



## Baltimore Capital Management

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### SAMPLE CLIENT LETTER

Dear Client

During 2008, your account has had a gain/loss of xxxx . This compares to a decline in the S&P 500 of 37%. Most of our accounts did better than the S&P and the NASDAQ decline of 40%. We also outperformed most foreign markets by a wide margin. Outperforming a lousy market is small comfort, however, and losing money is not something we take at all lightly. We are very disappointed with our absolute returns.

There is not much question that the 37% decline of the S&P 500 made 2008 one of the worst years I have seen in my 28 years in the investment business, although it is certainly not the first or only period of poor market performance. From January 1973 to December 1974 the Dow declined 45%, followed by a 39% increase the subsequent year. During the tech debacle from 2000 to 2002, the Dow declined 32% over a two-year period, followed by a gain of 30% the next year. You may also remember the 1987 crash, in which the decline was fast but not as deep, and ended within a quarter of a year. 2008 has topped them all.

The worst thing about 2008 is that there were few places to hide, other than cash or gold, which eked out a 4% gain for the year. Even municipal bonds declined 5%. Many categories of corporate bonds did much worse. And as bad as the US markets were last year, most foreign markets did even less well. Europe did worse than the US. Japan had a decline of 42%. Emerging stock markets had an even poorer performance.

If at the start of 2008 someone had told me that Bear Sterns, Lehman Brothers, Wachovia Bank and Washington Mutual would be gone within 12 months, I would have called it impossible. The fact that it actually happened demonstrates how difficult it was to predict anything correctly in the past year.

It was not just equities that did poorly in 2008. Oil started the year at \$96, got as high as \$150, and ended the year at \$44, with that final price boosted by a 14% gain on the last day of trading. Sadly, this volatility was not limited to oil. It was prevalent in all commodities and stock markets.

So now that 2008 is behind us, what can we look forward to? As noted above, big down years are usually followed by big up years. The well-regarded market strategist Vince Farrell recently pointed out that the 10 worst stock market years have been followed by five-year annualized

returns of 11%. There is now more cash on the sidelines than there has been in two decades. Cash in banks and money funds currently equals 74% of the market value of US companies. Since cash, at least short term government paper, yields 0%, it is only a question of when investors will decide to take more risk. That, combined with our seeing more attractive investments than we have in years, makes us feel guardedly optimistic about 2009.

While risks in the economy certainly remain, it appears that the market lows may have been reached in November and that poor economic conditions are already discounted by the stock markets' current low valuation and high dividend yields. Dividends exceed the current yield on 10-year government bonds for the first time since 1954. I can't remember a time when I have seen so many attractive income investments, be they dividend-paying stocks, preferred stocks, corporate bonds or REITS.

So, while there is always a risk that things can get worse before they get better, history and valuations are on the side of those who choose not to sit on short-term cash investments. While citizens may be opposed to some or even all of the government actions to address the economic situation, the odds are that some of those actions will help stabilize the real estate market, which has been a source of many of our problems. Of course, someone will have to pay for all the government support, which means more inflation and a weak dollar. Consequently, we will continue to hold gold and foreign equities as a hedge.

One might argue that although they certainly didn't cause the problem, the media and in particular CNBC helped talk us into a recession. Hopefully, reasoned analysis will move the media personalities to project some confidence going forward, but frankly they tend to just follow the latest short-term trend. Of concern too is a present generation of investors who have never made money in the stock market, and may be unwilling or unable to take the long view. They will return, but it will take time.

We are cautiously optimistic about 2009. We thank you for your patience and feel strongly that with time it will be rewarded.

Sincerely,

Alec Graham

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- If you wish to receive all your statements from BCM via email in the future, please notify us either by phone 410-727-4480 or via email: [sandrarossner@baltimorecapital.com](mailto:sandrarossner@baltimorecapital.com)

*Upon written request, we will deliver a copy of our Part II of the form ADV and a balance sheet.*