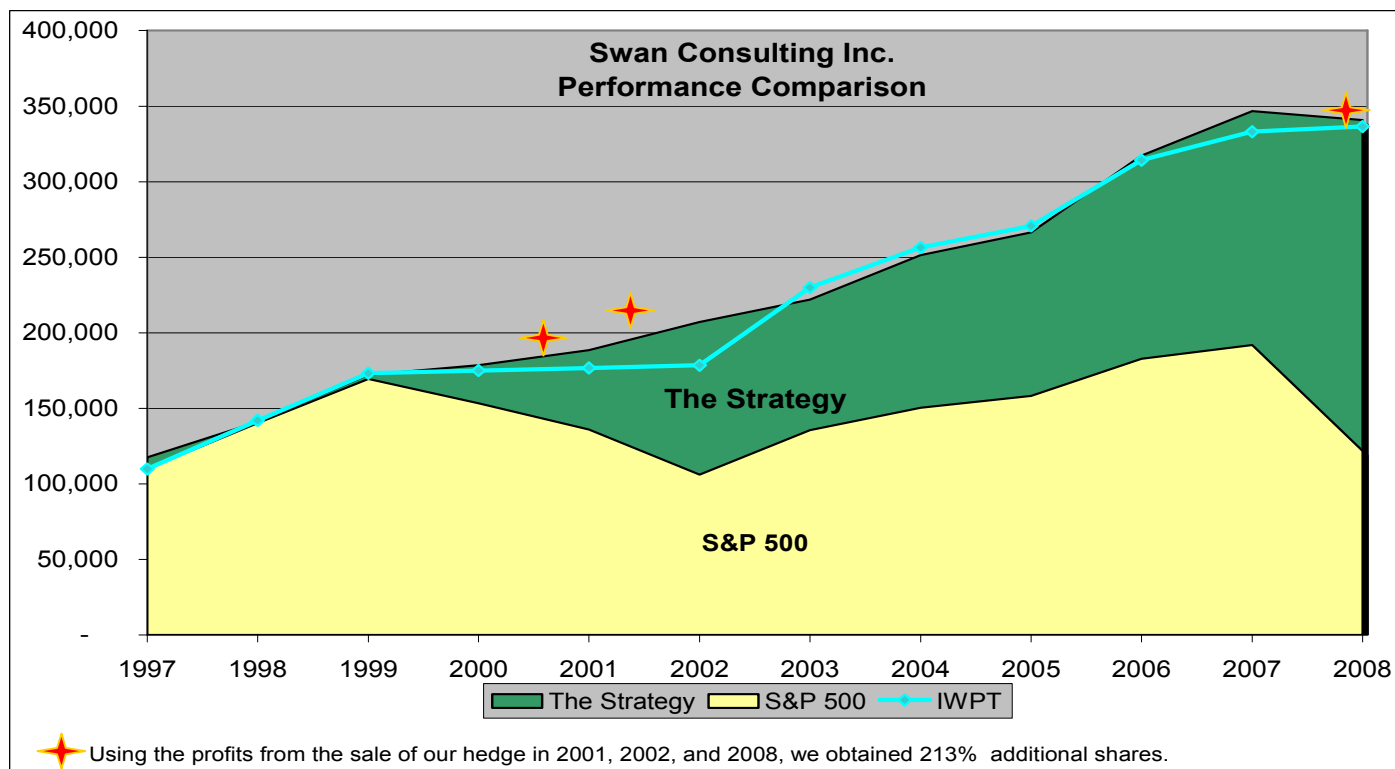


THERE IS STILL ROOM LEFT IN THE LIFEBOAT

SWAN CONSULTING, INC.
DURANGO, CO



Growth of \$ 100,000									
Year	S&P 500				The Strategy				Relative Performance % - Cum.
	Return	Value	Annualized Return	Standard Deviation	Return	Value	Annualized Return	Standard Deviation	
1997	9.98%	109,982	20.96%	0.00%	17.68%	117,685	38.50%	0.00%	7.70%
1998	27.43%	140,146	25.23%	8.72%	19.92%	141,125	25.82%	1.12%	0.98%
1999	20.99%	169,568	23.52%	7.20%	21.92%	172,056	24.24%	1.73%	2.49%
2000	-9.58%	153,315	12.99%	14.04%	3.72%	178,449	17.99%	7.14%	25.13%
2001	-11.32%	135,963	7.07%	15.69%	5.70%	188,617	15.14%	7.56%	52.65%
2002	-22.01%	106,034	1.07%	18.06%	9.80%	207,100	14.15%	7.06%	101.07%
2003	27.89%	135,609	4.80%	18.92%	7.10%	221,811	13.04%	6.87%	86.20%
2004	10.84%	150,306	5.58%	17.77%	13.32%	251,353	13.08%	6.43%	101.05%
2005	5.26%	158,211	5.55%	16.76%	6.01%	266,454	12.22%	6.39%	108.24%
2006	15.47%	182,691	6.55%	16.12%	19.05%	317,218	12.92%	6.45%	134.53%
2007	5.01%	191,836	6.40%	15.38%	9.29%	346,697	12.57%	6.22%	154.86%
2008	-36.55%	121,721	1.72%	19.07%	-1.73%	340,687	11.25%	7.08%	218.97%

Note: 1997 is 1/2 a year and Strategy returns are before fees. IWPT is a hypothetical calculation whereby an investor would have perfect timing on an annual basis. Example: The IWPT buys at year end in 1997 and 2002 and sold at year end in 1999 and 2007 and receives an annual dividend of 2.5% and 1% on cash.

January 16, 2009
Randy Swan

What a year this has been for the financial markets around the world. Fifteen months ago I remember reading and hearing about how this was the best economy ever and now a lot of people are asking are we going to survive.

The good news is that there is still room left on the lifeboat. The bad news is that if you are asking then you probably have already suffered severe losses in your portfolio.

I previously stated over the past decade there is risk in the markets and asked what are you doing about it? There are literally and figuratively options for the average investor.

This is the 4th article that I have written over the past decade that discusses the defined risk strategy implemented by my firm since 1997 (“*the Strategy*”). www.swanconsultinginc.com/library

The purpose of this article is to illustrate why I have been pounding the table since 1997. My claim is that *the Strategy* is superior to a buy and hold philosophy, market timing and asset allocation. My strategy has out-performed all three on an absolute and risk-adjusted basis. I do not offer hope. Hope is something that the politicians offer but rarely deliver. Politics aside, *the Strategy* has delivered results over the past 11 ½ years.

Instead, I offer a Defined Risk Strategy in the stock market that offers downside protection while allowing an investor to profit from either a rising market or a flat market. It also allows for the potential to manufacture income in choppy markets. The latter is important since I do not believe a new 30 year bull market is around the corner or at the end of the road.

During 2008, we had our best relative performance since *the Strategy* was implemented. On October 8, 2008 we adjusted our guaranteed sales price from 1450 to 1000 in the S&P 500 and obtained 40% more shares.

Visit www.swanconsultinginc.com for our results and previous articles.

Summary of Strategy

In case you have not guessed *the Strategy* involves using options to hedge the downside risk and provide income. It is important to note that *the Strategy* uses options as they were intended, to hedge not for speculation. It would be difficult to outline the details of *the Strategy*. However, the following are the some of the benefits of *the Strategy* previously discussed in **Exploring your Investment Options in the 21st Century** written in 2003.

Key Considerations of the Defined-Risk Strategy

(1) Upside participation in the equity markets

The portfolio performance is linked on the upside to the performance of indexes such as the S&P 500, DOW or NASDAQ.

(2) Defined risk upon initiation of investment

Your downside risk is capped and may be eliminated over a one-year period. This is not a claim of an 80% prior success rate that provides no assurance of future success, but rather a definable risk that is determined before investing.

(3) No predictive ability required to be successful

These strategies do not rely on stock selection, market timing, or asset allocation to be successful.

(4) Ability to profit from a market decline

After investing you will not only NOT CARE about a market correction, but also welcome it. Again, you will welcome a market crash. You will be able to profit, not recover, from a rebound after a correction because your investment after the market decline (initial cost and earned profits) will approximate your investment before the market decline. You can profit in two ways: (1) adjust your hedge to the existing market level that allows an investor to profit from a subsequent market rebound and (2) use the excess proceeds from the sale of your hedge to obtain additional shares. In essence, you have the ability of hindsight to buy shares at the current market levels even though you originally purchased shares at a higher level.

(5) *Protect future unrealized gains*

After initial investment, adjusting your hedge can lock in future unrealized gains. In other words, investors do not need to worry about protecting unrealized gains and thus avoiding having to sell thereby creating realized gains and missing potential future stock price increases.

In addition to the 5 key considerations, I have provided a little bit of perspective for investors to ponder.

◆Hedging ◆Time ◆Wealth
◆Flawed Strategies, may they Rest in Peace

Hedging

It is my belief that 'selective hedging' is futile. I have yet to meet anyone who can accurately time the market over the long-term. As a result of my 'continuous hedging,' people ask how much does your hedging cost. I have always answered "we will see." Since *the Strategy* was implemented in 1997, the answer is **zero, nada, zip**. Since the market is about where it started in July of 1997 and *the Strategy* has grown more than 241%, my hedging techniques provided most of the income. Let that sink in for a moment and let this be a lesson to those who believe that hedging is a cost. My experience is that the hedge is a profit center generating returns not incurring costs. A properly hedged position allows an investor to put more of his portfolio in stocks allowing for a greater long-term return.

Nothing But Time

Another benefit is that I believe that *the Strategy* affords me the patience to wait out this bear market whether it last another year or ten years. The reason is that my clients received approximately 40% more shares using the net proceeds from the sale of the hedge on October 8, 2008. This was in addition to the shares that were obtained in the previous bear markets. This allows my clients to profit from any market rebound instead of merely recovering losses. In addition, the increased shares should provide additional income via dividends and other option income generating strategies.

Are my clients:

- scared about losing a large portion of the portfolio,
- worried that they do not have enough time to recover and/or profit,
- worried that they will have dead money over the next ten years as is the case with the past ten years.

NO, they are worried that the market may rebound before they receive another round of *free shares*.

Wealth

Wealth is relative. Even in a year that my clients may not make any money, they are wealthier. Why? In 2008, my clients are at least 40% more wealthy because they were protected against significant losses that others suffered. In fact my clients are 219% more wealthy than the average buy and hold investor over the implementation period.

The Death Of: Buy & Hold, Timing and Asset Allocation

As previously mentioned in all of my literature, I have always had a problem with buy and hold, market timing and asset allocation philosophies. I am not saying there are not some benefits to each but rather the results do not deliver on the promises made by their respective proponents. For example, having a portion of your portfolio in fixed income products to generate cash flow may be necessary but counting on them to protect yourself in 2008 has not been productive.

The Strategy should be used in conjunction with your asset allocation preferences to provide a better return on an absolute and relative basis. In other words, this value added approach offered by *the Strategy* should replace the stock portion of your portfolio. I will briefly highlight the shortcomings of each of the mentioned investment philosophies.

Buy & Hold: What more needs to be said? The buy and hold investor has little to show for their patience since I began implementing *the Strategy*. Over the past century I know of three periods of when the buy and hold could not hold water: the Great Depression, from 1967 to 1982, and from mid 1997 to now. I am not saying that you cannot make money from stocks. In fact, I believe stocks are the only way to make money over the long-term. However, most investors do not have the patience or the fortitude to wait out long periods with no pay off.

Market timing: Market timing is more difficult to access since there are not really any comparable benchmarks. Regardless, I do not know anyone who has a proven track record that has accurately predicted the major moves in the market over the long-term. Milton Freidman said, "Markets can stay dislocated longer than you can stay solvent." Furthermore, the

pressure when the markets are moving against you, when you may ultimately be correct, is extremely difficult. Please review performance comparison on our website. www.swanconsultinginc.com

Modern Portfolio Theory: With respect to asset allocation, my problem has always been the risk reduction that its supporters have always claimed. Asset allocation works until it does not. It looks like 2008 may be the year that it did not deliver on its promises. My view was stated in 1997 when I wrote my book and it has not been changed. My view is as follows:

It is important to note that the great claim of asset allocation relates to the risk reduction achieved by diversifying over several broad asset classes (i.e. stocks, bonds, cash and real estate) without a similar reduction in return. However, the risk reduction is strictly theoretical (typically based upon relationships that existed over a particular period with no guarantee that these same relationships will continue in the future). This is the crux of where asset allocation or modern portfolio theory breaks down. Risk is not defined; instead it is merely expressed in historical standards.

What asset classes do you trust?

The question that I often ask others investors when discussing their asset class alternatives is what do you trust? Yields on government backed securities are less than the inflation rate, corporate and municipal bonds are being downgraded and real estate is an illiquid asset which is probably more overvalued than stocks. Banks deposits are guaranteed but only stocks offer any real long-term returns. Let me rephrase that. Only stock with a reasonable amount of protection and income generating opportunities are you only real bet.

When Will the Bear Market End?

I normally do not like to discuss what I think the market will do since I do not care because I believe *the Strategy* will make money regardless of what happens in the future. However, I think it is important to put the current situation in perspective.

I believe the bear market will be over when the following occurs:

- the dividend yield on blue chip companies is over 7.5%
- P/E ratio of less than 10
- current debt level of individuals, businesses and governments is decreased dramatically.

After all these things have happened, most investors will have given up on stocks and most investments in general. Remember, it took several decades to get to this point and it does not seem realistic that it would be over after one year. The main reason being investor confidence has been shattered and it seems apparent that it will take a lot longer than one year to rebuild that confidence.

What strategy will succeed in the future?

The interesting aspect of *the Strategy* is that it has only been implemented in raging bull markets (1997-2000 & 2003-2007) or bear markets (2000-2002 & 2007-). The future that makes sense to me is that once this bear market is over and a sustainable bottom is found there will not be a bull market (at least not like the last 30 plus years). Instead, I see a market that bounces around for another decade. For example, a 30% rise over 3 years followed by a loss of 20% over the fourth year. This cycle may repeat itself for a long time. You can not count on a bull market to save you. In other words, if you depend on stock price and or market direction to make money, you may be disappointed.

This type of market environment is when *the Strategy's* relative performance should do better than it has historically. Why is this case? Because, investors will not be able to simply buy and hold to save themselves, their portfolios, or their peace of mind. Only a strategy that can profit from rising, falling and flat markets can thrive. A successful investor will need to lock in previously earned gains and be able to manufacture gains.

Conclusion

The Strategy has been in place since 1997, and I am convinced that *the Strategy* offers the best long term profit and risk management potential. Most investment managers are relying on outdated philosophies and risk management techniques. The question I asked in a previous article was; What have you done with your "Investment Options" lately?

The good news is that there is still room left on the life boat.

Swan Consulting, Inc

www.swanconsultinginc.com

512.468.4578

info@swanconsultinginc.com