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Asset Allocation in Turbulent Times

I sat down to write this commentary this morning. It's now nearly 5 pm and I've thrown out everything I wrote during the day, which is a shame because I was going to tell you the 16 year history of the sub-prime mortgage mess with names, definitions, and a good dose of finger pointing—and I was going to do it in 500 words or less. Trust me, it was a great piece.

When I began to write this morning the stock market was up and it was up and down one to two percent all day. That was true until around 3 pm when it fell off the charts and closed down 680 Dow points. During the day I spoke with several of you and I've talked to many of you over the past 2-3 weeks. You are concerned and I am hearing this in a deeper, more frequent way than I have since 2001-03. So, while the down 680 day doesn't really change anything long-term, your concern preempts my thoughts on how we got here.

Instead, let's take a very frank look at where the portfolios are, what they are capable of doing, and where our risks and rewards might be.

Each of you has an asset allocation model built into our management plan and it's outlined in the Investment Policy Statement we wrote and agreed on. The allocation is usually built from a financial plan that we've done for you or in some simpler cases just a thorough review of your investment needs and risk tolerances. The allocation is generally long-

term in nature, because for most of you, your needs are long-term. The allocation is designed to have a stock/bond allocation that achieves your goals and that you can live with along the way. It anticipates both good times and bad times in the markets.



When we set your allocations, I reserve a certain amount of flexibility with regard to percentages of stocks and bonds and also cash holdings.

Now that I've set that up for you, let me get to the heart of the matter and tell you the reason I changed topics today. Beginning last fall, I have set up your portfolios anticipating a recession and trouble in the real estate and banking world. What this means is that—within the long-term asset allocations that we believe are correct— I hold a full or overweight bond position for you, a substantially underweighted stock position, and a significant amount of cash. I have positioned portfolios in this way because in volatile negative stock markets, bonds will usually rise in value and they continue to produce cash flow. Cash in money markets pays a small cash flow and is

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Special points of interest:

- Markets closed- Veteran's Day (11/11), Thanksgiving (11/27) and Christmas.
- We are now registered with the SEC. Our updated Form ADV is available upon request. Call if you would like a copy.

Third Quarter 2008 Market Wrap

Market Indexes	% Change in Q3
S&P 500	-8.4%
DJIA	-3.7%
NASDAQ Comp	-9.2%
MSCI EAFE	-21.0%
KLD Domini 400	-5.4%

Mutual Fund Yardsticks	% Change in Q3
Equity Income	-6.9%
Large Cap Growth	-14.1%
Balanced	-8.5%
Gen US Taxable	-3.6%
Intermediate Bond	-3.7%



The Sandwich Generation

Who is middle-aged and providing care to both children and parents? The correct answer is the “sandwich generation”. A far cry from a lunchtime snack, this term describes people (often women) being squeezed between the demands of caring for aging parents and simultaneously supporting their children.

How large is the sandwich generation? Estimates vary and depend on the definition of support. AARP figures indicate that 44% of 45- to 55-year-olds had both at least one living par-

ent and one child under age 21. Furthermore, this is apt to increase as 2/3 of the baby boom generation will be taking care of an elderly parent within the next 10 years.

Why the increase? Rising life expectancy is part of it. The burden increases for the caregivers because of shrinking family size.; there are fewer siblings to share the workload. Women are having children later in life which compresses the timeline—their parents are older and their children still young. Finally,

children are being supported for longer periods, stretching into their early and mid-20’s and beyond.

What does this mean for you? Stress. The sandwich generation faces enormous financial, emotional and time pressures because of their circumstances. Furthermore, the rise in dual income families makes it increasingly difficult for them to provide additional caregiver services.

What can you do? Read on...



Pat Sokolowski, CFP®



“Nearly 10 million boomers are now raising kids or supporting an adult child while giving financial aid to an aging parent.”

Managing Eldercare

The first step in managing the care of your aging parents is communication. Although these are difficult conversations to have it is critical to talk about their independence, their desires, and the plans that they have made before a crisis arises. Your goal is to avoid surprises and to help them discover and correct areas that may be deficient. Deal with their immediate health and lifestyle issues first, then tackle finances.

This is also the time to make sure that you have legal authority to act on their behalf if needed. A short checklist should include a durable power of attorney, a durable POA for healthcare, and a living will. Offer to set up a meeting with an estate attorney for a comprehensive review.

Help your parents plan a caregiver strategy; have an honest discussion about how much you

can do as a caregiver. Research what support options may be available in their area. Check out resources like Eldercare locator (eldercare.gov), National Council on Aging (benefitscheckup.org), and Natl Association of Professional Geriatric Care Managers (caremanager.org).

Ask for help and be realistic about what you can do.

Managing Boomerang Children

If your children are in their 20’s and you are still contributing to their support you are not alone. With rising college debt and staggering housing prices more and more college graduates are returning to the nest as a way to save money. This, of course, further extends the sandwich years and can put a severe crimp on saving for retirement. Here are some thoughts on how to manage:

- Avoid overextending yourself. Don’t let the return of the prodigal son or daughter derail your own retirement or debt repayment plans. Be honest with them about what you can do.
- Set your house rules. If you want them to pay rent (probably a good idea) establish the terms. Establish ground rules for household responsibilities and chores. Put it in writing.
- Set an endpoint. Discuss how long they will be there. Deadlines enforce goals.
- Supervise their financial planning. Work with them to budget and plan good financial habits.



Asset Allocation (cont.)

MARKET TALK

Sokolowski Investment Advisors
77 Falls Rd., Suite #1
Shelburne, VT 05482

Phone: 802-985-8400
Mobile: 802-233-1365
Fax: 802-985-8433
Email: rws@siawealthadvisors.com



**Wealth Management
& Financial Planning**

68% of people surveyed
don't have sufficient
emergency savings accounts.

very safe. Cash is also a way to move to the side in a bad stock market and have some buying power for a better day. It does not mean that the stocks you do hold won't go down on a bad day; they will simply be a smaller part of the portfolio and "hurt" less in the short-term. The whole idea is to "apply the brakes" when we're going down the hill and not let the car get away from us. I think that by and large I've accomplished this goal on your behalf.

I believe I have pro-actively "recession proofed" your portfolios in terms of risk and volatility. I have certainly had that goal in mind and I have honestly worked many hours toward accomplishing that result. I know that before all corrections or bear markets are over, we will reach a capitulation stage in stocks (the Stupid Stage, as I call it) where **all** stocks go down, both the "good" and the "bad". I know that your stocks, whatever stocks that we retain, will go down. The stark fact is I also know from history and experience that no one will be able to accurately predict the market's top or bottom. Rather, I know that if I balance your portfolios properly, hold high quality stocks, and shade the portfolios for good and bad times I can achieve a better overall return and reduce the volatility of your portfolios. We give you that information on the last page of our reports to you every quarter.

So here's the bottom line— I think we are deleveraging the worldwide economy. We have lived too high on the hog globally, though disproportionately. The industrialized nations have saved too little, spent too much, and are guilty of greed and

hubris. So be it. I think we may be nearing the end of a 10 year old process and it will be painful. We are in a global recession. Your portfolios should survive this recession—that's what I prepared them for.

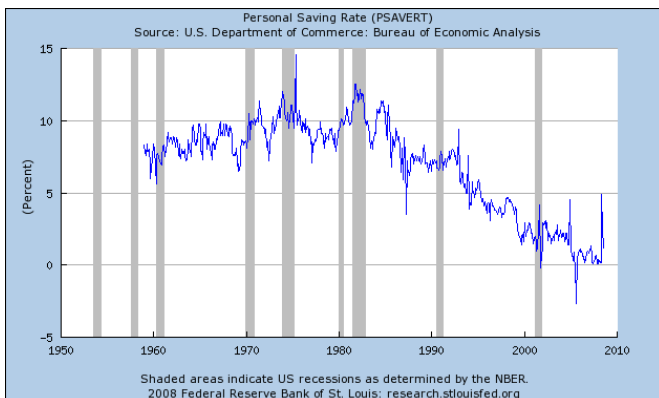
I do not believe we are heading for the next great depression. While there are some similarities to 1929, I believe we have learned from our mistakes of that period. We know now that we must expand credit and the money in people's pockets. We know that it is beneficial to expand international trade, not suppress it. We know that we lower taxes during stressful times, not raise them as Herbert Hoover did.

I believe we are in a stressful period, a painful period of recession. I have positioned your portfolios for that and I will continue to make them evolve to properly fit the situation on the ground. I believe that I have cut all the fat from the portfolios—further cuts will be to the long-term muscle and bone.

It appears to me that we are in the capitulation stage **right now**. I believe that the coordinated worldwide backstopping of the banking system and the huge liquidity injection provided by the US Fed will work. The majority of America's businesses are very sound. If conditions change for the worse I'll change the portfolios accordingly. If market conditions change for the better we're also well prepared for that.



Tightening the belt



US Savings Rate

After years of enjoying rapid increases in stock market and residential property wealth, low interest rates and easy credit Americans may be forced to change their ways. The U.S. personal saving rate is at an all-time low, declining from an average 9% during the 1980's to an **abysmal** .5% in 2007. As Senior Economist, Kevin Lansing warned in his Federal Reserve Bank Economic Letter of 2005, "aging workers should be building their nest eggs and paying down debt. Instead, many of today's workers are saving almost nothing and taking on large amounts of adjustable debt." Furthermore, the decline in the savings rate of households is predominantly in the top 20% income level!

Over consumption may be part of the problem. In tough economic times we need to reduce our spending, not increase our debt. Charting expenditures is often the first step to discovering areas of "opportunity" in discretionary spending. The next step is to make savings a priority by paying oneself first. A fiscally

responsible target would be saving 10% of your net income and establishing an emergency fund with 3-6 months of living expenses.

Developing a personal budget and changing spending habits can be challenging; call us if we can help.