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A WEALTH ADVISORY NEWSLETTER FROM HTG INVESTMENT ADVISORS

INVESTING IN A *Changing World*

As the world's dominant economic power, the US has conducted its economic affairs as if its citizens had inalienable rights to increase their standard of living indefinitely. But, the world is changing. Advances in global transportation, communications, trade, education, productivity, governance, and numerous other factors are producing a major shift toward a more economically balanced world. The US is no longer the sole dominant economic power, nor is it the primary source of global economic growth.

As the inevitable global competition for jobs and resources threatens our standard of living, the private sector, encouraged by our government, has prolonged the day of reckoning by taking on ever-increasing amounts of debt. Thus began an astonishing chain of events leading to the disappearance of several venerable financial firms, a freezing of liquidity in the US financial system, and extraordinary actions on the part of the US government in attempts to avert a major meltdown of the banking system.

As long-term investors, it behooves us to envision the future world order as a guide to determining our current investment strategies, especially in times of near-term dislocations. Mohamed El-Erian – the former head of investments at the Harvard endowment and now Co-Chief Investment Officer at bond giant PIMCO – in his recent book, *When Markets Collide – Investment Strategies for the Age of Global Economic Change,* suggests that the global economy is headed toward a destination involving several consequential changes for investors: First, emerging markets will be a primary driver for global growth; second, emerging markets will evolve away from reliance on exports toward internal consumption; third, this evolution will increase demand for US products and services (thereby helping the US economy become less dependent on debt-financed consumption) and will result in less vulnerability in the global economy; fourth, global inflation is likely to increase because of competition for natural resources and the gradual reduction in availability of lower-cost labor in emerging markets; and fifth, global allocation of capital will be influenced greatly by the tremendous growth of foreign sovereign wealth funds (country-owned investment funds).

If appropriate policy decisions are made, El-Erian envisions a period of global economic change resulting in high global growth, declining world poverty, and relative financial stability. However, he expects an extended "rather bumpy road" for investors during the journey.

El-Erian provides an "Action Plan for Investors" that is not unlike our approach at HTG. He cites the three basic steps of portfolio management as asset allocation, selection of

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SURVIVING *a Financial Crisis*

Are you wondering whether the drumbeat of negative news about the financial crisis will ever end, whether the stock market will ever recover, or whether you should put your assets under your mattress? We believe, that in times like these, it is helpful to reflect on the lessons of history and on basic investment principles.

UNCERTAINTY IS THE RULE, NOT THE EXCEPTION

While most investors desire less volatility and more certainty, uncertainty is the driver of above-average performance. If we knew what the future would hold, which companies would outperform others, and how strong the economy would be, prices would be bid up to a level that would provide low future returns. Over the last two decades, investors have dealt with a myriad of uncertainties, including the bursting of the tech bubble, Asian and Russian financial crises, corporate scandals and geo-political turmoil in the Middle East. Through all of this, the S&P 500 index rose 10%/yr for the past 20 years. But, it did so with great variability, up 48% during a 12 month period in 1998 and down 26% in 2001.

Uncertainty is the rule, not the exception.

FOCUS ON WHAT IS IMPORTANT AND KNOWABLE

A famous fund manager once said, *"If we accept that investing through uncertain times is the rule, not the exception, then the question to ask in my opinion is not whether or when to invest, but how to invest…."*[1] Instead of trying to predict the direction of the economy, interest rates, or oil and stock prices, which are all important but not knowable, we advise focusing your efforts on identifying proven managers who manage in a risk conscious fashion, who keep investment costs low and who have unique skills and strategies. In addition, your time may be better spent finding investment areas which may benefit from, or which may mute, the effects of a downturn, such as real estate, commodities, fixed income and hedge funds.

SET REALISTIC EXPECTATIONS AND TIME FRAMES

Most investors know that stocks beat bonds by a large margin (+/-5%/yr) over the long haul. Well-diversified investors have about a 1 in 4 chance of losing money in the stock market over any 12 month period. That chance declines to less than 1 in 20 when your time frame expands to 5 years. With a 10 year time frame, the odds of losing money are almost zero. Therefore, it is imperative that there is a clear connection between your investments and the timing of your consumption of those investments.

PRACTICE HEALTHY INVESTOR BEHAVIOR AND DEVELOP A PLAN

Investing is an emotional experience. Any investor feels less confident when prices are down and more confident when they are up. This behavior can lead to investing in areas of the market that have recently risen (*buying high*) and removing capital from areas which are down (*selling low*) – exactly the wrong strategy. The key to developing a counter-emotional strategy is to have an investment policy grounded in facts and logic, rather than emotion. Employing such a disciplined approach will go a long way to avoiding detrimental changes in the face of downturns. Without a plan, a common reaction to a loss is to search for safety or the most recent hot investment trend. The tendency of investors to switch stock funds at the wrong moment was documented in the 2007 Dalbar study which showed that, while the average stock fund earned 11.3%/yr from 1987 to 2005, the average investor earned only 4.3%/yr.

SAFETY ISN'T ALWAYS WHERE YOU THINK IT IS…

As emotions take over, investors naturally flee to safety. But what is safe? While it may feel good to stop the declines in the short-run, investors who need to build assets for the long-run, or for retirement, will be sadly disappointed by ultra-safe investments. Consider the performance of a top, low-cost money market fund over the past 5 years. It earned 3.23%/yr, while inflation was 3.5%. Was it safe? A moderately allocated portfolio earned 6.35%/yr over the same time period.

CALL YOUR ADVISOR

As you wrestle with the challenges of the current crisis, we recommend you call your advisor to discuss your concerns. ◆ **10/07/08**

[1] Shelby Davis, Davis Investors

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...Changing World

implementation vehicles, and risk management. Then, he emphasizes the importance of disciplined asset allocation, suggesting that investors should ask themselves "How would you allocate your capital among different asset classes if you knew you were going to go away for three years?" He does not mean that the allocation should not be changed along the way if circumstances change, rather that a sound plan can provide a target beyond the impact of day-to-day events.

Many of El-Erian's views regarding particular asset classes also are similar to our own. His principal conclusions regarding key asset classes include:

(1) The portfolio should be exposed to a globally diversified set of equities. It is especially important to avoid too much of a home bias; that is, the equity portfolio should not be dominated by stock from one's home country.

(2) Expect continued pressure on the US dollar because of our unfavorable trade balance, a global trend to diversify away from dollar dominance, and a greater inclination of Asian countries to appreciate their own currencies as their economies grow.

(3) Higher inflation will make "real assets" increasingly important and underexposure could be consequential. He includes inflation protected bonds, commodities, and real estate as real assets that provide strong protection against inflation.

(4) Bonds will underperform under his projected themes of robust global growth, higher inflation, and reduced holdings of bonds by sovereign wealth funds. Therefore, bonds should be viewed primarily as an important risk mitigation tool, not as a source of strong investment returns.

The current financial crisis is likely to be but one of several major dislocations that investors face as the world transitions from US economic dominance to a more balanced global economy. As investors struggle through these disruptive periods, we need to maintain our bearings by setting our sights not on the world as it is or as it was, but as it will be. ◆ 10/07/08

IS A HEALTH SAVINGS ACCOUNT RIGHT FOR YOU

The Health Savings Account (HSA) was created in 2003 as an alternative to traditional health insurance. It provides a tax-advantaged way to pay for qualified health expenses and to save for future medical expenses on a tax-free basis.

In order to take advantage of an HSA, you must be covered by a High Deductible Health Plan (HDHP). An HDHP is an insurance plan that charges a lower monthly premium and requires a higher deductible ($1,100 to $10,000).

WHO CAN ESTABLISH AN HSA?

Any adult can have an HSA if they have coverage under an HSA-qualified HDHP and:

- Have no other low deductible medical coverage
- Are not enrolled in Medicare
- Cannot be claimed as a dependent on someone else's tax return.

HOW DO I GET STARTED?

The first step is to obtain an HDHP. To qualify as an HDHP the minimum deductible is $1,100 for individual coverage, and $2,200 for family coverage. A list of health insurance companies that offer HSA-eligible HDHP plans by state can be found at HSAInsider.com or HSADecisions.org. The HSA account is opened through a financial institution as early as the first day of the month that follows the effective date of your HDHP policy.

WHAT ARE THE 2008 HSA CONTRIBUTION LIMITS?

For 2008, an individual can contribute up to $2,900 to the HSA and a family can contribute $5,800. Contributions can be made monthly, or you can make a lump-sum contribution any time before your tax return is due. Catch-up contributions of $900 (for 2008) are available to those over 55. Contributions provide an "above-the line" tax deduction, thereby reducing your taxable income by the amount you contribute to your HSA. You do not have to itemize your deductions to realize this benefit. Employers may also make contributions to an HSA on behalf of the employee; the contributed amounts are excludable from the employee's gross income.

DO MY CONTRIBUTIONS EARN A RETURN?

Yes. You can direct your contributions to a savings or investment option offered by your HSA account provider. Any interest and investment earnings on contributions grow tax-deferred until withdrawn and, like contributions, will be tax-free when withdrawn if used to pay qualified medical expenses.

HOW DO I USE MY HSA?

You can withdraw money from your HSA on a tax-free basis to pay for qualified medical expenses for your family and yourself. However, distributions for nonqualified expenses are considered taxable income and are subject to an additional 10 percent penalty.

Qualified medical expenses include most medical care and services, ambulance service, dental and vision care, laboratory fees, and prescription and nonprescription drugs. Expenses do not have to be covered by your HDHP to be qualified with respect to the HSA account.

DO I HAVE TO USE THE CONTRIBUTIONS TO MY HSA TO PAY FOR MY CURRENT EXPENSES?

Unlike a flexible spending account, HSAs do not have a "use it or lose it" provision, meaning that funds remaining in your account at the end of the year are not forfeited and will continue to accumulate tax-free until withdrawn. In fact, some participants choose to pay all their medical expenses out of pocket, allowing the funds in their HSA to grow tax-deferred.

If you need to withdraw money from your HSA for a non-medical purpose, there is a 10 percent penalty, plus the income tax due. After age 65, medical expenses paid with HSA funds will continue to be tax-free and non-medical withdrawals will be taxable with no 10% penalty.

Tax savings, affordability, flexibility, control, and portability are among the many advantages of a Health Savings Account. **To learn more, contact HTG Investment Advisors or logon to www.treas.gov and click on Health Savings Accounts.**

HTG news

- For the second year in a row, HTG Investment Advisors Inc. has been named in Wealth Manager Magazine's eighth Annual Compendium of Top Advisory Firms. To be considered for top Wealth Manager ranking, firms must be registered investment advisors who offer both investment and financial planning services.
- Robin Sherwood and Barbara Ollinger recently attended the Financial Planning Association's annual industry conference on Technology Trends for 2008 and Beyond.
- Barbara's daughter, Heather Stephens, is a freshman at Syracuse University. Heather will run cross country and track for the Orange.
- Jeanne Gnuse sang Carmine Barana at Carnegie Hall on June 14 with the Mendelssohn Choir of Connecticut. She also sang a premiere of Mack Wilburn's Requiem under the baton of Craig Jessop, a former conductor of the Mormon Tabernacle Choir.
- Tom and Jeanne's son John Gnuse has been named a Managing Director at Lazard. John is an investment banker in Lazard's San Francisco office.
- Susannah Hansley's daughter, Megan, qualified to swim with the United States Junior National Synchronized Swim Team. In August, the team competed in the Junior Olympics in St. Petersburg, Russia.
- Tom and Jeanne recently visited the ancient Greek city of Delphi. At the Temple of the Oracle of Delphi, Tom inquired as to whether the Oracle had any timeless investment advice from more than 2500 years ago. The guide pointed out an inscription on the entrance to the Temple. Loosely translated, it read "know thyself" and "nothing in excess". We see this as a clear admonition to have a personal investment plan and to diversify broadly.

CELEBRATE WITH HTG

HTG's 15th anniversary appreciation dinners will be held on:

Wednesday, November 5, 2008 at the Harvard Club of New York City

and on

Tuesday, November 11, 2008 at the Maritime Center in Norwalk, CT

All who have supported us in this venture are invited.

Contact Susannah at 203-972-8262 for detail and reservations.

We would be happy to add family members or friends to our newsletter mailing list. Please call or email Susannah at (203) 972-8262 or susannah@htgadvisors.com. Also, if you're interested in receiving your newsletter by email, please let us know.

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