1st Quarter 2008

PERFORMANCE AND MARKET OUTLOOK

The first quarter of 2008 was not a fun time to be an investor, with most equity benchmarks falling close to 10%. What made matters worse is that there was almost nowhere to hide – nearly every segment of both the stock and bond markets had negative returns to some extent. Commodities and high quality bonds were among the few areas to post positive results. Perhaps most striking about the past three months was the extraordinary volatility, not only day to day, but intraday. Daily moves (up or down) of 2% were fairly common, with the average day showing a change of over 1%. Intraday moves were even more astonishing. The average intraday fluctuation was more than 2% (low to high or high to low) with moves in excess of 3% occurring one out of every five days.

The prospects for gains in the foreseeable future seem bleak. Oil prices (and commodity prices in general) are high, the war in Iraq continues, the economy may be in a recession, and the sub-prime crisis keeps spreading. These are all certainly valid reasons for concern. There is one reason for optimism: pessimism. What does that mean? Historically when the vast majority of investors feel one way about the markets it is usually about time for the trend to change. When was the last time you heard anyone say anything bullish about the stock market? Can't remember, can you? Pessimism is so rampant that I believe we have reached, or will soon reach, one of those inflection points when such extreme sentiment signals a terrific time to be a contrarian.

In some ways the sub-prime crisis is unique in its particular manifestation. The quantity of home loan defaults and the fallout it has created in nearly every financial area is staggering. Yet, in many ways, this is a cycle that has played out in our economy over and over again. At its core this is a liquidity crunch - a fundamental shift in the appetite of banks to take on risk (make loans of any kind). It happened in 1990 with the Savings and Loans Crisis; it happened in 1998 with the fall of Long Term Capital Management; it is happening today; and I guarantee that it will happen at some point in the future. I have no idea what the specific future cause will be. Most likely it will be something that has never happened before. But at its root will be a shift in sentiment. Wherever human emotion is involved, there will be cycles of optimism and pessimism, risk acceptance and risk avoidance, bullishness and bearishness, fear and greed, etc. The point in all this is not that we should rejoice. Times like this are painful. But, if history is any guide, this, too, shall pass.

Investing for the long term can be difficult at times like these, yet this is exactly what **Asset Allocation** clients are doing. To be sure Asset Allocation spans a relatively large range of risk profiles – from aggressive to conservative. Regardless of your particular risk level, though, if you were in Asset Allocation in the first quarter you lost money. More conservative accounts lost about 4% while more aggressive clients lost 8% or more. Since Asset Allocation is the classic long term investing approach, results are best judged from a longer term perspective. From the start of 2003 through March of 2008 our aggressive Asset Allocation clients are up on average 102.5%, and the typical conservative client is up 72.4%. These represent average annual returns of 14.4% and 10.9%, respectively. Lest you have any doubts, these figures include the drops we have seen over the past five months. When it comes to evaluating the performance of your Asset Allocation Portfolio I am reminded of the old adage "can't see the forest for the trees." Focusing only on short term performance (the trees) can easily overwhelm the fact that longer term performance (the forest) has been terrific.

Of course Asset Allocation isn't for everybody, or at least not for 100% of everybody's portfolio. This is where our Wealth Preservation Programs come in. We do not expect these programs to be up as much in the strong up periods, but we do expect them to hold up better during the significant declines. Put more directly, periods like the one we are in now are when our Wealth Preservation Programs should shine. So, how did they hold up? Quite well! Every one of our Wealth Preservation Programs out-performed its benchmark.

Braver's Municipal Bond Program earned 0.70% for the first quarter of 2008. This is not a spectacular return until you realize that the benchmark index for municipal bonds lost 0.89% for the quarter. We were content to sit on the sidelines the entire quarter as the municipal market went through some turbulent and unprofitable times. At the end of the quarter prices in the municipal market stabilized enough for us to re-enter the market. We bought municipal bond funds on 4/1/2008, and as of this writing we are modestly positive on these positions.

Braver's High Yield Bond Program did have a losing quarter - just our seventh losing quarter over the 11 plus years we have been managing the High Yield Bond Program. As is typical of those seven losses, though, we lost less than buy and hold. We were down 1.2% whereas the high yield benchmark was down 3.6%. We never like losing money, and we know our clients don't. We must always look at the losses with respect to the markets in which we invest. Over the last year the high yield benchmark is down close to 5%. We are up 2% over that same time period. It is out-performance such as this over the negative periods that has allowed us to double the returns of the high yield bond benchmark over the last 11 years – with less risk. We began the first quarter invested in high yield bonds, sold in early January, and remained in cash until the end of March when we invested once again. Thus far our trades are positive. From a fundamental perspective, high yield bonds offer a better value today (in terms of the yield spread over treasuries) than they have in a few years. Of course this does not guarantee a winning trade. As always we follow our models and not anyone else's theory.

Braver's Strategic Portfolio and Tactical Allocation Programs held up quite well over this difficult period, falling 1.7% and 1.5% respectively. During a period when the overall market fell nearly 10% we consider these results quite successful. The Strategic Portfolio Program is under-weighted in equities and over-weighted in areas such as energy, commodities, global bonds, and inflation linked bonds - all positive sectors in the first quarter. Portfolios will remain invested this way until the July re-balance. Tactical Allocation Program accounts have been under-weighted in US equities for well over a year. Up until the fall, this cautious stance did not serve us very well. Since then however, the models have proven quite prescient. As of this writing, portfolios are 25% invested in equities, 25% in bonds, and 50% in cash.

While our **Diversified Asset Program** did indeed outperform its benchmark (balanced funds), it did so by a slim margin. In the end, accounts fell by 5%, and although this is down half as much as the market (S&P 500), we do expect better from the Diversified Asset Program. As I've written in the past, if there is one environment in which the Diversified Asset Program typically struggles, it is a volatile market with extreme short term swings both down and up - just the sort of market we are experiencing. As of this writing, accounts are about 70% invested and thus far we have seen modest growth to start the second quarter.

The lone disappointment thus far in 2008 is unquestionably the **Sector Rotation Program**. We've made no secret of the fact that this is our most volatile program. It is not uncommon for Sector Rotation accounts to drop when the market declines sharply. More often than not, however, we have been able to contain our losses to no more than the overall market. Unfortunately this was not the case in the first quarter as accounts fell from 14% to 18% (although it is worth noting that the NASDAQ was also down 14%). With the extreme market volatility, no sector was able to gain enough momentum to allow our models to take advantage. The good news is that as we start the second quarter we have already seen portfolios rise 8% in just the first few weeks.

COMPANY NEWS

As I write this newsletter we are finishing a flurry of last minute activity associated with tax season deadlines. For many it is funding IRAs or retirement accounts. For others it is freeing up some cash to pay taxes. I'm not an accountant, yet I'm exhausted! We do have a lot of accountants here, though, and I can hear them gathering down the hallway for their well earned tax day festivities. I think I'll head over to see if there are any leftover refreshments.

Daniel J. Traub