



A Brief on Investment Markets and Financial Planning Issues

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2005: Walls of Worry and a Disappointing Finish Make for a Below-Average Year

It seemed like every day in 2005 brought continued negative thinking. Iraq, terrorism and partisan politics were daily fodder for the news media. Add a steady diet of angst about inflation, interest rates, jobs, trade balances, government deficits, the weather and there was a general mood of worry.

There is an old adage on Wall Street that says the stock market climbs a wall of worry. And indeed, it struggled to climb that wall in 2005.

The insight to be gained, if we are to be thinking people, is the reminder that we seem conditioned to overemphasize the negative to the point of delusion. Chicken Little is alive and well and always proclaiming the same fearful message about the sky's imminent demise. Dumb cluck.

I kept hearing and reading about a "bad economy" in 2005. I'm still looking for it.

The reality for 2005 was that the economy did remarkably well. The Fed policy seems to have worked in keeping inflation at bay. That coupled with significant buying of treasuries by foreign investors kept longer-term interest rates from rising precipitously. Productivity boomed, allowing millions of jobs to be created thereby lowering unemployment without undue inflationary pressure. Tax cuts did their job as stimulus for economic growth resulting in increased hard dollar revenues for the government. That's right: tax rates were reduced and government revenues increased.

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Walls of Worry: 2005 Commentary

2005 Market Performance

2006: Will the Bull Continue?

Three Best Things to Do, IRA Deposits, Debt management and Estate Planning

There are problems to be sure. But we need to be reminded of the human tendency to be negative. And the media feeds this tendency. Or is it the other way around? Whether the media causes more negativism or our negativism causes the media to reflect it is for philosophers and sociologists and theologians to debate.

My point is that it takes objectivity and effort to overcome the worry and see truth. And the truth is that things are not as bad as many would have us believe. I've been saying this as long as I can remember.

If we want to be successful in our finances and

2005 Market Performance

International Markets Lead Hesitant US

Benchmark Performance*	2005
MS Foreign Large Blend Funds	14.55%
EAFE International Index	13.54%
MS World Stock Funds	11.74%
Wilshire SmallCap 1750 Index	7.87%
S&P 500 Stock Index	4.91%
Russell 2000 Small Co. Index	4.55%
Taxable Money Market Funds	2.50%
Lehman Bros. Gov't/Cred Index.	2.37%
Dow Jones Industrials	1.72%
Lehman Bros. Interm Gov't/Cred Index	1.58%
MS Short Term Bd Fds	1.43%
NASDAQ	1.37%
Average of Above Benchmarks	5.68%
Inflation	3.84%

investing, we need to consciously be on the lookout for the good as well as the bad. Both, in balance, will give us perspective and a better chance to obtain wisdom.

As you can see from the Benchmark Performance Chart, the investment year turned out to be a modestly positive one. It would have been better except for a year-end fizzle. 2005 clearly illustrates my long-time promotion of investing globally. It was the overseas markets that turned in above-average performance.

On a TV show aired on January 1, 2005, I suggested the S&P 500 would have a modest year, probably around 5%, maybe as high as 8% or so. It turned out I was within a tenth of a percent.

The area on which I was way off was the bond market. I had expected long term interest rates to rise and therefore stayed with short-term maturities. Fortunately, I had advised most clients to lighten up on bonds anyway and increase exposure to stocks, especially International stocks.

In the end, a balanced and widely diversified portfolio should have produced a total return in the 5% - 6% range. This would be a starting point in evaluating your own performance.

2006 And Beyond: Will the Bull

Continue?

On January 1, 2006 I again offered my views on the economy and the markets on the same TV show. If you would like to view the clips, just enter the following Internet addresses into your browser:

PART One: A Look Back at 2005 Economic Predictions
<http://kdka.com/video/?id=12125@kdka.dayport.com>

PART Two: A Look Ahead to 2006 and Tips For Making Money in 2006
<http://kdka.com/video/?id=12126@kdka.dayport.com>

At this writing, the economy is continuing to grow and most stock indicators are positive. The first week of 2006 saw a strong rise in stocks. As of January 11 The EAFE index (International) was up 4.9%, the Russell 2000 (small companies) up 5.6% and the S&P 500 up 3.7%. The major leadership shift seems to be toward the NASDAQ, which was up 5.7%, which is ahead of the S&P 500 and the Russell 2000 after trailing them last year.

I would expect a breather after this strong surge, but our indicators still show a good bullish trend in place. I think the upside potential of the S&P 500 is 8%-10% from the beginning of the year. It could hit that during the year and then retreat, but overall I think there is a reasonably good probability that levels will be higher at some point in the year than they are now.

I expect International stocks to continue to lead. I expect large company stocks to catch up a bit to small company stocks, maybe even do better than smalls in 2006. It also looks like tech oriented stocks may take some leadership.

As we get closer to 2007 it would not be surprising to see the economy slow a bit. Yes, sooner or later there will be another recession and another bear market, but I hesitate to try to forecast it now.

Finally, I cannot ignore the possibility of a bad event or series of events reversing these trends. There is still that "wall of worry" and some of the worries are legitimate. There are always risks. Therefore, a realistic perspective and vigilance is essential to protect assets.

The Three Best Things to Do for Your Financial Health in 2006

1. Set Your Review Meeting Date. Making an appointment puts your finances at the forefront for both you and me. I have generally considered annual reviews to be among the most important services I provide. We are able to evaluate, clarify and make appropriate changes to maximize your potential for success. We look at everything and can discuss your investment portfolios, real estate, education, estate planning and any other issues that are important to you. (Note:

Private Management and "STAARBASE" clients receive priority in scheduling.)

2. Attend "The Five Assets You Should Own to Be Financially Independent" Presentation. The Goal: **Get your money in the way of the money that is coming!** (Pittsburgh, PA 7:15 PM February 9. Ft. Lauderdale/Hollywood/ Miami, FL 7:30 PM Feb. 2) **Call 412-367-9076 for reservations and details.**

3. Spend less than you make and add to your assets on a regular basis.

Planning Corner

Still Need Deductions for 2005?

Traditional IRA contributions can be made until April 15. Maximum 2005 limits are \$4,000 per individual, \$4,500 if you are age 50 or older. SEP (Simplified Employee Pensions) also allow for contributions after year-end. Subject to income limits -- Consult your tax accountant or tax attorney.

Debt Management

Avoid consumer debt like the plague. Consumer debt is credit card debt, revolving consumer accounts, car loans and similar loans for purchase of items that depreciate in value or consumption that has no value after the service is completed, i.e. vacations.

Productive debt, i.e. mortgages and business financing, should be structured for maximum efficiency and flexibility. I define productive debt as the financing of appreciating assets. Lock in longer periods when interest rates are low. Generally use lenders that have no prepayment penalties. Make extra payments to principal when your cash flow is good.

Estate Planning

Make sure you have addressed the essentials with your attorney. Is your basic will up to date? Is a "living trust" appropriate? Do you have Powers of Attorney executed so that your affairs and decisions, including those for health care, can be made if you are incapacitated? Do you have a living will? Do you have the right amounts and types of life insurance? Are your beneficiary designations for insurance and retirement plans correct? Have you written an informal letter of instruction and testament, saying the things you wish to impart to your loved ones?

"The Five Assets You Should Own to Be Financially Independent": Ft. Lauderdale-Miami February 2. Pittsburgh February 9. Call 412-367-9076 for details and reservations.