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Quarterly Newsletter to Public Q4 2010
December 21, 2010

Executive Summary
Fears of double dip recession appear to have been dispelled as private sector economic growth returns. However, unemployment will likely remain high for some time, stock valuations remain stressed, and many structural challenges have not yet been addressed.

As we grow as an organization, we strive to learn how to better service our clients. Even clients who do not have current income needs often prefer lower volatile investments at the likely expense of long-term returns. The Retirement Spending Portfolio (RSP) is our attempt to answer this for clients as a supplement to our Long-Term Portfolio. The RSP and Long-Term Portfolio have performed admirably, protecting downside risk and providing significant excess returns to their benchmarks.

The Value Opportunities Portfolio is our contrarian strategy and may underperform over shorter time horizons but is also designed to control downside risk. This portfolio is particularly suitable for investors who seek a hedge fund like product with full transparency and lower fees, especially for investors who are skeptical about the market and seek an alternative strategy to the Long-Term portfolio or RSP.

Economic Update
The slowdown in economic growth that made us fearful of a double dip recession beginning in April appears to have turned the corner. Two leading institutions, we respect, the Economic Council Research Institute, and Lombard Street Research, have both determined that economic growth in the US will likely be above trend in 2011 and that unemployment may begin to fall. We respect these institutions because they earn their living by selling research, thus put their reputation on the line with their forecasts.

According to Lakhsman Achuthan, of ECRI, even during the Great Depression, from 1933 to 1937, the economy grew by over 10% per annum. "*The business cycle, once it turns, and it is turning, is much more powerful than a tax cut or spending*." He believes the business cycle has turned and we will see a revival over the few months in terms of job growth, output and sales at an accelerated pace. Video below:
http://www.businesscycle.com/news/press/2041/

This is comforting to investors because it mitigates fears of deflation and severe economic downturn. Nonetheless, even the best case scenario is unlikely to make a major dent in unemployment and without extensive worker retraining unemployment will remain above 7.5% for some time.

Overall equity valuations also remain high and US and other countries have hurdles that must be overcome to correct structural imbalances that took decades to build. We would like to see, for instance, an increase in consumption in Germany, Japan, and China and a commensurate increase in net exports from the United States to these countries before we feel a lasting structural change has occurred and an all clear signal can be sound.

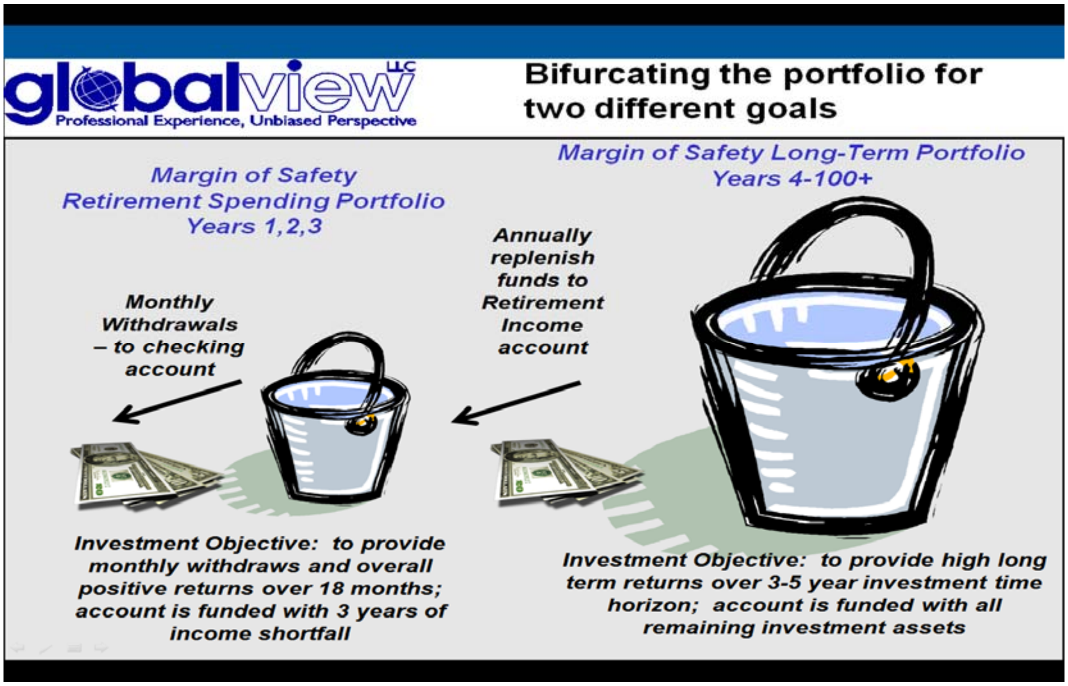
There are many obstacles to this. In Germany, the existence of the European Monetary Unit, the Euro, and inclusion into it of peripheral countries, makes the currency in Germany artificially low and is a stimulus to their exports. Japan has kept interest rates low since the 1990s, making the Yen inexpensive relative to the dollar. Finally, the Chinese pegged the Yuan to the dollar in 1994, reducing it in value by 50%. Since then, China has grown at incredibly high rates through exports. According to the Big Mac index, managed by the Economist, the Yuan is 40% undervalued relative to the dollar.

It is questionable to us that the Euro can continue to exist simultaneously encompassing both strong and weak nations, e.g. Germany and Greece. Only by allowing its currency to fall can Greece grow from its current problems. Its currency cannot fall until its currency is again the Drachma. This change appears to be inevitable and will likely cause continued stock market volatility. Similarly, it is unlikely that China can continue to grow its economy at its current rate. Some adjustment is inevitable and will likely cause continued volatility.

Overview of Portfolios and Asset Allocation

Our clients use a combination of three global Margin of Safety portfolios to meet their needs. The Retirement Spending Portfolio is designed to create positive returns over shorter time horizons of less than three years. The Long-Term Portfolio is designed to provide positive returns over periods of more than four years and to beat market indexes over the long run. The Value Opportunities Portfolio is a contrarian strategy designed to provide a hedge fund like product with full transparency and lower costs and to provide positive returns over a three year time horizon.

We plan on rebalancing portfolios in the first quarter, and will provide more detail on this shortly.



<u>Retirement Spending Portfolio</u>
In a perfect world, with truly rational investors, there should be a concern for volatility *only when it impacts immediate spending needs*. However, many investors are greatly placated by low volatility and have a tendency to overallocate to low volatile investments, despite having a long time horizon for investing. For this reason, the Retirement Spending Portfolio (RSP) is a popular choice for many investors, even for investors who do not have an immediate income need from investments.

The RSP is comprised of managers that have a focus on reducing volatility and providing high absolute returns in any market environment. We find the best global talent who use a margin of safety approach to investing in equity and fixed income and who seek low volatility. We offer two versions of this portfolio, depending on the level of current income required, and our client's income taxes.

Even long-tenured clients need a reminder that volatility is not the same as risk of permanent loss of capital. For clients who can understand this and consider the longer view, the Long-Term Portfolio will be a better choice than the Retirement Spending Portfolio for the bulk of their assets. However, in an environment where interest rates are likely to increase and traditional fixed income investments are unlikely to produce positive returns, the Retirement Spending Portfolio is an excellent choice for more conservative investors currently invested in traditional fixed income. Recently, despite a sharp drop in long-term bonds when interest rates strated to rise, this portfolio held up very well.

<u>Long-Term Portfolio</u>
Even if an investor had the necessary skill to analyse individual securities, it would be very difficult for him to replicate the characteristics of our Long-Term Portfolio. This portfolio owns 500 stocks. Of the top 5, 3 are not traded on US stock exchanges. Only one holding, Berkshire Hathaway, comprises over 1% of

the portfolio. The Top 25 stocks are 16% of the portfolio. The portfolio is about 70% in equity: 35% in US and 35% outside of US. It holds about 21% cash, well positioned to capitalize on a market correction.

Holdings are selected by the best global talent we can find. Analysts conduct in-depth forensic analysis instead of simplistic ratio analysis. Using simplistic ratios, such as price to earnings or price to book would be misleading. Typically when an investor looks at the price to earnings ratio, he looks at the current price in relation to the last 12 month earnings. This can be highly misleading as the last 12 month earnings are not likely to be indicative of the long-term trend. A margin of safety approach is necessary to determine likely earnings in the future, which is uncertain, and must consider both the company balance sheet and income statement. Making assumptions that earnings will grow higher than the underlying growth rate of the economies where the company sells its goods and services is often a recipe for disaster.

The overwhelming majority of our clients' long-term portfolios are invested in an allocation we call Moderately Aggressive, which has historically exhibited substantially superior performance to its benchmarks. While our long-term goal is for this portfolio to outperform market benchmarks, we expect it to underperform over short time horizons, particularly when the broad market rises quickly, and during speculative bubbles. We are pleased with this portfolio's continued performance and will provide clients with performance information in January.

Value Opportunities Portfolio

Value Opportunities is a contrarian strategy. Rod McGee is the manager of this portfolio. Rod believes that during a secular bear market it is unwise to be invested all long, in fact that an enterprising investor can be rewarded from betting against overvalued companies. This contrarian strategy is likely to underperform during periods of rapid market appreciation; however, provides substantial downside protection in the event of a downturn and should perform well when fundamental forces return and higher quality investments begin to outperform.

Currently, Rod is defensively positioned and believes the market will correct when some of the structural imbalances we discussed earlier are corrected. Over the last quarter, Value Opportunities, like many long-short strategies, has underperformed broad market indexes.