INVESTMENTS, INC.

MarketView

Fourth Quarter 2008

"Despite the headlines proclaiming the next Great Depression, this is no Great Depression—only a panic helped along by the short-term mindset of the financial industry. Financial media's job is to attract readership by sensationalizing news events, and financial institutions, which are built on commissions and fees, want to keep money moving in and out in order to bulk up their own revenues. So both fan the flames of panic."

The Motley Fool, October 8, 2008.

Standard and Poors 500 index returns, events and days to recover

Credit Suisse Research 2008

Number	Date	Days to Recover	Return	Event/Concerns
1	1/8/1988	22	-6.8%	NA
2	4/14/1988	23	-4.3%	NA
3	10/13/1989	22	-6.1%	NA
4	11/15/1991	22	-3.7%	NA
5	3/8/1996	17	-3.1%	Corresponding rout in bond market
6	10/27/1997	8	-6.9%	Concerns that slumping Asian economies to hurt US
7	8/4/1998	39	-3.6%	Asia economic woes to cut US corporate profit
8	9/30/1998	10	-6.8%	Russia devlaued currency and defaulted on debt
9	1/4/2000	13	-3.0%	Slowing US economy. Economic slowdowns abroad.
10	2/18/2000	5	-3.8%	Fed to raise interest rates to fight inflation
11	4/14/2000	10	-3.0%	Rising interest rate to hurt corporate profit
12	12/20/2000	3	-5.8%	Optimism exceeded valuation. Inflation pressures.
13	3/12/2001	3	-3.1%	Slowing economy taking its toll on profit growth
14	4/3/2001	24	-4.3%	Economic slowdown extending beyond tech sector
15	9/17/2001	3	-3.4%	Slumping corporate profits
16	7/10/2002	19	-4.9%	September 11th
17	7/19/2002	26	-3.4%	Accounting scandals. Slack profit growth
18	8/5/2002	7	-3.8%	Regulatory probes. Accounting scandals & low EPS forecasts
19	9/3/2002	3	-3.4%	Stagnant economic indicators. Recession fears.
20	9/19/2002	33	-4.2%	Slow economy, low earnings. Weak European & Asian markets
21	9/27/2002	19	-3.0%	Cut sales and earning forecasts across industries.
22	3/24/2002	13	-3.2%	Prolonged earnings misses caps worst quarter since '87
23	3/24/2003	21	-3.5%	Iraq War to last longer than expected
24	2/27/2007	22	-3.5%	Chinese equities fall by 9.2%
25	2/5/2008	15	-3.2%	Monolines downgraded. Service industries fall.
26	6/6/2008	38	-3.1%	Oil price goes over $138. Unemployment beats consensus
27	10/2/2008	N/A	-4.0%	"Bailout" approved
28	10/6/2008	N/A	-3.9%	Post bailout. Turbulence continues
29	10/7/2008	N/A	-5.7%	Post bailout. Turbulence continues
30	10/8/2008	N/A	-1.1%	Post bailout. Turbulence continues
31	10/9/2008	N/A	-7.6%	Short-selling ban lifted. Market ponders the Treasury's potential issuing of preferred stock

GS Investments, Inc.

Largest Stock Holdings

9/30/2008

Securities	Pct.
Ishares Trust MSCI EAFE Index Fund	2.83%
Wells Fargo Bank , NA	2.39%
US Bancorporation	2.03%
McDonald's Corporation	1.87%
Proctor and Gamble Company	1.80%
Johnson and Johnson Company	1.67%
Express Scripts, Incorporated	1.67%
PepsiCo Incorporated	1.62%
Wal Mart Stores Incorporated	1.61%
Stryker Corporation	1.50%

Here we go again

Despite the passage of the "bailout" package last Friday by the House and Senate, the market continued its precipitous decline. The S&P 500 index has fallen 18.35% in October alone led by the Financial and Energy sectors which fell 14% and 12%, respectively. Only three companies out of the 500 advanced over the 4-day period. September 29th, 2008 was the worst day in terms of performance for the index since the market crash of 1987; October 2 and October 6 are in the top ten as well.

To put this move in perspective, declines of greater than

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4% have happened just 13 times since 1988 – giving this move a probability of less than 1 in 436. Here, we look at the daily market returns for the last twenty years to get some insight into the magnitude of the move that we have just seen.

Since 1990, the S&P 500 has had 26 instances of a daily drop greater than 3%. Take heart, however as the average time taken by the index to recover to its pre-crash level after a single day drop of greater than 3% is 17 days.

Finally, we provide a list of such dates with corresponding events and concerns to explain the sudden crash. Examining the 26 market crashes over the last 20 years, we observe that recent market crashes tend to be driven more by fear reaction and speculation rather than abrupt changes in fundamentals or economic indicators.

At the heart of the "bailout" - Fannie and Freddie and CRA

By now you have heard multiple reasons for the 2008 market collapse. To be sure the fingers from each political party have and will continue to be pointed at one another from 'across the isle.' Many in the media blame the greed of Wall Street and 'deregulation' as the primary culprits behind the chaos that now surrounds us. Although Wall Street greed and de-regulation (of the financial services industry) are partly to blame, much of what currently ails the US economy is due to the absence of regulation, specifically as it relates to Fannie Mae and Freddie Mac.

In 1938 millions of families could not become homeowners, or risked losing their homes due to a lack of a consistent supply of mortgage funds across America. As a result, President Franklin D. Roosevelt helped to create Fannie Mae. Its purpose was to expand the flow of mortgage funds in all communities, at all times, under all economic conditions, and to help lower the costs to buy a home.

Initially, Fannie Mae operated like a national savings and loan, allowing local banks to charge low interest rates on mortgages for the benefit of the home buyer. This led to the development of what is now the secondary mortgage market. Here, companies such as Fannie Mae have been able to borrow money from investors at low interest rates because of the financial support that they (the investors) receive from the Federal Government. It is the ability to borrow at low rates that allows Fannie Mae to provide fixed interest rate mortgages with low down payments to home buyers.

For the first 30 years, Fannie Mae held a veritable monopoly over the secondary mortgage market. Due to fiscal pressures created by the Vietnam War in 1968, Fannie Mae was privatized by Lyndon B. Johnson and removed from the national budget.

In order to prevent Fannie Mae from becoming the sole monopolistic entity in the secondary mortgage market, Freddie Mac (previously titled Federal Home Loan Mortgage Company) was created in 1970. Like Fannie Mae, Freddie Mac sought to improve the quality of life by making the American dream of decent, accessible housing a reality. The hope was to link "Main Street" to "Wall Street" by purchasing, securitizing and investing in home mortgages, and ultimately providing homeowners and renters with lower housing costs and better access to home financing.

From this point forward, Fannie (and Freddie in 1970) began operating as government sponsored enterprises (GSEs), generating profits for the shareholders while enjoying the benefits of exemption from taxation and oversight as well as implied government backing. Despite numerous attempts to introduce oversight and regulation, the House Finance Services and Senate Banking Committees, have been unwilling to "get involved."

Lastly, the government-created Community Reinvestment Act (CRA) of 1977, prohibited banks/financial institutions from employing 'discriminatory' or 'red-line' lending practices, thereby forcing them to lend money to those

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who could not re-pay the loans.
Fast forward to September, 2008. The combined assets of Fannie and Freddie were 45% greater than those of the largest bank in the United States. Their combined debt represented 46% of the national debt in the United States.

Additionally, Freddie and Fannie were the only two Fortune 500 companies that were not required to inform the public of any financial difficulties they had been experiencing.

Lastly, add to this this the hundreds of millions of dollars in loans granted by banks that have been written down or off (CRA and non-CRA loans) and one has concocted the perfect recipe for disaster. In short, this is yet another chapter in the well-intentioned, yet ill-fated "New Deal" shop of horrors. Three things seem certain. First, we have yet to realize the full scope and depth of the "credit" problem at hand. Second, the American taxpayer is officially "on the hook" for most of it, including the recently approved $700 billion bailout. Third, the federal government will now be in charge, to a large extent, of both the mortgage and banking industries; Webster defines this as classic Socialism. The last time we looked, this reviewed our basic definition Frightening prospects, one and all.

ECONOMIC FORECASTS	
↓	**GDP growth** A sluggish 1% in '09
↔	**Interest rates** Prime interest rate falling to 4.5% in '09, 10-Year T-Notes yielding 4.25%
↓	**Inflation** Moderating in coming months
↑	**Job growth** Fewer monthly losses in '09
↓	**Crude oil** Averaging $100/barrel in '09
↑	**Housing sales** A small pickup during '09
↓	**Retail Sales Growth** Around 1% next year
↓	**Trade deficit** Just over 3% of GDP in '09

Source: Kiplinger

'Market to market' accounting and its effect on the market

Loans and securities make up the bulk of a bank's assets. As such, the method the bank uses to establish values for these securities when preparing its financial statements affects shareholders' equity. (Shareholders' equity = assets – liabilities, remember?) This, in turn, has an effect on a bank's profit and loss statement. This is also true for insurance companies.

Mark-to-market accounting sets the value of (or "marks") of assets (loans) on the balance sheet to reflect the "market" or "selling" price of the asset. This may sound simple but it's not.

Not all securities are as liquid as Microsoft shares, for which anyone can look up the price on the Internet at any given moment. Some mortgage securities may not even trade once a day; how do you price them?

The problem with mark-to-market accounting is that the valuation methodology relies on the notion that the market is an asset's best arbiter of value. Most of the time, this is a fair assumption, but it breaks down in a market crisis as we have recently witnessed (AIG in particular).

Why is this issue so important? Because auditors, obligated to 'sign-off' on the corporate books and records of the banks/financial services companies they review, can mandate potentially exaggerated write-downs of company assets. Earnings then disappear as does a good portion of the strength of the institution's balance sheet.

When this happens, the rating agencies (Moody's and Standard and Poors, in particular) move in and reduce the 'rating' of the affected institution. In many cases, the reduction in rating results in a loss of the company's 'investment grade' status. Subsequently, the bonds of these institutions must be sold as they are no longer compliant with many investment policy statements. Company stock suffers as well as rating decreases push valuations down.

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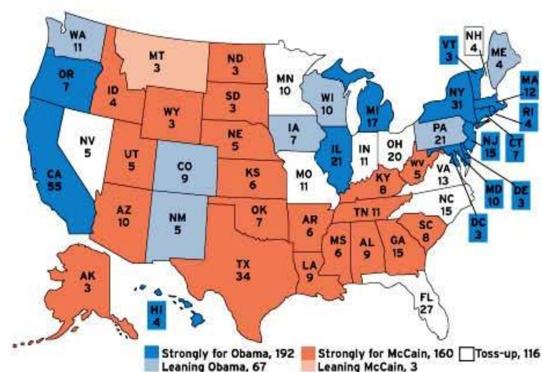
Selling of both bonds and stocks intensifies. The valuation of the affected institutions decreases as well, forcing the company to seek capital infusions in an effort to meet its liquidity demands. The result is a vicious downward spiral, much like we are witnessing today.

This has become such a pressing issue that the Financial Accounting Standards Board (FASB) and the SEC issued a recent clarification of the accounting rule known as FAS 157, saying that the price of "disorderly" trades (distressed selling or forced liquidations) isn't "determinative" when measuring fair value. It is our opinion that serious consideration be given to changing or temporarily suspending the current mark-to-market rules that, in our opinion, have promoted the 'fire-selling' of many valuable, long-term assets in irrational fashion and have devastated the financial markets in the process.

So, where do we go from here?

Picture, if you will, a car (propelled by a combustible engine). Two things are required for the engine to run, oil and gasoline. The oil (liquidity) provides the engine with the lubrication necessary to keep it from seizing up. The gasoline (interest rates) give the engine the necessary energy to move the car.

In direct terms, the recent passage of the $700 billion bailout bill by the Senate and House represents the "oil." The simultaneous lowering of interest rates by the US, China, European Central Bank, Canada, Sweden and Switzerland, in addition to the reduced-tax effect of falling oil prices (from $147.27 on July 11 to $88.83 on October 8) represents the "gasoline." The length of response time required and the magnitude of the response is anyone's guess. Rest assured however, the 'car' is currently being overhauled and will drive again.



Source: Kiplinger

GSI Tenets

Who is GSI?

GS Investments, Inc. is an investment management company specializing in individual and institutional asset management. Privately owned and operated, GS Investments, Inc. is run by its two principals, Glenn H. Steinke, C.F.A., and John G. Steinke, M.B.A.

Glenn Steinke brings over 45 years of investment management experience to the business. Previous capacities include Vice President and Senior Investment Officer with a major pension fund ($1.8 billion under management) and Senior Vice President with a major Minneapolis-based financial institution ($3 billion under management).

John Steinke offers a broad financial services background with 14 years of portfolio management experience and 7 years of banking experience including capacities as a Vice President of a $50 million bank and as a private banking officer for a large, Minneapolis-based financial institution.

GSI Investment Philosophy

GS Investments, Inc. utilizes a balanced approach for the majority of its accounts although each account is tailored to the individual needs of each client. Taxable or tax-exempt bonds are used along with a common stock component. The division between bonds and stocks is determined by the personal objectives of each client. A need for income and a willingness to assume risk are also determinants of an account's bond/stock mix.

GS Investments, Inc. emphasizes the purchase of quality securities and employs a long-term investment style as market timing, frequent shifts in asset allocation and interest rate forecasting are not consistent with the firm's philosophy. In depth market analysis and many years of experience support this approach.

GSI Fixed Income Strategy

GS Investments, Inc. emphasizes a staggered maturity approach when purchasing bonds. Individual security investment grades and call protection are considered when making these investments. Quality grades of "A" or higher are favored with tax-exempt issues. Government bonds are dominant among taxable securities.

GSI Equity Strategy

GS Investments, Inc. favors stocks emphasizing quality and growth. Appropriate cyclical growth stocks and small capitalization growth stocks are used periodically as well. Additionally, GS Investments, Inc. believes that a growth oriented philosophy tends to result in less frequent trading and lower tax payments (for taxable accounts) on realized capital gains. This provides a lower cost approach for the client.

GS Investments, Inc. emphasizes client communication. Written investment objectives as well as periodic oral and written reports are used to heighten the understanding between the client and investment manager. In addition, easy to read, detailed reporting is provided by state of the art investment software in order to inform the client of portfolio progress.