STAAR℠ Strategies Report

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A Monthly Brief on Investment Markets and Financial Planning Issues
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10/1/02 Market Comments

Prepare Thyself!

It isn't pretty. Prepare yourself for discouraging quarterly statements from your brokerage firms, mutual funds and retirement plans. Here's the scorecard:

Index	Third Quarter Return	Year To Date
S&P500 Index	-18%	-29%
Dow Jones Industrial Avg.	-18%	-24%
NASDAQ	-20%	-40%
Russell 2000 (Small Companies)	-22%	-25%
EAFE (International)	-20%	-22%
Lipper Corporate A Rated Bonds	+ 5%	+ 4%
Lipper US Gov. Bonds	+ 5%	+ 9%
3 Month T-Bill	+ 0.4%	+ 1%

Now that you are prepared for your statements, prepare yourself for the probability of a better market. The longer we go, the closer we are to the next upturn. There are three general scenarios that I can see for the next quarter and next year.

Scenario #1: WORST CASE: The markets slide even further, consumers pull back their spending and so do businesses. The war on terrorism stalls with either no action on IRAQ or a war that does not go well at the beginning. In this case we would slide back into recession. Stocks would suffer, moving another notch or two downward or moving sideways. While a scenario like this is possible, I think it is not very probable. A depression with deflation would be even less likely, but possible.

Scenario #2: BEST CASE: The market finds bottom near DOW 7500 (it's current level is 7592). Businesses increase their spending and consumers hang in there. If there is a war, it becomes apparent early on that we are winning and that it will not drag on. By November positive economic and business news overshadows negative news. The country's general psychology turns from pessimistic to optimistic. Money would flow back into stocks and the market would rise 50% or more within three to six months. I think this to be a bit more probable than #1, but not much.

Scenario #3: SOMEWHERE IN BETWEEN: The markets either bottom out near 7500 or no lower than 7000. Business news improves, consumers hang in there and the war on terrorism brings some resolution with IRAQ. The DOW reaches 9000 or better by the end of the year (up between 15% and 20%). 2003 sees reasonable economic growth and a more tame, but orderly market closer to historical returns, i.e. 10% annualized. I think this scenario has the higher probability.

If you are significantly concerned that we are heading for Scenario #1, you may want to decrease your stock holdings and increase intermediate bonds or cash.

If you think Scenarios #2 and #3 are where we are headed, stick with your long-term asset allocation or even increase your stock holdings.

If you have a large amount of new money, i.e. a lump sum distribution, dollar-cost-averaging would make sense. This is where you put an equal dollar amount into stock funds on a weekly, bi-weekly or monthly basis. That way you participate if the market goes up but spread out your risk if the market continues to slide.