

# 3<sup>rd</sup> QUARTER 2007

## Stocks Reach New Highs!

*U.S. and international stocks hit all-time highs early in the quarter, then dropped over 10%, and then posted a spectacular recovery in September - ending the quarter just below record levels. This marks our 5<sup>th</sup> consecutive quarter of positive stock gains. More importantly, we are now expecting strong 4<sup>th</sup> quarter stock gains and should easily exceed our beginning of the year forecast of 9.5%.*

### INVESTMENT REPORT

It was a volatile quarter to say the least! Continued strong earnings propelled stocks to record highs in early July. Then the credit crunch sent the market down over 10% with the usual media hype predicting the end of the world. However, when the actual depth of the subprime problem was examined, the markets shrugged off the bad news (and \$84 per barrel oil!), and resumed the bull market climb. Small company stocks, as measured by the Russell 2000, posted the only losses for the quarter. One-year CD and money market interest rates remained near or above 5%, while YTD bond returns languished in the 3.9% range. Inflation held steady at 2.3%.

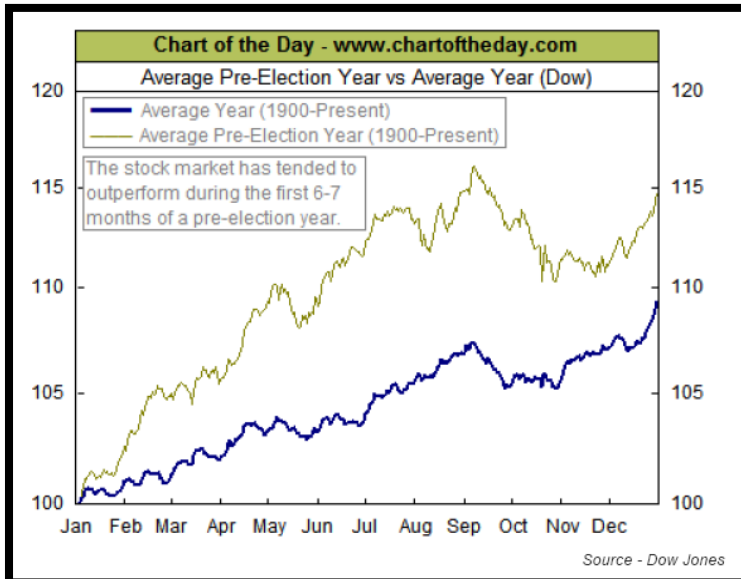
	<u>3<sup>rd</sup> Qtr. 2007</u>	<u>YTD</u>	<u>5-Year Annualized</u>
Dow 30	+4.2%	+13.3%	+15.5%
S&P 500	+2.0%	+ 9.0%	+15.4%
Nasdaq	+3.8%	+11.8%	+18.2%
Russell 2000	- 3.0%	+ 3.2%	+18.8%
MSCI EAFE (International)	+1.7%	+10.9%	+20.7%
Lehman Aggregate (Bonds)	+2.8%	+ 3.9%	+ 4.1%

### MID-QUARTER MARKET CORRECTION CREATES OPPORTUNITY

The 10% stock market correction that occurred mid-quarter created a unique opportunity to buy stocks at beginning-of-the-year prices. Accordingly, we increased our stock holdings at a low point, experiencing significant gains by the end of the quarter (remember- buy low, sell high). **As we anticipate double-digit stock gains this year, you may expect that your taxable gains will be higher than normal. For taxable accounts, we try to minimize tax impacts. If you need taxable gains to off-set accumulated capital losses, please let us know as soon as possible.**

## SAM OUTLOOK & STRATEGY

Strong global economic growth based on solid fundamentals should continue to drive stock performance through the end of this year and well into next year. From a historical standpoint, the up-coming presidential election year may also give the stock market a boost, as seen from this chart.



Near the beginning of the 4<sup>th</sup> quarter, we anticipate making some strategic adjustments to our models as we shift some sectors of our portfolios to areas of greater profit potential. We still see no negative factors on the horizon that could contribute to a prolonged, major stock market decline. As we have said before, the two most prominent factors that warn of a coming bear market, poor economic fundamentals and investor euphoric sentiment, are not present in the current market environment.

**REAL ESTATE:** Housing and the subprime loan situation continue to be a concern, with real estate prices likely to slide even further. While this will slow U.S. economic growth, we do not expect a recession or depression.

**BOND & CASH STRATEGY:** With interest rates near historic lows and short-term CD and money market rates near or above the 5% range, buying or holding traditional bonds or annuities of any type makes no sense. When interest rates rise, bonds will lose money and annuity payments will be lower than bank returns.

**LONG TERM CONCERNS:** As we look forward to the next decade (Wow, only two years away!), we will be monitoring a few key areas of concern. As Fed Chairman Ben Bernanke stated last week, our continuing trade deficit cannot continue. Add to that our horrific deficit spending, and we could be headed for difficult economic times by the middle of the next decade. Today, we see the U.S. dollar at record low levels against several major world currencies. Our continued unbridled government spending will exacerbate this situation.

We have already taken one major step to keep the value of our clients' investments intact. Currently, one third or more of our clients' funds are invested either directly or indirectly in non-dollar denominated investments. We will diligently monitor this situation and will endeavor to take the appropriate steps to preserve the buying power of the investment funds which you have entrusted to our care.

## YEAR END PLANNING

*It's Less Than 90 Days To Year-End! Time to start thinking about...*

- **Tax planning:** Schedule an appointment with your CPA or tax preparer
- **IRA and retirement plan contributions:** Be sure to fund by the IRS deadlines
- **RMD's (Required Minimum Distributions):** Charles Schwab will notify clients who are 70½ or older in 2007 of their Required Minimum Distribution (RMD) from all types of IRA accounts. The RMD must be taken this year in order to avoid severe penalties, and can be taken in periodic payments or in a lump sum. If you have any taxable account with us, we can arrange to have the RMD amount directly transferred from your IRA to your personal account- no hassle! Just call our office at 658-5193, toll-free 1-877-658-5193.
- **Gifting:** There are major advantages in donating appreciated securities instead of cash. When you donate an appreciated security, you don't have to pay capital gains tax on the gain, and generally, you get a tax deduction for the full value of the security on the day it is donated. Giving appreciated securities instead of cash can save you hundreds or even thousands of dollars versus a cash gift. See your tax preparer to find out if you should take advantage of this unique way of giving.

**HOLIDAYS:** 'Twill soon be the time of many holidays. We will be closed for Thanksgiving on Thursday & Friday, November 22<sup>nd</sup> & 23<sup>rd</sup>; for Christmas Eve & Christmas Day on Monday, December 24<sup>th</sup> & 25<sup>th</sup> and for New Years Day on Tuesday, January 1st. **Our office will be open on Monday, December 31<sup>st</sup> until the markets close at 1:00 pm.**

**Sierra Asset Management ended the 3<sup>rd</sup> quarter of 2007 with a record \$89 million in assets under management, up \$20 million from one year ago. We sincerely appreciate your continued trust and the many wonderful referrals this year. If you know of someone who you think could benefit from our service, please give us a call toll-free at 877-658-5193 and we will mail a company brochure for you to give them.**