



## K&A Asset Management, LLC Daily Illumination Newsletter

### The Grinches who stole Christmas

By now it must be clear to readers of Illumination that the Christmas rally we had been anticipating is not happening. In fact we were stopped out of all ProShares index long positions yesterday. They were sold at sizeable losses in all models that owned them. It was not pretty and not a happy day around here.

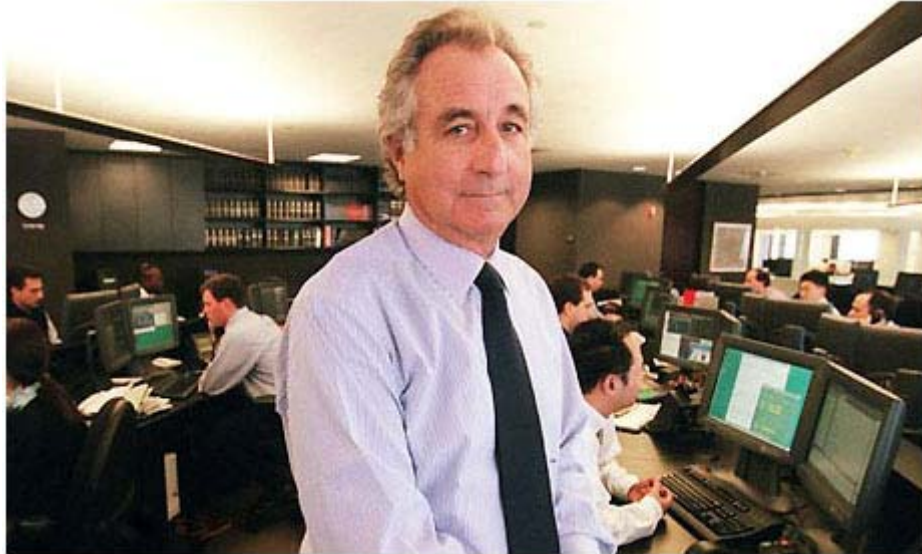
We continue to be hit by bad economic news on a daily basis, so it should stand to reason that this trade turned out poorly. But the markets had started to show definite signs of shrugging off bad news as if the worst was factored in—at least for now. The technical set up of the market was improving rapidly and right through last Thursday we were very encouraged and excited about the potential outcome of the prospective rally. On Thursday afternoon several of the models were up nicely for the month. That all changed on Friday and it got worse yesterday (Monday).

In a recent newsletter we told you that all the components for the year-end rally were in place except for the Big 3 auto bailout. President Bush announced the package before trading opened on Friday and the markets received the news very well. The DJIA traded up 150 points on Friday morning and our confidence grew that the set up was complete. We got to feel that way for a few minutes, until Rick Waggoner, CEO of GM, started his press conference responding to the President's announcement. Let me cut right to the chase on this one.



Mr. Waggoner's press conference, while probably well intended, was one of the worst we have ever watched. It was useless in that he had nothing reassuring to say and it knocked the rally right on its proverbial "arse". It was "game over" following that press conference. George Bush has never been one to light fires under markets to get them to go up. But he did so Friday and his message and delivery were right on point. Not so Mr. Waggoner's.

We offer this wise counsel to the CEO of GM. We call it the Thumper Theory, as in Thumper the rabbit from Bambi. "If you can't say something nice, don't say nothin' at all." In other words, you should have graciously accepted the money and kept your mouth shut. You knocked down your own stock and the entire market with that press conference. But in the grand scheme of things Mr. Waggoner was a bit player in the demise of the rally. The real skunk is pictured below.



It is clear to us now that the market has not yet fully absorbed the news of the Bernie Madoff scandal. The market simply does not yet understand the magnitude of the scandal.

The news was originally broken on December 12 and one would think that there has been time to factor it in but that does not seem to be the case. Every day brings new revelations. No one seems to have a handle on just how far and wide this convoluted web has been spun.

Today this grim story broke: (excerpt from story)

**NEW YORK (AP) -- The founder of an investment fund that lost \$1.4 billion with Bernard Madoff was discovered dead Tuesday after committing suicide at his Madison Avenue office, marking a grim turn in a scandal that has left investors around the world in financial ruin.**

**Rene-Thierry Magon de la Villehuchet was found sitting at his desk at about 8 a.m. with both wrists slashed, New York Police Department spokesman Paul Browne said. A box cutter was found on the floor along with a bottle of sleeping pills on his desk. No suicide note was found.**

**Associated Press Writers Rachel Beck and Joe Bel Bruno in New York and Jim Fitzgerald in New Rochelle, N.Y., contributed to this report.**

We could be wrong, but our considered opinion is that absent the Madoff scandal these markets would be celebrating year end right now—as they have done so often in the past—regardless of negative economic news. But that would be the world as we think it should be and not the world as it is. In the real world the rally is OFF.

As of tonight our models are down roughly 7% to 15%, with more closer to the latter number. We hate it. We know you hate it. But we are no longer focused on 2008. We are focused on 2009 and generating positive returns for all the models no matter what happens.

We are grateful that we have avoided the worst of the damage this year.

Next week we will finish off our series of newsletters on “looking forward to 2009”. We will expand on our

recent comments on bonds and then offer perspective on equities and commodities for 2009.

Our team will be here for a short day tomorrow, if you need us. The markets close at 10:00 a.m. tomorrow. Lee and I will be on duty on Friday as the market is open all day.

We hope you have a very nice holiday.

All the best, PK

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*Overcoming the Crisis One Day at a Time*

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Disclosure and Disclaimer - Updated last on August 13, 2007 by Paul Krsek:

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K&A manages accounts with various histories and investment objectives. Various accounts may be managed differently from time to time.

Krsek makes frequent reference to the model portfolios called Hatteras, Mendocino, Halifax, Bonavista, Fresnel and The New World. During 2005 Paul Krsek was appointed Chief Investment Officer of K&A, and as such is responsible to make all trading and management decisions for all client accounts which are being managed according to a specific portfolio model. A description of each of our models can be found on our website at <http://www.kaassets.com/choices.htm>.

Not all accounts managed by K&A are "modeled" accounts. We strongly urge our clients to understand which model, if any, are being used to manage their accounts.

As of July 3, 2007 Lee O'Dwyer joined K&A as a portfolio manager. Paul Krsek and Lee O'Dwyer frequently discuss investment ideas, model portfolio strategies and the investment policies of K&A. But when it comes to the implementation of those policies Krsek is primarily responsible to manage the accounts that fit into each model portfolio description. He generally makes all final investment and trading decisions relative to those accounts that are considered to be "modeled." However, in Krsek's

absence O'Dwyer does have the authority to trade all client accounts. He has been actively trading accounts in the various models since joining K&A.

From time to time K&A receives requests from clients to purchase securities that are not included in the model portfolio to which they are assigned. Effective May 24, 2006 K&A has encouraged clients to hold such securities in a separate account for the client. Because K&A is a "fee only" registered investment advisor" it charges its normal management fee for monitoring such securities in the separate accounts in which they are held.

K&A makes every effort to exclude securities that are 'requested by the client' from the modeled portfolio accounts.

The investment objectives of various accounts and models may be substantially different from one another. Therefore topics or investments mentioned in E-Illumination may or may not apply to specific managed accounts and/or models.

Trades or adjustments to accounts mentioned in ELLUMINATION may or may not happen in every account managed by portfolio managers at K&A.

If you are not satisfied with the investment results in your account it is your responsibility to inform Krsek or Andreae and to discuss possible changes that can be made to the account to accommodate and satisfy your needs.

The assets held in managed accounts at K&A Asset Management, LLC may include stocks, bonds, cash, commodities, foreign exchange or mutual funds or exchange traded funds (ETF's), money market accounts or limited partnerships that represent the same. They are subject to market fluctuation and the potential for losses. The assets are not insured. The value and income produced by these investment products may fluctuate, so that an investor may get back less than they initially invested.

The portfolio managers at K&A Asset Management, LLC do not guarantee results.