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“I see we got smacked around last year, but not as much as some others got smacked.”
-- *MJB Asset Management client, discussing his portfolio with me last week*

Dear Clients and Friends:

“That’s \$1.70, please,” said the young woman at the cash register after I ordered a cup of coffee. Some of us find it shocking that a small coffee costs \$1.70; at that moment, however, most shocking to me was the inclusion of the word “please” in her sentence. In all the visits over the years to Starbucks, Dunkin’ Donuts, et al., I do not recall ever hearing “please.” That small act of human connection greeted me on my first day back to the office in 2009. I often feel that much of what ails us as individuals and as a society stems from a basic lack of human connection, a complete disregard for the effects of our actions on other human beings. As I sat down to write this letter and looked back at what had transpired in the investment markets last year, it became clear that on a basic level, the current financial crisis emanated from a lack of humanity -- a complete disregard for the consequences of one’s actions on others. Certainly, other factors contributed to the mess (e.g., interest rate policy, regulatory policy and political maneuverings). But as best I can tell, given the investment environment of the time, it still requires a complete disregard for the human consequences of your actions for unscrupulous mortgage lenders to push exotic mortgages on homebuyers who cannot afford, or perhaps even understand, them. On the flip side, the same disregard enables unscrupulous borrowers to lie on their loan applications to borrow more money than they are able to re-pay. The list can go on, but perhaps most sickening of all, it is that same disregard that enabled a Bernie Madoff to look friends in the eye and ask for money he had no intention of re-paying.¹

So before I get to the substance of this letter, I offer a heartfelt thank you for the faith and confidence you have placed in me. It is a blessing to be able to go to “work” each day loving what I do and being able to do it in service of others. I am deeply grateful for our relationship and for the opportunity to serve as your investment advisor. If you have any questions or concerns about your accounts or anything else, please call me.

Even though celebrating the New Year on January 1st is a social convention that has little predictable effect on the investment world,² it can be an appropriate time to pause, reflect on where we have been and consider where we want to go. In that context, I offer the following *brief* assessment of the investment year past, a brief thought on what could lay ahead and a bit longer assessment of the present environment:

¹ As the lawsuits begin to mount, we can see that people are doing more than simply disregarding the consequences of their actions; they are refusing to accept any responsibility for their actions at all.

² Indeed, as of this writing, some investors are referring to January '09 as the thirteenth month of 2008!

The year past: Getting “smacked around” is technically not an investment term, but it sure fits what went on in 2008. As the U.S. sub-prime mortgage fiasco morphed into a global financial crisis, stock markets plummeted worldwide. U.S. markets declined close to 40%; many overseas markets, particularly emerging markets, declined by much more.³ Corporate and municipal bonds – typically safe havens during times of stock market turbulence – also declined as panicked investors fled to the safest haven of all: U.S. Treasuries. Our portfolios declined as well, but as with my above-quoted and straightforward client, the declines in all cases were less than the market. Our most conservative accounts declined roughly 10%-15%; our moderate accounts declined roughly 20%-25%; our more aggressive accounts declined roughly 30%-34%.⁴

The year ahead. Others might know the future, but I do not. I sense the worst of the downturn is ahead of us and the worst of the market decline is behind us, but that is speculation. The government is pumping massive amounts of medicine into the economy; the patient likely will live, though the timing the recovery is unknown. In this regard, the economy resembles a large ship turning at sea; the captain turns the wheel, but it takes a while before the vessel shifts direction. Markets, on the other hand, can turn on a dime. This suggests that the economic recovery likely will be slow but steady whenever it takes hold, and markets will remain volatile.

The present. Stating the obvious, we are somewhere in the middle of a recession. The good news is that recessions are cyclical and, as painful as it feels right now, this one is likely to pass.⁵ In the meantime, it is creating investment opportunities:

- Corporate bonds. The maelstrom started with a meltdown in the credit markets; the healing must start in the same place. It is beginning to happen, albeit slowly. So-called “spreads” between the interest rate a corporate borrower must pay and the interest rate the U.S. Government must pay are beginning to narrow from historic highs a few months ago back to “normal” levels. When spreads begin to narrow, it indicates that corporations are able to get access to credit more easily, i.e., lenders are requiring less of a premium to lend to corporations. This is healthy for the corporate bond market; as corporate lending gradually returns to normalcy, the prices of existing corporate bonds – pummeled in the credit meltdown and the recession – are beginning to rise, making this a terrific time to invest in such bonds. In other words, prices are low and yields are high, enabling investors to lock in the yields while also benefiting as bond prices rise. We have begun to increase our positions in corporate bonds by adding to or establishing new positions in the FPA New Income Fund and/or the Loomis Sayles Bond Fund.
- High quality, dividend-paying stocks. As the bond market heals, so should the stock market. The double whammy of the credit crunch and the recession has driven the prices of many high quality stocks to bargain prices. Many of them, e.g., AT&T, Merck and Verizon

³ The low point for U.S. markets occurred on November 20th, when the S&P 500 Index closed at 750, down more than 50% from its most recent high of 1,565 reached back in October 2007.

⁴ “Conservative,” “moderate” and “aggressive” are definitional terms for portfolios only and not intended to have personal, social or political connotations.

⁵ More than that, we are in a broad-based economic and investment malaise that is the culmination of years of social and economic choices that might (or might not) have appeared to be good ideas at the time, but that have brought us dangerously close to an all out financial catastrophe, fortifying along the way a culture of greed and materialism and a concomitant decline in civility in our society. It came to a head toward the end of last year, as we lived through another ugly political campaign, an erratic response by our government to the deepening financial crisis and the disclosure of a massive fraud by a supposed stalwart of the investment community. As mentioned in the main text, I am confident that the recession will pass. I pray the malaise will go with it.

to name a few, pay high dividends and have little if any direct exposure to the financial crisis. At current prices, their dividends translate into yields of as much as 6% -- on top of the potential for capital appreciation. In other words, the pickings are good ; we are gently increasing our positions in stock market funds while valuations remain compelling.⁶

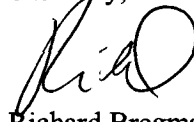
- Distressed securities. This area of investing involves buying securities of companies facing financial distress, such as a restructuring of their debt or perhaps a potential bankruptcy. Such securities can come from any part of a company's capital structure, e.g., common stock, convertible bonds, trade debits, etc., and often are available at enormous discounts, leading to the potential for very large gains.⁷ Distressed investing has unique risks and requires specialized knowledge (e.g., bankruptcy law, creditors' rights, etc.). We are fortunate to have access to several highly qualified managers with the requisite experience and expertise: Marty Whitman of the Third Avenue Value Fund; Bruce Berkowitz of the Fairholme Fund; Steve Romick of the FPA Crescent Fund; and Dave Embler of the Franklin Mutual Recovery Fund.

Market swoons are as natural as they are unpredictable. We do not expect to avoid them completely.⁸ Our goal is to lessen the blow, as study after study shows that avoiding deep potholes is a crucial component of creating long-term wealth. In essence, the climb back up from a 20%-25% drop – psychologically as well as mathematically – is far less daunting than the climb back up from a 40% drop. In that context, we had a reasonably successful 2008. Now, however, our job is to focus on the present opportunities, as described above. We do not know how long it will be before these opportunities change and/or disappear completely. We are grateful for their appearance now; as change arrives and new opportunities present themselves, we will make appropriate adjustments to our portfolios.

It is healthy to keep change in mind. Change is inevitable; its exact nature and timing are unknowable but its occurrence is inevitable. Change will come to the economy and to the markets. It is easy to fall into the old habit of believing that things will stay this way forever. That is living in the past and speculating out into the future. We look instead for opportunities in the present moment that will enable us to help create the future that we want. Notwithstanding the stormy environment, where the news appears to be unrelentingly negative and the swells of fear among investors is palpable, I write to you here in the early part of 2009 filled with optimism, looking forward to each day as it arrives and to the opportunities that each day brings.

Thank you again for your continued confidence. Best wishes for the upcoming year.

Sincerely,



Richard Bregman

⁶ As always, the timing of a rise in stocks is highly uncertain. Given such uncertainty, we are maintaining a strong commitment to our hedged and alternative strategies.

⁷ A current example would be purchasing certain bonds of General Motors, which is in dire financial straits. A five year bond paying 7% might be purchased for 20 cents on the dollar. In such a case, the \$7 of annual interest paid on a \$100 bond is now paid on a \$20 investment, which translates into a 35% interest rate.

⁸ Given that downturns – as well as upturns – are unpredictable, to avoid them completely would almost by definition require being completely out of the market all of the time. That is not our mandate.