



"In the long run we can't continue to spend as if deficits don't have consequences, as if waste doesn't matter, as if the hard earned tax dollars of the American people can be treated like monopoly money, that's what we've seen time and time again, Washington has become more concerned about the next election than the next generation."

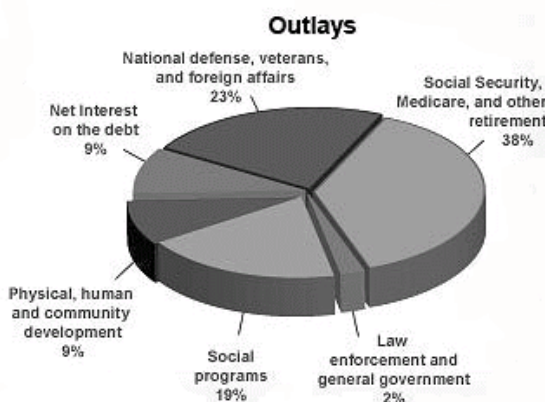
President Barack Obama, December 21, 2009, pretending to be President Ronald Reagan

The last decade was filled with important events and nonevents. One of the biggest nonevents was the whole Y2K scare that amounted to nothing more than a panic fabricated to sell software and computers. The entire fiasco forced those of us in the financial industry to develop written pre-catastrophe plans and post-catastrophe plans, run software tests and retests and generally waste tremendous amounts of time and money. I recall this episode because I just tossed the three-inch file filled with the evidence that I had complied with the rules.

Many commentators believe the seminal event of 2009 was Obama's inauguration. While all inaugurations are special, this one simply continues America's long history of electing presidents who are long on promise and short on delivery. My feeling is that Obama will be remembered less for his race than for his financial irresponsibility. On January 20, 2009, Obama's inauguration day, the Federal deficit was \$10.6 trillion. On January 1, 2010, the deficit had grown to \$12.2 trillion. That's more than \$1.5 trillion in less than a year of this administration. And that doesn't include the effects of the health care "reform" scheme working its way through the Congress. Don't forget the push for a second "stimulus" plan because the first one didn't work as expected.

"Oh yeah! Well, what about Bush?" President Bush takes lots of heat for today's financial problems. After all, his deficit tally was a near doubling of the debt from \$5.7 trillion when he took office to \$10.7 trillion at the end of his eight years. Included on his watch was 9/11, the start of a war in Iraq and the financial excess that led to the 2008 financial system meltdown. To counter, many Democrat commentators on TV talk about the "Clinton surplus" as evidence that the Clinton years were fiscally responsible ones. Unfortunately, the debt grew from \$4.2 trillion to \$5.7 trillion while he was in office. It seems that facts never get in the way of a good myth.

We finished the decade with a criminal event on a Northwest jet that the chattering classes refuse to recognize as a terrorist attack. Obama himself said the "alleged" bomber had been "charged" with attempting to blow up an airplane. These are lightning words for me. "Charged" means the criminal has been read his rights and is now in the middle of a legal cat fight where he will plead "not guilty" and plug the court system for years. We can't get any information from the "suspect" because he may incriminate himself and anything he says can be used against him. Even though he knows of future attacks, this non citizen is being afforded all the Constitutional protections of a citizen. "Alleged" is the most overused word on TV and it belongs in a courtroom, not in the media. What is "alleged" when a plane passenger is tackled after setting his crotch on fire ten minutes from landing? Someone on the plane had a smoking lap and I think it would be very easy to spot that person. What is "alleged" when an Army major shoots up Fort Hood, killing or wounding forty-two people, getting shot himself, gets treated to the best medical care available in the world, surviving to plead "not guilty" to murder? OK. Innocent until proven guilty but flaming pants on one "suspect" and bullet wounds in another seems pretty guilty to me.



The terrorist events are important because government will have to spend more to keep us safe. This pie chart shows what government spends money on, or did, in 2008. Please notice the items we can control and those we can't. According to the latest tables, only 17% of government spending is discretionary and another 15% is national defense. Fully 68% of the federal budget is beyond the control of Congress no matter how nasty the economy gets. Congress views defense spending as a slush fund which makes defense vulnerable to cuts in the 2010-2011 budget. Most clients own one or more defense stocks and cuts would hurt not only our portfolios but our national safety as well. I'm betting that national defense will be a growth area for the next

several years. Our representatives will do almost anything to get elected but cutting the defense budget while our enemies try to kill us doesn't seem like a winning strategy to me. In a few weeks we will get Obama's view of national security when he delivers the State of the Union speech to Congress. I will be encouraged if he sounds more like Reagan and less like Carter.

Microsoft investors must be glad the dreadful decade is over. Yes, the company recently established a 52-week high over \$30 and the stock was as low as \$15 in March. You could have doubled your money this year! But you didn't. As for the decade, Microsoft started 2000 (yes, ten years ago) at \$52.00. So in ten years, shareholders managed to lose almost half their investment despite the new 52 week high. Some analysts on CNBC say this could be the decade for Microsoft and other technology issues to shine. I doubt it. The most recent big product to emerge is "Windows 7" which wags label as the third update of Vista, the less than successful operating system that took seven years to build. I am typing this letter on a Vista-based machine and constantly get bombarded with little pop-ups telling me to check my User Account Control. This pesky "feature" shows up every time I try to change a setting or add a new program.

Most computers today use Windows XP. If you decide to upgrade to Windows 7, you have to start over with a clean hard drive, reinstalling all of your programs and recreating your settings. Apple is taking advantage to suggest that computer buyers switch to their more reliable machines. I believe that millions of other users are like me, waiting for someone else to install the new system. When it comes to new software, I like to recall that it is the second mouse that gets the cheese.

Maybe you didn't know but the "Windows" franchise just celebrated its twenty-fifth birthday. The Windows pre-release version was made available on November 10, 1983 and the public version came out in 1985. Where was the party this year? No party. Microsoft doesn't want you to remember that Windows is as old as a Cabbage Patch doll and the invasion of Grenada. I will admit that Windows made computer use less of a hobby and more of a necessary office tool. Not many product lines survive that long unless the products are made by Procter & Gamble or Pepsi.

Chris Liddell was Microsoft's chief financial officer for four years. He left this job two months ago to "pursue an opportunity with greater responsibilities." Mr. Liddell wasn't at Microsoft long enough to get truly rich because the stock went nowhere despite \$14 billion in stock buy backs and dividend increases during his tenure. While the company was buying stock back, in the last twelve months corporate "insiders" (executives and directors who are supposed to know what is going on) sold 82.7 million shares in 65 transactions. Not one of these decision makers bought a single share of stock. Bill Gates sold 78 million shares of the total, all of it below the current price. Yes, Mr. Gates does have a lot of stock but you would think that he would slow his sales if he thought Windows 7 was going to be a big hit with consumers. The same is true of the other insiders and if they don't buy or hold in anticipation of a new product cycle, why would anyone else?

Mr. Liddell resurfaced just before Christmas as the new CFO and vice chairman of General Motors. GM filed for bankruptcy in June after sucking \$50 billion out of the Treasury to stay afloat. GM is now 60% owned by the federal government with a majority of the rest owned by the Canadian government, the United Auto Workers and former bondholders. Mr. Liddell now works for the government, charged with the responsibility of cleaning up GM's finances so the company can become a public corporation sooner rather than later. To get investors to buy the new stock, GM has to show that it can make it as going concern with good products, quality products, growing sales, satisfactory relations with the unions and the potential for profit. I'm not sure that a government-run business can produce any one of these let alone doing all of them and doing them well consistently.

It will be fun to watch GM's progress from the sidelines just as I plan to watch Microsoft from the sidelines. I still like the prospects for energy, health care and the industrials, all over weight in portfolios. Inflation will come back, and interest rates will rise, probably sooner than later. All in all, a good and prosperous new year for stocks.

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