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AT A GLANCE

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Bond Market Overview

Happy New Year! Or maybe better put — “Happy that the Old Year is Gone!” From an investment standpoint, we have never been quite so happy to usher out an old year and look forward to a New Year.

A Year of Worst

The year 2008 was a record setting year of worsts as everyone that has opened an investment statement knows. We will run down a few of the “worsts” to put the year in perspective: The S&P 500 stock index was down 38.5% in 2008 which made it the worst year since 1937 and the third worst in 100 years. 2008 was the worst year ever for the 37-year old NASDAQ Composite which fell 40.5% including the 39.3% fall in 2000 after the tech-stock bubble burst. International markets performed even worse as established international markets fell 43.0% and emerging markets fell 50.0%. The average large-cap growth mutual fund was down 40.67% and the average intermediate fixed income fund was down 4.70% both as reported by Morningstar.

The carnage was almost impossible to fathom when looking at the performance of some well-known individual companies. GE fell 56% in 2008, Bank of America fell 63.14%, Citigroup fell 76%, Google 55.5%, Fannie Mae and Freddie Mac each fell 98% and AIG was down 97.3%. And then there were the renowned companies that vanished completely—Bear Stearns, Lehman Bros., and Merrill Lynch is now part of Bank of America.

The downturn brought the long-term stock market average gain (since 1927) down to 9.7% from 10.4% and, according to the Wall Street Journal, the 10-years ending 2008 are now the worst ever for large-cap stocks since 1827. The volatility of the past quarter was also brutal. Four of the worst day declines and two of the best day rises in the history of the Dow Jones Industrial Average took place in this quarter.

As we have discussed at length in previous newsletters and client letters, it was as if a light switch was turned off in the credit markets in September and October. Heading into 2008, we felt it was going to be a tough year for the investment markets and that investors would be rewarded for maintaining quality, but we had no idea the economy would come to an abrupt halt like it did.

Keep the Faith

Okay, we have proved our point—it was a tough year and there was almost no place to hide. For a few days in September when money markets came under significant pressure it appeared as if cash equivalents and CD's were no place to hide either.

We have written a lot about the fact that we believe it is important to stay invested at this point and not the time to be selling into this market. We are by no means calling a market bottom, and as we have also written, we believe we are in for a “long, hard [economic] slog.” However, it is illuminating to look at the activity of the market from the near-term bottom on November 20th. It is difficult to believe, but since that day through the last day of 2008, the S&P 500 is up 20.5%. The time period was much longer, but the results were similar during the Great Depression. The Dow Jones Industrial Average bottomed at 41, down from 381 in 1929. By 1937, the Dow had risen to 194—a 300%+ increase. To make money back, investors need to stay invested.

This is not to say that the market will move up in a straight line and we will not be rushing to move cash into stocks or move out of fixed income and into stocks. The economy will continue to suffer as the effects of a dramatic slowing of economic activity work their way through the system. The world is in the midst of a massive deleveraging and it will take time for credit to loosen up to the point that the economy begins to grow again. U.S. consumers will not be quick to lift the world out of recession as in recessions past.

During the past several years, consumers (and banks for that matter) used increasing amounts of debt to buy assets that are now falling in value. Consumers are now working as fast as possible to reduce the debt and get rid of the assets and increase their level of savings. There is an economic phrase called the “paradox of thrift” where, in a recession, increased savings and decreased borrowing and spending exacerbate

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the economic woes. Ultimately, the increased savings rate may lead Americans to once again live within their means, which is a good thing. However, in the near term, deleveraging involves less consumer spending and less lending by banks, two critical engines of growth.

After doing macroeconomic and sector research, we buy stocks based on several factors, the most important of which are our expectations of future corporate earnings growth compared to the company valuations. With the "paradox of thrift" already in full swing, decreased consumer spending has led to a fall in current and expected earnings growth driving the stock market down to current levels.

The good news is that the world is determined to move in unison to get us out of the depths of the economic crisis. Fed fund discount rates continue to be cut around the world and there have been some signs of thawing credit in interbank lending and demand for the highest grade of corporate bonds and other securities. Economists surveyed by the Wall Street Journal believe, on average, that the economy will continue to contract through June, and start growing again in the second half of 2009, albeit at a slower than normal rate.

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The Madoff Scandal

A quick word on the Madoff scandal. Hedge funds are not exactly our industry and we have always understood that hedge funds are not magical, but simply a much more poorly regulated investment vehicle. The crime perpetrated by Bernard Madoff, however, does not necessarily help the

reputation of our industry. While we have always been exceptionally transparent and honest in our dealings with clients, there are also several reasons why a firm like Howe & Rusling could not perpetrate fraud in this manner. The following is quoted directly from an independent third party, a Wall Street Journal article by Brett Arends, entitled "These Red Flags Can Signal a Ponzi Scheme."

"Still, there are other red flags. The key one: Look out for an investment manager who wants complete control of your money, and asks for checks to be made out to him or a company he controls. You are safest when the funds are held separately in custody at a big broker-dealer firm regulated by the Financial Industry Regulatory Authority and backed by the Securities Investor Protection Corporation. Get copies of your statements directly from the broker. If your adviser manages your investments, but the funds are actually held at, say, Charles Schwab or Fidelity, it's almost impossible for him or her to run a Ponzi scheme. Other scarlet signals? Any broker who "guarantees" investment performance, boasts a track record that looks amazing, or who tries to hustle you aggressively into investing. And double-check any investment record that looks too steady over the long term: Ponzis like to keep the boat steady to avoid redemptions."

You can count on the integrity of our systems (a third party reputable and strong custodian holds your investments) plus H&R operations staff and managers review and reconcile your custodian's statements. We are experiencing one of the worst breakdowns of investor psychology, which probably will be improving with the passage of time. FDR said it well during our Great Depression: "We have nothing to fear but fear itself." Although shaken, our financial institutions are strong, our corporate balance sheets for the most part are strong, and this current mess will sort itself out. The companies we own are strong leaders in their industries, and valuations are low to reasonable on an historic basis.

You May Waive Your IRA Required Minimum Distribution (RMD) for 2009

On December 23, "The Worker, Retiree, and Employer Recovery Act of 2008 was signed into law by President Bush. This new law will grant a temporary waiver of the required minimum distribution (RMD) from retirement accounts for the 2009 tax year only. The waiver would apply to individual retirement accounts (IRAs) and employer-provided contribution plans (QRPs, Keoghs, Individual 401(k)s, and 403(b)(7)s).

We suggest that you contact your tax accountant as soon as possible, to determine if you should waive your RMD amount for the 2009 tax year. Then, please let us know your plans, so that we can adjust our cash planning for your account and assist you with any paperwork you may need to complete.

Requirements for 2008 remained unchanged. So, clients who were over age 70 ½ in 2008 were required to take their RMD by December 31, 2008, and if they just turned 70 1/2 in 2008, they are still required to take their 1st RMD by April 1 2009.

We look forward to hearing from you very soon.

4th Quarter 2008 Bond Market Overview

From the bursting of the credit bubble, the markets begin the stabilization process

In our last newsletter we focused on the near collapse of the credit markets and some of the unprecedented events that led to the largest decline in corporate bond prices since the major indices began tracking performance statistics. The extraordinary Government intervention that we spoke of last quarter has continued and would appear to have had a positive impact on the credit markets as we can see from this past quarter's performance.

Start Date: 9/30/2008 End Date: 12/31/2008

Index	Return for Period
Intermediate U.S. Government / Credit	4.85%
U.S Treasury: Intermediate	6.45%
U.S. Agency: Intermediate	5.60%
U.S. MBS Agency Fixed Rate MBS	4.45%
Intermediate: Corporate	2.44%
Invest. Grade: Financial Institutions - Intermediate	6.72%
Invest. Grade: Utility	-0.10%
Invest. Grade: Industrial - Intermediate	-0.79%
Municipal Bond: 1-10 Yr Blend (1-12)	3.02%

Source: Barclays Capital, Inc, 2008

While the best performing sectors were still government bonds, it is encouraging to see that the financial sector of corporate bonds has shown tremendous improvement. In the 3rd quarter, performance of the financial sector was approximately -14% while this past quarter the financial institutions sector returned 6.7% and 8.1% for intermediate and all maturities respectively. Some of the best performing sectors were also bonds of longer maturities as expectations for inflation have given way to increased expectations of deflation.

Best Performing Sectors

Start Date: 9/30/2008 End Date: 12/31/2008

Index	Return for Period
U.S. Long Government/Credit	13.06%
U.S. Treasury	8.75%
Invest. Grade: Financial Institutions	8.07%
U.S. Government	8.05%
U.S. Gov/Credit: 5-10 Yr.	7.23%

Source: Barclays Capital, Inc, 2008

Now that the NBER (National Bureau of Economic Research) has officially declared a recession dating back to the 4th quarter of 2007 and short-term rates are approaching ZERO, the demand for bonds of longer maturity has increased. Conversely, bonds of shorter maturity have lagged in price appreciation as a result of the pessimistic expectations for economic growth which has currently dampened inflationary price pressures.

Worst Performing Sectors

Start Date: 9/30/2008 End Date: 12/31/2008

Index	Return for Period
Invest. Grade: Utility	-0.10%
Invest. Grade: Industrial	1.58%
1-3 Yr Gov/Credit	2.68%
1-5 Yr Gov/Credit	3.60%
Foreign Local Government	3.61%

Source: Barclays Capital, Inc, 2008

Trying to fully explain how our economy (and to a greater extent the global economy) is reacting to the monetary and fiscal stimulus that is being injected into the capital markets is nearly impossible. The short-term objectives of the economic stimulus are fairly clear: Stabilize the credit markets and create increased demand for investment and consumption. However, the longer term consequences of the stimulus are far from known. Just as low interest rates earlier in this decade facilitated excess consumption and an increased debt burden on the entire economy, the current stimulus may have unintended consequences that are not clear now. Right now the most important belief is that we have avoided a severe credit collapse that parallels that of the 1930's.

Is Government intervention helping or hurting the economy?

The immediate response would have to be that some of the fiscal and monetary policies are indeed helping our economy by preventing a bad situation from getting worse. Perhaps the two most important programs that have positively affected the credit markets with added liquidity are the Federal Reserve Bank's Commercial Paper Funding Facility and the FDIC's Temporary Loan Guarantee Program. The commercial paper funding facility is designed to support issuers that use this short-term borrowing market for working capital needs.

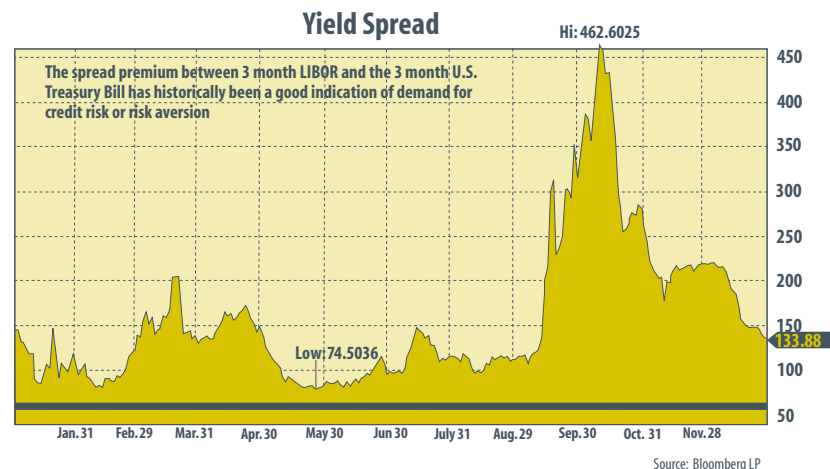
Working capital is needed by just about every company in its day-to-day operation. Because it is not always practical or possible for companies to perfectly anticipate when revenues are received many fund themselves through the use of these programs to meet some of the most basic obligations like payroll. After the events of this past September, this market virtually ceased to function. Many companies had to rely on using their existing lines of credit with their banks; and in many instances banks were reluctant to lend. So, the commercial paper funding program was extremely important in ensuring our economy did not completely "seize up."

Another major issue facing our banking system and economy was the inter-bank lending market. After the default of Lehman Brothers and the subsequent events that raised doubts about

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the solvency of other banks and brokers, many banks stopped lending to each other. Interest rates that banks charged each other for overnight loans became excessive in an effort to discourage borrowing. One of the most commonly monitored short-term interbank lending rates is the London Inter Bank Offered Rate (LIBOR). Through the FDIC's Temporary Loan Guarantee program the government is basically insuring against the default of banks within the system.

We can see from the following chart the spread differential between 3 Month LIBOR and the 3 Month U.S. Treasury bill for all of 2008. The risk aversion and premium yield that investors require to assume credit risk reached an all time high of 462 basis points (4.62%) over the risk-free Treasury bill. Consider that the comparison is for a short-term investment of 3 months and spreads for bonds of longer maturity would be significantly greater. Notice also that the horizontal line is the average spread between these two interest rates over a 25 year period and normally is little more than 0.50% (50 basis points).



While the spread premium is still relatively high, we are encouraged by the decrease in the risk premium between the two rates cited. The decreased risk aversion exhibited by the reduced spread, as well as the stronger performance of the financial institution sector of the corporate bond market, is directly attributable to the government's efforts to support inter-bank lending.

The concerns we have about government intervention relate to the uncertainty of how the markets will react once the government removes the stimulus and discontinues its direct participation in the capital markets. Another uncertainty we have is to the timing of the government's withdrawal from direct market participation. The key to achieving greater clarity about the government's exit from the capital market is subject to the return to health of the banking system and renewed confidence and trust in our financial institutions.

In our opinion the banking system will continue to face pressures in 2009 as the recession will lead to higher unemployment and increased delinquencies and loan defaults. There will be renewed regulatory scrutiny and pressure for banks to consolidate. We would expect Congress to continue its questioning of how public monies have been invested in our ailing banking system and whether these capital investments through the Troubled Asset Relief Plan (TARP) have benefitted the general public and not just the shareholders of troubled banks.

The uncertainties are indeed many, but we do believe the large banks will continue to be very selective with lending in the near future while they continue to restructure their balance sheets. There is a misperception that banks are unwilling to lend. It is in their best interest to lend. However, to whom they lend is a different matter and at the moment the greatest demand for credit is most likely coming from consumers and businesses that are greater credit risks. It is our opinion that

the added stimulus in our economy is intended to encourage investment and consumption from those who are not currently overindebted. Further debt and consumption by those who can least afford it does not make sound economic sense.

In conclusion, the continued stability of the credit markets depends on not only our own domestic monetary

and fiscal policies, but also those of other major economies worldwide. We can't fully discount what effects worsening economic conditions in other parts of the world will have on our own economy. To be sure we are in the short-term, benefitting from uncertainties in other parts of the world with increased capital inflows from foreign investors. This is evident by the increased value of the U.S. dollar versus the Euro but less so versus the Japanese yen. If this continues (or for how long) is a key in our own economic health longer term. We are still a very wealthy nation even though some of that wealth has "evaporated". Our economy is now performing below its potential. This state will be reversing, but who knows when? We are confident that this recovery will occur once this cycle has run its course.