TRIAD
INVESTMENT MANAGEMENT

2nd Quarter 2010 Investment Review

"The greatness of America lies not in being more enlightened than any other nation, but rather in her ability to repair her faults"
-**Alexis de Tocqueville**

Yes, there is plenty to worry about. Double-dip recession, high U.S. unemployment, November elections, healthcare reform, financial industry reform, Gulf oil spill, looming tax increases, increasing government regulations, still-depressed home prices, consumer debts, Federal and State budget deficits, European debt crisis, Chinese growth slowing, interest rate uncertainty, inflation/deflation?. I'm sure I missed a few too. Given all the worries, the stock market--the public's short-term voting machine--is reflecting the negative vibes. The pendulum, representing the cycles of greed and fear, optimism and pessimism, is constantly in motion, whether we are discussing the stock market or public opinion. Remember, we buy when others are fearful, and sell when others are greedy. The current situation seems to reflect more fear than greed. So, we sit tight with our long-term investments and wait for sunnier skies to arrive.

While you won't find me making long-term stock market forecasts, I'm happy to see other people stick their necks out and do so. It's not out of fear that I refrain from stock market forecasts. It's a reflection of having been in this business for a while, and having firsthand experience with guesstimating the future. To quote Warren Buffett yet again, *"We've long felt that the only value of stock forecasters is to make fortune tellers look good"*. That pretty much sums it up. Forecasting is a waste of time, whether you are trying to forecast the stock market, economy, oil prices, politics or the weather. Now that I've provided cover for myself, let me offer a forecast.

I subscribe to a research service called Value Line Investment Survey. It's been in business since 1931 and provides research reports for approximately 3,500 publicly-traded companies. It provides a report every three months for each of the covered companies. I like that it's impartial; unlike a "Wall Street" firm, they employ no highly-compensated, well-dressed salespeople trying to sell investment banking services or looking for trading commissions.

I recently received the July 2nd issue and included was an update for the Dow Jones Industrial Index: Earnings and Dividends. Twice a year Value Line provides estimates for this index. I won't bore you with all the details. Suffice to say I believe their methodology is reasonable and based upon fundamental analysis of each company's historical performance and potential future results. What caught my eye was the range of expected target prices that Value Line now projects for the Dow Jones Index for the period of 2013-2015: the Low target is 15,379 and the High target is 19,801. The Dow Jones as I write this in early July 2010 is at roughly the 10,000 level. I'll do the math for you:

		Annual compound returns	
		2013	2015
Dow Jones low target	15,379	15%	9%
Dow Jones high target	19,801	25%	15%

These are the annual returns investors would earn should the Dow reach these levels by the years shown. This excludes dividends, which would increase the return in each case by approximately 3% per year. The worst case return would then be 9% plus 3% or 12% per year for the next 5 years. Not bad. In fact, in all cases these returns are above the long-term average return from stocks: around 10% per year over the past 75 years or so. Remember, this is Value Line's neck I'm sticking out, not mine. But I wouldn't have brought this to your attention if I thought it was unreasonable.

The Value Line price targets correspond with my view of our company investments. I believe we own many undervalued investments, which ***should*** perform well over the next 3 to 5 year period. What happens in the next 6 to 12 months is less important. This is not an instant-gratification business; nevertheless, I'm confident that we are invested in quality businesses, run by capable managers with significant personal stock ownership. Most importantly, the current valuations are very reasonable, in my view.

But didn't I say earlier that forecasts are a waste of time? The subtle difference is this: while we can't know with certainty, the **odds or probabilities** seem to be strongly aligned in our favor as long-term investors at this point in time. So the odds suggest better times ahead. When the probabilities are in your favor, it's time to place your bet. Of course as in life there are no guarantees. Meanwhile, I remain focused on the playing field (business results) and not on the scoreboard (current stock market conditions). If the businesses we own prosper over the longer-term, as shareholders we should do well.

Another observation: as of June 30th, the S&P 500 has provided the ***worst*** trailing 10 year performance on record. In case you're wondering, the data go back over 100 years. Only at two other points in time did the trailing 10 year return approach these low levels: 1938 and 1974. The good news is returns over the next 10 years ***after*** the 1938 and 1974 lows were much better. I'd be surprised if the next 10 years is a repeat of the past 10 years. Again, this is not a forecast, but an assessment of the probabilities. And although I'm relatively optimistic now, it's not due to some genetic defect. It's because there is so much pessimism today and more importantly, market valuations are relatively low. When more optimism surfaces and valuations become more generous, I'll start looking for the exits. But I don't believe we are there yet.

Lastly, Morningstar (a mutual fund research firm) recently published the results of a poll taken February 26th that included 815 investor responses. Over 92% of respondents expect 3-10% stock returns over the next decade. Only 4.6% expect better than 10% per year. When asked to choose if the U.S. is entering a long period of high growth, stagnation/low growth or decline, 77.6% chose stagnation/low growth. Such sentiments hardly suggest rampant bullishness. I'm also a believer that most of the time, the crowd gets it wrong. When the crowd zigs, look to zag.

Our stock portfolios continue to be represented by companies that should benefit from a stronger economy, such as industrial, manufacturing, energy and real-estate related companies. As expected, our economy-sensitive holdings have declined as fears about the dreaded double-dip recession have grown stronger recently. Our ability to look beyond the next 3 to 6 months allows us to hold on to these companies. I have added to some positions that had been reduced earlier this year after reaching fair, or intrinsic value; recent price declines have brought these companies back to attractive values. I look forward to Mr. Market giving us more of these opportunities. Remember, volatility is the friend of the long-term investor.

As I have attempted to take advantage of market volatility, our sales have resulted in realized capital gains. The good news is we made money on our investments. The bad news: Government is your silent (and needy) partner who takes a cut of every gain (except for non-taxable accounts). I have time before yearend to make further changes, but you should anticipate some amount of 2010 capital gains for taxable accounts when estimating your taxes. I do analyze the tax consequences of each sale, and generate taxable gains only when I believe the probabilities favor recovering over time the upfront tax payment. Please review your June custodian statement for a year-to-date summary and call me with any questions.

"A pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty"
-**Sir Winston Churchill**

As a country we have been through many difficult times; we've managed to navigate the tough periods and improve our standard of living. Churchill, who dealt with much more adversity than most of us ever will, frames the present situation well. As investors, we will look for opportunities amidst the difficulties.

As always, I appreciate your patience and loyalty. It makes difficult markets a bit easier to navigate.

Sincerely,

John Heldman, CFA