



# NCM Client Notification

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To Our Clients:

The next two paragraphs were published in the September 28th, 2008 edition of the Wallstreet Journal.

"As in every preceding crisis, the main cause was far too large a mass of credits -- that is, of debts -- for the amount of cash in which they were redeemable. Trade and speculation had long been so active, and too often recklessly expanded, that this disproportion had become dangerous, and a menace to our safety...a serious reaction, a serious revolution, was inevitable unless we moderated our pace and mended our ways."

"That is a description of the Panic of 1907, courtesy of financier Henry Clews, who in 1908 wrote the book "Fifty Years in Wall Street." Mr. Clews also investigated the American stock panics of 1812, 1823, 1825, 1837, 1857, well, you get the idea, all the way through the Panic of 1893. The common denominator: too much debt, too much speculation."

Finally, most germane to the current situation.....

"In every panic very much depends upon the prudence and control of the money-lenders...this is tantamount to saying that all depends on the calmness and wisdom of the banks." Now we might define "calmness and wisdom" as restrictions on lending, but "if they lose their heads and indiscriminately refuse to lend, or lend only to the few unquestionably strong borrowers, the worst forms of panic ensue,".

The market is reacting to the myriad of worries tied to the financial sector. Will the bailout package work? What is the immediate impact on current economic conditions? What will the current economic situation do to corporate earnings?

Said another way, the market is trading on fear.

Interestingly humans have the capacity to dispassionately look back on panics of the past, either those cited above, 1929 or 1987. We can logically evaluate resulting recoveries. Finally we have the capacity to see the wisdom of remaining in the markets through such periods.

However, when it comes to living through such a panic our dispassioned, evaluative capabilities quickly wither and instead are replaced with one of the two most destructive human emotions associated with investing...fear (the other being greed). Wisdom and foresight are easily lost.

Our role as a financial advisory firm is to attempt to evaluate situations devoid of emotion. Evaluate the economy, earnings, Federal Reserve policies, governmental programs, the state of the credit markets among other things. With this data we then prognosticate about potential outcomes. From these prognostications investment strategies are formed and implemented.

Our belief is the bailout bill, coupled with Fed interest rate cuts, coordinated central bank and global government actions and a likely government stimulus packaged aimed at the housing market will prevail.

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It should serve as no surprise banks are still not lending. The Treasury is still loading it's credit bazooka. It is only after the shooting begins we will see results.

In our opinion panic has gripped the markets. When panic exists, opportunities are created. Investment Committee member David Holloway noted "today - and perhaps for the next several weeks - we may witness one of the largest transfers of wealth in our history." His comment is premised on the knowledge that for every investor who is selling, another is buying (except on the New York Exchange...too involved to go into). Suffice to say, somebody is buying stocks at these distressed prices. When share prices recover it is they who will reap the benefits leaving liquidated shareholders only with losses. Therein lies the transfer of wealth.

We cannot say this is the bottom of the market with any degree of certainty. We can tell you capitulation is occurring at some level. We have received a small number of client calls requesting liquidation at all cost. Capitulation generally occurs near a bottom.

Looking ahead there are two diametrically opposed positions with not much left in the middle. Either the myriad of programs currently in place plus those which will be put into place worldwide by governments and banks will fail or succeed.

If they fail, we will be living in an environment unlike any of us have witnessed before.

If they succeed, we will recover as we have from every other historical panic.

Remember our role as your advisor is to dispel emotions, including optimism, from our thought process. We believe the current financial crisis will be resolved. Based upon that belief, we intend to continue to hold our positions.

If any client would like for us to instead liquidate their account and attempt to re-enter the market at some later date, we will do so. However, we can convincingly argue the results will be more favorable for those who chose to hold steady.

To conclude, in 2002 we attempted to mitigate losses and pacify clients by raising cash during a similar market slide. In the end, it may have made for a more comfortable ride, but profits were reduced during the recovery stage.

Please share any concerns you may have...outside of the obvious. We will continue to provide you with insights into our actions and beliefs during these trying times.

Investment Committee  
Northern Capital Management, Inc.