

What a Difference a Decade Makes

A look back at the haves and have-nots in the financial markets in the year just past reveals a contrast rarely seen. By far, the best performing sectors were commodities and heavy industry, and the source of strength was not rooted in the United States. During 2007 the focus of investments, both domestic and foreign, was clearly on the “BRIC’s”, as well as industries providing services to the energy markets. The collective economies of Brazil, Russia, India and especially China continue to advance at a healthy clip, and strong demand for basic goods and services from these emerging markets is forecast to continue well into the future.

A decade ago the world was abuzz over the newly created Internet, and the technology bubble was approaching lift-off. Back then, investments in the basics was looked at derisively as being out of synch with the new paradigm centering on technology and telecommunications. We all know the result of that school of thought. Pity the timing of Bethlehem Steel, once the second largest steel company in the US founded in 1857. Bessie failed on a number of fronts in the post WW II domestic economic boom, in particular upgrading their processes, and as a result could not successfully compete in the coming global marketplace. The company was liquidated in 2003, just missing out on one of the greatest bull markets of all time in one of the most basic of commodities, steel.

We get to read and listen every day to stories about the have-nots of 2007. That popping noise you hear is not the uncorking of a bottle of your favorite bubbly, it is the sound emanating from the residential real estate market. With the benefit of hindsight, it surely seems reasonable to call the recent home building boom a bubble, at least in many regional markets that are now suffering a long and painful deflation. Anyone who thought that Wall Street was on the straight and narrow after the Enron and WorldCom disasters in the early part of the decade can think again. Those creative lads managed to cook up some mythical financial models based on home loans that some people could not afford, which resulted in billions of dollars of losses. The stocks of homebuilders, finance companies and banks had a tough year as they worked through a cyclical slowdown in real estate that appears to have, judging from inventory levels, a way to go. At year’s end the 10-year Treasury bond hovered just above the 4% level, a historically very attractive level that will make mortgages available to credit worthy borrowers once they have the courage to reenter the market. In the meanwhile, prospective and qualified buyers continue to sit on their wallets waiting for a better deal.

Corporate earnings slowed somewhat during 2007, and the upcoming fourth quarter reports will be closely watched. Companies with large components of foreign sales are expected to do well, and those related to the aforementioned real estate correction will undoubtedly suffer additional write-downs. We have endured our share of pain in 2007

from ownership of financial stocks, a sector that represents about 20% of the Standard and Poor's 500 Index. However, we do recall that somewhere back in Stocks 101 the professor said that you "gotta buy 'em when nobody wants 'em". And while exact timing is as much luck as skill, we have a feeling that this may be the case with this beaten up sector. "Fast Money" investing is synonymous with fad investing, so we will take our lumps and stick to the basics. If the global economy continues to expand as expected, and when, not if, the real estate market begins to improve, the unloved sectors will reward investors with significant gains for their courage. There is nothing like a new year to inject a shot of optimism into an out of favor investment theme, so count us in. Perhaps we should all take a lesson from Bethlehem Steel; stick to the basics and be there when the game begins.

2008 promises to be an interesting year. The presidential election, oil approaching \$100 per barrel as this piece is being written, and an uncertain economy will provide ample fuel for investors and the press to chew on. And for the locals, throw in a legitimate shot at another Super Bowl win along with a defending world champion baseball team, and how far away can spring be? Here at Abbot Financial, we are hitting a milestone in 2008 as this year marks our 25th year of operation. We want to take this time to thank our clients and we look forward to offering you another quarter century of continued investing success. Happy New Year!

Scoreboard 2007

Dow Jones: + 6.4%

S&P 500: + 3.5%

NASDAQ: + 9.8%

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