BEYOND THE HORIZON

4th Quarter, 2007 Issue

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MARKET UPDATE

This October marks the 20th anniversary of the 1987 stock market crash, the biggest one-day post-war percentage drop for the U.S. markets. Despite the crash, $10,000 invested in the Dow on Friday, October 16th, the last trading day before the crash, would have more than quintupled if held until the present.

The crash has made October notorious for being the toughest month psychologically for the markets. Could it happen again? Though there are parallels between October 1987 and now, there are significant differences. One of the biggest differences today is that interest rates remain close to multi-year lows and that inflation, too, is low.

One disconcerting parallel, however, is the concern over credit. In 1987 the problem was with the savings and loans. Today, it is concerns over subprime lending. This concern, combined with the slowdown in the housing market, created a tumultuous ride for the equity markets this summer. But the subprime market, according to American Funds research, is an $800 billion market in what is a $30 trillion bond market. If subprimes are only a 2.67% slice of the pie, why has it caused such a mess? American Funds' portfolio counselor Mark Macdonald points out that what is subprime to one banker may not be subprime to another. Therefore, the markets are not being very discerning, taking all mortgages down with it, not just the subprime mortgages. The result is that even those with good credit are having trouble getting mortgages.

For now 70% of mortgage foreclosures have been contained to seven states, according to Kiplinger. However, state and federal regulators have already begun to jump in to help. Congress, as well, is moving to thwart future problems.

The bottom line is how this problem might trickle down to the consumer. With woes in housing and credit expected to continue into next year, what is the potential impact this might have on the overall economy? Though it will most likely cause a further slowdown, will it send us into a recession? To answer that question, we should look at an official definition of recession. According to the National Economic Bureau of Research, a recession is when a "significant decline in economic activity spreads across the economy, lasting more than a few months." Though we have seen a slowdown in certain areas of the economy, we continue to see growth as well. Additionally, the Fed's recent move to cut interest rates , the first cut in more than four years, should help. The action was intended to help forestall some of the adverse effects on the broader economy from recent disruptions in the financial markets and to promote growth.

Though the risk of a recession has been growing, it most likely will not occur. Our economy is resilient. According to MarketWatch, the economy, over the past 17 years, has been in recession for only eight months. As we have stated in past newsletter articles, the U.S. economy is diverse enough that a slump in one sector usually does not have that much of an impact on the economy as a whole. Based on continued gains in the equity markets this year, perhaps the markets agree. They may already have factored in the concerns over subprime loans and the housing market. After all, the markets are leading indicators of what is to come, not what has already taken place.

As for stocks, U.S. companies continue to see profits rise. The third quarter earnings reports are expected to be positive, once again. One contributing factor is strong global growth. In contrast to 1987, markets today are so globalized. About half the sales of S&P 500 companies today are registered overseas, according to Kiplinger. Current P-Es (the ratio of stock prices to their earnings per share) around 17 are fair and at normal levels, according to Ron Muhlenkamp, indicating continued valued in stocks.

At the close of the third quarter, the S&P 500 was up 7.60% for the year with the Dow and Nasdaq up 11.5% and 11.8%, respectively. Do we expect these healthy returns to continue? No one knows for sure when the next market cycle will occur. We will continue to watch interest rates, GDP growth, jobs growth, consumer spending, etc. Although there is no way to predict what will happen next, we believe there will always be opportunities for the investor who exercises patience and discipline and who takes the long-term perspective to investing.

Sources: MarketWatch article “Could it happen again?”, “The Ides of October”, “Fed Cuts Rates…”, “What Will send the U.S. into recession?”, “What Is A Recession?”, The Kiplinger Letter , 9/21/07 and 8/10/07 issues; Hays Advisory Morning Market Comments on “Sector Review”, American Funds Market Outlook 9/7/07, “Harvesting Profits on Wall Street” by Ron Muhlenkamp.

PROTECTING YOUR IDENTITY

We recently attended a conference at which a representative from the U.S. Postal Inspection Service spoke about safeguarding your personal information from identify theft. The following are suggestions and guidelines offered by the Service:

1) Instead of leaving your outgoing mail in your mailbox, deposit it at a Post Office, a blue U.S. Postal service collection box, or give it directly to your letter carrier.

2) Shred or tear up unwanted documents that contain personal information before discarding them.

3) Review your consumer credit reports annually.

4) Never give personal information over the phone or the Internet unless you initiated the contact.

5) Delete e-mails from those you don’t know. Never open file attachments from unsolicited e-mails as well.

6) Don’t carry your Social Security card or number with you.

7) Don't use your birth date as your password.

8) Sign your new credit cards as soon as you receive them. To take it a step further, we recommend not signing the card but notating "Ask for I.D." instead. That requires the cashier to match your driver's license to the name on the card you are presenting to insure it is your card.

9) Check expiration dates on credit cards and contact the issuer if you don't get a replacement before they expire. Ditto for monthly financial statements and bills.

10) Match credit card receipts against monthly bills and check financial statements for accuracy.

11) Never leave receipts behind—at the ATMs, on counters at financial institutions, or at retail centers or gas pumps.

12) Report lost or stolen credit or bank cards to the issuer immediately.

For further information on identity theft, the Postal Inspection Service suggests you visit these web sites: www.usps.com/postalinspectors; www.consumer.gov/idtheft; www.secretservice.gov.

F.Y.I.

- The National Association of Securities Dealers (formerly known as the NASD) merged with the New York Stock Exchange. The merger created FINRA, the Financial Regulatory Agency.

- There are tax benefits to executing a Direct Rollover from your employer-sponsored retirement plan (such as a 401(k), 403(b) or Savings Plan) when you leave an employer and change jobs. One of them is the ability to use the "stretch IRA". For the same reason, avoid naming a Trust as the beneficiary of an IRA, if possible.

- There are ways to draw on retirement accounts, such as your IRAs, before the age of 59-1/2 without incurring the penalty. One of those ways is by taking "72(t) distributions". Under section 72(t)(2)(A)(iv) of the IRS Code, distributions prior to age 59-1/2 will avoid the early withdrawal penalty if taken as part of substantially equal periodic payments. These payments are calculated using IRS tables and must last for at least five years or until you reach age 59-1/2 (whichever is later).

- In the event of a long-term illness of a spouse, annuities can offer protection to the non-confined spouse for spend-down purposes. In some instances, the annuity could be converted to income for the non-confined spouse thereby protecting the annuity, as an asset, for Medicaid qualification.

- If it's time to draw on your child's investment(s) for college expenses, which account do you spend first? If they have Coverdell or 529 accounts, you may want to cash out of the taxable assets first due to the recent change to the "kiddie tax" law. Starting in 2008, the kiddie tax age will be extended to include children under age 19 and full-time students under 24 whose earned income does not exceed one-half of their support. Under the kiddie tax, earnings are taxed at the parent's tax bracket instead of the child's, potentially resulting in higher taxes.

INVESTMENT CORNER

We are pleased to announce a new service that Horizon Financial Advisors is launching. The service is designed to provide investment advice to individuals who participate in an employer-sponsored retirement plan (such as a 401(k), 403(b), Thrift Savings, SEP or Simple IRA).

We are introducing this service because it is one that has often been requested by our clients and their co-workers and where we can fill a current void in the investment advice our clients require. For most individuals and families, the retirement plan at work is their largest asset but the one that gets the least amount of attention and professional advice.

Here's how the new service works. Every six months we will contact you to get a copy of your most recent statement or printout on your retirement plan at work. (We DO NOT ask that you give us on-line access to your account.) After reviewing your account, we will get back to you with recommendations regarding any potential changes that should be made to the investment allocation on the existing balance as well as your future contributions. We will respond to you via phone, mail or e-mail, whichever you prefer. In addition to an automatic review of the account every six months, we will also guide you through any changes in the plan that might occur, such as new investment choices being offered or the employer moving the plan to another custodian.

The annual fee for this service will be $150 to review one plan or $200 to review more than one. This is a nominal fee considering the importance of the asset. Let's say your 401(k) balance is $150,000. We feel that 0.10% per year is worth the professional advice or "second opinion".

Proper asset allocation and investment selection can significantly affect overall performance. Diversification is not enough to avoid risk. As professionals, we have access to data on many of the funds being offered in company-sponsored retirement plans — data that is not available to the employee. A common mistake made by investors is selecting investments based solely on past performance. As stated by Jim Rothenberg, Chairman of Capital Research and Management and Portfolio Counselor for several of the American Funds portfolios, you "shouldn't be buying today what you should have bought five years ago".

We are currently in the process of sending notices about the new service to our pre-retiree clients. To opt into the service, you will simply sign the advisory agreement that will be included with the letter and return it to us along with your check and a copy of the most recent statement or printout on your plan. We'll then review your account and get back to you within two weeks. We are also making this service available to those who are not existing clients. **If you have a co-worker, friend or family member that is in need of this service, please feel free to give them our name and contact information.**

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