



2010 Quarterly Client Letter

Philosopher Henry David Thoreau is credited with saying, "It's not enough to be busy. The question is: What are you busy about?"

If you've been busy second-guessing your investment strategy amidst the latest headlines and resulting market fluctuations, we'd like to redirect your energy to the ends versus the means of your portfolio: **your long-term goals.**

Have you thought about your goals lately?

By definition, current events come and go, but something noteworthy always is happening. The markets are continuously acting and reacting to global events by almost instantly adjusting prices accordingly. Should you buy or sell *fill-in-the-blank* holdings as the *name-the-latest* news unfolds? Can timely trading help you avoid looming disaster or enable you to cash in on promising opportunities?

We believe these are deceptive questions, and acting on them seems an ill-advised way to stay busy. We'll get to that point in a moment. Instead, the critical question is not whether the world has changed – but whether you have.

Trying to respond to the whole, wide world can feel demoralizing at best. But assessing and adjusting to significant events and transitions within your own life helps you manage the details that can be within your control. This seems to us like a far more effective and satisfying way to stay busy.

When you became a Northstar client, before we reviewed your balance sheet, before we recommended an asset allocation for your portfolio, before we made a single buy or sell recommendation, we began by discussing ... you. Who are you? What values, relationships, possessions and pursuits are important to you? What challenges keep you awake at night worrying? What rewards are you looking forward to achieving?

Only after fully exploring the dynamics of your life did we suggest wealth solutions to reflect them. To do otherwise would have been like taking your measurements and discussing your tastes *after* we'd tailored your suit.

Because we designed your investment portfolio based on your personal circumstances, it makes a great deal of sense to regularly revisit whether those circumstances have changed in significant ways. Here are a few examples of life changes that may warrant alterations to your financial plans:

- Inheritance or other sudden money
- Career changes
- Marriage or divorce
- Birth, death or changes in health
- Relocations (and buying or selling homes)
- Achieving other milestones such as college graduation or retirement

At the end of the day, achieving your personal financial goals is the reason you're investing to begin with. So, beyond periodic rebalancing to remain true to your investment plan, we don't recommend you adjust your portfolio in reaction to the ever-evolving, uncontrollable world around you. Instead, when your own life evolves, as life will do, it makes sense to consider whether to adjust your portfolio, your accounts, your asset allocations or other components that may impact the management of your wealth (such as wills, trusts or insurance policies), to ensure your investment plan is still a good fit for you.

Market Returns: Making Them Personal

So, we believe that the best way to expect to capture broad market returns is to determine asset allocations that make sense according to your goals, and remain true to those allocations through all the

news the world has to throw at you. Consider the following diagram, which shows the growth of the S&P 500 Index during the past 80+ years:

Volatility: Short- and Long-Term January 1926–December 2009



The S&P data are provided by Standard & Poor's Index Services Group. Indexes are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. Not to be construed as investment advice.

If you viewed a chart of other asset classes besides large-cap (as represented by the S&P 500), you would see similar patterns.

At a glance, this data tell us two things:

1. Close up, the monthly or daily rides are painfully bumpy. Regardless of the particular asset class, when you're in the thick of things, it's practically impossible to tell what's going to happen next.
2. Viewed from a comfortable distance, the markets have steadily grown.

In other words:

Accepting some amount of market risk into your portfolio is expected to yield higher long-term returns.

But there's a flip side to this coin.

You must withstand the risk when it occurs and remain in the market (according to plan) as the expected returns happen.

That's easy enough to say, but it can be very hard to do when you read headlines about entire countries threatening to default on their debt. If you feel your discipline slipping from the daily news jolts, consider these points.

By the time you hear the news, it's too late to trade on it. As good or bad news occurs, it's incorporated into market pricing almost immediately. Studies estimate that prices adjust within nanoseconds. This makes it essentially impossible to prevent loss by selling holdings that are in current disfavor or to capitalize on favored holdings that you don't already own.

Good news has outweighed bad, but not on schedule. There has been a long-term tendency for bear markets to be followed by even better bull markets — but, alas, you can set neither your watch nor your investments to when those trains are going to pull in and out of the station. This has been true for domestic and international stocks.

Blink and you may miss it. Missing out on even a few days of high returns in the stock market can substantially erode your long-term performance. For example, from 1970–2009, the S&P 500 index yielded an annualized compound return of 9.87 percent. But if you happened to be out of the market during the 25 best days during that time period, returns dropped to 6.01 percent.¹ Few people would be quite that unfortunate in their bad timing, but why risk it when accepting long-term, globally diversified returns seems to work so well (with the added bonus of reduced transaction costs through less-frequent trading)?

The Grand Conclusion: Busy Is as Busy Does

Once we look at the body of evidence, it again points to the logic of tying your asset allocation decisions to your personal risk tolerance and your financial goals, rather than to the unpredictable bumps in the road (no matter how alarming or exciting they may seem at the time).

Make adjustments to your investment plan when your own circumstances warrant it. But then stick to the plan you've chosen. By remaining steadfastly invested in this personalized way, you stand the best chance for efficiently and effectively capturing expected long-term market growth in accordance with your unique goals and risk tolerances.

Then get busy doing what you love to do with all your free time.

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