

October 15, 2008

A number of highly respected money managers published letters last weekend after one of the worst weeks in stock market history. Nearly all of these letters made at least two main points. First, stock markets have been tumultuous. Actually nearly every letter used that word or a variant. We agree, although an even more accurate word might be terrible. The portfolios are all down substantially since the end of September, although slightly less than the market's drop. Stock markets have been struggling with repercussions from the decline in house values and mortgage securities for over a year. These problems have proven to be contagious, resulting in widespread problems in credit, real estate, commodities and the general economy. What had been a difficult period became downright brutal in October as it became apparent that there were no quick fixes. Despite several new initiatives, including the coordinated action of U.S. and foreign authorities, as well as the commitment of hundreds of billions of dollars, stocks continued to fall.

The second point most of these letters made was that this is an opportunistic time to invest. We agree with this premise, although we hasten to add that there is no way of picking the bottom. Valuations are attractive. In fact, you may recall in June of 2006 we published a letter with a number of valuation (P/E, P/B, P/CF, etc.) histograms, showing quarterly plots going back as far as eighty years in some cases. Even though we were not near a stock market peak in the summer of 2006, valuations were still in the eighth to tenth decile (expensive) for most ratios. Those histograms came courtesy of the Leuthold Group and when they are updated we will share them with you in a regular quarterly missive, but our back-of-the-envelope calculations today show that most valuations are in the fourth or fifth decile. Considering the prevailing interest rate environment and the fact that inflation is now falling rapidly, the valuation argument now appears to be in our favor. From a psychological or emotional standpoint, we also think it is an attractive time to invest. Prevailing sentiment is about as negative as we have ever seen. Historically, times of deep pessimism give rise to excellent long- term investment returns.

We want to assure all of our clients that we have confidence not only in the viability of the equity markets, but also in our own ability to make profitable stock picks, *provided the investment time horizon is sufficiently long enough to capture a full market cycle*. FMI portfolios have a superior long-term track record that emanates from diligent research, contrarian thinking and the application of common sense. Once in awhile chaos and irrationality dominate the scene, setting the stage for much happier times for those who keep a level head and have the courage to either remain invested or add to their equity exposure.

We appreciate your confidence in Fiduciary Management, Inc.