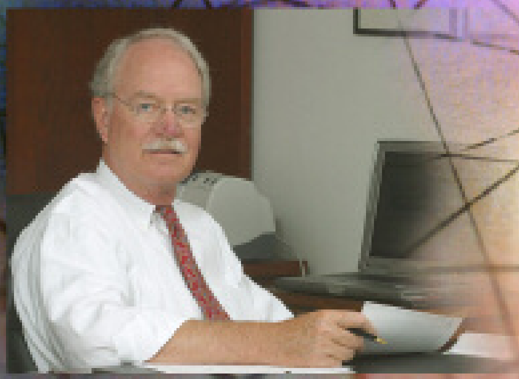

# Soaring

The eagle's perspective on wealth management

Joseph M. "Jette" Browne, CFP®

July 2008

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## Sometimes the best offense is a good defense

In the last NFL Super Bowl, the underdog New York Giants came from behind to upset the heavily favored New England Patriots in the final minutes of the game. Most of the football experts credit the Giants defense with winning the game because they were able to keep relentless pressure on Patriots quarterback Tom Brady and keep him from running up an insurmountable score. By keeping the game close with their pressure defense, the Giants were able to pull off a major upset with one excellent drive late in the game.

Defense is also extremely important for us as investors. During a long broad bull market like the one we had from 1982 to early 2000, it was easy to undervalue defensive investment strategy because almost all stocks were consistently going up in price and everyone seemed to be an investment genius. With the severe market pull back in the early years of this decade, however, those folks who played good defense tended to come out just fine. Since last October, the stock market has again been correcting strongly with a pull back of about 20 percent from the high point. This is the level of pull back that's usually referred to as a bear market.

Successful investors over the full market cycle, both up and down, tend to be those who play good defense when a market is in a correction like the one we've been experiencing of late.

I like to tell folks that the best money you make in the market is the money you don't lose during a correction and the math really bears this out (no pun intended). For example, if your portfolio drops by 10 percent, you only have to earn a return of 11 percent to get even. If, however, your portfolio drops by 50 percent, you need to double your money from there just to get even. That's pretty hard to do.

So the defensive strategy is really pretty simple – take small losses, if you must, but avoid large losses entirely. This is emotionally difficult to do for many folks and I think the reason is that people usually hate to admit that they made a mistake, so they want to hold on to their losers, hoping a losing position will turn around and recover its losses. Selling losers early, however, preserves capital and positions the portfolio to better deploy that capital into more productive opportunities as they arise.

Here's how I handle the emotional aspect of this strategy. I expect to make mistakes! That way, when a stock we own drops in price on heavy volume, I know that some big investors with better information than I have are bailing out and we aren't going to wait and try to figure out why, we just cut the loss and move on. Occasionally, a stock will rebound just after we've sold it. This doesn't feel very good. On the other hand, many times the stock we sold continues to decline and we're very thankful to be done with it.

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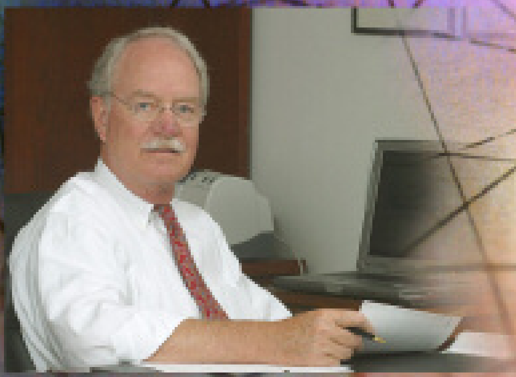
*"Experience is that marvelous thing that enables you to recognize a mistake when you make it again."*

Franklin P. Jones



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A specific example of this was Garmin, the company that makes portable GPS navigation systems. This had been a very profitable stock in many of our portfolios throughout 2006 and early 2007. In early October, however, it pulled back from $120 a share to just under $100 a share on fairly heavy volume. We, therefore, sold the stock at $95 and moved on. Subsequently, Garmin's stock rallied back to almost $120 – Ouch! Then it declined again and currently trades around $42 a share – Whew!

Sticking with this very simple sell discipline has gotten us all out of the real estate sector in early 2006 and out of the financial sector in early 2007. This has helped our portfolios weather the current storm pretty nicely. We have also raised a lot of cash which helps steady the ship in these rough waters and is the dry powder we'll use when the opportunities are right.

Bear markets are famous for sucker rallies and we had one of those this spring. Because the market volume was pretty weak as the indexes rose this spring, we stayed pretty much on the sideline, except with selected energy related companies. When the savage recorrection occurred in June, we did just fine.

Eternal vigilance, however, is still the hallmark of victory and we must assess the investment landscape every day to make sure we're in the best posture, not only to minimize losses, but also to take advantage of true opportunities when they arise. We expect to be a little late on seizing these opportunities so as to minimize the chances of being sucked into a trap. It's the second mouse that usually gets the cheese, so we want to see compelling evidence of an opportunity before we pull the trigger.

Currently the clouds are numerous and dark and the winds are howling. We're staying pretty close to the storm cellar with Dorothy, Toto and Auntie Em. We know, however, that the sun will shine again in Kansas after the storms and we'll be well positioned to move on out to the yellow brick road.

Warm Regards

Jette

Jette

*"What makes the flag on the mast to wave... What makes the dawn come up like thunder? Courage!"*

Cowardly Lion
*The Wizard of Oz*