KALORAMA Wealth Strategies

A Beautiful View To Your Financial Future℠

First-Quarter 2007 Market Review ~ Portfolio Spring-Cleaning Revisited

April 2007 - A wave of merger and acquisition activity continued to lift stock prices in the first quarter of 2007. Offers beyond trading prices propelled the values of companies in sectors in which suitors were buying businesses. But spring was on time on Wall Street, as March came in like a lion and went out like a lamb. A late-February sell-off in equity markets evaporated year-to-date gains. The long-awaited correction began when the Chinese government changed rules to curb speculation in their stock market. The Shanghai Index soared more than 130% in 2006, and was on an even steeper trajectory in 2007 before the pull back, with an advance of more than 40% through February 26th.

Notwithstanding the global retreat, stocks rebounded and posted across-the-board gains in the first quarter. International Developed Markets Large Cap led the pack with a 4.2% rise, followed by Real Estate, jumping 3.7%, and International Developed Markets Small Cap, adding 3.3%. U.S. Corporate High Yield was not far behind, expanding 2.6%. Reflecting the Federal Reserve's continued on-hold stance regarding interest rates (the Fed Funds rate remained at 5.25%), the yield on the 10-year Treasury Note was off just six basis points for the quarter at 4.64% (the yield as of April 12th was 4.74%).

Below are rates of return for selected market indices for the first quarter of 2007, full-year 2006, and the three, five, and 10-year averages as of December 31, 2006.

	1Q:2007	2006	3-Yr. Avg.	5-Yr. Avg.	10-Yr. Avg.
Equity (Stock) Indices					
Domestic Large Cap					
Russell 1000 – Growth	1.19%	9.07%	6.87%	2.69%	5.44%
Russell 1000 – Value	1.24%	22.24%	15.09%	10.86%	11.00%
Russell 1000 – Blend	1.21%	15.46%	10.98%	6.82%	8.64%
Domestic Small Cap					
Russell 2000 – Growth	2.48%	13.35%	10.51%	6.93%	4.88%
Russell 2000 – Value	1.46%	23.48%	16.48%	15.37%	13.27%
Russell 2000 – Blend	1.95%	18.37%	13.56%	11.39%	9.44%
Real Estate (Dow Jones Wilshire REIT)	3.74%	35.97%	27.26%	23.79%	15.27%
International Developed Large (MSCI EAFE)	4.15%	26.86%	20.52%	17.02%	9.96%
International Developed Small (MSCI EAFE)	3.26%	19.67%	25.86%	26.46%	NA
International Emerging Mkts (MSCI EM)	2.35%	32.59%	31.03%	28.67%	13.99%
Fixed-Income (Bond) Indices					
Lehman Brothers					
Global Aggregate	1.29%	6.64%	3.81%	8.09%	5.75%
U.S. Aggregate	1.50%	4.33%	3.70%	5.09%	6.31%
U.S. Corporate High Yield	2.64%	11.85%	8.57%	10.66%	6.97%
Municipal	0.81%	4.84%	4.28%	5.55%	5.82%
International Emerging Markets	2.16%	9.96%	11.37%	14.66%	11.31%

Source: www.russell.com, www.wilshire.com, www.mscibarra.com, www.lehman.com

Portfolio Spring-Cleaning Revisited

Although this year clocks were moved ahead earlier for Daylight Saving Time and we have a couple of extra days to file tax returns, it must still be time for Portfolio Spring-Cleaning! Last year at this time, we published a Portfolio Spring-Cleaning article with the anticipation of providing follow-up emails for "how" and "why" we do it. Well, we must have cleaned so well that the follow-ups got swept away. So, to restart the anticipated series, we offer Portfolio Spring-Cleaning Revisited (and improved).

Has your investment portfolio been in hibernation so long that the cobwebs are longer than Rip van Winkle's beard? Is the aroma more akin to musty moth balls rather than the sweet smell of spring flowers? Below are some things to consider for organizing and optimizing the performance of your portfolio.

Is the portfolio still relevant to your goals? Identifying and prioritizing goals is the first step to determine the relevance of your portfolio. When saving for any financial goal, be it retirement, a home purchase, or education, it is important to know how much you will need to accumulate and how long it will take. Along the way you also need to monitor the progress to make sure you are still on track to meet your goals. You may have to invest more or increase risk, or conversely, you may be ahead of your targets and be able to invest less or reduce risk.

Is the portfolio risk level appropriate? Your individual circumstances will determine your tolerance for risk. If things have changed since the last time you developed your asset allocation, your current risk profile may no longer be suitable. Events which could require a re-evaluation of investment approach include marriage, divorce, the birth or adoption of a child, retirement, inheritance, or the start or sale of a business.

Is the portfolio asset allocation still in balance? The asset allocation should be consistent with your goals and risk tolerance. Since the equity markets have recovered from their 2000-2002 downturn, Domestic Small Caps have outperformed Large Caps, International has surpassed Domestic, Equities have exceeded Fixed Income, and Real Estate and Energy/Natural Resources have been among the top-performing market sectors. When was the last time you rebalanced your portfolio to account for these trends? There is no easier way to "sell high and buy low" than to reduce outperforming assets and reallocate to out-of-favor sectors.

Is the portfolio adequately diversified? Just because you hold a lot of investments, be they stocks, bonds, or mutual funds, does not mean you do not have all your eggs in one or a few baskets. The best strategy is to broadly diversify among many market sectors and asset classes. This way you will always capture the returns of the best performing assets classes.

In a recent study by the Center for Retirement Research at Boston College, it was revealed that nearly half of the 401(k) participants are not adequately diversifying their portfolios. Based upon holdings in 2005, they found that 33.3 percent of 401(k) participants in the study had no equities, while 15.8 percent had almost all their investments (90 to 100 percent) in equities.

Are the portfolio holdings appropriate? Investing is not just buy-and-hold, it is buy-and-homework! This includes making sure your reasons for buying an investment still hold, and the underlying style or strategies of the holdings have not changed. Also, are the investments held in the best type of account? Most investors have both taxable and tax-deferred accounts. Investments have varying tax characteristics that lend themselves to be held in either a taxable or tax-deferred account.

Finally, what returns did your portfolio generate in 2006 or prior years? You will need to know how your portfolio has performed to determine whether you are on track to reach your goals. Reviewing portfolio and investment performance relative to a benchmark will also provide insight into how your portfolio and its holdings stack up against other similar or alternative investments.

So now we know the “what” of Portfolio Spring Cleaning, but “how” and “why” do we do it? Where do we begin? In a series of email briefs over the coming months, we will lay out the “how” (Does Your Financial Advisor Follow an Investment Management Process?) and “why” (Does Your Financial Advisor Have an Investment Philosophy?) of organizing and optimizing the performance of your portfolio to achieve your goals.

Kalorama Wealth Strategies can help you create a plan to invest your assets in a manner providing professional management, diversification, marketability, and liquidity. For more information, please see our web site at www.kaloramawealth.com.

Thank you for your business, trust, and referrals. Please feel free to provide a copy of this newsletter to friends and colleagues who can benefit from information about investing and financial planning. If I can be of any assistance to you or anyone you know, please do not hesitate to contact me.

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Fee-Only Investment Advisory And Financial Planning

David M. Taube, CPA, CFA, CFP®, CRI
Founder and President
Kalorama Wealth Strategies
2136 12th Place, NW, Suite 100
Washington, DC 20009-7507
202.550.7262
Fax: 480.247.5620
Email: dtaube@kaloramawealth.com
Web site: www.kaloramawealth.com