Robshaw & Julian Associates, Inc.
Trusted Investment Advice Since 1979

Investment Matters

For the quarter ended December 31, 2008

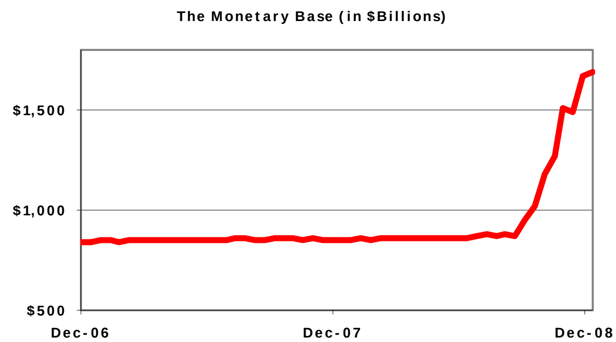
The End of the World or a Great Investment Opportunity?

The similarities between today's economic situation and the beginnings of the Great Depression are sobering. Both were preceded by low inflation, low taxes, excessive borrowing and outlandish speculation. Both involved precipitous stock market declines and widespread failures in the financial system.

The crucial question for investors today is whether the economy will recover normally or fall into a new depression. The 1929 crash was just the beginning of the stock market slide. In 1930, 1931 and 1932 stocks dropped 23%, 42% and 9% respectively. If a depression is coming, stocks could go much lower than they are today.

This is extremely unlikely. The Great Depression was not inevitable. The downturn which resulted from the economic excesses of the 1920's was allowed to snowball into a depression as a result of government policy errors—errors which are not being repeated today.

The most important error was by the Federal Reserve. Fearing a return of speculation, the Fed did not expand the money supply. With money in short supply, prices plummeted. One-by-one banks failed, businesses closed and jobs were lost. By



THE FED ALMOST DOUBLED THE MONETARY BASE IN JUST THREE MONTHS

the time debt-financed government spending programs were in place during the Roosevelt administration, a deflationary spiral was in place, and nothing short of war could reverse it.

President Hoover and congress added to the problem by enacting the Smoot-Hawley Tariff in 1930 and by raising the top income tax bracket from 25% to 63% (Roosevelt later raised it to 79%!). The tariff led to an international trade war which further depressed economic activity. The high tax rate discouraged investment (capital investment dropped 80% in three years), which was needed to create jobs

Today the Fed is taking the opposite approach. During the past three months the Federal Reserve has almost doubled the size of the monetary base. In addition to flooding the economy with money, the Fed and the Treasury are doing almost everything possible to prop up the financial system.

Although President-elect Obama promised to raise the top income tax rate, recent developments suggest this will be deferred until the end of 2010 when the Bush tax cuts expire. Trade, which is a far larger part of the U.S. economy than in 1930, has not degenerated due to protectionist measures, although this bears watching.

Based on hard-earned lessons from the past, we expect a normal cyclical recovery in stocks and the economy beginning this year.

Dividend Stability

In the past ten years, total returns from stocks have been negative, even before accounting for inflation. In the same period, the stock market has declined 50%—twice! One might assume that investors who live on dividend income from their stock portfolios would be struggling to make ends meet. It's not necessarily true.

The reason is that dividend payments are much more stable than stock prices. At the end of 1998 companies in the Standard & Poors 500 Index paid $16 in dividends. Today, the same companies pay $27, an annual increase of about 5%. This was about twice the rate of inflation over the last ten years.

While it's certainly possible that dividend payments could be reduced, history shows this seldom happens. Stock dividends were cut in half during the Great Depression, but they have risen steadily ever since and at a rate nearly twice that of inflation.

Financial planners recommend that retired investors take only about 4-5% out of their portfolios to live on every year, giving themselves an annual increase based on inflation. Right now a diversified portfolio of good quality stocks paying 4-5% would be easy to assemble. This portfolio would provide all the income an investor needs, even if stocks remain

Continued on page 2.

Dividends: continued

volatile or take years to recover.

It seems paradoxical, but for the investor looking for retirement income, a high quality, diversified stock portfolio may be a promising route to security. and peace of mind.

For every dollar in the stock market there is 48 cents in money market funds, the highest percentage in 30 years.

Including the last quarter of 2008, there have been only four quarterly declines in the stock market of more than 20% in the last 58 years. Returns in the following two years were 20% per year or more.

Enduring Market Wisdom

Over four decades, from his post as a technical market analyst with Merrill Lynch, Bob Farrell observed the ups and downs of financial markets. His "Ten Market Rules to Remember" is considered a classic and may be helpful in considering the current situation.

1. *Markets tend to return to the mean over time.* Prices neither grow to the sky nor descend into a bottomless pit.
2. *Excesses in one direction lead to excesses in the other.* Markets are self-correcting.
3. *There are no new eras -- excesses are never permanent.* Sir John Templeton once said that the four most dangerous words in investing are, "It's different this time."
4. *Exponentially rapidly rising or falling markets usually go further than you think, but they do not correct by going sideways.* Big ups are followed by big downs and vice versa.
5. *The public buys the most at the top and the least at the bottom.* Uninformed investors tend to follow the crowd.
6. *Fear and greed are stronger than long term resolve.* Easy to remember; hard to apply.
7. *Markets are strongest when they are broad and weakest when they narrow to a handful of blue-chip names.* The 1999-2000 boom is the best example. The bull market was largely limited to large cap technology companies.
8. *Bear markets have three stages—sharp down, reflexive rebound and a drawn-out fundamental downtrend.* Reflexive rebounds are often quite large but fundamental problems need to be resolved before a true bull market returns.
9. *When all the experts and forecasters agree – something else is going to happen.* Even if you believe this, it's hard to buck the experts.
10. *Bull markets are more fun than bear markets.* Bob is a regular guy. He loved his work and it showed.

Bob's ten rules focus on developing a long term plan and sticking with it through thick and thin. Be aware of how strong emotions can lead to bad investment decisions. Be a contrarian, never let the crowd influence your decisions. Think for yourself.

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On December 23rd President Bush signed a law which exempts most IRAs from the requirement to take a minimum distribution in 2009. See your financial advisor to determine how this may affect your IRA.

The Bottom Line: 12/31/2008

Market Indicator	Current Value	One Year Change
Large company stocks *(S&P 500 Index)*	903	-37.0%
Small company stocks *(S&P Small Cap Index)*	269	-31.1%
Short term interest rates *(3 Month T-Bill Yield)*	0.3%	From 3.2%
Long term interest rates *(10 Year T-Bond Yield)*	2.2%	From 4.2%
Inflation *(Consumer Price Index)*	213.1	+1.1%
Energy *(West Texas Intermediate Crude Oil)*	$44.60/bbl.	-54%
The economy *(Inflation adjusted GDP)*	14.4 trillion	0.8%

QUOTABLE

"I contend that for a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle."

Winston Churchill

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