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The past does not repeat itself, but it rhymes. ~ Mark Twain

State of the Market

Given the precipitous drop in stocks this year, investors and clients are wondering if we're at or near the bottom. I would usually have written this newsletter a month ago and included everyone's year to date returns. However, October became so brutally ugly, so fast, that I decided instead to write after month's end and include 10/31 returns. The following points represent my view of where the markets stand currently:

The S&P 500 has dropped 46% from its peak in October 2007 to its 10/27 low point; 34% from 12/31 to 10/31. This is in line with the worst bear markets going back sixty years. Based on historical perspective, we would expect the worst to be over. Still, while history offers guidance, it offers no assurances.

Stocks have reached levels that offer real value, given current and future earnings expectations. This means that today's prices should translate to good returns for patient investors. If and as prices drop further, stocks only become more attractive long term investments.

Unfortunately, a fair or compelling valuation does not mean that the market will not make further lows. In a bear market, final lows are not reached until the desire to sell has been thoroughly exhausted, usually through emotional, panic selling. We won't know it's over until we observe broad, enthusiastic buying. The bottoming process could continue for months. We could see further declines, a frustrating sideways pattern or the bottom could have been reached already. The markets may also be awaiting further clarity on the Obama presidency.

Aggressive accounts have been partly in cash since summer (moderate and conservative accounts proportionately more), meaning we have not borne 100% of the decline. My plan is to return to fully invested as the market statistics begin to show the enthusiastic buying typical of a new bull market cycle.

Future Plan

I believe that the mainstream market averages and stocks may offer mediocre returns in the next bull market cycle. I don't anticipate a rah-rah bull market where every stock tip makes money and everyone is an expert. We can look to past periods where the market averages made very little money for years – such as 1968 to 1982. Just the same, during those periods, there were selected industry sectors and regions which made healthy gains. I am optimistic that

Kay Investments' active, targeted strategies will prove profitable during the next bull market cycle. I am already looking ahead to sectors that may outperform, such as energy services, infrastructure, certain foreign regions, medical equipment and yes, financial and banking.

If you would like to discuss your risk orientation or investment model, please contact me by reply email or phone. I will be publishing 10/31 year to date returns very soon.

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