The Commonsense

INVESTLETTER

Volume 6 Number 10

Wall Street:

- DJ 9337
- S&P 500 969
- NASDAQ 1721

Expert…Not

Experts can perform many wonders. Ensuring that the greedy act honestly and with integrity is not one of those wonders.

When is an expert not an expert. Corporate executives, hedge fund managers and other finance power brokers play the role of experts. Chief Executive Officers are the experts at running their business. They are supposed to be able to guide their company and get the most out of the talent labor and equipment they have to operate with. Hedge fund managers are the equivalent of financial engineers who are able to use sophisticated financial transactions to outperform the markets and achieve outsized returns with below average risk. Each experts in their own field.

To borrow from the Spiderman comics; "With great power there must also come great responsibility." Executives justify the pay they receive because of the responsibilities they shoulder. However it shouldn't be responsibility without accountability as that would have kind of a hollow ring. As part of their responsibility we expect them to be accountable for their actions. The big pay packages are supposed to be linked to the creation of large amounts of value for other stakeholders and commensurate with the responsibility. Hedge fund managers are responsible for their investor's wealth, their retirement nest eggs. They are trusted to perform to the best of their ability for their clients. Clients hold them accountable by being able to move their money to another manager if their performance does not live up to the hype.

Recent events have shined some light on how far from the truth this often is. Corporate executives like to take credit for events they have no control over when it suits them and to disdain responsibility for events they do have control over when it could impact their wallet. An example that is almost too hard to believe was written up in an article in the Wall Street Journal. Robert Rubin, a former Treasury Secretary, has been put on the hot seat over his $113 million in pay since 1999. As a member of the Board of Directors of Citigroup, where he also functions in an advisory role, he played a role in approving managements foray into increasingly risky investments. When explaining the decision to increase risk Mr. Rubin had this to say: "It gave room to do more, assuming you're doing intelligent risk reward decisions." He went on to say that in the current crises, "what came together was not only a cyclical undervaluing of risk, but also a housing bubble, and triple-A ratings were misguided." What he said next was the clincher, "there was virtually nobody who saw the low probability event as a possibility." As a result the company has had losses in excess of $20 billion over the last year and received $45 billion in government bailout money.

Low probability events do happen as the events of this year can attest to. A business that operates as though low probability events cannot happen are a leading cause of the situation we are currently stuck with. Shouldn't those who made the decisions bear some of the responsibility for the repercussions of this failed line of thinking? Apparently Mr. Rubin does not believe so.

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continued

The decisions that set up Citigroup's collapse were not made this year. They have been made over the course of several years; years that they have reported excellent earnings and people like Mr. Rubin have been compensated well for their "great performance". The earnings were an illusion while the compensation was not. So, Mr. Rubin and many like him keep their outrageous compensation while the taxpayers step up to bail out the company. We will foot the bill for the mistake that those running Citigroup made because they feel it was outside forces that caused them. When that same risk generated fat profits that they could use to justify their outrageous pay packages, the profits where due to excellent management.

Collecting fees on assets the have been misappropriated adds insult to injury for those who have had their investments stolen.

Our second expert, Bernard Madoff played on the appearance of being an expert; and it is always better to appear an expert when your objective is to get your hands on others money. Alas, he also had a whole stable of experts to help carry out his financial genius. One hedge fund outfit whose primary purpose was to feed money to Mr. Madoff was Fairfield Greenwich Group. They had $7.5 billion of their $14.1 billion hedge fund assets under management invested with Madoff. The firm was compensated princely for their efforts to the tune of $250 million for 2007. Four of the firms partners received more than $5 million in compensation. On their website they detail how they investigate those responsible for investing their client's money and how weekly they verify the trading activity so they can be assured that the assets are reported accurately. $250 million certainly should be more than enough to cover this expense and the firm did only report $200 million in profit, still leaving plenty for their detailed oversight. The customers of the hedge fund were reported to have paid 1% of their assets invested and 20% of any investment returns for the skill this firm had in handing the money off to Madoff to invest on their behalf. Fortunately the investors had the previously mentioned foolproof oversight to assure the safety of their investments. Much to their surprise, the money vanished.

The investors have not noticed any reduction of the fees they paid for investments that would have yielded more feeding them through a crosscut shredder. (At least with the shredder you can recreate much of the money and get it replaced.) It cost millions for the privilege of having Fairfield make their money vanish. Fairfield didn't even posses the magic box used by Madoff , they were compensated for holding out their hand and passing the money to Madoff to feed in the box.

Even though the fees Fairfield received were for investments that did not exist, there has been no mention of any refund for their investors. The fees were based on returns that were pure fantasy and assets that did not exist. I am pretty sure it was out of their control.

The amount of debt has not decreased with any government bailout made in the past few months. Debt has been transferred from private companies to the taxpayers. Those who received most of the profits get to keep all that they "earned" even though these profits were as much an illusion as the assets and fees of the Fairfield hedge fund.

You have heard us state it in the past and we will repeat it again. Keep your assets under your control unless you have complete trust in the person you are dealing with. You need to have access to the records to verify how your assets are being invested or have other forms of protection like FDIC insurance covering your money in a bank. Secondly, don't have any faith in anyone who is only responsible for decisions that work out well and not responsible for any bad decisions they make.

Needless Complexity

Needless complexity strikes again. The former Chairman of the NASDAQ stock market, who was running his own investment firm, was just arrested recently for a $50 billion ponzi scheme. Not many of the details are know as to what happened to the money, but it is clear that many rich friends, fellow country club members, college friends, other hedge funds, banks and the list goes on and on, have been affected by this fraud. Madoff's hedge fund has lost billions of dollars and charged a premium price for doing it. Fees associated with hedge funds are exorbitant. A representative fee structure has a fee of 2% of assets under management and 20% of investment returns. A $50 billion hedge fund that earned a 20% return would generate fees of $2.5 billion. Having more assets under management certainly gives a nice boost to a manager's bottom line. Madoff reported a huge amount of assets under management. The minor annoyance of having lost much of these investments was not an impediment in any way to maximizing his take.

Investors chose to ignore the fact that hedge funds have very lax oversight as their industry happens to a have a few dollars to fund a cadre of lobbyist second to none. The hedge fund industry does not want oversight so the money they spend on their favorite friends in high places ensures they don't have to deal with needless bureaucracy. It sure has been sexy to invest in hedge funds over the past few years. Everyone has been doing it and those who were with Madoff even brought their friends into the game. Madoff was reported to have used a big money derivative investment strategy to generate nearly foolproof regular monthly gains to his investors. The game is up and it was all a big fraud. Needless complexity in the form of exotic investment vehicle using exotic strategies amounted to exotic fraud. Many have lost their life savings, he mismanaged assets of company retirement plans , hurt countless individuals, companies and not for profit organizations. Just more helpless victims in our lax regulatory oversight framework. Very rarely are you rewarded for added complexity. We will stick with our preference that we oversee our own dollars and urge you do the same. The more people that are involved, the more fees you will pay for the privilege of added exposure to more sticky fingers.

Company	November price	October price	Change from October	P/E	52 Week High	52 Week Low	Estimated '08 EPS	Dividend Yield
Alico/ALCO	$34.34	$39.39	-12.82%	n/a	$50.32	$22.34	n/a	3.20%
American Pacific/APFC	$10.14	$11.55	-12.21%	9.3	$18.89	$9.11	$1.07	n/a
Amtech Systems/ASYS	$3.47	$6.41	-45.87%	11.1	$16.66	$2.25	$0.27	n/a
Arch Coal/ACI	$15.38	$21.41	-28.16%	6.0	$77.40	$10.43	$2.43	2.30%
Atrion/ATRI	$96.20	$98.96	-2.79%	12.9	$133.88	$63.00	n/a	1.30%
Consolidate Tomoka/CTO	$34.35	$36.90	-6.91%	14.8	$67.13	$24.00	n/a	1.20%
Culp/CFI	$2.32	$2.88	-19.44%	5.6	$8.60	$2.31	$0.32	n/a
Graham Corp./GHM	$9.10	$21.00	-56.67%	5.1	$54.91	$6.85	$1.62	0.90%
Landauer, Inc./LDR	$57.42	$54.06	6.22%	24.0	$73.52	$46.82	$2.48	3.70%
Mesa Labs/MLAB	$18.49	$17.00	8.76%	12.9	$27.00	$16.00	n/a	2.20%
Rayonier/RYN	$33.40	$33.08	0.97%	18.7	$49.54	$26.58	$1.99	6.00%
Schuff International/SHFK	$18.00	$16.00	12.50%	2.8	$35.00	$15.00	n/a	n/a
Servotronics Inc./SVT	$6.80	$6.00	13.33%	9.2	$22.48	$5.20	n/a	2.20%
Span America Medial Sys/SPAN	$10.20	$12.00	-15.00%	6.0	$13.52	$8.03	n/a	3.50%
Tejon Ranch Co./TRC	$26.11	$29.06	-10.15%	89.8	$44.50	$20.40	$0.56	n/a
Torm/TRMD	$11.72	$16.44	-28.71%	3.9	$42.50	$9.73	n/a	n/a
Twin Disc/TWIN	$6.64	$7.75	-14.32%	3.5	$37.47	$4.02	n/a	4.20%

The Investletter Portfolio

We have been going thorough our investments and making sure that the investments we own still make sense in the post crash world. It is easy to buy companies with a margin of safety in the current environment. That doesn't mean their price still can't swing wildly.

The companies we own because of their operating prowess all make a great deal of sense in today's market. Each company is selling at less than it is worth in our estimation. We tweaked our numbers for worst case scenarios to add an extra margin of safety. Astronics is valued at $8 in the market while we view the company as worth at least $15. We view the operating business of Gencor worth $4 to $5 dollars. Add the $6 in cash per share and the company is conservatively worth $10 or $11. K-Tron is valued currently at $74 and we see them as worth no less than $130.

Values could remain out of whack for years. When we sold Gencor earlier this year when we felt they became overvalued in the $20's and that lasted for a couple of weeks. Prior to that they were undervalued for years. If the economy doesn't turn, many of these undervalued companies will remain undervalued companies. Our best hope in the short term is the Obama stimulus package that will be gaining headlines as we move into January. The low gas prices and the lower food prices they will bring, low interest rates and a healthy dose of government spending will give us a needed push.

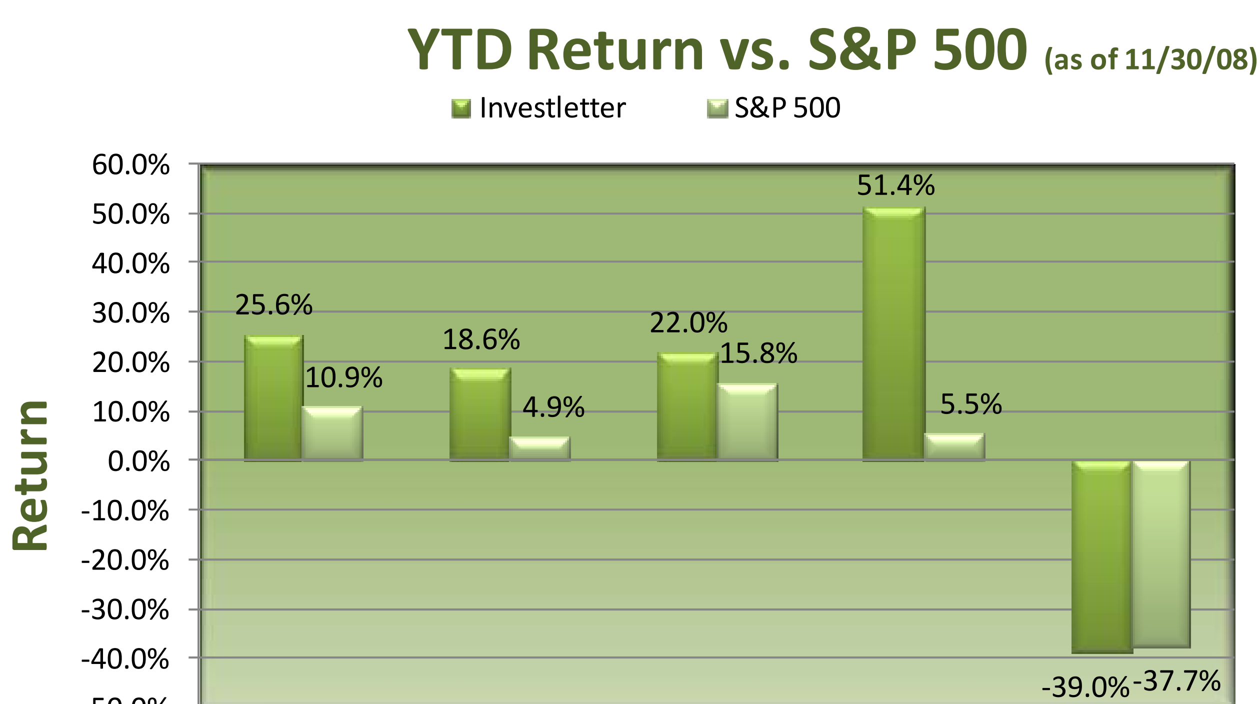
Date	Security	Symbol	Price	Order Type	Qualifiers	% Portfolio or Position	Outcome
12/03/2008	Constellation Energy	CEG	$28.00	sell	limit	50%	filled
11/16/2008	Rohm & Haas	ROH	$73.00	buy	limit	6%	filled
11/14/2008	Anheuser Busch	BUD	$68.75	sell	limit	n/a	filled
11/10/2008	Constellation Energy	CEG	$24.05	buy	limit	6%	filled
11/02/2008	Rohm & Haas	ROH	$69.80	buy	limit	5%	open
10/22/2008	Anheuser Busch	BUD	$60.10	buy	limit	4%	filled
10/19/2008	Anheuser Busch	BUD	$62.50	buy	limit	4%	filled
10/10/2008	Atrion	ATRI	$93.00	sell	limit	n/a	filled
10/10/2008	Asta Funding	ASFI	$4.00	sell	limit	n/a	filled
10/10/2008	Amtech Systems	ASYS	$6.70	sell	limit	n/a	filled
09/24/2008	Rayonier	RYN	$46.00	sell	limit	n/a	filled
09/22/2008	Consolidated Tomoka	CTO	$48.50	sell	limit	n/a	filled

Company	Portfolio Percentage	November price	October Price	Percentage Change	Buy Price (less than)	P/E	Dividend Yield
American International/AMIN	**6.40%**	**$2.00**	**$2.14**	**-6.54%**	**n/a**	**n/a**	**n/a**
Astronics Corporation/ATRO	**11.00%**	**$8.10**	**$12.50**	**-35.20%**	**$8.25**	**7.1**	**n/a**
Berkshire Hathaway B/BRK.B	**8.70%**	**$3,499.00**	**$3,790.00**	**-7.68%**	**$3,500.00**	**20.6**	**n/a**
Cash	**27.00%**	**$1.00**	**$1.00**	**n/a**	**n/a**	**n/a**	**n/a**
Chesapeake/CHK	**4.20%**	**$21.97**	**$21.97**	**0.00%**	**$20.00**	**5.4**	**1.70%**
Constellation Energy/CEG	**7.30%**	**$24.47**	**$24.21**	**1.07%**	**$24.00**	**12.6**	**7.80%**
CSP Inc./CSPI	**7.20%**	**$2.85**	**$3.67**	**-22.34%**	**$4.00**	**5.9**	**n/a**
Gencor/GENC	**5.20%**	**$7.00**	**$6.25**	**12.00%**	**$6.50**	**4.2**	**n/a**
K-Tron International/KTII	**8.90%**	**$71.95**	**$93.99**	**-23.45%**	**$95.00**	**7.9**	**n/a**
QEP Corporation/QEPC	**7.30%**	**$3.03**	**$3.65**	**-16.99%**	**$3.50**	**3.2**	**n/a**
Rohm & Haas/ROH	**6.80%**	**$68.41**	**$70.35**	**-2.76%**	**$69.00**	**21.4**	**2.4**

Performance

November saw our performance slip back behind the returns generated by the S&P 500 average. The continued poor performance by our smaller companies is acting as a millstone on our returns. It is hard to tell what happens next when markets trade so detached from asset values. We do however see signs that well situated companies are starting to take advantage of the situation. Our arbitrage play on Constellation Energy's (CEG) buyout has attracted another energy company as a bidder. This particular French energy company that happens to owns 10% of CEG does not want to see their investment bought out at a discount to what they feel CEG is worth. So, they bid to buy less than half of the company for nearly the same price as the buyout offer on the table.

Several companies have announced large buybacks and a couple of Dutch auctions have been announced to buyback a large number of shares in one fell swoop. When the economy starts to show sign of strengthening we expect to see a rise in mergers and acquisitions as well positioned companies start to buy up companies that can be had on the cheap.



	2004	2005	2006	2007	2008
Investletter	25.6%	18.6%	22.0%	51.4%	-39.0%
S&P 500	10.9%	4.9%	15.8%	5.5%	-37.7%

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