Going the Distance

How to build endurance for difficult markets

Northwestern Mutual
FINANCIAL NETWORK®

The Dow posts a record high…the markets tumble in heavy trading. It can be difficult to maintain a long-term perspective during challenging economic times. But as top athletes will tell you, the only way for them to win is to avoid distractions, remain *focused* through difficult times, and keep the goal in mind.

The same is true for investing. While maintaining a long-term perspective through volatile markets isn't always easy, it can be rewarding. How can you avoid the distraction of short-term market moves and build endurance for the long run?

Here are some time-tested principles of successful investing that can help you stay focused regardless of what's happening in the markets.

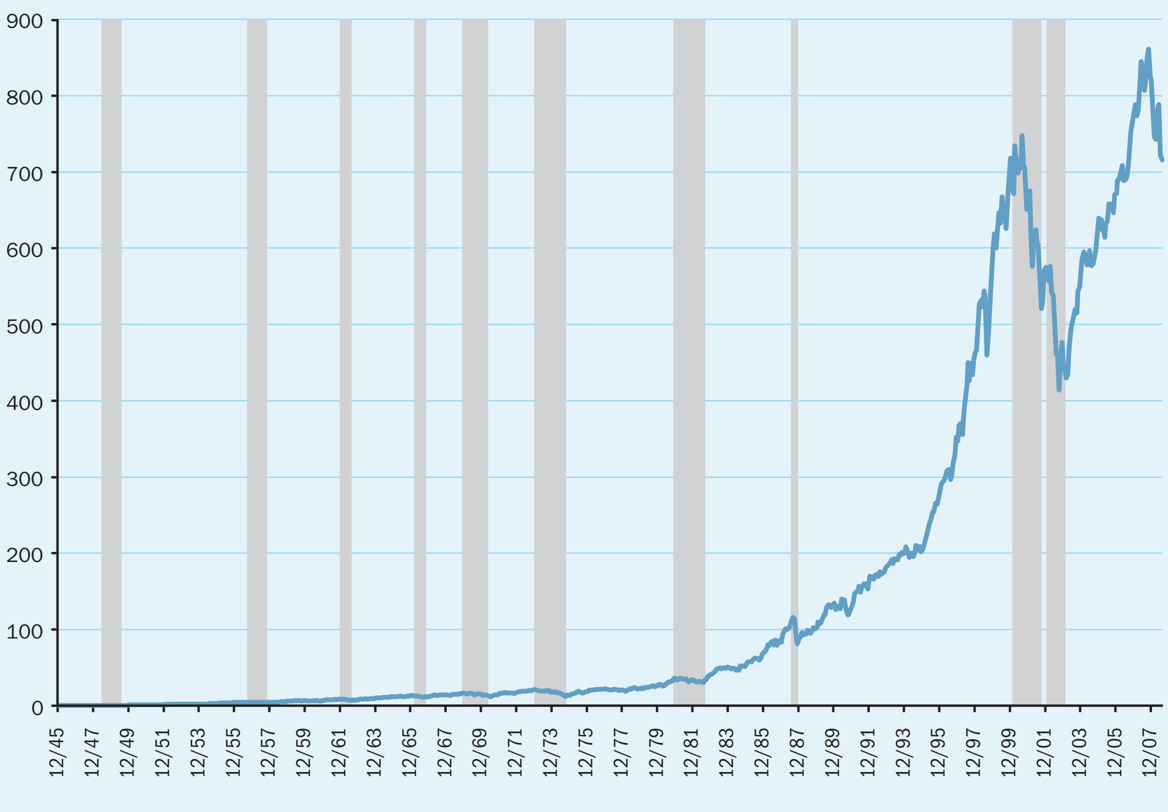
Take advantage of market opportunities

In volatile markets, investors are frequently faced with an emotionally difficult choice: whether to keep investing even during periods of market turmoil. Yet for long-term investors, falling stock prices aren't all bad news. In fact, during market lows, you may have the opportunity to expand your portfolio with quality investments at attractive prices.

While historical performance is not indicative of future performance, the market has trended upward over the long term, and investors who purchased when equity prices were relatively inexpensive experienced a significant gain.

Corrections should be recognized as part of the normal market cycle; savvy investors acknowledge this, and over time, are confident the capital markets will recover. The market has experienced 20% or greater market corrections 10 times in the past 60 years. Despite this, if an investor had invested $100 in the S&P 500 Index 60 years ago, the initial investment would have grown to over $78,000 today! Your financial representative can help you put market volatility into perspective and work within your investment plan to help you invest appropriately.

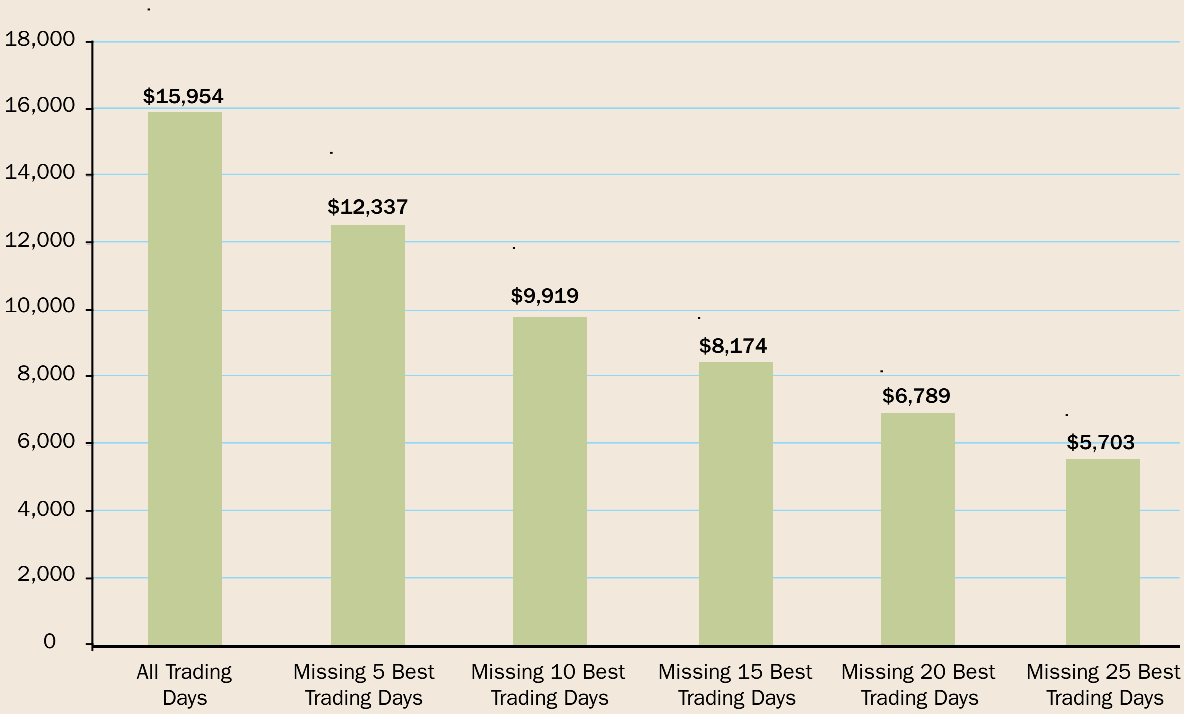
Market Corrections of 20% or More From 12/46 Through 7/08



Source: Bloomberg

This is for illustrative purposes only and not indicative of any investment. The data depicts the Standard & Poor's 500® Index, which is an unmanaged group of securities and considered to be representative of the stock market in general, from 12/31/46 through 12/31/07. Shaded areas represent market declines of 20% or more. Returns assume reinvestment of all distributions. It is not possible to invest directly in an index. The index is unmanaged and does not take transaction costs into consideration. Past performance does not guarantee future results.

Consequences of Missing the Best Trading Days in the S&P 500 Index



Source: Bloomberg.

This is for illustrative purposes only and not indicative of any investment. The chart depicts the ending investment value of $10,000 in the S&P 500 Index for all trading days as well as for time periods in which the best trading days are missed. Returns assume reinvestment of all distributions. It is not possible to invest directly in an index. The index is unmanaged and does not take transaction costs into consideration. Past performance does not guarantee future results.

Don't try to time the market

The simple investment maxim of "buy low and sell high" generally produces positive results. However, complete success at market timing requires consistent knowledge of when the high and low points have been reached. This is a talent beyond the capabilities of even the most seasoned professional. The odds of successfully timing the market become even slimmer when you consider that, historically, the biggest market gains are often clustered into very short time periods. So even if you're able to avoid significant downturns, missing just a portion of a recovery can impact substantially your portfolio's long-term performance.

As the above chart shows, if you were out of the market on the 10 best trading days over the last decade, you would have lost nearly 37 percent of portfolio growth. A hypothetical $10,000 investment on September 30, 1998 in the S&P 500 Index would have grown to $15,954 by September 30, 2008. Missing only the five best days would have lowered your portfolio value to $12,337. The lesson? History has shown that, for most investors, the most important factor in long-term success is time in the market, not timing the market.

Don’t go it alone

As the past few years have shown, the markets are unpredictable and rife with volatility. This makes the value of working with an investment professional to build a sound, time-tested investment strategy even more critical.

The mission of the Northwestern Mutual Financial Network is to develop enduring relationships with our clients by providing expert guidance for a lifetime of financial security. “Financial Security” means bringing to our clients a feeling of confidence that they will realize their financial goals through the actions they are taking today; actions that are based upon a process that integrates both insurance and investment products. It is an integral part of our investment philosophy.

Your Northwestern Mutual financial representative will work with you to help you understand the actions needed to meet your future financial goals. As part of this process, he or she is guided by Northwestern Mutual’s 10-point investment philosophy and asset allocation approach.

This proven investment approach will help your representative to:

1. Solve your risk-based needs first.
2. Provide expert guidance to help develop your long term investment strategy.
3. Create a strategy consistent with your risk tolerance, time horizon, and goals.
4. Determine a diversification strategy using asset allocation to meet goals.
5. Use professionally created quality investment portfolios designed to match your asset allocation strategy.
6. Use rebalancing to remove emotion from decision making.
7. Manage the impact of taxes and inflation.
8. Evaluate the asset allocation relative to your long term goals and benchmarks.
9. Help you resist the temptation to change your strategy during up or down market movements.
10. Encourage you to start early, invest regularly, and use dollar cost averaging.

Of course, no investment strategy can assure a profit or protect against loss in declining markets. Investors should consider their ability to continue to purchase through periods of low price levels.

Talk to your Northwestern Mutual financial representative for more information. He or she can show you how sticking to a solid investment strategy and maintaining a long-term perspective can help you build endurance to reach your financial goals even during times of market uncertainty.

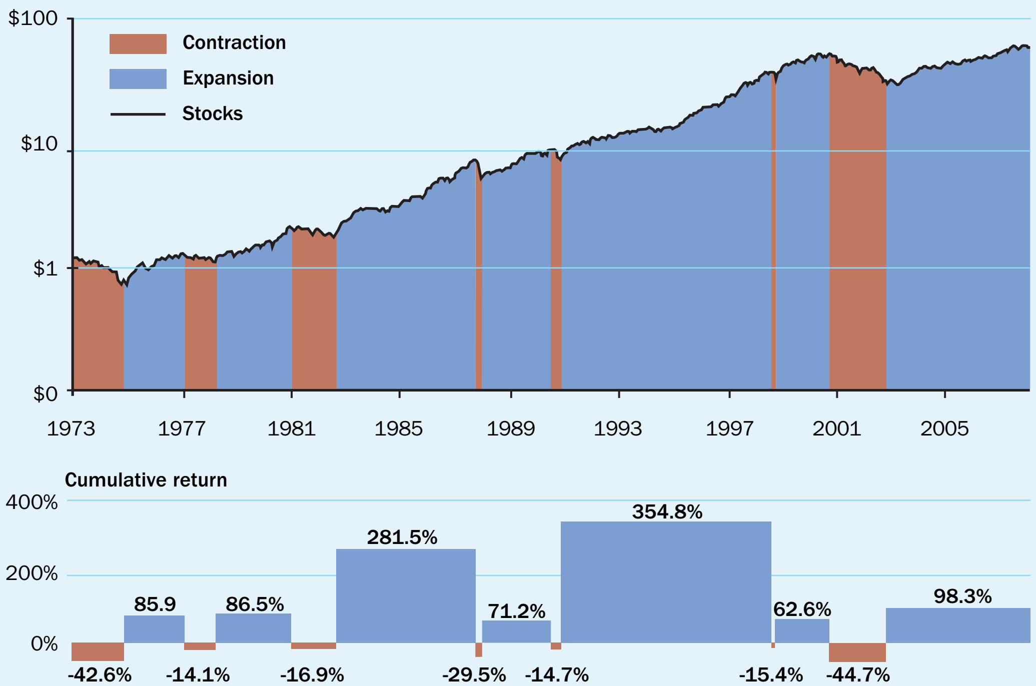
Stay the course

A market downturn can test the resolve of even the most focused investor, causing them to second-guess their long-term financial decisions and sell at precisely the wrong time. However, there's compelling evidence to support the importance of "staying the course."

Understanding general stock market behavior can help you maintain a disciplined approach to investing, especially during difficult markets. The regions shaded in red highlight the contraction phase of a stock market cycle, and the blue regions show the expansion phase. A contraction is defined by a time period when the stock market value declined from its peak by 10% or more. These declines seem to happen at random and last for varying time periods. Since 1973, the market has experienced seven market contractions. While some periods of decline have been severe, overall the market has grown with time. For instance, the stock market fell from its peak at month-end May 1990 to its trough in October 1990 by –14.7 percent, but grew by 354.8 percent from November 1990 to its next peak in June 1998.

Of course, this does not mean stocks will experience positive returns every year and no one can predict market declines with certainty. However, the stock market can add real value to your portfolio over the long term. The important lesson is to not let short term declines keep you from reaping the gains of long term investing. The key is to work with your financial representative to formulate a plan to fit your goals, time horizon and risk tolerance – and then stick with it.

Stock Market Contractions and Expansions
1973 - 2007



Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index.

Returns and principal invested in stocks are not guaranteed.

About the data

Large company stocks in this example are represented by the Standard & Poor's 500®, which is an unmanaged group of securities and considered to be representative of the stock market in general. An investment cannot be made directly in an index. The data assumes reinvestment of all income and does not account for taxes or transaction costs.

Market Leaders Vary Over Time

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
HIGHEST RETURN	International 32.9%	International 8.1%	Large Cap 37.4%	Real Estate 35.3%	Large Cap 33.4%	Large Cap 28.6%	International 27.3%	Real Estate 26.4%	Real Estate 13.9%	Core Bond 10.3%	International 39.2%	Real Estate 31.6%	International 14.0%	Real Estate 35.1%	International 11.6%
	Real Estate 19.7%	Cash 4.2%	Mid Cap 30.9%	Large Cap 23.1%	Mid Cap 32.3%	International 20.3%	Large Cap 21.0%	Mid Cap 17.5%	Core Bond 8.4%	Real Estate 3.8%	Small Cap 38.8%	Small Cap 22.6%	Mid Cap 12.6%	International 26.9%	Mid Cap 8.0%
	Small Cap 18.8%	Real Estate 3.2%	Small Cap 30.0%	Small Cap 21.3%	Small Cap 25.6%	Mid Cap 19.1%	Mid Cap 14.7%	Small Cap 11.8%	Small Cap 6.5%	Cash 1.7%	Real Estate 37.1%	International 20.7%	Real Estate 12.1%	Large Cap 15.8%	Core Bond 7.0%
	High Yield Bond 17.1%	Large Cap 1.3%	High Yield Bond 19.2%	Mid Cap 19.2%	Real Estate 20.3%	Core Bond 8.7%	Small Cap 12.4%	Core Bond 11.6%	High Yield Bond 5.3%	High Yield Bond -1.4%	Mid Cap 35.6%	Mid Cap 16.5%	Small Cap 7.7%	Small Cap 15.1%	Large Cap 5.5%
	Mid Cap 14.0%	High Yield Bond -1.0%	Core Bond 18.5%	High Yield Bond 11.3%	High Yield Bond 12.8%	Cash 5.1%	Cash 4.7%	Cash 6.0%	Cash 4.1%	Mid Cap -14.5%	High Yield Bond 29.0%	High Yield Bond 11.1%	Large Cap 4.9%	High Yield Bond 11.8%	Cash 4.7%
	Large Cap 10.0%	Core Bond -2.9%	Real Estate 15.3%	International 6.4%	Core Bond 9.7%	High Yield Bond 1.9%	High Yield Bond 2.4%	High Yield Bond -5.9%	Mid Cap -0.6%	Small Cap -14.6%	Large Cap 28.7%	Large Cap 10.9%	Cash 3.0%	Mid Cap 10.3%	High Yield Bond 1.9%
	Core Bond 9.8%	Mid Cap -3.6%	International 11.6%	Cash 5.3%	Cash 5.2%	Small Cap -1.3%	Core Bond -0.8%	Large Cap -9.1%	Large Cap -11.9%	International -15.6%	Core Bond 4.1%	Core Bond 4.3%	High Yield Bond 2.7%	Cash 4.8%	Small Cap -0.3%
LOWEST RETURN	Cash 3.1%	Small Cap -4.8%	Cash 5.8%	Core Bond 3.6%	International 2.1%	Real Estate -17.5%	Real Estate -4.6%	International -14.0%	International -21.2%	Large Cap -22.1%	Cash 1.1%	Cash 1.2%	Core Bond 2.4%	Core Bond 4.3%	Real Estate -15.7%

Source: Large-Cap S&P 500; Mid-Cap S&P 400; Small-Cap S&P 600; Real Estate NAREIT Equity; International MSCI EAFE; Core Bond LB U.S. Aggregate; High Yield Bond LB U.S. High Yield; Cash CITI 90 Day T-Bill

This is for illustrative purposes only and not indicative of any investment. The data assumes reinvestment of all income and does not account for taxes or transactions costs. This chart is based upon past index performance and is not indicative of future results. Indexes are unmanaged and cannot be invested in directly.

Build a well-diversified portfolio

It's important to remember that the market is made up of many parts – small-cap and large-cap stocks, growth and value stocks, domestic and international stocks, bonds of different countries, maturities and qualities, and cash equivalents.

Each of these asset classes has different risk and return characteristics. The market cycle dictates that they will go in and out of favor – some have positive years when others are negative; some have record gains when others experience average gains or even losses.

The most widely accepted way to help reduce the risk of investing is diversification – spreading money among a variety of investments as opposed to investing in just one. If you diversify your portfolio across different asset classes, your financial security isn't tied to the fluctuations of a single investment. However, it is vital to understand that diversifying won't provide any down side protection in broadly declining markets.

Another important lesson to keep in mind is that chasing the performance of last year's winners doesn't guarantee future success. Instead of trying to predict which asset class will be the winner, your financial representative can help you invest in a well diversified portfolio, based on your goals, risk tolerance and timeframe, to maximize your returns while minimizing your volatility.

Be a consistent investor

While you can't control how markets perform, you can control how much you invest and when. Like the fabled race between the tortoise and the hare, the investor who moves steadily toward his or her goal may be more likely to succeed than the one who darts in and out of the market.

Although past performance does not guarantee future results, history shows that by investing regularly over the long term, you can reduce the impact of market fluctuations on your overall portfolio. With dollar cost averaging, a set amount is invested at regular intervals, no matter which direction the market is headed. That way you buy more investment units when the market is down and fewer when it is up. This helps even out the average price per unit, hence "dollar cost averaging," and decreases market timing risk. The result of a lower average cost may ultimately equate to a higher return when the market bounces back.

Dollar-cost averaging may be a way to gradually approach volatile markets. In the example below, an investor systematically investing $600 a quarter would have purchased 114 shares by the end of the 4th quarter (30 + 40 + 24 + 20 = 114), representing a total investment of $2,400. Divided by the total number of shares purchased, the average cost per share is $21.05. This is less than the average market price of $22.50 ($20 + $15 + $25 + $30 = $90/4 quarters = $22.50).

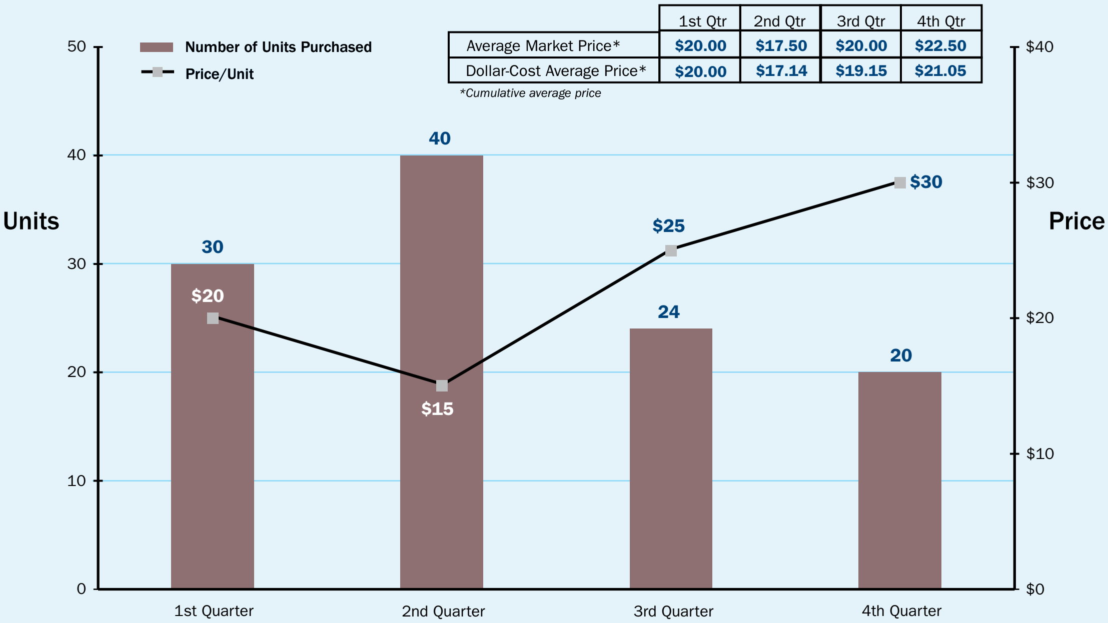
Dollar-cost averaging will not protect against losses, but your financial representative can help you determine if using this strategy as part of your overall plan may help you get more from your investments.

Standing Up to the Bear

Dollar Cost Averaging: A hypothetical $600 invested systematically for lower average cost per share

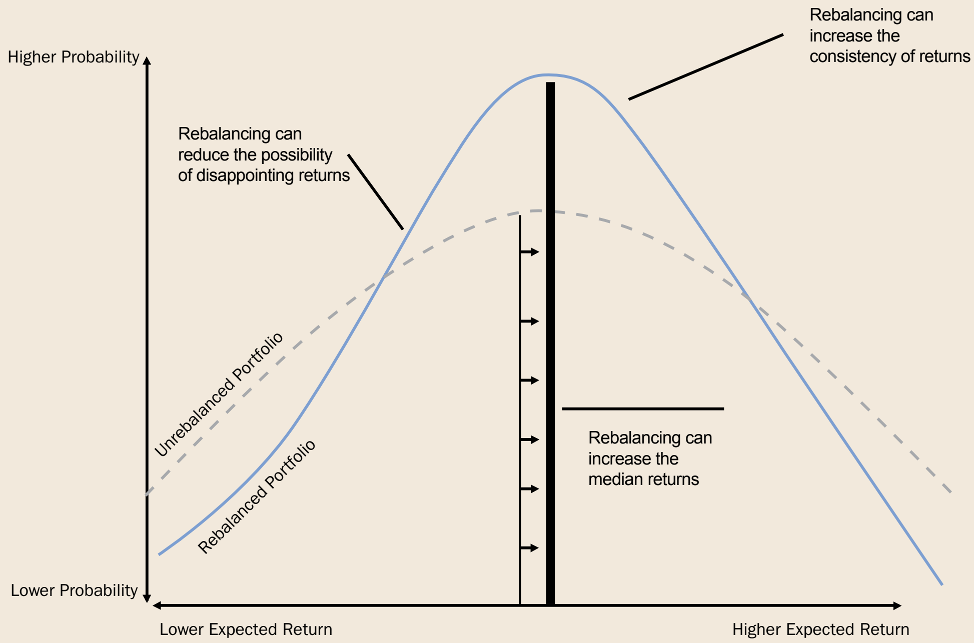
	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr
Average Market Price*	$20.00	$17.50	$20.00	$22.50
Dollar-Cost Average Price*	$20.00	$17.14	$19.15	$21.05

Cumulative average price



For illustration only. The data does not represent any particular investment. No investment is risk free, and a systematic investment plan does not ensure profits or protect against losses in declining markets.

Rebalancing Can Change the Shape of Portfolio Risk



Source: Northwestern Mutual Wealth Management Company

Let rebalancing work for you

Even during difficult markets, some of your investments may perform better than others. This means that the percentage of each of your asset classes may have shifted from your original target. That's why it is important to rebalance your portfolio, if necessary, to bring your asset allocation back into line with your goals, risk tolerance and time frame.

A systematic approach to rebalancing also is an important way to help keep emotion from interfering with a portfolio's performance. It's easy to see why an investor might find it hard to sell even a part of an investment that has helped them significantly improve their net worth. Unfortunately, that sentimental attachment to the holding can make it easier to lose the returns it has produced. Emotion causes the investor in this case to increase his or her investment risk – and the fact that it is unintentional doesn't make the potential negative impact any easier to take.

Your financial representative can help you take an objective approach to periodic rebalancing, keeping your overall performance and goals in sight. Intensive analysis has gone into weighing the return potential of the different assets against their risk profiles to create an optimal portfolio mix. Your representative understands that getting that dynamic right is critical to achieving your long-term financial goals. As the performance of the various assets in the portfolio differ over time, the mix that was so carefully created will change. Your representative will work with you to correct any imbalances in your portfolio helping to ensure that your investments continue to reflect your desired risk/reward profile.

All investments carry some level of risk, including the potential loss of principal invested. Indexes and/or benchmarks are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment. Although stocks have historically outperformed bonds, they also have historically been more volatile. The securities of small capitalization companies are subject to higher volatility than larger, more established companies and may be less liquid. Bond investors should carefully consider risks such as interest rate risk, credit risk, securities lending, repurchase and reverse repurchase transaction risk. Greater risk is inherent in investing primarily in high yield bonds. They are subject to additional risks, such as limited liquidity and increased volatility. There is an inverse relationship between interest rates and bond prices. Investing in foreign securities is subject to certain risks not associated with domestic investing such as currency fluctuations and changes in political and economic conditions. Specific sector investing such as real estate can be subject to different and greater risks than more diversified investments. Declines in the value of real estate, economic conditions, property taxes and tax laws and interest rates all present potential risks to real estate investments.

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