



Registered Investment Advisor

## STEIN WHITTINGTON DENIEL INVESTMENT ADVISORS

# Wealth Manager

### April 09 HOW DO INVESTORS MAKE MONEY IN EQUITIES OVER TIME?

Since October, 2008, the equity markets have gyrated dramatically. For example, the DOW was at almost 10,000 on October 6th and it hasn't been even close to 10,000 since then (Closest was 7608 on March 31st, 09). The S&P 500 was at 1,057 on October 6th and it hasn't reached the 1100 level since (Closest was 798 on March 31, 09). The most dramatic aspect of this reporting is the fact that the equity markets experienced one of the most robust bull moves in its history during the 17 day period from March 9, 2009 to March 26, 2009. During these 17 days, the Nasdaq Index rose about 25% and the DOW and the S&P 500 each rose more than 20% during. (Please see enclosed article by James Stewart published in the WSJ).

Yet, notwithstanding these dramatic increases in each of the three major indices, the closing averages on March 31, 2009, are far below the value of these averages one decade ago. **Ten years of buy and hold investing and not a penny to show for profit, indeed a loss!** Without discussing the global markets specifically, suffice it to say that during the past approximate 15 months, China, India, Europe and other recognized global markets have suffered large declines even more than the U.S. The weaknesses of the U. S. economy have infected the entire world; as the United States faced economic uncertainty and malaise, exports from the Far East and elsewhere plummeted, bringing widespread adversity to these nations.

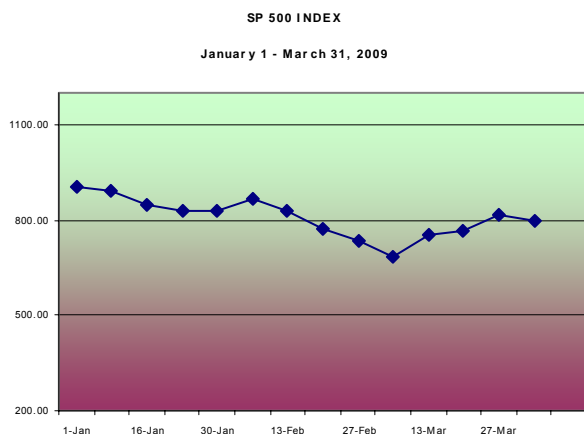
The implications of the above facts are quite startling, particularly when one considers that the long term, patient, buy-and-hold strategy has been the standard to save for a retirement nest egg. Now the facts show that a buy-and-hold

investor must also pay attention to markets and economic risk. At Stein Whittington Deniel, we recognize the extreme difficulty of gauging the direction of the equity markets. "Talking heads" offer their opinions on TV; many of these persons are extremely knowledgeable and they often have different viewpoints. It is also paramount to appreciate the fact that a discussion about the economy does not necessarily provide any great insight as to how the stock markets will perform. This is true for many reasons, but one of the fundamental reasons is that: Stock markets are often emotionally driven and market direction proves as allusive as analyzing the power of emotions on human behavior - impossible.

The discipline inherent in Covered Call Writing ensures that the investor does not find himself ... in the position of the buy-and-hold investor

Hence, the best portfolio managers necessarily must employ either (a) consistently good stock picking skills (often claimed but rarely achieved) or (b) a strategy that is reliable and works well in almost every market environment. Based upon expert research and verification as well as our firm's empirical data, we are confident that Covered Call Writing offers an excellent investment strategy for most investors. Covered Call Writing presents a significantly different approach to a buy-and-hold investor. For example, in Covered Call Writing, we set a "strike price" at which our clients agree to sell their stocks. If the strike price is met, the stock is sold at the strike price and the funds received are re-employed. Usually the underlying stock or ETF is held for a short period and we take a small profit each time. The investor makes his or her money on the Covered Call premium received as well as any additional monies which are received if the strike price is above the purchase price (usually the case). The emphasis of the Covered Call investors is receipt of short term capital gains and constant reinvestment — completely different from a buy-and-hold investor. The discipline inherent in Covered Call Writing thus ensures that the investors do not find themselves in the position of the buy-and-hold investor — no gain after ten years of investing.

## THE QUARTER IN REVIEW



Following the dismal performance during the 4th quarter of 2008, the first quarter of 2009 saw more of the same followed by a sharp rally that began March 9th. For the quarter, the major indices performed as follows: DJIA, ↓13.30%; S&P 500, ↓11.66%; and NASDAQ, ↓0.03%. So far, the advances are continuing during the first few days of April. It is interesting to note that the DOW and the S&P 500 are both significantly below the levels registered on September 17, 2001, when the markets reopened following the attacks of September 11. The NASDAQ is only slightly below its September 17, 2001 value.

As to the U.S. and worldwide economies, there is little to be optimistic about. The deflation suffered by natural resources has hit Russia, Brazil and much of Asia very hard. The weak consumer demand in the U.S. and worldwide has left Japan, China and other exporting nations in crisis. In the face of adversity, however, the U.S. has not sat by idly but rather has decided to spend trillions of dollars to prop up the economy. The national budget now under consideration proposes deficits in the trillions of dollars with optimistic assumptions as to repayment. The budget is likely to be approved over the objections of those that disagree. There remains a serious question whether or not the economy can support deficits of this magnitude over the long run. The resulting corollary to government financing is that there will be greatly increased government surveillance/oversight of private key sectors of the economy, a prospect which many free market advocates abhor. The potential adverse affects on business are quite real if government intervention were to have a negative effect.

The only bright spot, lies with China, which is projected to grow at about 7% per annum; however, this is far below its prior growth rates of 11% or more per annum. Since about October, the Chinese stock markets (closed to foreigners) have risen dramatically and, after a dismal 2008, the Chinese indices and stocks which trade on U.S. exchanges have shown much more strength during the past quarter.

The Organization for Economic Cooperation and Development, which tracks 30 industrialized nations, estimates that these nations face shrinkage of 4.3% this year. Worldwide, the shrinkage is expected to be approximately 2.75% for the year. The World Bank projections are only slightly more optimistic. While inflation is expected to remain low this year, with the United States, China and other countries pumping large amounts of cash into their economies, it is entirely possible that inflation could reappear within the next 12 months. Periods of sharp inflation, which lead to rising interest rates, could dampen any sustainable recovery.

Against this backdrop of so much negative news, however, real estate prices have dropped resulting in a more affordable housing market; at the same time, the stock market is now fairly reasonably priced, by most estimates, thereby reducing market risk.

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