Comprehensive FINANCIAL PLANNING INC.

October 19th, 2007

Here is our 3rd Quarter 2007 newsletter we send to clients.

Cash Management

One of the often neglected aspects of our financial lives is how we handle our cash. By cash we mean totally liquid funds in our checking and savings accounts at the bank, money market accounts and certificates of deposits (CDs). We use these accounts to fund our current needs, fund short-term goals and provide a financial cushion for unexpected events that would require additional capital. Holding these cash instruments enables the ability to access our funds immediately without loosing any of our principal and to earn some interest at the same time. Having adequate cash in place will prevent having to borrow money or sell long-term investments when an unexpected drop in income or increase in expenses occurs.

As part of our financial planning service, we offer many specific recommendations concerning cash management. Here are a few of the more common recommendations.

1. Make sure you have adequate funds to handle your worst case scenario. If you drive your car into your house and end up in the hospital and unable to work for some time you could be paying significant out-of-pocket expenses not covered by insurance plus suffer a loss of income. Evaluating your insurance policy coverage goes along with determining how much is enough. As a note, I find about as many families that have more cash than needed than those that don't have enough.
2. Make sure you're earning a fair interest rate. Rates are currently dropping for savers with the recent Fed Funds Rate cut of 0.5%. One can find lots of good information at www.bankrate.com . Currently 1 year CDs are averaging 4.65%, $10,000 Money Market Accounts (MMA) are averaging 3.94% and $25,000 MMA are averaging 4.45%. I've often find people with $50,000 or more in an account that has not been touched in years and their earning 2% to 4% less than a competitive rate. As always, pay attention to any fees that may reduce your net yield. Also, know if the account is FDIC insured or not. Most MMA accounts are not insured.
3. Consider alternatives such as online bank accounts. With today's technology of linking accounts and electronic transfers, there is no need to have all your funds at one institution. Many of these are currently offering savings accounts that are FDIC insured and earning 4.5 to 4.75% with no account or service fees. If you

want to stay with your local bank but are earning below market rates, talk to them and see if they will negotiate. Some will give you a higher rate if you just ask.

In the past I have not encouraged clients to consider the cash alternatives at TDAmeritrade where most of my client's investment accounts are held. Recently their offerings have changed with a money market account at 4.5%, or if you have over $250,000 at TDA, a higher yielding account at 4.9% currently. You can write checks or use debit cards similarly to other accounts you're familiar with at your local bank. You should have received information on the new accounts and I would be happy to talk about these options with you.

Where is the Herd Running to Now?

According to the Investment Company Institute, Americans added a net $160 billion into stock mutual funds last year, of which 93% went to funds investing in foreign companies. For over six years now the foreign stock markets have been outperforming the U.S. market by around 10% per year on average. This is particularly true for the China and India markets that have risen about 80% and 60% respectively over the last year. While we like these and other emerging markets, we will continue our disciplined process and limit our holdings in the emerging markets to about 5% of the equity portion of our portfolios. In our bond portfolios we also have a significant allocation in our Developing Local Markets Fund in the emerging debt markets.

I was quoted in the August issue of the Consumer Reports Money Adviser Newsletter where I discussed how much of a portfolio should be invested in the foreign markets. Currently our all-equity portfolios are about 30% foreign equities. This includes about 5% that is located in our domestic mutual funds. Why don't we have more overseas? The reasons are many, but one thing most do not realize is that almost one half of the revenues of the S&P 500 companies are derived from their overseas operations. When you're investing in large cap U.S. companies you're investing in economies all over the globe. Going forward, if overseas markets continue to appreciate more than the U.S. markets, we will trim our holdings there to maintain our allocations as we have done in the past.

Where is the Herd Running From?

Up until recently the herd has been running to housing with investors buying multiple houses in hopes of flipping for big profits and homeowners using their home equity like a bank account. No more. We've been talking about the housing bubble for some time and how it should slow the U.S. economy down for some time. The Case-Shiller 20-city price index fell 3.9% year-on-year thru July. The price declines have been accelerating and will likely get worse before hitting bottom.

There was real concern when the credit markets froze up in August. I sat in on a couple of interesting conference calls with Pimco. One analyst asked "What is a sub-prime mortgage?" His answer was "they used to call it rent". In other words, those that did not have the financial ability to buy a house used to rent because even if they tried, they could not get a loan. In the last few years many have been able to get a loan no matter their financial ability to pay off the loan. Perhaps this was because the non-bank lenders were able to sell the loans to investment banks who then repackaged them to investors looking for higher yields than more traditional bonds were paying. Once the market starting seeing foreclosures rising and house prices falling the credit markets reacted like a “deer in the headlights”. All of a sudden, the lenders could not find enough buyers for their loans. Interestingly Pimco indicated the credit squeeze has created some opportunities for long-term investors to buy high quality mortgage-backed securities as discount prices. They are taking advantage of those opportunities in the Harbor Bond fund that we invest in.

What does all this tell us? Don’t expect much, if any, price appreciation on your house or rental for the next five years. Chances are the price will drop. The herd is running somewhere else now.

A Good Time for Tax Planning

At the end of this year two tax breaks will be ending. The first is the ability to fund your Health Savings Account (HSA) with your traditional IRA. This is a smart move since payments for medical expenses will avoid taxation. Any funds you withdraw in retirement from your traditional IRA will all be subject to income tax at your ordinary income tax rate.

The second concerns the kiddie-tax rules that were modified this year to include those under 18, up from 14 years old. Starting at the beginning of 2008 these rules may apply for someone up to 24 years old.

If your financial situation has changed or there has been some one-time event, act now before the end of the year. Higher or lower than normal taxable income usually offers opportunities. You cannot take advantage of those opportunities for 2007 when you’re filing your tax return in the spring.

Market Commentary

The market volatility, credit crunch, housing market problems, and hedge fund debacles make it hard to believe the overall stock market was in the black during the third quarter. But it was, with the S&P 500 gaining 2%. Moreover, through September the index was up 9.1% on the year. While the numbers for the overall stock market were quite satisfactory over both periods, there was a wide degree of variation across asset classes. Value benchmarks were in the red for the quarter, with smaller-caps doing worst. Growth benchmarks did quite a bit better, and for the year growth stocks are ahead of value by a wide margin after seven consecutive years of underperformance. International stocks gained over 4% in the quarter, extending their run of impressive returns. With the exception of high-yield bonds, fixed-income asset classes had a solid quarter, with investment-grade bonds climbing almost 3%, and emerging-market short-term bonds returning almost 5%. Commodity futures gained over 6% for the quarter.

Over the last year our most aggressive portfolios have returned 19.5%, outpacing our benchmarks by over 3%. Our bond allocations have also added value because we stuck to high quality bonds in general and because our allocation to emerging-market short-term bonds has done very well rising 16.5 over the last year%.

Looking ahead, the driving factor for returns over the next year will likely be the health of the U.S. economy and its impact on corporate profits. The credit crunch and continued deterioration in the housing market, which drove this summer's volatility, has made economists and everyone who follows them believe a recession more likely than it was earlier in the year. So does all this uncertainty make us change our allocations? No. Even if we could predict when the next recession will come, we still would not know what the market's reaction to it would be. We know the economy could fall into recession, but it could also avoid recession and surprise on the upside with the aid of Fed easing, a weaker dollar that stimulates exports, and global growth driven by emerging markets. While the stock market could (as it always can) drop 10, 20% or more, trying to predict the unpredictable short-term moves of the stock market is not what we do. Instead we make sure each client's asset allocation is appropriate for their financial and emotional ability to take on risk.

Thank you for your continued trust, confidence and referrals.

Sincerely,

Stan Johnson, CFP(R)
Certified Financial Planner
Registered Investment Advisor
Comprehensive Financial, Inc.