%	2.36%
WGO	7.71%	12.28%
WGO II	9.15%	13.35%
WGO II-A	11.61%	18.87%
ETF	-8.17%	-2.02%
BBH-S	1.93%	11.73%
BAP	-2.06%	1.97%

## October through April Historically the Best Time to Invest

The strong half of the year for the stock market has historically been the end of October through the end of April. The vast majority of the gains in the S&P 500 and Dow Jones Industrials Average\* have been made in this period since 1950. While this pattern doesn't always play out — notable exceptions were 1973-1974 and 2000-2001 — and past performance is not a predictor of future returns, the trend gives us hope for a strong close to what has been one of the more volatile years on record.



Source: Chart of the Day, www.chartoftheday.com

## Hyman Minsky Was Right

An economist who died in 1996 at the age of 77, Hyman Minsky's economic theories were largely discredited by the "efficient market" theorists of the day. Minsky believed that financial systems are inherently susceptible to bouts of speculation that, if they last long enough, end in crises. Rather than efficient, he maintained that financial markets have a tendency toward excess and upheaval.

The *Wall Street Journal* explains...

"At its core, the Minsky view was straightforward: When times are good, investors take on risk; the longer times stay good, the more risk they take on, until they've taken on too much. Eventually, they reach a point where the cash generated by their assets no longer is sufficient to pay off the mountains of debt they took on to acquire them. Losses on such speculative assets prompt lenders to call in their loans. 'This is likely to lead to a collapse of asset values,' Mr. Minsky wrote.

"When investors are forced to sell even their less-speculative positions to make good on their loans, markets spiral lower and create a severe demand for cash. At that point, the Minsky moment has arrived."\*

While we have a ways to go to see how the current credit crisis finally ends up, the good news is that in every crisis is an opportunity... provided you haven't a mountain of debt to prevent you from capitalizing on the opportunity. In an "efficient market" there is little leeway for investors to outperform the indices. In Minsky's market with bouts of speculation and crisis, investing is a lot more interesting.

\* "Mr. Minsky Long Argued Markets Were Crisis Prone; His 'Moment' Has Arrived," Justin Lahart, *Wall Street Journal*, August 18, 2007.

\* Past performance is no guarantee of future results. The S&P 500 and DJIA are indexes and as such cannot be invested in directly.

## When Good Stocks Go Bad

One of the most frustrating aspects of a market downturn can be watching stocks that you hold, which have nothing to do with the crisis of the day, drop precipitously in value. The company's attractiveness hasn't changed. It may still pay a great dividend. But its value is significantly less.

The reason for your stock's fall is the reason diversification has limited value in protecting a portfolio in a major downturn. All too often, it's the good positions that are sold first in a market downturn, fueling the fall of key indices and the spread of fear in the market.

In the current sub-prime situation, mortgage lenders and home buyers began to rely too heavily on steadily increasing home prices to bail them out of bad loans. Income and asset documentation requirements were dropped for many loan originations and speculation abounded in hot markets. We are now seeing the effects with respect to the housing market.

What is a little less obvious is its impact on major institutional investors with leveraged portfolios that included mortgage-backed securities in their many derivative forms.

When the banks noticed the quality of these investors' portfolios declining

with the increase in defaulting loans, they increased their margin requirements on the monies these investors had borrowed to achieve their leverage. Since the banks had no way of knowing which investors held the most endangered securities, the margin calls impacted a broad range of institutional investors.

These investors had to come up with sometimes millions to meet their margin calls at a time when the value of the mortgage-backed securities was in question. The problem with selling an asset when no one is exactly sure of its value is that you are going to get a minimal offer. If the underlying asset still has value, the investor may be better off to hold on until the market regains its perspective, and avoid selling the security for a fraction of its real value.

As a result, many investors opt to instead sell their "good" stocks where they can lock in gains. Unfortunately, good stocks sold into an uncertain market are still going to fetch a lower price than they might have two months ago. In addition to depressing market demand, the sale of good stocks can actually trigger a downward cycle where other investors, seeing values dropping, opt to sell the stock as well.

It's basically momentum investing in reverse. Any asset which gets priced in a

free market will be impacted by variations in other assets in that market. Good stocks are not immune.

Ideally, the good stocks are the first to bounce back and regain their former value when the correction ends. This is the hope of the buy-and-hold investor.

The active investor takes a different approach and views a declining value as reason to exit a position regardless of the value of the underlying stock, adhering to the old market truism, "Don't fight the tape."

The goal of the active investor is to have funds when the decline ends to buy back into good stocks at a discount. When the stock begins to bounce back, the investor's objective is to gain real value, rather than simply hope to get back to break even. Whether or not the plan works depends in part on when the position is sold, how low it subsequently drops, whether the investor is able to buy back in below the price at which the security was sold and whether or not the stock regains its value as anticipated.

Remember all investing has risks. There is always the potential for loss as well as gain. What is important is that you have a plan and rationale for how you invest and that your plan has an exit strategy.

## Two Vital Documents – A Living Will and a Power of Attorney

The following is a true story related by an associate that points out the importance of planning for the worst. Bad things can happen to good people, but they don't have to be made worse by a failure to plan.

A year ago an old friend suffered a severe stroke that left him with extensive brain damage, dependent on a ventilator and feeding tube to survive. He had lived a long, successful life and accumulated a sizeable retirement portfolio that would leave his wife in comfort for the remainder of her life. After consulting with his doctors, she asked that they discontinue medical treatment and allow her husband to pass away.

Then life became difficult. One of the couple's sons sued to force the hospital to continue treatment. My friend had left behind no living will setting limits on how long he wished life-supporting medical treatments to continue. Nor had he established a

power of attorney to allow another to make decisions on his behalf should he become incapacitated. Without that level of instruction, there was little the doctors could do.

A significant portion of the comfortable

retired, the wife's serenity destroyed, and my friend still lies unresponsive in a hospital bed.

Improved medical technologies have brought with them the ability to prolong life, but the decision of whether or not to do so typically rests on the individual once he/she reach the age of legal consent. When that individual is unable to make decisions and has left no instructions, his or her care can fall into a legal limbo. Regardless of your age, health or family status, you should have a Living Will and a Power of Attorney agreement.

A Living Will is a legal document that sets out guidelines for dealing with life-sustaining medical procedures in the eventuality of the signor's incapacitation. It can be very general or very specific.

A Power of Attorney is a legal instrument that is used to delegate legal authority to another to make property, financial and



retirement portfolio has since been eaten away by medical and legal costs and unprofitable investments that cannot be sold without my friend's authority. The family has been shat-

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## The importance of an exit strategy

There is a point in all aspects of life when an exit strategy is a very good idea. It may be when the weather turns against you, or the highway comes to a complete stop with news that an accident will close the road for hours. You may want an exit strategy in terms of a living will that says when further medical intervention is not wanted. Or even a pre-nuptial agreement that spells out how assets will be divided in the event of a divorce.

Exit strategies acknowledge risk. In investing, your exit strategy should revolve around protecting the value of your assets. Buy-and-hold investing relies too heavily on diversification to minimize losses to your portfolio. There's no exit strategy that says enough is enough. Good investments still have risks. A rising tide may raise all boats, but the reverse is also true.

*Included with this newsletter is an overview of the team serving you at Wall and Company.*

## Two Vital Documents

*continued*

other legal decisions for the principal (the individual who executes the instrument). It can give broad or very limited authority and specifies in what circumstances the "agent" is to have this power and when it terminates. The Power of Attorney is frequently used to help in the event of the principal's illness or disability or in legal transactions where the principal cannot be present to sign necessary legal documents.

Most states have statutory forms, i.e. written model forms for Living Wills and Powers of Attorney that residents can rely on as being legal. Depending upon the complexity of your situation, you may want to consult with your legal advisor to develop these forms.

A living will and power of attorney are not giving away control, but rather taking control of your life. Everyone over the age of legal consent should have both.

## Is Buy-And-Hold Really the Answer to Successful Investing?

Market downturns inevitably seem to lead to a resurgence of articles supporting buy-and-hold investing, complete with back-tested studies of fictional investors proving that trying to "time" the market doesn't work. But before you opt for a passive approach to your investments, take another look at the studies and ask these questions:

### 1) What is the length of the study?

Most studies supporting buy-and-hold investing use periods of 20 years or greater. Given the market's historical upward bias over longer time periods, the impact of down markets is reduced.

Investors who are looking at a shorter investment span, where they will need to withdraw assets not in 20 years, but in 5 or 10 years, or perhaps are withdrawing funds now, could face a very different scenario. Based on historical data, it takes three to eight years to recover from a bear market. If you need your money during that time it doesn't matter that the long-term trend is up.

### 2) Do the studies look at the value of missing down markets?

There's two sides to taking a more active approach to investing. One is obviously to be invested when the market is going up. The flip side is to move out of vulnerable investments when a downtrend appears to be taking shape.

This is risk management at its most basic. Many studies supporting buy-and-hold investing are full of the risk of missing up days, but light on the value of preserving capital when the market drops.

### 3) Are the assumptions reasonable?

One of the statistically "impossible" arguments against active management is the impact on performance of missing the best days or months of the time period. Whenever you encounter this argument, you can be virtually sure the flip side (which is also statistically impossible) – missing just the worst days or months – is omitted.

Before you take the buy-and-hold argument to heart, look at the assumptions of

the study and ask yourself if they ring true for your situation.

### 4) If mention is made of moving in and out of the market in response to market trends, what are the criteria used for moving out and back into equities?

Good active management is based on carefully developed and back-tested principles of market behavior. The investment manager looks for relationships and trends that reoccur over time and indicate a likelihood that the market will move in a similar fashion this time. Emotions and media coverage have no place in the criteria.

### 5) Do you have the temperament to endure sustained losses?

Buy-and-hold investing can work for investors over longer time periods. But it goes counter to human nature. Studies supporting buy-and-hold investing typically deal with smaller account values. If an account of \$10,000 loses 25% of its value, i.e. \$2,500, it doesn't sound so bad. If your \$500,000 account loses \$125,000, it sounds a lot more like real money.

Which is why few investors truly buy and hold. When the pain gets too great, they sell. And, without a plan to reenter equities, they lose opportunity when the markets recover.

Investing is a risky way to make money. It only makes sense to look at ways you can control some of those risks. Looking back at market history and saying...well, the market has always recovered so it will this time as well...is taking a lot for granted. With each market decline, the circumstances change. Different investments tend to move to the forefront, risk return ratios shift.

Our goal in managing client assets is to always take a thinking approach to where you should be invested and why. We believe buy-and-hold investing is far too risky for most portfolios and we welcome the opportunity to show you why.

# PERFORMANCE REPORT

## WALLCO DYNAMIC ASSET ALLOCATION ILLUSTRATIONS

Third Quarter – Ending 9/30/07 (Total Returns Net After Maximum Fees)

Hypothetical Asset Allocations (Net after Maximum Management Fees)	2007 3rd Qtr %	2007 YTD %	2006 Annual %
<b>Aggressive Growth Allocation</b> 50% World Growth Opportunity (WGO) 50% Better Buy & Hold-Stock (BBH-S)	4.82%	12.01%	19.41%
<b>Capital Growth Allocation</b> 40% World Growth Opportunity (WGO)      20% Bond Allocation Program (BAP) 40% Better Buy & Hold-Stock (BBH-S)	3.44%	9.77%	17.14%
<b>Balanced Growth Allocation</b> 30% World Growth Opportunity (WGO)      40% Bond Allocation Program (BAP) 30% Better Buy & Hold-Stock (BBH-S)	2.07%	7.54%	14.88%
<b>Conservative Allocation</b> 20% World Growth Opportunity (WGO)      60% Bond Allocation Program (BAP) 20% Better Buy & Hold-Stock (BBH-S)	0.69%	5.30%	12.61%
<b>Preservation Allocation</b> 10% World Growth Opportunity (WGO)      80% Bond Allocation Program (BAP) 10% Better Buy & Hold-Stock (BBH-S)	-0.68%	3.07%	10.35%
<b>MARKET INDICES</b>			
<b>S &amp; P 500 Composite Index (with dividends)</b>	2.05%	9.17%	15.81%
<b>Lehman Brothers Aggregate Bond Index</b>	2.85%	3.85%	4.33%
<b>US Treasury Bill (3 months)</b>	1.24%	4.01%	4.91%

**IMPORTANT DISCLOSURE INFORMATION** W. Wall & Company, Inc. (“WCI”) performance results represent the actual results of three different existing WCI managed model programs (WGO, BBH-S, and BAP) in various hypothetical asset allocations during the corresponding time period. The performance results reflect the reinvestment of dividends and other account earnings, and are net of applicable account transaction and custodial charges, the maximum investment management fee that would have been charged by WCI during the corresponding time period, and the separate fees assessed directly by each unaffiliated mutual fund holding that comprised each portfolio. WCI utilizes its three model account programs to monitor how existing client in these programs may have performed. Prior to 6/30/07, bond allocations and related performance illustrated a 50/50 investment between the BBH-B and BAP programs. The BBH-B program was discontinued April 2007. As such, as of 6/30/07, the illustrated hypothetical bond allocation and performance only reflect the performance of the BAP bond program.

Past performance may not be indicative of future results. Therefore, no current or prospective client should assume that future performance will be profitable, or equal either the WCI performance results reflected or any corresponding historical index. The composition/percentage weighting of each corresponding WCI index (i.e. S&P, Lehman Bond) is also disclosed. For example, the S&P 500 Composite Index (the “S&P”) is a market capitalization-weighted index of 500 widely held stocks often used as a proxy for the stock market. Standard & Poor’s chooses the member companies for the S&P based on market size, liquidity, and industry group representation. Included are the common stocks of industrial, financial, utility, and transportation companies. The historical performance results of the S&P (and those of or all indices) do not reflect the deduction of transaction and custodial charges, nor the deduction of an investment management fee, the incurrence of which would have the effect of decreasing indicated historical performance results. The historical S&P performance results (and those of all other indices) are provided exclusively for comparison purposes only, so as to provide general comparative information to assist an individual client or prospective client in determining whether the performance of a WCI portfolio performance meets, or continues to meet, his/her investment objective(s). A corresponding description of the other comparative indices, including the Lehman Brothers Aggregate Bond Index (i.e., a fixed income index) is available from WCI upon request. It **should not** be assumed that WCI account holdings will correspond directly to any such comparative index. **Please Note:** The WCI hypothetical performance results do not reflect the impact of taxes. WCI’s model investment programs generally involve an above-average turnover, which could negatively impact upon any net after-tax gain experienced by an individual client in a taxable account.

**For reasons including** variances in portfolio account holdings, variances in the investment management fee incurred, market fluctuation, the date on which a client engaged WCI’s

investment management services, and any account contributions or withdrawals, the performance of a specific client’s account may have varied substantially from the indicated WCI composite model portfolio performance results. In addition, the underlying individual mutual funds which have comprised, and that continue to comprise, the model programs are subject to change at the discretion of WCI. Historical information pertaining to the underlying mutual funds and changes thereto is available from WCI upon request.

**The hypothetical allocation results have inherent limitations**, including: (1) the hypothetical results do not reflect the results of actual trading using client assets, and, (2) for various reasons (including the reasons indicated above), WCI’s clients may have experienced investment results during the corresponding time periods that were materially different from those portrayed in the model.

**In the event** that there has been a change in a client’s investment objectives or financial situation, he/she/it is encouraged to advise WCI immediately. Different types of investments and/or investment strategies involve varying levels of risk, and there can be no assurance that any specific investment or investment strategy (including the investments purchased and/or investment strategies devised or undertaken by WCI) will be either suitable or profitable for a client’s or prospective client’s portfolio. **Accordingly**, no client or prospective client should assume that the above model portfolios (or any component thereof) serve as the receipt of, or a substitute for, personalized advice from WCI, or from any other investment professional.

**All performance results** have been compiled solely by WCI utilizing the performance results reported by each respective mutual fund (and other holdings) that comprised the portfolio, are unaudited, and have not been independently verified. WCI also maintains all information supporting the performance results in accordance with regulatory requirements. Information pertaining to WCI’s advisory operations, services, and fees is set forth in WCI’s current disclosure statement, a copy of which is available from WCI upon request.

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# Meet the Wall & Company Team!

**B**ehind the success of every Wall & Company client is the focused effort of a dedicated team of financial professionals. We would like to take a moment to introduce you to the team of Wall & Company and to invite you to stop by and say hello next time you are in the neighborhood.



**Warren Wall - MBA, CFP™ and Chief Executive Officer,  
Ext. 19, [warren@wallco.com](mailto:warren@wallco.com)**

President of Wall & Company, Warren has over 25 years of experience in the financial services industry. He is a Certified Financial Planner™ who is dedicated to creating wealth and financial security for Wall & Company clients. Warren is also the co-author of two books on retirement and is a well-respected financial educator. He enjoys hiking, boating, skiing and exploring the great outdoors with his wife Lauren and stays active keeping up with his three adult children — Justin, Sarah and Rachelle, and his two grandchildren — Hailee and Jasmine.



**Bruce Dannenberg - MBA,  
MS, Vice President, Ext. 15,  
[bruce@wallco.com](mailto:bruce@wallco.com)**

Bruce has been in the insurance, investment, and financial planning arena for over 22 years. He holds a Master of Business Administration degree from the University of Vermont and a Master of Science degree from Clemson University. He has owned his own insurance and investment business

in addition to working for several high profile companies. Bruce lives in Black Mountain with his wife Susan and their two boys, Jesse and Isaac.



**Andrea Robertson -  
Office Administrator, Ext. 18,  
[andrea@wallco.com](mailto:andrea@wallco.com)**

Andrea has six years of accounting experience. She graduated from Asheville-Buncombe Technical Community College with her Associate of Arts in Accounting in 2001. She is the correspondent for the company's accounting, compliance and trading needs. When she isn't working,

Andrea takes pleasure in spending time with her family, husband Patrick and son Elijah, two cats and one dog. She also enjoys camping, viewing fast and/or antique cars, and music.



**Kim Carver - Trade Manager and  
Client Service Assistant, Ext. 22,  
[kim@wallco.com](mailto:kim@wallco.com)**

Kim entered the financial services realm with Wall & Company after six years in front office administration. She graduated from Asheville-Buncombe Community College with her Associate of Arts degree in Business Administration in 2000. Kim handles daily trades and assists

clients with service needs. She enjoys spending time with her family, husband, Chris, and her four children Quentin, Kaitlyn, James, and Mikaela, going to the lake and being a cheerleading instructor in her spare time.



**Jenni Gregory - Client Service  
Team Manager, Ext. 17,  
[jenni@wallco.com](mailto:jenni@wallco.com)**

Jenni comes to Wall & Company with over 15 years experience in accounting and administration. She holds an Associate Degree in Accounting from Blue Ridge Community College and is Wall & Company's Client Service Team manager. Jenni is responsible for making sure all customer

service needs are being met in both an accurate and timely manner. She is a native of Henderson County and currently resides in Flat Rock with her husband Stephen and two children — Lindsay and Colton. Jenni enjoys spending her free time at the lake with her family, attending concerts and reading.



**Mary Cluer - Receptionist,  
Ext. 10, [mary@wallco.com](mailto:mary@wallco.com)**

Mary comes to Wall & Company with a background in front office administration. She worked for a family practitioner for over 10 years and within the service administration area for a manufacturing company for more than eight years. Mary moved to Asheville from Southern California with her husband, Allen. They have

two grown children, Justin and Courtney. She enjoys antiquing, reading and cross-stitching.



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