CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

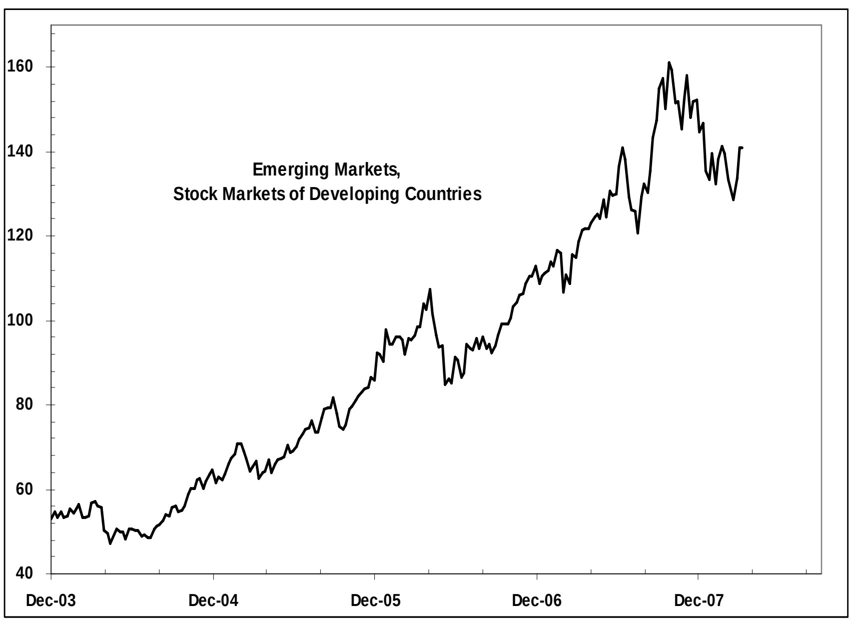
April 7, 2008

Bear Stearns . . .
. . . The Turning Point

The decisive action by the Fed over the weekend of March 15 to rescue Bear Stearns makes clear the Fed's willingness to act to aid the financial markets. A resolution of this credit market crisis is underway.

We expect emerging markets to do well over the next year.

The weekend rescue of Bear Stearns by the JP Morgan bank and the Federal Reserve, announced on Sunday evening three weeks ago, may mark the climax (or the nadir) of the credit crisis. The collapse of Bear Stearns would have caused enormous chaos and huge losses in financial markets and banks around the world. By putting the credit of the United States behind Bear's obligations, the Fed became the "buyer of last resort" for mortgage-backed securities no banks would touch. By explicitly extending its credit to the other major investment banks, Goldman, Merrill, Lehman, and Morgan Stanley, the Fed has forestalled runs on those brokers.



Losses from the sub-prime crisis continue to mount. UBS, the giant Swiss bank, announced another $15 billion in losses from these instruments in the first quarter, but both UBS and Lehman Brothers announced successful efforts to raise new capital. Banks will announce more losses, and credit instruments (other than the pools of sub-prime mortgages) may cause more losses, more fear of bank failures, and more waves of panic selling in the markets. But by placing its balance sheet behind the US financial system, the Fed has staunched the bleeding. Having focused our attention on the preservation of clients' capital in these recent months, we can now plan for economic and financial markets recovery.

To date, credit market problems in the United States and the liquidity issues with US and European banks have had only a small impact on economic activity in developing economies. Most of these countries now have huge currency reserves, built by exports of manufactured goods and/or oil. Economic growth in Asia and Latin America remains strong; the boom in commodities has barely been interrupted by the US slowdown and our credit problems.

By

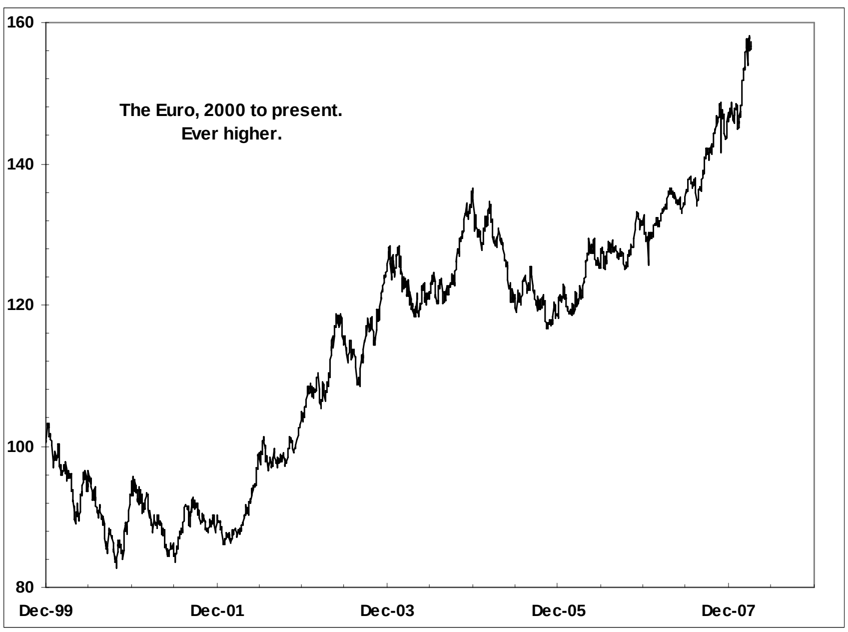
Jack Mayberry

Despite the continuation of robust economic growth in emerging markets, their stock markets have fallen sharply in recent months, many suffering declines larger than those of American stock markets. (See the nearby chart of emerging market stocks.) Central bank actions, especially by the Fed, in lowering interest rates and pumping reserves into the system have created conditions that support rising stock markets in the US and abroad.

The long-standing themes--growth in developing countries, decline in the value of the dollar, demand for commodities--are intact. Other assets--banks and technology stocks--are newly attractive. As we consider investing cash reserves, we find many attractive opportunities.

Investments, Risks and Opportunities. As the credit crisis widened in recent months, we sold positions in clients' accounts and raised cash. We invested much of the proceeds of our sales in foreign currency money market funds, providing some benefit as the US dollar fell sharply in the first quarter. The S&P 500 fell by 10% in the first quarter of this year; in the aggregate Core's accounts declined by slightly more than 3%. (As always, there is variation in the returns of individual clients' accounts, generally because of different levels of risk in different accounts.) It was the worst quarter in the US stock market in several years, and many foreign markets performed worse than American markets. The dollar continued its years-long decline; the nearby chart shows the astonishing levels reached by the euro, which is now worth $1.57.

Past performance is not a guarantee of future returns.



We are not prepared to declare victory and pile back into the market in an aggressive way. Despite the promising interpretation of the Fed's actions discussed above, the sub-prime crisis may not be over. In addition, of course, mortgaged-backed securities are only one arena of credit risk. There has been an enormous increase in the use of debt in recent years and problems may arise in credit instruments other than those backed by residential mortgage. In fact, banks and other pools of capital around the world are 'deleveraging', that is, lessening the amount of debt they hold. This process may extend for many months, perhaps for years, and may present problems akin to the Bear Stearns collapse.

And, we can not know whether the clear economic slowdown in America will become worse nor whether Europe and Asia may suffer economic contraction. The decline in home prices in America is not over; other countries, including Britain, Ireland and Spain, may well suffer similar housing market declines.

Each year Core Asset Management files with the SEC a form ADV with information about our company. If you would like a copy of Part II of Form ADV, please contact us.

Accordingly, we will continue to invest carefully, but now with a bias toward increasing our investments. Commodities and the stock markets of the developing countries seem attractive, as discussed. The bank stocks themselves, in which we have already made a small initial investment, offer opportunity. Selling since the mortgage crisis began last summer has been severe; prices in many markets are quite low. It is likely that the credit crisis will find a resolution and that losses will be manageable. Central banks are flooding the world with liquidity and interest rates are quite low. These conditions strongly favor a robust recovery in stock markets in the coming year. It behooves us to invest some of your cash reserves in these markets.

Financial crises are periodic--almost regular--events; as they unfold, they are very scary. In the crises of recent decades, problems have been resolved and losses contained within tolerable levels. The Fed may have been slow to act last summer and autumn, but it has been decisive and creative since then. The odds favor a reasonable resolution of this crisis, as well.

CORE Comments

CORE ASSET MANAGEMENT
108 Caledonia Street
Sausalito, California 94966
(415) 332-2000 • (800) 451-2240
fax (415) 332-2151
www.coreasset.com
info@coreasset.com