

Market Commentary Period ending June 30, 2008

Global equity markets posted their worst first - half performance in 26 years, with all the major broad market indices posting material declines. The S&P 500 retreated 11.91%, the Russell 1000 Value backpedaled 13.57%, the Russell 2000 was down 9.37% and the MSCI EAFE gave back 12.70%. Truly, a challenging environment.

The most important point to be taken from the statement above is that it is past tense, a key point for the long-term investor to keep in mind. Prudent investing must focus on the future. Despite some reasonably accurate fears about the litany of global economic issues, the price to value of much of what we own is as attractive as we have seen in years.

Arne Alsin's observation last month in *The Financial Times* is apropos in this environment. "More than any other variable, investors think too much about price. It is fair to say that a significant percentage of investors obsess about this. Instead of setting you up for success, a focus on price sets you up for failure. It is the single, biggest reason why most 'thinking investors' (oxymoron?) make dumb mistakes. Why is price such a problem? It's because price is meaningless when viewed in isolation. Without a frame of reference, price means nothing. The frame of reference required is a calculation of value."

Consistent with past experiences, our disciplined Large Cap value process held up much better than the major indices. The price trend in financial markets has remained essentially intact for the last year – commodity and energy stocks go up while economically sensitive or financial related stocks go down. Conversely, the absolute and relative value of each of the groups in general has moved in exactly the opposite fashion. The timing of when the price to value of stocks in each of these respective sectors begins to matter remains elusive, but our research suggests that when we look back three years from now, it will seem clear in retrospect that “leaning against the wind” once again is the prudent course for long-term investors. With stocks in emerging markets down 15% - 50% year to date (often a precursor to an economic slowdown), the US in a de facto recession and Europe slowing as well, we find it difficult to see how these anchors will not weigh on the current momentum in commodities. On that basis, we purchased Boeing, HSBC Holdings Corp., and Vulcan Materials during the last three months. These are high quality companies whose stocks have been punished over the past year due to what we believe are short-term cyclical issues as well as bouts of near hysteria from the general investor class. While timing is elusive, buying excellent businesses at 70 cents on the dollar is a solid long-term strategy. Cyclical “problems” are by definition cyclical and thus buyable.

We admit being taken back by the volatility in some of the stocks in our Small Cap portfolio, a number of which we owned for years, sold at superb prices, and then got clobbered when we bought them back at what we considered to be excellent values. Obviously, timing mistakes were made. In some cases, business models and values changed and we took our lumps and moved on. But in most cases, the underlying business values have not materially changed and

the stocks are morbidly inexpensive and are begging to be purchased. Our portfolio is the least expensive on a price-to-value basis that we have experienced since 2002, and possibly since inception. We have not lost our conviction to step to the plate in stocks where little has changed but the price. During the quarter we purchased First American Corp and PHH Corp, two very different financial companies with exposure to housing construction volume, but not housing credit risk. We bought Liberty Media Capital, an odd and misunderstood amalgamation of assets trading at a significant discount to the sum of its parts. We added United Online, an operator of consumer websites funded by its “never-say-die” internet dial-up business, and Scotts Miracle-Gro, the branded, dominant player in the lawn and garden service industry. These are high quality companies whose stocks have been punished over the past year due to short-term cyclical issues.

We reduced positions in a variety of stocks that were excellent performers and sold our entire position of Hilb Rogal & Hobbs, which was acquired, and Carbo Ceramics, which was a superb winner for us in oilfield services. We also sold our only bank stock, Boston Private. Investing in small cap banking stocks is a minefield given the current economic environment overlaid on what is generally an undiversified asset base.

The fixed income markets remained choppy as credit concerns initially subsided but then returned in full force late in the quarter. Multiple threats – economic softness combined with the perceived risk of rate increases to combat inflation and a weak dollar – led to disdain for anything beyond the highest quality securities. For the year, the fixed income indices are up; however they pulled back in the second quarter. RCB's approach has performed relatively well, as we remain invested in shorter-term, high-quality securities. Treasuries became less attractive as the flight to safety drove their yields down in relation to other high quality issuers. We will allocate holdings as warranted while maintaining our focus on quality.

While we are under no illusions that the global economy is anything but troubled, the price mechanism of generally free markets enables security pricing to at minimum “adjust,” and as is often the case at market extremes, over-adjust. The adjustment has been severe in some cases and is just now rolling through the markets.

Our firm and investment team are in excellent shape, which aside from cheap stock prices is the best indicator we have to expect solid long-term performance. We appreciate your continued support and look forward to working with you and your clients through this challenging environment and beyond.

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