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THE RAY REPORT

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Bernanke Gets An F

I hate to say it because hopes were high, but Ben Bernanke already has an F in the handling of this economy. The sad part is there were so many opportunities to do something constructive, but we are left picking up the pieces. It is important to realize that the ill effects that are manifesting themselves were readily apparent in August. Bear Stearns and a French bank were having issues with hedge funds as early as last summer. On 8/13/07, in our commentary sections of our website, www.geraldray.com, I stated, "The Fed continues to inject liquidity in the system without lowering rates. I would like to see a rate cut but this may be a start."

A couple of other comments from August:

8/21/07 — My fear is that Bernanke is new and looks like he can be pushed around by the likes of inflation idiots, Lacker and Poole. I hope I am wrong.

8/27/07 — (after Bernanke cuts the discount rate but not the funds rate.) Bernanke and the Fed fiddle so the financials are down. Bernanke speaks this week, but I am not optimistic that he understands what needs to be done.

The fourth quarter was extremely difficult. After Bernanke's 50 basis point rate cut on September 18, I thought that maybe Ben and the

other members of the Fed had awoken to the realities of the situation. I believed that the financials, given adequate support both by the Fed and the government, could rally. Unfortunately, that support never came. One week after the September rate cut, Bill Poole of the St. Louis Fed talked about the perils of inflation. Meanwhile, Paulson refused to raise Fannie Mae and Freddie Mac limits pointing to past misdeeds. Despite this blindness, stocks held on through December as Citigroup and others got new heads and liquidity infusions from foreign governments that helped stabilize the situation. It was precisely December 11 that the market lost faith in Bernanke. Needing to cut a half point on both the discount rate and the federal funds rate, he only cut a quarter of a point on both. This lack of sensitivity to what the markets, both stock and credit, needed is why we have been down ever since. As financials hit new multiyear lows, there are significant opportunities in the sector. However, Bernanke's inability to show leadership has made everyone want to go away while the inevitable, but previously avoidable, recession looms.

The carnage of the last two weeks of December in important areas like financials and technology reflect a no confidence vote on the economy and Ben Bernanke. The swiftness of the pullback was amazing, especially in light of what is traditionally a strong time

Market Performance For The December 2007 Quarterly Period

<i>Dow Jones Industrials</i>	-4.01%
<i>Standard & Poor's 500</i>	-3.36%
<i>Russell 1000 Growth</i>	-1.06%

for stocks. The fact that portfolio stalwarts like Intel, BankAmerica and JP Morgan could suffer for the ills of other more distressed stocks showed the indiscriminate nature of the December sell-off.

We are disappointed with the way 2007 ended, after a very promising beginning. We believed that high quality holdings could hold up despite stress to the system. We also overestimated Ben Bernanke's and the federal government's ability to properly and adequately respond to the problems in the system. As we look forward to 2008, we expect decisive action is forthcoming and we expect stocks to respond from these depressed levels. I encourage all of our clients to call to discuss any questions you may have concerning the markets or your portfolio.

Regards,

Joseph H. Ray, President

2007 Heroes and Goats

Heroes

Men and women of our Armed Services — The progress in Iraq is astounding. Their sacrifice appreciated.

Jaime Dimon — sidestepped most of the mess so far at JP Morgan. My guess is Sandy Weill wished he had kissed and made up.

Sol Barer and Bob Hugin, Celgene — Despite and undeserved late year slide in the stock, Revlimid is a blockbuster with more drugs ahead.

Seth Rogan, from Knockedup to Superbad — a bull market for sophomore comedy.

Goats

Chuck Prince - could not run a 5k, much less Citigroup.

FDA - their hard line on approving new drugs and encouraging new therapies have cost more lives than their caution has saved.

Ben Bernanke - inflation vigilance? Rhetoric replaces action.

Congress - spent more time on the baseball steroid issue than the economy.

Why We Advocated Cuts?

As early as last spring, we suggested broad rate cuts were necessary to keep the economy afloat. This was earlier

than many believed was necessary. The argument against cutting rates were numerous. They included a dollar that was in steady decline, record oil prices and poor inflation readings on gold and other commodities. It was our argument that many of these factors were out of the Federal Reserve's control or simply not true. Oil was affected by foreign demand and the dollar by stronger growth abroad. We believe we are in a deflationary environment caused by more production overseas. We believed that the consequences of not cutting rates were much more dire than the somewhat elevated inflation numbers that could be the result of cutting too quickly. If the Fed had cut early and often, then the possibility of averting a financial crises in real estate and in the derivatives market was real.

We also believed that if we were wrong, you could simply raise rates. In this environment by waiting, we exacerbated the losses to financials and the lack of liquidity in certain markets. Let's hope that now that the Federal Reserve has awoken, it is not too late.

No Intelligence Required

Lastly, this little tidbit on why not everyone should be allowed to run for office.

U.S. Congresswoman Marcy Kaptur came to a House committee hearing on Thursday, January 8, prepared to ask U.S. Treasury Secretary Henry Paulson tough questions about his involvement in the subprime mortgage crisis.

Unfortunately, she was questioning the chairman of the Federal Reserve.

The Ohio Democrat, at a House of Representatives Budget Committee hearing, said she wanted to know what Wall Street firms were responsible for the securitization of subprime mortgages.

She then asked: "Seeing as how you were the former CEO of Goldman Sachs ..." But the only person testifying at the hearing interrupted.

"No, no, no, you're confusing me with the Treasury Secretary," said Federal Reserve Chairman Ben Bernanke.

"I've got the wrong firm? Paulson, Oh, OK. Where were you sir?" Kaptur said.

Bernanke noted that he was head of the Princeton University economics department.

"Oh, Princeton, oh, all right, sorry. I got you confused with the other one ... I'm glad you clarified that for the record," she said.

Paulson was chairman and chief executive of Goldman Sachs before Bush tapped him to head the U.S. Treasury Department.

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