

TIM MEDLEY

President, Client Advisor; Founded Medley & Brown 1988; Among Worth magazine's 250 Best Financial Advisors in America 1998 - 2002 and Medical Economics magazine's 150 Best Financial Advisors for Doctors; First Certified Financial Planner in MS 1977; BS Business University of Southern Mississippi.

KEVIN ANTHONY

Client Advisor; Joined Medley & Brown January 2001; Former Vice President of Finance and Chief Financial Officer Atlanta Falcons; MBA Finance and Management Emory Business School; Woodruff Scholar Emory University; BA Economics and Psychology University of North Carolina at Chapel Hill; Phi Beta Kappa.

CECIL BROWN

Vice President, Client Advisor; Joined Medley & Brown 1995; Previously with Investek Capital Management; Chief Fiscal Officer State of Mississippi 1988 - 1992; Founder Tann, Brown & Russ, CPAs; Member AICPA and MSCPA; Personal Financial Specialist (PFS); MPA The University of Texas; BA University of Mississippi.

JULIUS RIDGWAY, CFA

Portfolio Manager; Joined Medley & Brown July 2002; Investment advisor/portfolio manager since 1999; Trustmark National Bank 1989 - 1997; Member CFA Society of Mississippi; M.Sc. Accounting and Finance London School of Economics; MBA Millsaps College; BA University of Mississippi.

MEDLEY & BROWN, LLC
FINANCIAL ADVISORS

795 Woodlands Parkway, Suite 104
Ridgeland, MS 39157

P.O. Box 16725
Jackson, MS 39236-6725

PRSR STD
US POSTAGE
PAID
JACKSON, MS
PERMIT #369

Call us or visit our website today for more information:

601.982.4123 • 1.800.844.4123 • www.medleybrown.com

Spring 2006 Investment News

In Search of Philly Phenoms

In March, Tim, Kevin and Julius hit the road again in their ongoing search for great mutual fund managers. This time they headed to the City of Brotherly Love to call on a couple of managers whom they have known for several years and to meet a few new ones about whom they have grown curious. In all, they had five meetings during their two-day trip but still found time for a walk through historic Philadelphia where they attended the Ash Wednesday service at the 311-year-old Christ Church, dinner at a south Philly trattoria and a last minute visit to the Liberty Bell. Following is a recap of their fund due diligence meetings.

Arnie's Army

No, not Palmer. We're talking about the other Arnie from Pennsylvania, **Arnie Schneider**, President and Chief Investment Officer at Schneider Capital Management. We met Schneider and Portfolio Advisor **Steve Darby** at their offices in Wayne, just outside of Philadelphia. There we reviewed their investment

philosophy and process and discussed new developments since we first became acquainted with Arnie four years ago.

Schneider founded the firm in 1996 after leaving Boston's highly-respected Wellington Management Company where he was the firm's youngest partner and head of a Value team. With the help of six research analysts, he now manages \$4.3 billion for 39 clients including a couple of mutual funds bearing his name. (You know, there's just something about a manager who's confident enough to put his name on the fund!)

There's no doubt about who's the general at Schneider. As Darby put it, "We're not management by committee here. Arnie decides unilaterally." Darby was referring to the investment process at the firm whereby Schneider generates new ideas, instructs the analysts what to work on, and then makes all of the investment decisions. It is apparent that this intensive research-driven process has been very effective, largely because of Arnie's extraordinary abilities.

MEDLEY & BROWN, LLC

Composite Performance*

Average Annual Time-Weighted Returns (%)
Period Ending March 31, 2006

	Balanced Accounts	Growth Accounts
5 Years	7.95 %	8.77 %
10 Years	8.79 %	9.43 %
15 Years	9.51 %	10.35 %

**All client portfolios invested primarily in mutual funds with a combined allocation of less than 18% in cash and bonds are included in the Growth Composite. All client portfolios invested primarily in mutual funds with a combined allocation of 18% or more in cash and bonds are included in the Balanced Composite. Performance is net of management fees and reflects the average time-weighted return for all portfolios included in our Growth or Balanced Composite. Performance data includes reinvestment of dividends and capital gains distributions and changes in principal value. The larger a portfolio is in relation to others in the composite, the more weight its performance will have in the composite's time-weighted return. For several reasons including, but not limited to, asset allocation and investment choices, the performance of individual portfolios in the composite may vary significantly with some higher and some lower than the average. An analysis of variance is available upon request. Past performance may not be indicative of future results. Investment returns and values of client accounts fluctuate such that at any time an account's value may be worth more or less than the total payments into the account. Because accounts contain both US and international securities, results will depend on both management performance and underlying market and economic conditions throughout the world.*

Schneider and his team practice a deep value philosophy. That is, they typically like to buy companies that are at earnings troughs, are experiencing the headwinds of cyclical downturns, or have somehow shot themselves in the foot. They are attracted to out-of-favor companies where there is undue pessimism and situations where depressed earnings will likely be reinvigorated over the ensuing two to three years. As Schneider once put it, "We're looking for the companies that will be able to get up off the operating table." The decision to invest in such companies usually comes six to twelve months before signs of any fundamental turnaround, when the clouds are still very dark.

As you might imagine, this style of investing tends to produce somewhat volatile results. According to Darby, this approach leads to "more extra base hits and whiffs than singles." However, if you check Schneider's record, you'll find a very healthy slugging percentage,



Kevin and Julius visit the Liberty Bell

allowing them to easily surpass their three-to-five-year goal of 300 basis points (3%) per year over the Russell 2000 Value Index. (We should note that lower quality companies have proven to be especially fertile investing ground for the last few years, further enhancing Schneider's results.)

Schneider's small company stock mutual fund has done so well that it was recently recognized by **Lipper**, a leader in mutual fund analysis, as the 2006 Best Small-Cap Value Fund. Additionally, **Morningstar** has tabbed it as an Analyst Pick, one of its five favorite funds in the small value category. (Unfortunately for those who would like to invest, the Schneider Small Cap Value Fund is currently closed to new investors.)

It's hard to poke holes in Schneider's work, but Arnie did offer this observation about his approach: "If there is a criticism, it is probably that we are too disciplined." By that he is mostly referring to the firm's rigorous sell discipline. You see, they determine a price target for each investment, they trim the position as the target is

approached and they sell completely when it is reached. There is no letting a stock run beyond its perceived value, even though stocks can have a tendency of getting ahead of their underlying values. As a result, Schneider admits, "We leave a lot of money on the table because we don't play Greater Fool." The Greater Fool Theory, to which he is referring, says that if you buy (or hold) an investment at a price above its value, you have to hope that there will be a greater fool who will come along and buy you out at an even higher price.

"We're the Third Little Pig."

We're comforted by this self description from **Dave Baldt** and **Dan Scholl**, managers of the Schroder Municipal Bond Fund. Our lunch meeting with them was quite a contrast to the Schneider meeting. There's no investing under dark clouds here. This is more of a *belt and suspenders* approach, which is precisely what we like to see from a bond manager. Baldt and Scholl, whom we have known for years, focus on high-quality securities and treat low volatility as a priority. We think such risk aversion is important, especially during rising rate periods like we are experiencing now. Looking back to 1994, another rising rate environment and one of the bond market's worst years in recent memory, Baldt's predecessor fund was one of the very top performers.

A recent management discussion about their municipal bond fund summarized their work this way: "Although we analyze bond market trends, we believe our value lies not in our ability to forecast the market, but rather in our ability to exploit the municipal bond market's inefficiencies." Calling it one of the most inefficient bond markets in the US and perhaps the world, Baldt and Scholl spent a few minutes detailing the many factors that can cause pricing inefficiencies in the muni market. Scholl provided us with several live examples of this pricing inefficiency, complete with trade data.

The investment process at Schroders is a fundamental, bottom-up approach designed to uncover bonds whose intrinsic values are greater than their market prices. This is the same concept we look for in stock managers. In fact, Baldt, a former Morningstar Fixed Income Manager of the Year, likes to refer to himself as "a small-cap value manager."

In discussing this idea, he spoke to the size advantage of his fund in exploiting the market inefficiencies and offered this analogy: "Imagine several bond managers on a lake, each in a 65-foot boat, and then imagine us in a kayak. We can simply get into some small areas where the others cannot go." He explained that most managers tend to focus on larger issues (think City of Chicago or State of New York) where demand produces higher prices and lower yields. Baldt, on the other



Tim, Julius and Kevin are pictured with Dave Baldt (back, center) and Dan Scholl (front, left) of Schroders Investment Management

hand, is able to focus on smaller regional issues that fly under the radar and present better opportunities (i.e., Gwinnett County, GA or Pingree Grove, IL). Fishing in these waters does require more due diligence, but judging by their track record, the folks at Schroders appear to have the necessary resources, analytical expertise, commitment and patience.

Let's Get Acquainted

While in the suburbs, we had the opportunity to meet for the first time with **Jim Stratton**, manager of Stratton Growth Fund, another 2006 Lipper Fund Award winner (Best Multi-Cap Value Fund). We were joined by **Jerry Van Horn**, manager of the Stratton Small-Cap Value Fund and **Jim Beers**, manager of the Stratton Monthly Dividend REIT Shares for a discussion of their firm's investment philosophy, process and performance.

A second get-to-know-you meeting, and our last session outside of the city, was at The Killen Group, investment advisor to the Berwyn Fund, where we talked with **Lee Grout**, Portfolio Manager and Head of Research, and **Ray Munsch**, President.

Back in downtown Philadelphia, we traveled to the offices of Cooke & Bieler for our final "first" meeting. There we met with Partner **Sam Ballam** and Principal **Daren Heitman**. Although Heitman just recently joined the firm, we have known him from his days at Skyline Asset Management in Chicago and more recently at Schneider Capital. When we mentioned to Daren that we had been to see Schneider, he responded, "You got some of Arnie's time? That's a real coup. He spends 95% of his time thinking about investing."

With a desire to take on portfolio management responsibilities that were unlikely at Schneider, Heitman made the move to Cooke & Bieler. There, a team approach is used to manage \$8.2 billion of assets

including two mutual funds for Wells Fargo. When asked to identify their edge, Ballam responded, "We have seven very experienced [analysts/portfolio managers] each responsible for ten to twelve stocks." Their investment philosophy is to focus on downside risk ("only one down year in the last 31") by concentrating on high quality companies and their business prospects over the next three to five years. They like to buy when there is the potential for 30% to 50% price appreciation. We like this type of thinking.

Other Recent Travels

In November, Kevin attended Litman/Gregory's AdvisorIntelligence Conference in Lafayette, California. Speakers included **Paul McCulley**, Managing Director and Portfolio Manager at PIMCO, **Robert Hagstrom**, Portfolio Manager at Legg Mason and author of "The Warren Buffet Way" and **Bill Nygren**, Portfolio Manager at the Oakmark Funds.

While in California, Kevin went to San Francisco to meet with **Kevin O'Boyle**, Portfolio Manager of the Presidio Fund. O'Boyle was previously the longtime manager of the Meridian Value Fund.

In December, Julius attended a seminar in Boston hosted by the CFA Institute entitled Equity Research and Valuation Techniques: Finding Fundamental Value in a Low-Return World. Speakers included **Aswath Damodaran**, Professor of Finance at NYU, **Michael Mauboussin**, Chief Investment Strategist at Legg Mason and **John Gunn**, President and Chief Investment Officer at Dodge & Cox.

In March, Tim attended Thornburg Investment Management's Investment Masters Conference in Santa Fe. Among the speakers was **Bill Fries**, former Morningstar International Fund Manager of the Year for his work on the Thornburg International Value Fund. Fries also manages a portion of the Masters' Select International Fund.

In the News

Medley & Brown, LLC was included in Nelson Information's **World's Best Money Managers** for its fourth quarter performance last year. Nelson ranked Medley & Brown's Balanced Portfolios composite 18th in the category of International Balanced/Multi-Asset and its Focused Equities composite 21st in the category of US Growth and Value Equity.

We Have Grown

We are pleased to announce that **Lizz Gardner** has joined the firm as an operations team member.