Quarter Notes

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April 2008 | Second Quarter 2008 | Volume 16 No 1

In this Issue

- Market Summary
- Strategic Changes
- Fed Response to Slowdown
- Client Update Notes

Fed Actions
The Fed has now cut interest rates six times since September, most recently lowering rates to 2.25%. While the Fed has been dropping rates to stimulate our economy, the dollar has dropped in value against the world's currencies. The dollar has fallen 11% against the Euro and 14% against the Yen since the beginning of the year.

Oil and Gold
Since both oil and gold are priced in dollars, both commodities have increased in price; oil is up 34% and gold has risen 40%.

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Fed Moves Quickly to Soften Expected Recession

Queasy yet? The markets have been weak, rocky, and downright unsettling since the end of last year. The most challenging part is not the level of market decline. After all, we have seen worse: a 50% decline at the beginning of the decade. The difficulty lies in assessing the risk to the economy and to investor confidence in a time of a severe credit crisis. As is true in all bear markets, rational market analysis is the source of long-term confidence but offers no short-term assurances. Markets are at times driven more by emotion than by economic fundamentals, and in bear markets the predominant emotion is fear.

The Dow suffered its worst quarter since 2002 losing 7.6%. The S&P 500 index fell 9.9%. The NASDAQ composite index retreated 14.1%. The Russell 2000 index of smaller companies, lost 10.2%. International stocks fared little better, falling 9.5%. With a flight to quality bonds, 10-year Treasuries finished the quarter with a yield of 3.43%, and a total return of 5.95%

Index	3/31//2008	% YTD
Dow Jones Ind.	12262.9	-7.6%
S&P 500 Index	1322.7	-9.9%
Nasdaq Comp.	2279.1	-14.1%
Russell 2000	687.97	-10.2%
MSCI EAFE	2038.6	-9.5%
10 Year Treasury	3.43%	5.9%

Fed Responds Decisively to Credit Crisis

The Federal Reserve Bank has responded decisively to the credit crises, which began last summer with problems in the sub-prime markets. In order to increase liquidity and ensure the continued functioning of the financial markets, the Fed has cut the discount rate and the Fed funds rate (the interest rate banks are charged for borrowing from each other and from the Fed). Additionally, the Fed has expanded the types of securities that can be used as collateral for Fed loans. In a precedent-setting move, the Fed also extended loans and loan guarantees to investment banks, and orchestrated a takeover of Bear Stearns, which had been on the brink of insolvency.

(Continued Page 2 Column 2)

Evolution of Our Tactical Strategies

Looking at today's investment world, we have identified many new opportunities to add to our asset allocation palette. Because we forecast lower than average stock and bond market returns, the investments in the category we call "tactical" have assumed a more important role in portfolio development, allowing us to better manage risk and expected return. We have incorporated tactical investments in our portfolios for more than a dozen years, because they provide clients with positions that have low correlations with the traditional stock and bond markets.

Low correlation simply means that the investment doesn't behave in sync with the overall markets. Investments with low correlations benefit portfolios through diversification and risk reduction. Historically, international stocks and bonds have provided us with lower-correlated investments. However, the recent globalization of the world's economies has caused correlations on international holdings to rise.

Real estate was our first tactical investment. We held it as a separate asset class. When we formally added tactical as a

(Continued Page 2 Column 1)

Side Bits

Measuring the Market "If you want to know what is happening in the market, Ask the Market." - *Japanese Proverb*

Buy Low Sell High "Don't try to buy at the bottom and sell at the top. It can't be done except by liars."-*Bernard Baruch*

Planning Data Update
To make sure we have your most up-to-date information and communications preferences, we are sending out a client supplemental data update form. Your form will be mailed under separate cover with a return envelope. Please make every effort to return it to us at your earliest convenience.

Tactical Investments
(Continued from Page 1 Column 2)

major asset class, we described this class as a place to put investments that didn't fit neatly into any other category. When the dollar began to fall and inflation became a threat, we added commodities, metals, some oil and gas MLPs (master limited partnerships), and even limited hedge funds in selected portfolios. As they became available, we added some mutual funds that use hedge fund strategies. Sector funds, which invest narrowly in single industries like health-care or technology, were also included in the tactical allocation.

Over the years, the tactical category became somewhat ill-defined and lacked the clarity that we wanted to give clients and ourselves. We recognized the need to review our tactical holdings. We looked first at the funds that were already in the tactical bucket. These could be segregated into three distinct types: alternative asset funds, including funds which invest in commodities, long/short (funds which can sell short), market neutral (another variety of long/short); multi-strategy funds, for the go-anywhere-do-anything manager; and sector funds.

We also determined that the tactical investments could achieve their full potential only if we expanded their portion of the investment mix. We had already considered real estate and tactical as part of the same slice. So the first move was to formally include real estate in the tactical category.

Many of the tactical strategies we are now incorporating have until recently been available only in a hedge fund, limited partnership format. Robert Isbitts describes "the TLC of hedge funds: Transparency (not enough of it); Liquidity (not enough of it); and Cost (too high)." Further, hedge funds get some of their attractive returns by using leverage. Leverage means buying investments by putting down a fraction in cash and borrowing the balance. Leverage magnifies both the gains and losses. Just last month, excess leverage caused the collapse of investment banker Bear Stearns.

However, one hedge-fund technique previously unavailable to mutual funds is highly advantageous: the ability to sell short.

Just adding short-selling to a fund goes a long way to lowering its long-term correlation with the overall markets. We can now access these tools in mutual funds or exchange-traded funds (ETFs). Our first criterion for adding these positions is that they must be transparent; that is, we want to know the managers' process and holdings. Second, expenses must be justifiable. Finally, we need to have daily pricing and liquidity, so that our clients can buy or sell at any time at the current market price.

These changes are really more evolutionary than revolutionary. We have been moving subtly in this direction for the better part of a decade. Now, our reports will more accurately reflect our commitment to these investments. In client meetings, we will review investment policies and as we rebalance portfolios, we will be make some of the changes discussed here. In summary, we expect that these new tools will help our clients achieve their objectives of owning portfolios with moderated volatility and a better chance at more consistent long-term results.

Fed Responds
(Continued from Page 1 Column 1)

Regulators relaxed the capital requirements for Fannie Mae and Freddie Mac, and expanded the pool of mortgages qualifying for purchase. Both "Fannie" and "Freddie" are publicly owned, for-profit entities, but are considered quasi-government agencies. They inject liquidity into the mortgage market by allowing mortgage lenders to package and sell loans and thus to keep lending.

Other efforts are being considered in Congress. Rep. Barney Frank and Senator Chris Dodd have proposed allowing the Federal Housing Authority (FHA) to guarantee up to $400 billion in mortgages as a way to support and stabilize the market. The difficulty lies in knowing where housing prices will settle. Some doomsayers believe we are in a continued free fall after a series of asset bubbles which began a decade ago. Others believe that the Bear Stearns takeover was the turning point.

Although we appear to be in a recession, we won't be certain until after two quarters of negative GDP growth have been recorded. The Fed, Congress, and government agencies are making sure that liquidity is in the system. If we observe what is happening in the real economy, it's still moving along, and very few have lost their jobs. We believe that you will see reasons for optimism. The worst may be behind us.