

# LFM&P

*Your Personal Financial Advisor*

January 1, 2005

## **Outlook & Trends**

This Outlook & Trends is different than past editions. The economy continues to expand, albeit at a somewhat slower pace than some would like, the stock market has reasserted its rising trend with a new three-year high, and bonds remain overvalued, but have performed better than most expected a year ago. Rather than discuss economic conditions that may be evident to many readers, we would like to highlight another trend that is of utmost financial importance to everyone, but often is not recognized or well understood. While financial advertising focuses almost exclusively on the potential for investment profit, increasing reliance on self-directed 401(k)s, concerns about the viability of Social Security, and ever-present inflation are transferring significant risk to individuals. Consequently, management of financial risk is becoming evermore critical for individuals regardless of their wealth.

You can think of “risk” as the probability that something will turn out worse than you want it to.

**Planning risk** is the risk that you will not have the financial resources to meet your future goals. Veteran readers of this letter know we have frequently exhorted you to identify your goals and map out a plan to reach them. Just considering your risks in advance, through planning, goes a long way toward helping your future turn out the way you want.

**Investment risk** is a bit different, because it is inextricably coupled with expectations of gain. To receive a greater return, you must assume greater risk. The opposite is not true, however. The mere act of accepting risk will not produce profit. In fact, higher risk means there is a greater chance of loss!

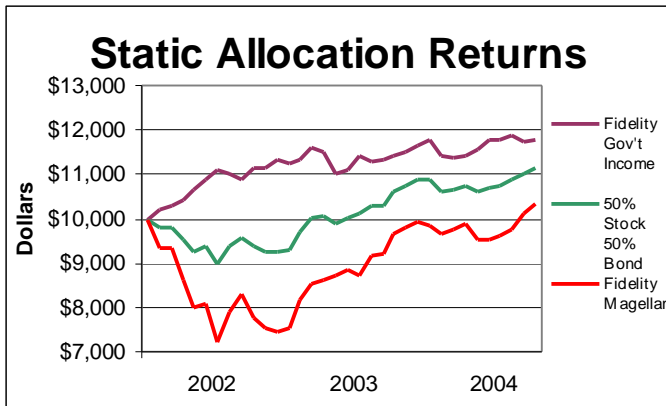
Unless you are one of the few who can live out your retirement years on a guaranteed pension and a savings account that will keep you ahead of inflation, *you will need to deal with investment risk*. Are you handling it effectively? Many people allow their emotions to dictate their actions, ignoring risk and thinking only about potential gains when stock prices are high, like the late 1990’s, (“Give me a chance to get into that hot IPO!”); and thinking only about risk when stocks prices are low, like 2003 (“I’ll only trust savings accounts and real estate from now on!”). A steadier, well-considered approach is required.

Stocks are necessary to own as a foundation for producing retirement income and wealth, because over the long-term they have generally produced greater gains than bonds and inflation. But they also carry more risk, meaning that there is a chance of not meeting your goals or of outright loss. How can you become comfortable with this financial complexity and uncertainty? Providing on-going personal solutions to these challenges is the essence of *LFM&P*’s financial management services.

Managing investment risk is key. Providing diversification is very important. (Readers holding a lot of their own company’s stock in their 401(k) plans please take note!). Mutual funds can provide valuable diversification, but a typical mutual fund is not designed to manage your overall investment risk.

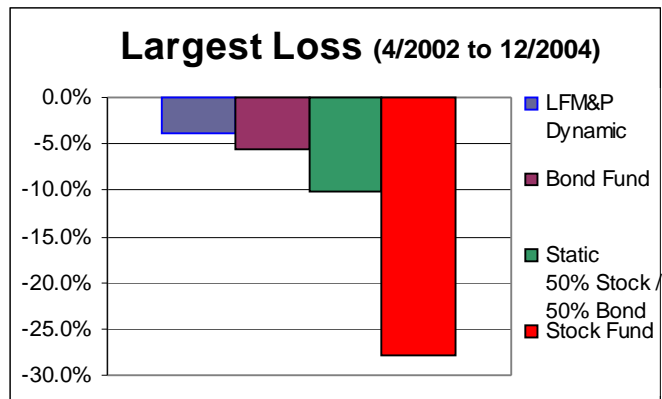
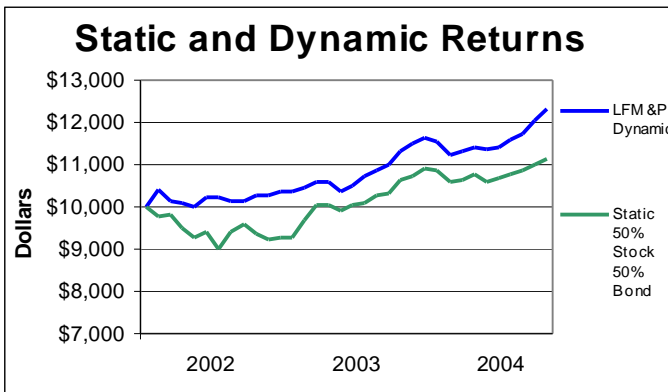
Properly allocating investments between different types of assets also helps to control risk. If you use “static” asset allocation, you choose an appropriate asset mixture based on long-term historical results

and maintain this mixture over time. *LFM&P* can assist you to build and maintain this type of portfolio. We also offer our “dynamic” MarketAware<sup>SM</sup> approach, which goes further, seeking to smooth out some of the fluctuation in portfolio values, by reducing exposure to stocks during higher risk periods.




Examples of these approaches are shown in the graphs. The “Static Allocation Returns” graph, on the left, shows the recent return of a hypothetical \$10,000 investment and the associated risk for a typical no-load stock fund (red), bond fund (purple), and a simple 50% stock / bond static allocation (green). One of these results would probably resemble your own experience, depending on the allocation you have chosen.


The lower set of graphs illustrates the actual performance of a composite of all *LFM&P*'s individually managed accounts (blue line). They mostly use our “dynamic” MarketAware<sup>SM</sup> approach. The 50% / 50% allocation result (green) is included in all three graphs for ease of comparison. The “dynamic” result provided a higher return with less interim loss than any of the “static” choices\*. This is largely because the dynamic approach was able to limit



losses early in the period by reducing stock risk while allowing stock gains to be realized later.

Managing risk is crucial to long-term financial success, regardless of your financial position. If you would like help managing your investments or planning to reach your financial goals, please give us a call or send an e-mail.

  
David C. Linnard  
President

  
Barbara V. Linnard  
Vice President

\*The period shown begins in April 2002 when *LFM&P* was incorporated, and ends today, 12/31/04, including both up and down markets. The comparison includes all fund management fees, commissions, and adjustments for deposits and withdrawals. It does not include taxes paid or advisory fees. The allocation of the actual “dynamic” results changed with market conditions throughout the period. The returns of the strategies shown will be different in the future and it should not be assumed that results will be profitable.

Linnard Financial Management & Planning provides investment management, financial planning and financial analysis services for people who value unbiased assistance and advice. Since we sell no products and accept no commissions, we are able to evaluate the best solutions for each client. Our mission is to know each client personally and design and manage financial solutions that match their needs and goals. We will be happy to help you analyze a financial question, plan and achieve your own path to financial success, or manage your investments.

LINNARD FINANCIAL MANAGEMENT & PLANNING, INC.  
46 CHESTER ROAD  
BOXBOROUGH, MA 01719

LFMP@LINNARDFINANCIAL.COM

978-263-0025

A Registered Investment Advisor