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Happy New Year! May we all enjoy a healthy, calmer and more profitable 2009. The holidays are a good time to reflect upon where we have been, to reason where we are going and to set a prudent course for the future. We would like to take this opportunity to share our thoughts with you.

Last year the Standard & Poor's 500 Index (S&P 500) was down 38%, its worst performance since 1931. Though we outperformed the market in 2008 by a wide margin as we have for the past five and ten years, it is small consolation for the fact that our client's portfolios' suffered as a result of the market collapse in general and the credit crisis in particular.

Our concern for the economy caused us to reduce our common stock holdings in the summer of 2007. We then began adding bonds and preferred stocks, as we have many times during our 35 years in business, to achieve good income with minimal risk. What we did not foresee was the sudden and severe credit crisis that developed during the fall. The impact of the credit crisis accounted for much of the drop in our portfolio values during 2008. On the plus side, the bonds and preferred stocks we own continue to pay interest and dividends, and most of these positions are well off their recent lows and near or approaching the price we paid.

The economy, on the other hand, entered what will almost certainly be the worst recession since the 1930's. Employment (people with jobs) was down 2.6 million last year and could drop another two million this year. Corporate earnings were down 43% in 2008 and the latest estimates, which are often optimistic, indicate a further decline of 12% for 2009. Housing prices were down 20% in the year to October (latest available) and commercial real estate fundamentals are weakening. Finally, all of the developed economies in the world are also in recession, particularly Europe and Japan, which does not help.

As to the "trillion" dollar question - when will this end? The consensus, which may be optimistic, is that our economy will bottom out toward the end of this year while home prices may not bottom out until 2010. The loss of value in U.S. investments and home prices means the recovery could take longer and be more gradual than any since World War II. Twenty-five years of living beyond our means (on credit) will not be corrected quickly or easily. The exporting nations of the world (China, Germany and Japan) can help by stimulating their domestic consumption. In any case, a healthy recovery will come to pass; the United States has been one of the most resilient economies in history. In the mean time, the stock market, a leading indicator, normally bottoms out six months or so before the economy. Signs of progress we are looking for include:

- An easing of credit. The rise in prices for corporate bonds and preferred stock indicates that this process has begun. Conversely, the record low returns on U.S. Treasury securities, the safe haven du jour, indicates we still have a ways to go.

- Lower market volatility. The volatility index is now half of last year's record high but still twice its long term average value.
- Less mutual and hedge fund redemptions which were heavier than normal in December.

We are convinced that many good investment opportunities will arise as the economy and markets stabilize. We will take advantage of these opportunities by carefully analyzing the business fundamentals and evolving conditions to determine true values. This is what we do and why we are in business. Our extensive research and patience have provided our clients' with a 39% return since the turn of the century. Over the same period, the S&P 500 lost 37% while the NASDAQ plummeted 60%.

Please call us if you have any questions or wish to discuss our philosophy and strategy. We look forward to working with you in 2009 and beyond.