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A SPECIAL LETTER FROM RS CRUM

The Markets Are Treacherous, But We're Okay

Financial markets have been troublesome. They began to tilt downward in the latter months of 2007 and, thus far into 2008, they have become even more treacherous. There have been substantial losses incurred by many investors but our clients are not among those casualties.

Running counter to this trend we wound up making profits for everyone both during this last six months of 2007 and for the year as a whole. And, thus far into 2008 we appear to have again dodged most of the difficulties and find our investors little affected. This is our seventh straight year of strong performance and continues a rather extended level

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We'd guess any year in which every client captures a profit should be considered to be good, but this time around personal asset protection became our primary mantra and focus. We were clearly of a defensive mindset and most investment decisions were made with that in mind. We have always favored excess safety over excess risk. Perhaps we were a few months early with these preparations but it is now pretty evident that we're going to be well rewarded.

** An Investment Performance brochure is available in our office that measures our investment results over the past ten years. We will happily send it to you if you request. We have also compiled an even longer term chronology of our performance and will forward that as well should you choose.*

The Culprits: The Double Bubble

We are in the process of watching not one but two huge bubbles burst.

The first of these is housing and most of the media attention is being directed to it. Sales have come to a virtual standstill and prices are falling anywhere from 5% to 25% or lower depending on one's location.

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And, it goes far deeper than this. The entire machinery surrounding housing has come to a crunching halt and it matters little whether you are talking about lenders, title companies, builders or brokers. All have been devastated. All of their public share prices have been crushed. Investors have been buried. We do not own any of the companies that have seen their stock price mangled in this wreckage.

Consider too that this real estate appreciation thing has not just been a domestic affair. There has also been a global boom in housing prices, and we are seeing the negative fallout from declining prices beginning to take effect. Most interna-



tional economies now appear to be weakening and security prices have begun to tumble as well.

We have not been caught by any particular surprise. We have been talking to you about this topic and the potential for negative fall-out for well over a year.

Credit constriction is the second bubble and we believe it will ultimately become even more troublesome than the housing thing. Suddenly, we see lenders in every type of market becoming uncomfortable with their potential risk. They fear a recession may be in the offing and are reassessing their lending standards. They are starting to question whether they will be repaid on their present loans. Should they even consider new ones? Or, if they do, what should their new margin of safety be? Some are quietly exiting all lending markets in their entirety.

For example, in December one of housing's premiere equity loan originators mailed out notices to over 120,000 of their homeowner/borrowers notifying them that their future borrowing power was instantly kaput. Remember, these are lines of credit that had already been approved and were in place. Many of these borrowers were counting on this money being available to them and had already executed contracts for future expenditure! This lender has flat out reneged on its commitment. There will be other of these ugly surprises as home values decline and lenders' perception of their own risk heightens.

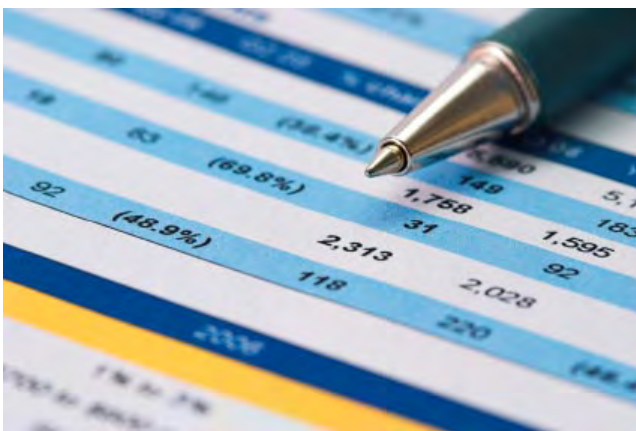
This attitude of risk aversion is spreading way beyond the mortgage market and finding its way into the market for auto loans, the issuance of credit cards



and new business loans as well. One large Midwest banking institution just recently dumped their entire portfolio of auto loans and exited this market entirely. All types of credit are currently being curtailed, reviewed, restricted or aborted.

At the very core of economic growth lies a lender's willingness to make new loans. But, its polar opposite is what we are witnessing today; and credit-contraction is the precursor for an economic contraction. And, as we've said before financial markets do not perform well in the face of this kind of uncertainty. This risk aversion-credit constriction mentality may well wind up becoming an economic self-fulfilling prophesy, and if true is a most unpleasant thought.

In any event we believe you will all be reading way more about this credit meltdown in the months to come. Moreover, we do hope you are not adversely affected.



So, What Are We Doing?

Our goals are simple to articulate, but challenging to achieve. We strive to protect our investors' capital from harmful market influences, while at the same time planning for the future.

We have pursued six separate courses of action:

- 1.** We already mentioned that we had become worried about certain risks in bonds and other fixed income investments. We felt there would be many holdings that might appear to offer safety but instead could present ugly surprises (sub-prime mortgages, junk bonds and insured bonds to name just three). We eliminated as many suspicious holdings as we could possibly identify and refortified everything else in this (bonds/fixed income) asset class.
- 2.** With respect to our dividend-rich, equity income category we have continued to identify new prospects while deleting others. This single area occupies as much of our energy, research and careful thought as any other. We are well aware of the cushioning stability that it has provided as high levels of income pour continuously into each and every account. This is time well spent.
- 3.** We continue to trim and spread all holdings. Most portfolios are comprised of anywhere from 40 to 60 distinct assets. Rarely, will we allow any given position to represent too high of a percent of the total (the exception might be a given mutual fund, yet even it may be diversified by 100 or more individual hold

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ings.) We do not intend for any given portfolio to be dominated by (or captive to) the whims of one or two individual holdings. This activity demands and receives our constant attention.

4. We have also been directing spare funds into (what we perceive to be) safer pockets of liquidity. Many of these dollars have been parked in holdings that might accrue only 4% to 5% annualized return. Our primary goal in so doing is not the earnings these funds might achieve; it rests with our ability to retrieve these moneys quickly, and in their entirety, to reinvest elsewhere as other more lucrative opportunities might develop.

5. We began to add Gold as an alternative investment and portfolio hedge type position anywhere

from 12 to 15 months ago. We have been rewarded as this metal recently touched \$900 per ounce.

This holding was primarily included for its inverse characteristics in that its price has had the tendency to increase while that of other types of financial assets decline. This provides a cushioning effect for us and delivers to our portfolio some of the important checks and balance that we seek.

6. With respect to the future we believe both the delivery of health care services and water resources will become increasingly inadequate in the face of rising demand. If we are right, this scarcity will translate into future profit. We want to own these kinds of assets when ever markets do calm and new trends emerge.

So Then, What's Next?

Market corrections are a fact of life. They neither go straight up or straight down continuously. Losing markets are never fun, yet they are inevitable. What we do know for sure is that when they do fall the investor who loses the least wins. This was one of our goals and thus far, in the wake of this mess, we have been pretty darn successful.

Our second goal is to be patient yet ready. Right now we can not see how long this whole episode will take to play itself out. What we do know, however, is that historically the initial upswing coming out of a flat or dismal period has offered us our single quickest and most profitable advantage. Those

who have been with us for any length of time know just how true this is.

We are also aware that we might either be premature or incorrect in our analysis of current events so, as always, we avoid any 100%, all or nothing, positions. Our primary objective is to be both resilient and adaptable. If we are wrong we will find out soon enough and alter our mix. If not, then we like where we are, comfortable in what we perceive to be our safer haven. This approach has served us so very well over so many years and market fluctuations.