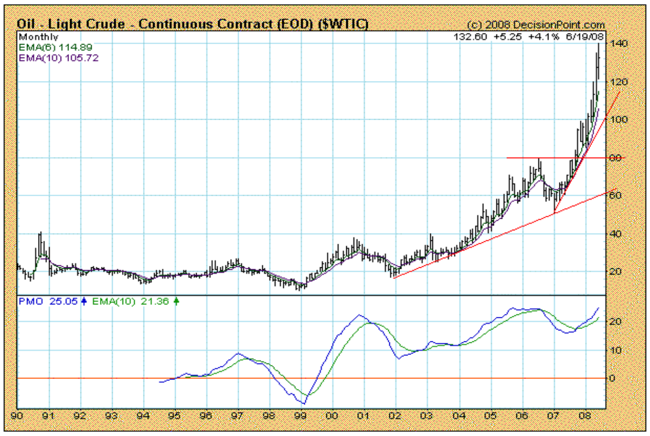
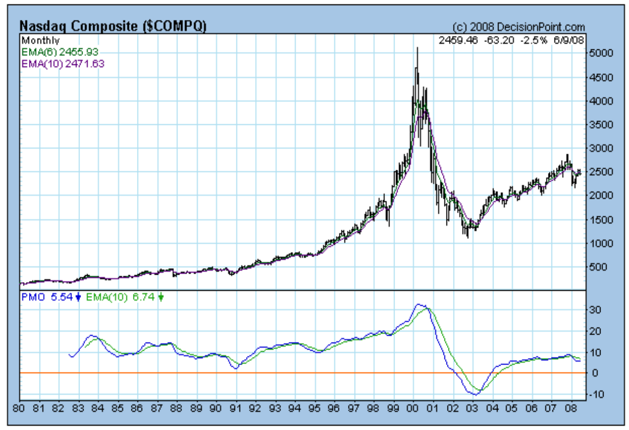
QUARTERLY INVESTMENT COMMENTARY
SECOND QUARTER 2008

Major Market Indices
Percentage Changes: Quarter Y-T-D
Dow Jones Industrial Average: -6.73%; -13.0%
S&P 500 Index: -2.67%; -11.7%

An American Hero. Close your eyes and imagine…….you're in an Air Force fighter jet in the final stages of World War II. Your job - soften up Nazi strongholds at Normandy Beach before the impending invasion of allied troops. It's June 6, 1944 and enemy anti-aircraft artillery are making failed attempts to knock you out of the air. I have a hard time imagining those events. But in a cozy bar on Marco Island, Florida I met a kindly old gentleman who not only could imagine those events, he was actually there! So, over the course of way too many beers he entertained us with thrilling tales of World War II heroics. Pictured with my better half Barb (left) and our good friend, Joyce, is Dick Thackston, 84 years young. A mere 67 years ago Dick, forging a birth certificate, enlisted in the Air Force at the ripe young age of 17. Stationed in Britain, he flew in more than 40 bombing missions including Dresden, Normandy and Berlin. He talked about knowing a swashbuckling war hero by the name of Clark Gable who told stories to the troops far into the night. His commanding officer was Jimmy Stewart whom he described as a "no-nonsense" guy and a real patriot, something you don't see very often in Hollywood these days. I asked him to relate his closest encounter with death. He answered – "every time I climbed into the cockpit!" According to Dick, we almost lost the war, the war was about a "pick-em" up until D-day. Fortunately, the Germans finally ran out of gas, literally (fuel), and succumbed to the overwhelming effort of our guys. Dick Thackston, Clarke Gable, Jimmy Stewart…… these guys were the real deal!! Dick, it was a pleasure to meet you. Thanks for all you did for us!

The Case for Lower Oil Prices. I'll go out on a limb here, and make a call for lower oil prices in the near future. I'll even invite the possibility of being wrong on a massive scale by predicting not only a decline in the price, but a sharp, vertical decline. Currently both the forces of supply and demand are working in favor of lower prices. New supply sources (both existing and potential sources) coming on stream are significant – Saudi Arabia pumping out an extra 500,000+ barrels a day, increasing Iraqi production levels (up 25% year-over-year), Nigeria production increasing (200,000 barrels per day), Canadian oil sands bringing progressively greater supplies into the market, potential for monster reserves such as Colorado oil shale, conversion of natural gas to liquid fuel. The list of increasing supply sources goes on and on. Meanwhile, demand destruction is occurring as higher prices are finally causing behavioral changes by consumers. These changes include massive car-pooling efforts underway within government institutions, sharply increasing mass-transit usage, an implosion in the market for gas-guzzling SUVs, super fuel-efficient automobile technologies becoming available (witness the 300 MPG Aptera available in California, and imminently available 100 MPG+ plug-in hybrids), etc. In addition to actual supply and demand factors, I would also note that the upward trend in the price of oil is now mature (six years old) and has gone parabolic (definition - prices rising in an accelerating upward curve that eventually becomes near vertical). Parabolic price trends are a reliable sign that price is in the process of topping out. Lastly, investor sentiment is super-bullish on oil, with the usual emergence of latecomers to the move, and analysts falling all over themselves to raise their price targets. The angle of ascent of the price of oil resembles the straight-up parabolic price pattern of the NASDAQ index in early 2000 (see similar chart patterns below), as does the "off-the-charts" bullish sentiment. Parabolic price spikes tend to end the same way, by dropping vertically when the price trend eventually reverses – I fully expect the drop in oil to resemble the magnitude of the NASDAQ drop of 2000-2002.





Bear Market Scorecard. In April of this year, I reported that we were in a bear market that began in October 2007, and that it was roughly half over at that time. I noted that while early signs of an end to the bear market were beginning to emerge, I would also caution that, as the great Yogi Berra wisely stated – "it ain't over till it's over". The second quarter 2008 contained a sharp bear market rally that carried the DOW nearly 10% to over 13,000 in late May before dropping sharply to a new bear market low at the end of June. Investor psychology has deteriorated to new lows as sentiment indicators have moved overwhelmingly to the bearish side – an eventual bullish setup. For instance, at month-end, the investor poll of The American Association of Individual Investors had dropped to 31% bulls/ 52% bears. From an anecdotal standpoint, several days ago I took special note of an "Armageddon" type of forecast issued by The Royal Bank of Scotland (RBS) who stated that the S&P 500 was set to plunge 25% by September. While recognizing that RBS just might be right, I quickly referred back to my own internal notes on "bear market phase III behavior". I found the notation that you will know you have entered bear phase III when you begin to hear statements like "The DOW will be cut in half again within 6 months". The dire RBS forecast meets this requirement. In addition, I have noted much discussion on CNBC as to both the virtues and techniques of short-selling. Again, referring to my internal notes I find that "bear phase III is marked by a rise in the quantity of new short-sellers, those shorting on obviously bad news/ shorting is now too popular to be the correct thing to do". The type of rhetoric echoed by RBS and discussed on CNBC is an alert to me that it is getting late in the bear cycle, likely having progressed into phase III. However being *late* in the bear cycle, and being at the *end* of the bear cycle are two different things. Being early in increasing one's level of aggressiveness could prove to be costly, since losses are most severe at the end of the bear move, as final capitulation of the buy-and-hold crowd occurs. I would offer the opinion that the financial sector (investment banks, lending institutions, etc.) already is in the process of capitulation. Also, market internals have not yet stabilized as evidenced by the operating company advance-decline line which has dropped sharply during June. So while I think the bear trend has progressed in predictable fashion and is maturing to an inevitable conclusion, I would not be confident that the bear move is over until psychological phase III (characterized by investor panic and capitulation) accompanied by stabilized market internals has been fully revealed.

The fundamental background has an eventual bullish resolution if just the above predicted implosion in energy prices were to take place. A huge amount of capital will likely exit the over-crowded energy trade and find its way to the stock market. Additionally, general level of valuations is good and dividend yields are improving due to lower stock prices and still-improving dividend payout rates. I believe there is a major reward lying just on the other side of "bear" valley in the not-too-distant future. But patience is a virtue at the moment.