Martorello Money Management, Inc.

Year End Report

REGISTERED INVESTMENT ADVISOR

INSIDE THIS ISSUE:

HAPPY NEW YEAR!

Look fine in 2009 and take action to setup / update your financial plan. Discover MMM's tools that can help make the most of your situation.

Goal Tracker

We can help you develop / update your financial plan and track your progress to ensure you are staying on the right path.

Mortgage Refi Program

Rates are at all time lows, and we have already identified $713K in savings for Clients and Friends. While we are not mortgage brokers, our mission is focused on helping our community.

College Savings Plans

There are many options for college savings plans and we can help you make the right choice and stay on track throughout the years.

MMM hosted an Investment Strategy Discussion for 2009. A full audio /video download is available for a limited time:

http://www.yousendit.com/download/WnBRek91Uzc4aVBIRGc9PQ

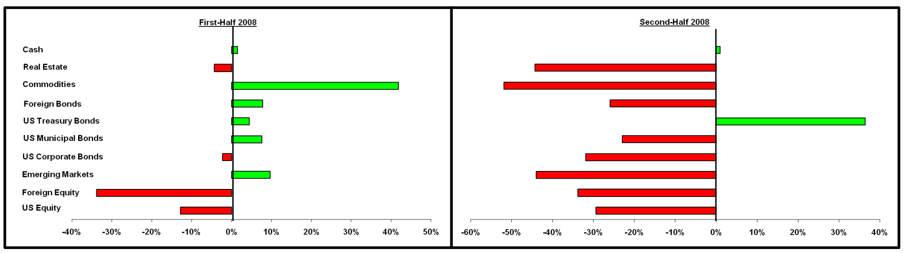
Please fast forward 5 minutes to where the discussion begins.

www.MMMwealth.com

2008 Market and Portfolio Review

Investment markets suffered one of their worst years ever in 2008. During the first half of the year, the S&P 500 declined close to 13%, but there were areas to profit from in emerging market equities, US and foreign bonds, and commodities. MMM portfolios significantly outperformed during this time period by our accurate prediction of a US slowdown, and positioning of portfolios in positively-performing asset classes. However, in the second half of the year, almost all assets declined in a rapid manner (see Chart 1).

Chart 1: Returns By Asset Class (1H/08 Versus 2H/08)



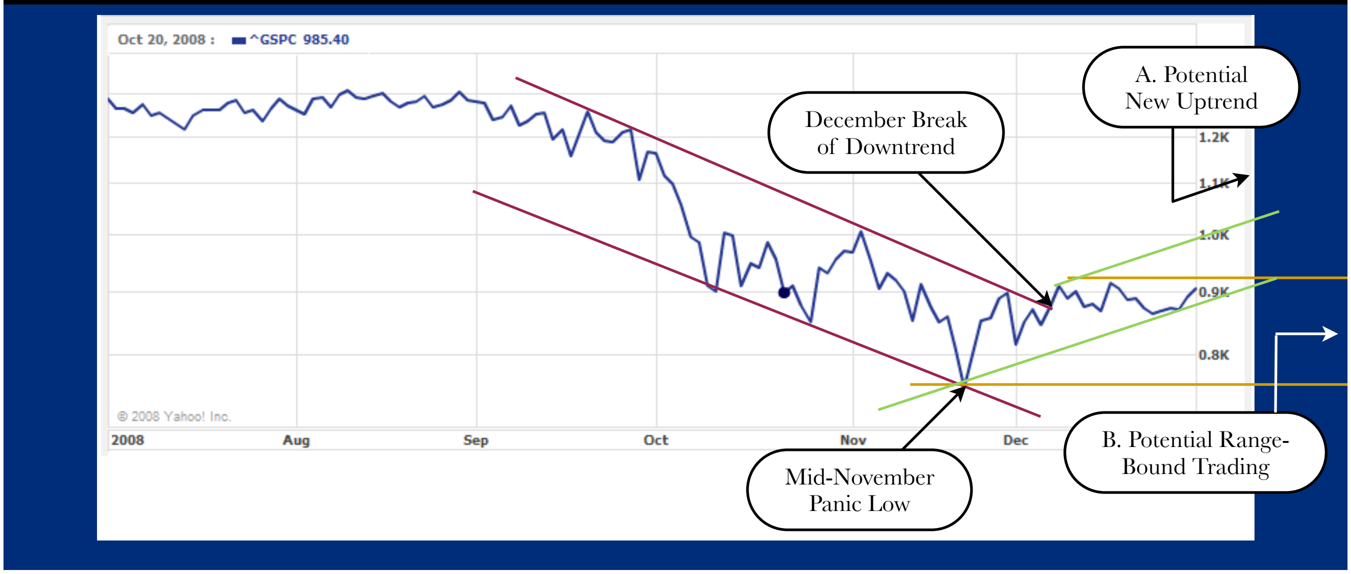
The declines of 2H/2008 included some massive drops in the bond markets, an area that has traditionally been recession proof. In some cases, bond funds dropped by more than twice the S&P 500 due to dried up liquidity from institutional buyers that were forced to preserve and / or raise cash (e.g. hedge fund liquidations, bank re-capitalizations, etc). One research outfit handicapped the odds for such massive declines as being a one in several hundred million chance event. Needless to say, this outcome was not foreseen by our investment models, and client portfolios suffered with larger than market declines despite their conservative positioning (see Chart 2 for illustration of our larger than normal allocation to typically recession-proof investments).

Chart 2: July 1 Allocations to Typically Recession-Proof Investments

	Base Case	July 1 Allocation
Aggressive	10%	35%
Moderate	20%	40%
Conservative	40%	58%

October and November ushered in the maximum pessimism as the credit crunch went from bad to worse. There were many contributing factors, including the following:

- The continued decline of US housing prices and their loans held by the banks.
- The failure of Lehman Brothers, a major backbone of our system, which caused the lock up of funds in the system (especially within hedge funds who were then forced to sell other "good" assets to raise cash for redemptions).
- The failed response of Congress and the Treasury to get the $700B TARP bailout passed and implemented in a timely and effective manner.
- The SEC rule change to ban short-selling, causing net-neutral investment funds to sell their long positions to offset the shorts they had to close out.



2008 Review (continued)

Furthermore, there were a number of historical enablers that exacerbated the problems. The elimination of market slowing mechanisms during the last two decades, such as the uptick rule and human specialists, resulted in a more rapid decline in assets during the panic, with few stopgaps to slow down the movement. Additionally, the mark-to-market accounting rules, implemented during the Enron scandal, forced healthy banks to write down their assets to the distressed-level-prices of the lowest common denominator bank. Finally, the financial media was feeding the fury with record levels of viewership through their sensationalized reporting of the next great depression.

The breathtaking drop in markets turned around in December, due to:

- Extremely low valuations attracted value investors
- A massive panic blow-off bottom in mid-November attracted technical investors
- Obama's moderate appointments and public policy statements improved investor confidence
- Government stimulus began to improve credit conditions (Libor, TED spread, mortgage rates)
- Passing of redemption dates for hedge funds eased forced liquidations / selling

While most asset classes participated in the short-term December rally, the most liquidity-constrained assets rose the furthest. In particular, the corporate bond market rebounded in the 30-50% range while the S&P rose 18-20%, helping to re-energize client portfolios. We believe that there is more room to the upside for corporate bonds, prior to a greater rebound in the wider equity markets. Unfortunately, the short-term rebound was hampered by the discovery of massive fraud in a number of hedge funds (e.g. Bernie Madoff). Regardless, December still ushered in stability, easing the credit markets, and allowing some equity market gains. As discussed in our next section, we evaluate whether or not the mid-November lows were the bottom of the market (see Chart 3).

2009 Outlook

While we are not in the business of predicting market movements in the near-term, our clients often ask us for our opinion on the outlook in front of us. With that said, we are happy to discuss the factors that could influence the market, some potential outcomes, and the resulting investment strategies we would employ.

While we believe that another great depression is off the table, this belief is predicated on the continuation of stimulative and non-protectionist government policies. Furthermore, we are still left with a very significant recession, a massive credit contraction, and a lack of savings at the individual level. A few of the potential scenarios that we foresee include the following:

1. Most Likely Scenario: A short-term rebound in the investment markets to a level 10-15% higher from current levels but far below the 2007 peaks. Thereafter, a plateau or pause in economic growth, with muted investment market returns, while the world retrenches for the next round of growth. During this time period, consumers in the developed world would rebuild their personal balance sheets by reducing credit card debt and increasing savings. Companies would improve profitability through downsizing of their plants / overhead and reduction of head count to drive productivity with those that remain. Coming out of this period, new industries would be developed (e.g. green energy, nanotechnology), and the emerging market populations would begin to contribute to global consumption and the next wave of growth as they mature. This is the healthiest of the various scenarios that we describe from a long-term stability perspective.

2. Lower Likelihood Scenario: It is possible that the government's massive stimulus provides a significant jolt to our economy, allowing for a sharp and extended rebound,

with markets rising during 2009-2010 in response. Under this scenario, there would likely be a resurgence of hyper-inflation through the devaluation of currencies around the globe. Assets that would stand to benefit the most include all forms of commodities, from pure hedging investments such as gold, to more utilitarian assets such as agriculture, oil, and metals. Under this scenario, the reserve banks of the world would eventually tighten monetary supply, causing us to experience another seesaw of massive ups and down's in the investment markets.

3. Lowest Likelihood Scenario: It is possible that the government fails to provide stimulus, or that the stimulus provided is overwhelmed by the continued trend of deflation. If this occurs, the equity market lows of November could be broken, with further short-term pain to the downside. Furthermore, this scenario would be coupled with additional economic weakness through increased levels of unemployment and contracting GDP. This is the darkest scenario, requiring further flushing of the system before basing and rebounding could occur in the longer-term future.

Clearly, 2009 is shaping up to be an epic battle between government stimulus and credit contraction / economic weakness. Given that equity markets are voting mechanisms in the short-term, we expect there to be many counter-trends during 2009, as investors flip-flop between the excitement of government stimulus / recovery and the fear of worsening economic reports. This bi-polar action will not lend itself to trend trading, but rather to short-term trading to "buy the dips and sell the rips."

We will participate in this process through our automatic rebalancing programs that force portfolios to sell high and buy low, while also attempting to catch tradable moves with our active trading system for all client accounts that qualify. Regardless of which scenarios play out, we are sure to see worsening economic conditions ahead (e.g. contracting GDP, rising unemployment, etc.). It also goes without saying that we will see more and more sensationalized reporting from the media. More scandals will be uncovered, and more fear will be disseminated.

However, markets should turn to the upside prior to full economic recovery. Those investors with a long-term focus, with the will power to invest through the darkest hours, and with an ability to enjoy their lives without getting wrapped up in the day-to-day fluctuations, will emerge on the other side in an even stronger position (recall our analysis in previous newsletters of the benefit from continued investing through bear markets).

We look forward to hearing from you, and as always, encourage you to pursue life's dreams as we help to achieve your long-term goals.

Warm Regards,

Raphael & Megan Martorello
MMM - Martorello Money Management, Inc.
LotusGroup Advisors, LLC.

QUESTIONS?

As always, we are available to discuss any questions you may have regarding our progress towards your financial and investment objectives.

REFERRALS?

We appreciate your referrals as they are the lifeline to our business. Please let your family, friends and colleagues know about our wealth management services.

Contact Us

Phone 415-793-8014
Email info@mmmwealth.com