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Advisory services offered through Optimus Advisory Group, a Registered Investment Advisor.

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Eight Baskets Portfolio Update & Market Commentary

Recap of 2008

There is no doubt about it, 2008 was a very challenging year. So many indices suffered incredible losses that I'm not sure I have enough room to disclose all of them.

According to MarketWatch.com, the Dow Jones Industrial Average dropped 34%, its worst showing since 1931, and the S&P 500 dropped 38.5%, its worst year since 1937.

In order of "best" to "worst," here are some other major asset classes and their 2008 performance (Source: Worden Brothers Telechart):

- World Gold Index +5.29%
- Dow Jones Corporate Bond +1.80%
- PHLX Gold/Silver Sector -28.52%
- US Small Cap Stocks: Russell 2000 -34.80%
- CRB (Commodity Research Bureau) -36.01%
- US Large Cap Stocks: S&P 500 -38.50%
- AMEX Int'l Market ADR Index -39.32%
- Nasdaq Composite -40.54%
- MSCI US REIT Index -41.51%
- Tokyo NIKKEI Index -42.12%
- AMEX Commodity Related Equities -42.20%
- European Top 100 Index -43.21%
- BONY Emerging Markets 50 ADR Index -49.94%
- Light Sweet Crude Oil -53.53%
- China: Shanghai Se Composite Index -65.39%

As noted, gold bullion and some bonds were the only bright spots during the year. Actually, other than US government bonds, most corporate bonds took a huge hit during the last third of the year, only bouncing back during the final several weeks of 2008. Also, any high yielding varieties of corporate bonds took extra large losses, with many taking hits equal to the US stock market in general.

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Unlike the last bear market of 2000-2002, diversification did not ride to the rescue. As noted above, REITs, commodities and precious metals were not exactly shooting out the lights. Fortunately, reducing risky asset exposure and hedging against major losses was the order of the day. Although the Eight Baskets Portfolios did suffer some losses, those losses were nothing compared to the overall global equity markets. Those second and third lines of defense made all the difference. I expect that those same techniques and tools may well be needed again in 2009 and beyond.

What to Expect in 2009

The 2009 forecast can be summed up in one word: Volatility. 2008 was marked with extended periods of gut-wrenching volatile markets, with multi-decade record up days and down days. Because of the volatility and insanity in September through November, we were tied to our computer monitors until the market closed at 1:00pm Pacific Time. Each early morning and late night was spent monitoring overseas markets for clues into what to expect in our markets here in the US. In order to get a better grasp of the financial crisis as it unfolded, countless hours were spent scouring the Internet for independent data and research articles. We expect 2009 to bring more of the same.

The list of trouble spots keeps growing. We have the possibility of municipal bond issuer defaults (including our beloved State of California), Emerging Market economies imploding (keep an eye on Eastern Europe and any countries reliant on natural resources exports), an endless line of US industry groups seeking government bailouts (including the US auto manufacturers coming back to the government trough very soon), Corporate Bond defaults, Commercial Real Estate defaults, continued declines of Residential Real Estate (especially here in Southern California)... the list goes on and on.

Investment Opportunities in 2009

Investing opportunities in 2009 depend on many factors. Deflation (falling prices, especially all types of Real Estate) and the government's attempts to stop the downward price spiral will bear continued monitoring. With both short-term and long-term interest rates at multi-decade lows, there isn't much upside left in US Government bonds. Consequently, we continue to look for opportunities to hedge against rising interest rates.

The US Dollar will continue to be an area for close scrutiny. After a multi-year collapse in the Dollar, the US currency staged a remarkable rally during the 2nd half of 2008. It has since lost its upward momentum, which may be a sign of either a trend change or just a brief rest. Thanks to the newer foreign currency exchange-traded funds (ETFs are funds that trade on regulated exchanges, like stocks), we have several investment possibilities. We can invest for a rising or falling US Dollar.

Commodities of every shade took a beating sometime in 2008. It was astounding to watch Crude Oil soar to nearly \$150 per barrel in the first half of 2008, only to completely collapse down to \$45 by year-end. If commodities stage a comeback rally sometime in 2009, that may present us with another avenue to pursue. As with the US Dollar, we have the capability to invest in rising or falling commodity prices.

Finally, we believe all equities (US, Foreign, REITs, Natural Resource stocks, etc.) will experience dramatic price changes throughout the year. All we really want are some kind of sustainable trends. With the ability to invest for up or down markets, what would benefit our portfolios most are trends that last several weeks to several months. Those type of moves present us with the greatest probability of success in capturing gains during those extended up or down moves.

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New low risk portfolio model for 2009

After a few client requests, I decided to develop a new low risk portfolio model. I had started working on it months ago, but the unprecedented financial crisis left me with very little time to finish the project. Now, with a bit of sanity briefly returning to the markets, I hope to finish testing the model portfolio this month.

The new model will be geared for low risk money, for those of you that want little to no stock market exposure, but are willing to take some risk in order to have the possibility of income and growth. Also, if demand warrants it, a tax-free model may be developed as well. Both the taxable and tax-free versions will be actively managed, which will be key in 2009 and beyond.

If you have an interest in either portfolio, please let us know.

Keeping watch,

Steve K. Rumsey
Eight Baskets Portfolios
Optimus Advisory Group

An Index is a portfolio of specific securities (common examples are S&P, DJIA, NASDAQ), the performance of which is often used as a benchmark in judging the relative performance of certain asset classes. Indexes are unmanaged portfolios and investors cannot invest directly in an index. Past performance is not indicative of future results.

Investors need to be aware that no investment plan/asset allocation can eliminate the risk of fluctuating prices and uncertain returns.

Figures quoted are for illustrative purposes only and are not necessarily indicative of past or future results of any specific investment. They do not include consideration of the time value of money, inflation, fluctuation in the principal of, and in many instances, taxes.

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