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summaries

SIGMA INVESTMENT COUNSELORS

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As The Haze Clears

In forecasting circles, it is often said, "If you must forecast, forecast often!" The events of the past year bear out the wisdom of that adage. The epitaphs for 2008 have been many. Suffice to say that it was a difficult year from almost any perspective. Of course, it is important to study history for clues about how events may unfold in the future. That is the thrust of this letter - divining how 2009 may pan out - and using those clues to help us structure investment portfolios.

In previous newsletters, we commented on the housing bubble, the need for the consumer to deleverage, the slowing economy and the likely return of more rational pricing in the equity markets. What we, and many others, did not fully comprehend was the extent that financial institutions had overextended their balance sheets and employed very complex and difficult to understand financial instruments to magnify their financial leverage as a means to enhance their own profitability.

In 2008, this "house of cards" collapsed, negatively impacting homeowners, consumers, investors, financial institutions and the economy. The collateral damage is extensive and it will take some time before we can work ourselves out of the mess we are now in.

From an investing perspective, it should not be too surprising to note that few asset classes were left unscathed last year. For example, broad domestic stock indices saw price declines in the range of 30% to 40% and many international indices fell by an even greater amount. Many fixed income securities also posted substantial losses, as did commodities, real estate and other hard assets.

As we enter 2009, it is important to keep in mind that shortly, Barack Obama will be sworn in as the 44th President of the United States. As he takes office, President Obama will have a herculean task of dealing with a record budget deficit, rising unemployment, and stalled economy. Obama plans to tackle these issues with a massive stimulus plan aimed at creating more jobs and jolting our economy out of recession.

While we remain hopeful that President-elect Obama will be successful in achieving these lofty goals, it will take some time before the economy will benefit from these actions. During the interim, we are prepared for more bad news regarding the economy and unemployment. However, as the current state of affairs has been so broadly communicated in the press, the equity markets may have already factored much of this news into current prices. Thus, while we do not see a sustained market rally in the near term, we do not see the equity markets falling below the lows registered in the fall of 2008.

As we progress through 2009 and set our sights on 2010 and 2011, we believe the consumer will crawl out of his bunker and begin, ever so slowly, to resume more normal activities. While his purchasing power may be lower than before, we believe that the consumer is learning to adapt to the current economic environment. This should lead to an improvement in discretionary spending, albeit at a modest level. As spending increases, factories orders should be positively impacted and the economy should show signs of recovery. As the stock market is forward looking, stocks may show a sustained recovery in price well before economic statistics show up in the press.

Thus, we are actively seeking opportunities in which to invest. While we search for areas to deploy our capital, we are also reviewing our clients' financial plans, asset allocations and investment strategies to insure that our

portfolio management is reflective of the unique investment goals, time horizons and risk tolerances of our clients. Moreover, we recognize that investment goals and circumstances change over time and we wish to remain as current as possible with these changes.

Finally, we do not take lightly the loss of market value experienced by a majority of our clients in 2008. While volatility is to be expected when investing in equities and fixed income securities, the magnitude of the decline in 2008 will go into the record books as one of the worst years since the Great Depression. Yet, we appreciate the overwhelming show of trust and confidence that has been shown to us by our clients and we are grateful for the privilege to serve as their advisors.

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I would be remiss if I did not touch on the challenges in the financial regulatory landscape, both in the United States as well as around the globe, and the anticipated changes on the horizon. At Sigma Investment Counselors we abhor excess regulation as much as anyone given the impact on economic growth. However, we also recognize that frequent fraud and malfeasance destroys (has destroyed) confidence and it is only confidence that prompts investors to part with their capital so that it can be employed in productive ventures and in turn, serve to grow the economy.

To that end I have been involved in providing policy input through our professional organization, CFA Institute, and now have the privilege of serving as Chair of the Capital Markets Policy Committee for CFA Institute's Centre for Financial Market Integrity. CFA Institute is our professional association with over 100,000 members in 134 countries around the world. The organization has learned that it can be far more effective as advocates rather than lobbyists and has built a reputation with legislators and regulators worldwide as an advocate for the principles of fair, ethical and transparent markets for all investors. The committee I chair is comprised of a cross section of senior investment professionals from around the globe who are active in various areas of the capital markets. Our focus now is on assisting in the preparation of CFA Institute's positions and recommendations for the debate that is about to unfold. We are well positioned to provide input and contributions to the coming "legislative overhaul" President-elect Obama and his team have referenced in recent interviews. We are suggesting that the new regulatory framework be holistic and imbed the regulatory process that incorporates 21st century systems and disciplines to promulgate fair, ethical and transparent capital markets for all investors. In this regard, the U.S. now has the opportunity to take a leadership role within the global regulatory community to address the problems at hand and it is certainly expected that constituents at Sigma, our clients, will be well represented in this endeavor. In this regard we are hopeful that this crisis will prompt politicians and regulators to seize the opportunity to significantly enhance the foundation on which our capital markets are based.

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