AR SCHMEIDLER & CO
INVESTMENT ADVISORS
A Hudson Valley Bank Company

The Outlook

June 4, 2008

As of June 4, 2008		
Index	**YTD % Change**	**Market Value**
Dow Jones Industrials	-6.6%	12,390.5
S&P 500	-6.2%	1,377.2
Nasdaq Composite	-5.6%	2,503.14

Looking back over many decades, we do not find any period that is comparable to today's environment and where the investment opportunities as well as the risks are so striking. We are in one of the greatest periods of global change from an economic, social and political perspective. The impact of this distinctive period will be felt for a considerable period of time. Over the past several years the environment has been a challenging one in which to build capital yet a rewarding one for those recognizing the beneficiaries of these times. We have found it typical for many to compare past decades with the present, but if we are correct that this business cycle is particularly distinctive, then an emphasis on past similarities could lead to incorrect conclusions and disappointing investment results.

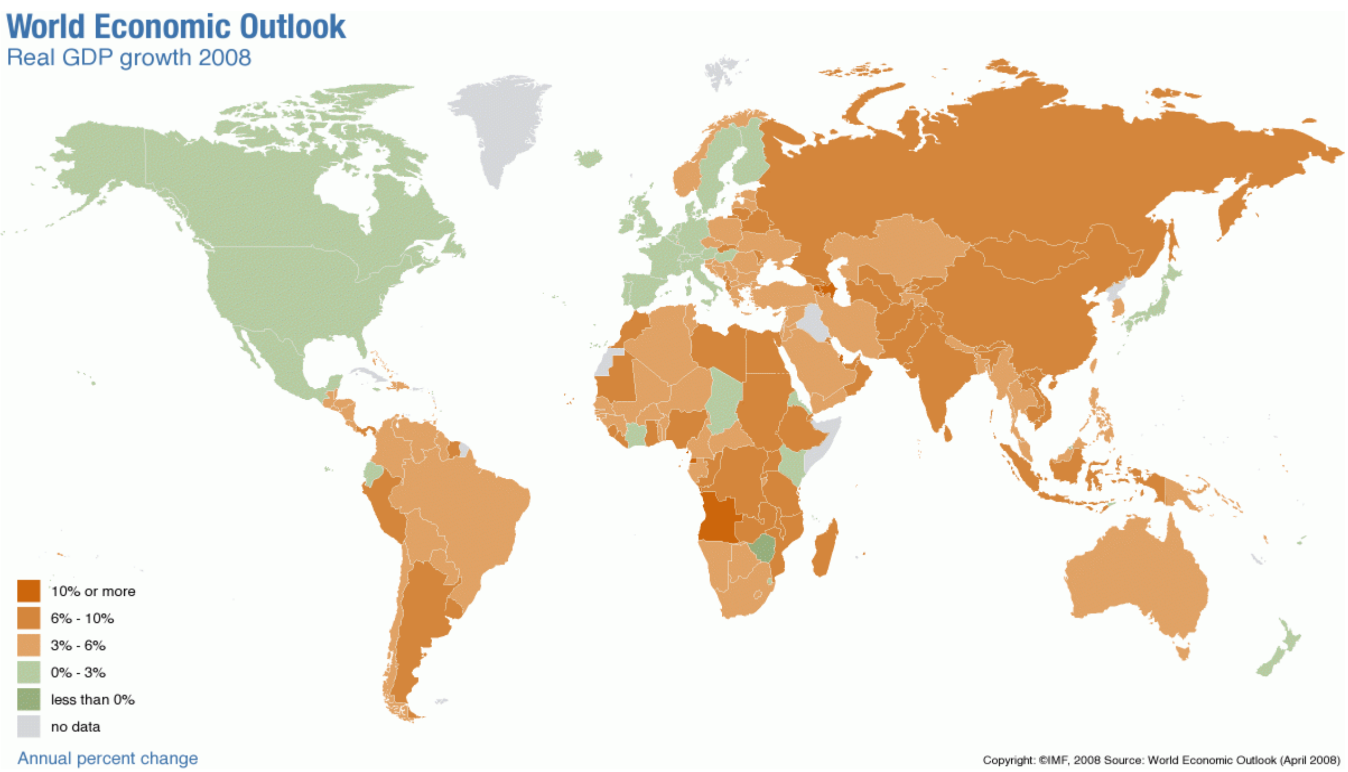
Category	Past	Present
World Population	4 billion	6.6 billion
United States	Leading creditor nation	Leading debtor nation
U. S. Dollar	Leading reserve currency	Strong competitive currencies & U.S. dollar leadership in question
U.S. Banking system	Regulated and low risk profile	Less regulation/oversight, more risk
Financial system	Few complex financial products	Proliferation of complex and unregulated financial products
Exchange rates	Fixed	Managed and Floating
U.S. Energy posture	Net exporter	Net importer
U.S. Fiscal and Dollar policy	Low trade and fiscal deficits as a percent of GDP	High trade and fiscal deficits as a percent of GDP
Inflationary forces	Disinflation	Rising inflation
Investment Sources	Domestic and National pools	Growth of Sovereign wealth funds for cross border investments
Global resources investment	Low commodity prices resulted in under-investment	Under-investment has led to major shortages and higher prices
World leadership	USSR & U.S. leading powers	U.S. & Multiple emerging powers
BRIC: Brazil, Russia, India, China	Small global GDP contributors	Greater size and strongly growing
Energy	Low cost	High cost
Industrial materials/power generation	Global surpluses	Global shortages
Agriculture	Food surpluses	Food shortages
Skilled labor/access to equipment	Easy availability	Shortages
Consumers	Under-leveraged	Over-indebted

The drivers of our Outlook are the continuing power of the global economic environment and the impact of systemic underinvestment in critical areas such as energy, infrastructure, food and materials. Investors who have benefited from the major drivers of world economic growth should realize that these trends will not be going away any time soon. Those who analyze the U.S. economy and investment opportunities must, more than ever, take into account the needs of the global marketplace.

We believe the historic growth rates we have seen in the U.S. over the past ten years will be difficult to achieve for the foreseeable future because they were based on increasing use of borrowed money. Today, the banking system is attempting to repair its capital base, and its ability and desire to lend have been seriously curtailed. Consumers, municipalities and banks are all being forced to repair their finances at the same time. This should result in slower U.S. growth and will require the Federal Reserve and the federal government to maintain an expansive monetary environment (in other words create more money).

World Economic Growth Is No Longer U.S. Centric

Secular growth in demand is derived from the rising living standards of more than 3 billion people in economies that are industrializing. As shown below there is broad-based global growth occurring in areas greater than just the BRIC countries (Brazil, Russia, India and China). In fact over 70% of the growth in the industrializing economies is occurring outside of China. While all eyes are focused on our troubled financial system which remains under considerable stress involving the de-leveraging of the financial system, write-offs in the banking system, increasing home foreclosures and the need for debt reduction by consumers, the global industrial economy is in an upward trend of considerable magnitude.



The Impact of Global Underinvestment

A global supply/demand tipping point has been reached as evidenced by the extreme shortages in agriculture, equipment, power, transportation and water. This is made apparent by riots in various countries over food shortages. Underinvestment in farming over many years, the diversion of resources from important agricultural needs, droughts and changes in dietary habits in industrializing countries have taken a serious toll on the world's food supply. Currently there is a scarcity of other essentials needed to address society's basic needs. **Unprecedented shortages and seismic changes are going to have significant ramifications on what we sometimes take for granted. It will impact political leadership, government policy and the educational focus in both the U.S. as well as other countries around the world.** Entry level Geologists in the mining and energy industry are now being paid more than MBAs in the financial industry, for example, and Geologists saw a 44% increase in compensation during the last year due to the lack of available trained personnel. According to the National Association of Colleges and Employers there has been a year-over-year shift in the salary direction and rates for newly graduated students in several professions as highlighted in the chart below.

Profession	Salary	% Increase	Profession	Salary	% Decrease
Product Engineer	$62,542	16.8% ↑	Accountant	$46,430	3.2% ↓
Aerospace Engineer	$62,454	14.3% ↑	Teacher	$32,345	0.4% ↓
Design/Construction Engineer	$55,357	13.6% ↑	Management Trainee	$41,740	0.3% ↓

The Global Demand for Steel

Today nearly 90 percent of world demand for steel is derived from outside the United States. This is being led by strategic investments in infrastructure by many countries particularly the BRIC, Southeast Asian and Middle Eastern nations. They are undergoing extensive industrialization including the building of airports, railways, power generation facilities, schools, bridges, dams and hospitals. In China, the demand for steel will increase further as it rebuilds after the recent earthquake tragedy. Steel prices have recently been raised with iron ore pellet prices being increased by 87% over the past several weeks. In addition, carbon steel and hot rolled steel, among other products, are all going up sharply in price.

Demand for steel exceeds supply and major U.S. steel companies are the prime beneficiaries of this imbalance. The amount of steel required for a single facility was well highlighted in a recent *Wall Street Journal* lead article on the $7 billion expansion of the Motiva oil refinery in Port Arthur, Texas. Once expanded it will be the largest crude oil refinery in the United States. What is particularly relevant in terms of our ongoing views of infrastructure spending is that this refinery expansion alone will consume more than 27,000 tons of structural steel and require 450 miles of pipe. This will increase the capacity of the refinery from 275,000 barrels per day to 600,000 barrels per day by 2010. Most of the world's oil is of the heavier or acidic type, which means that significant additional investment will be required over time to refine this lower quality oil. **This is a reminder that the quantities of steel and other raw**

materials needed for global infrastructure development are necessary, vast and will be ongoing well into this century.

Oil Supply, Demand, and Disruptions

Among the reasons the major oil companies have not been able to boost oil production relative to demand are production declines in older major fields that have not been sufficiently offset by new discoveries. Reserve replacement has been extremely difficult and costly. Furthermore, a large percentage of the world's known petroleum reserves are located in politically difficult areas such as Iran, Iraq, Nigeria and Venezuela. Problems such as attacks on oil facilities in Nigeria are currently reducing world production by an estimated one million barrels a day. In addition Iraq's production capabilities are still short of reaching their pre-war level. The solutions to reducing global energy demand growth and increasing supply continue to prove extremely difficult to implement in the current geo-political environment. At the same time, global demand has been rising, contributing to higher oil prices.

Monetary Creation

Since our last Outlook of February 27, the Bear Stearns rescue operations by the Federal Reserve to protect the financial system, and therefore the U.S. economy, have been imaginative and correct actions. **The U.S. Federal Reserve continues to make vast amounts of money available to the U.S. economy. The Central Bank is committed to injecting up to $150 billion per month for the next six months into the U.S. economy to offset the capital losses in the financial system and to counter the contractionary effects of the banks' inabilities and unwillingness to lend.** The Federal Reserve continues to significantly expand this program and is, for the first time, accepting credit card debt, student loans and auto loans as collateral from banks to counteract persistent liquidity pressures in the U.S. and Europe. This is an unprecedented change in the role of the Federal Reserve. In addition, their newly-created Term Securities Lending Facility can lend up to $200 billion to twenty different banks and investment firms. This monetary creation increases our concern that down the road we will be looking at a significantly higher rate of inflation.

Deficit Spending & Trade Deficit

The U.S. federal budget deficit is now expected to be well over $500 billion because of the slowdown of the economy. The supplemental budget for Iraq and Afghanistan is adding to this deficit and is likely to bring it to $700 billion. In addition, the trade deficit, which continues to be burdened by imported oil at rising prices, will bring the total U.S. deficits to between $1.4 and $1.5 trillion, or more than 10% of the U.S. Gross Domestic Product. **At this time, industrial prices, energy prices, raw materials prices and agricultural prices are all rising and are expected to create real headwinds for consumer spending while reducing tax revenues.** These growing deficits create major policy challenges for the next President and Congress.

Inflationary Pressures

The inputs of production have been rising in price, and manufacturers have no choice but to pass these cost increases on to their customers. On May 29th Dow Chemical announced a 20% price increase on all of its products. Several companies followed with increases of their own. Separately, the railroads have continued to raise freight rates, and there are indications that they may continue to do so at a 7-8% rate per year for the next several years. Companies are considering or have implemented fuel surcharges as another way of increasing prices. Those who expect U.S. inflation to moderate in the second half of the year may be understating the impact of the current price increases. These inflationary pressures are being augmented by deficit spending and a required easy monetary policy.

Conclusion

From the global dynamics described we believe a successful investment strategy should continue to reflect the forces at work which are notably different from past periods. We will therefore continue to invest in and look for high quality and undervalued companies, many of which are U.S.-based, that benefit from the secular trends that are now in place. To meet the demands of the global marketplace, significant and sustained increases in spending will be necessary. Companies benefiting from this flow of capital will continue to represent the best opportunities for investment returns and are typically the least represented in the broad market indices. The challenges of identifying the beneficiaries and capturing investment returns over the past eight years can best be observed in the underperformance of the S&P 500. Investors in the index have experienced significant volatility and, at the same time, would have lost money both before and after adjusting for inflation.

The competing dynamics that investors face today involve global growth versus diminished U.S. growth. It is our view that as long as global growth continues, the beneficiaries, both domestic and foreign, will continue to be among the most rewarding investments that can be made. Given the enormous amount of dollars in the global economy, large amounts of capital will continue to flow to those regions and industries where investors can feel comfortable that returns can be significant and risks well-contained. One should continue to avoid the industries that had benefited from the over-leveraging that had occurred over the past decade and which now are retrenching and repairing their balance sheets at a cost to their existing shareholders. Furthermore, investors should be mindful not to expose themselves to industries and companies which cannot pass on their rising costs. **We believe investment in the beneficiaries of global growth will continue to offer the most attractive rates of return over time even as the U.S. becomes a smaller piece of the total world economy.**

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