

Are We There Yet ?

If we do not incur another major surprise from the financial services industry we may have begun to experience the first signs of a bottoming in the U.S. economy. The recent expanded efforts by the Federal Reserve and the Treasury are providing the necessary measures to stabilize the banking and related industries to begin the process of repair. These actions coupled with the just passed fiscal stimulus package will go a long way toward slowing the economic decline and eventually reversing it.

We are beginning to experience a bottoming in those sectors that precipitated the collapse of the banking system. Housing starts appear to be leveling off at a rate of 500,000 units annually. This is less than one third of the peak levels achieved at their high. Mortgage rates have trended lower stimulating an increase in refinancing which has helped to stabilize the housing market. A fair amount of toxic assets have been either removed from the balance sheets of the leading financial institutions, or more equity has been added to help to ensure their viability going forward. Actions by both the Fed and Treasury have loosened the frozen credit markets. Recent new corporate bond issues have been successful providing the necessary funding for corporations to grow. New programs by the government have also helped to revitalize the securitized debt market which had become an important part of the financing enjoyed by economies around the globe. As these programs expand they should further loosen the frozen securitized debt market.

As inventories have been reduced, production has declined. We are beginning to see signs of a restocking of inventories to meet the new lower levels of demand. This will have a positive impact on production which has been in a sharp decline. Consumers have adjusted their spending and savings to a newfound sense of reality. Savings are increasing and debt levels are being lowered by individuals at all levels of economic wealth. As these changes begin to spread, Consumer confidence should begin to slowly improve. This confidence is further strengthened by the strong and positive action government is taking to increase and strengthen the regulation of the financial services industry.

Beyond these announced efforts that have transpired, Government, Business and the Consumer are gaining more experience in addressing the rapid changes they face. Expenses have been reduced to adjust to the new lower levels of activity. Advances in technology have provided more and faster information flows, which have helped to make better decisions. We believe the speed of information flows, as well as the ability to process this information more rapidly, was partially responsible for the precipitous global economic decline. Although still too early to make a judgment, these same capabilities may have a positive impact on shortening the time to restart the global economies.

We have identified several positive signs which indicate we are flattening the slope of the economic decline and may be approaching a leveling. Most economists agree that the success of efforts to achieve this objective is centered on the ability to stabilize and restart the global banking system. The current administration with the aid of the Treasury and the support of the Federal Reserve has embarked on a massive program to accomplish this objective. It is this concentrated focus and the many new initiatives, which will go a long way to be successful in these efforts. The U.S.

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apparently was the catalyst for the global economic decline, and will be the catalyst for its stabilization and eventual rise.

The financial markets appear to be stabilizing from a recent period of loss of confidence, created by the fear of a need to nationalize the U.S. banking system that was on the verge of bankruptcy. Recognizing that we have witnessed short periods of relief from falling stock and bond prices in the past 18 months, this time we believe there is a reasonable chance that we could be witnessing a market bottoming. Although, there is the potential for more unexpected surprises, we do believe the probabilities are more favorable now that we have seen the depth of the broad measures of decline in both bond and stock valuations.

As economies repair and confidence is restored both in Business and the Consumer, Investor Confidence will most likely improve. We do agree with the consensus that the road to recovery will be long and hard with a variety of stops and pitfalls along the way. Beyond the economic issues identified, there are a large number of geopolitical issues to solve. Certainly the plate is full of uncertainty, all of which will take time to address and hope to resolve. In such an environment it would be difficult to envision any quick return to either Consumer, Business or Investor Confidence levels that we had experienced in recent years.

We at AHB had structured client portfolios to endure the difficult period that transpired during the previous 18 months. Fortunately, client bond portfolios avoided being impacted by all the unexpected tragedies that affected many bond investors. Client equity portfolios held up significantly better than that of all market indices. Although client equity portfolios declined, they declined significantly less than those of the market indices as well as most other investment managers. AHB's emphasis on continuous client interaction has enabled clients to arrive at an appropriate asset allocation of bonds and stocks to meet their investment objectives and risk tolerance levels. When AHB client investment experience is considered, taking into consideration asset allocation, AHB clients have endured the market turbulence quite well, and are now well positioned to participate in the anticipated market advance.

Looking to the future, we have begun to invest a portion of the cash reserve created prior to and during the market decline into those areas that offer attractive opportunities for long term investment.

As always, please feel free to contact us to discuss our economic and investment outlook or more specifically your portfolio(s).

Investment Policy Committee

Abner, Herrman & Brock Asset Management

Founded in 1981, Abner, Herrman & Brock Asset Management manages portfolios individually structured to assist each client in achieving their investment objectives. Stock portfolios are managed utilizing a Core Equity philosophy, investing in both large capitalization value and growth disciplines with an objective of long-term, after-tax appreciation and below market volatility. Portfolios are diversified across economic sectors, industries and companies. Bond portfolios are managed to provide a high rate of current income and total return. Portfolios are invested in staggered maturities of U.S. Treasury, government agency and investment-grade corporate bonds and where appropriate, investment-grade municipal bonds. Portfolio managers are available to meet with clients upon request.

Please visit our website at www.ahbi.com for a more detailed description of our investment **Philosophy, Process and People**.