

Quarterly Newsletter

4th Quarter - 2008

Market Overview:

The year that many would deem the most extreme year in the markets in 70 years was concluded in a fitting fashion in the 4th quarter. Volatility increased to a sustained level not seen since the Great Depression, and the year of 2008 closed out with 17 days that saw a greater than 5% move in the S&P500 index. To be frank, while I firmly believe that volatility creates opportunity, I am not sad to see this year fully framed in the rear view mirror. Put bluntly, this year was dismal for our accounts; the fact that it was less dismal than the stock markets on average is of little solace. Losing greater than 25% of your money in a year is not why you pay me, and for this reason, all management fees to Remick Capital will be waived this quarter as I do not feel it is appropriate to add insult to your financial injury. All commission waivers for this quarter will be rolled forward to reduce future management fees.

Returns* ended 12/31/2008:	1 Qtr Return	1 Year Return	3 Year Return (annualized)
Wilshire 5000 Index (Ticker: VTI)	-22.71%	-36.66%	-8.22%
MSCI World Index (Ticker: EFA)	-19.75%	-43.15%	-7.36%
Lehman Aggregate Bond Index (Ticker: AGG)	+5.22%	+5.87%	+5.52%
Remick Capital (Account Composite)	-27.74%	-26.19%	N/A

As you can see from the above table, it was not hard to lose a ton of money in 2008 by investing in stocks. Those who reached into the overseas investment sphere to hunt for returns were punished the hardest. With the exception of those who invested in conservative bonds (and a few very skilled, or very lucky, stock pickers), there were no winners in 2008. Of the [three goals](#) I attempt to achieve in all accounts managed by Remick Capital, I have only succeeded at one since inception (and through 2008); outperforming the US Stock Market. Beating "inflation +10%" and "not losing money" have both been elusive targets so far.

As disappointing as 2008 was for our accounts, I still believe over 3-5 years these goals are attainable, and I will continue to work as hard as I can to achieve them.

Given that the investments we hold are quite a bit different on average from the composition of the market, I thought it might be instructive to capture some statistics about our holdings with respect to the market. I have done my best to keep this table condensed, while also explaining terms so you do not feel as though you are reading a finance textbook. As always, please note that for accounts with under \$100,000 in assets the concentration levels, individual holdings, and returns will all vary (perhaps quite widely) from the Remick Capital account composite.

As disclosed in my company [overview document](#) I believe the best way to approach investing is to pick a small selection of the best and cheapest investments available. For this reason, our portfolios will rarely (if ever) resemble 'the market.' The table on the following page shows how our accounts match up against the market averages on a few key metrics. These metrics will be constantly changing, but this table gives a snapshot of our accounts at the end of the 4th quarter.

* The [Wilshire 5000 Index](#) is a collection of stocks that is designed to approximate the returns of the entire US Stock Market.

The [MSCI World Index](#) is a collection of stocks that is designed to approximate the returns of the global stock market with US stocks removed.

The [Lehman Aggregate Bond Index](#) is a collection of bonds that is designed to approximate the returns of the entire US Bond market.

All above returns are based on Exchange Traded Fund (ETF) market returns to make the numbers representative of actual investor returns.

For Remick Capital performance data, please see our [performance disclosure](#) document for the basis of results.

Composite Portfolio Summary as of 12/31/2008

	Remick Capital (Account Composite):	Wilshire 5000* (US Market Index):	Discussion:
# of holdings in the top 75%	Six	>500	Remick Accounts are highly concentrated; our top six investments represent just over 75% of total account value.
Weighted Average Earnings Yield	20.41%	8.20%	The metric measures the level of earnings of all portfolio companies divided by the current market price. A higher earnings yield means that, for the same amount of investment dollars, our portfolios are buying more company earnings for a given amount invested. This ratio is simply the inverse of the commonly cited price/earnings (p/e) ratio.
Weighted Average Dividend Yield	4.83%	2.80%	The dividend yield measures the amount of dividends and interest that is paid by the portfolio investments as a ratio of the price. A higher dividend yield means that, for the same amount of investment dollars, our portfolios are getting more cash income for a given amount invested.
Top Industry Weighting	75% (Financials)	28% (Consumer Non-Durable)	Remick portfolios are heavily concentrated not just in individual companies, but also by industry group.
Average (Mean/Median) Market Capitalization	\$14.1 Billion / \$749 Million	\$2.1 Billion / \$160 Million	On average, the market capitalization (value) of our portfolio companies' equity is greater than the average US company. This metric is not particularly relevant from a business standpoint, but many investors like to categorize their investments by size.

* Wilshire 5000 market data obtained from <http://www.wilshire.com/Indexes/Broad/Wilshire5000/Characteristics.html>.

Investment Updates:

Below is a summary of a few of our portfolio holdings and how they performed during the quarter. Please note that these investments are not listed in any particular order and are just meant to be a sampling of some of our holdings. For those of you short on time, I can summarize this section quickly: everything went down during the quarter. However, if you are interested in the details, please read on.

Accredited Mortgage Loan REIT Trust, 9.75% Cumulative Preferred, Class A (OTC: AHHAP) – Our shares of Accredited ended the quarter down slightly (including dividends). During the peak of the insanity (and extreme illiquidity) in the market, the shares traded down more than 50% at one point but later returned. Overall, Accredited continues to originate loans, and our dividends continue to be paid as contracted.

Sears Holdings (NASDAQ: SHLD) – Sears was not in any way a star performer for us this quarter as the shares dropped greater than 50%. The company continues to be dragged down by its poor execution and lack of clear corporate vision. However, given its very attractive valuation and management team that I feel is well incentivized and honest, I still believe good things are in store for us here.

Fairfax Financial (NYSE/TORONTO: FFH) – During the November market low Fairfax announced that they had unhedged their stock portfolio. This hedge has helped to protect the value of Fairfax's equity investments during these

tumultuous times, but the company believed that it was no longer worth maintaining due to the many stock bargains they were finding. In the short term the company has been right, and this should help them report great results in Q4. In addition to the adroit moves by their stock picking team, the Fairfax bond team was also making a few aggressive bets on long term government bonds. These kinds of bonds increase in value sharply as interest rates drop, so while I offer no precise prediction of how Fairfax will report having fared in the 4th quarter, I can only assume that it will be generally good. But, despite all this, Fairfax shares dropped around 10% during the quarter.

Wells Fargo (NYSE: WFC) – While the very high pricing for Wells Fargo stock at the end of the 3rd quarter gave us opportunity to sell a few of our shares, we certainly would have done well to sell more. Wells Fargo shares dropped over 20% this quarter as investors struggled to decide what the company was worth. In the midst of all the mayhem, Wells has completed their acquisition of Wachovia and expanded the companies’ business reach. I believe that while this acquisition adds some execution risk and some uncertainty to our Wells Fargo investment, I think the price paid was good. Within two or three years it will be clear whether this was a fair acquisition or a great one, but I am very confident that it will not be a bad one.

Update: After the close of the quarter, Wells Fargo shares plummeted from around \$28 to around \$10. I believe the story for Wells is unchanged despite the media uncertainty surrounding government actions and all accounts have been purchasing Wells Fargo shares and preferred stock at these (very) attractive prices.

Compton Petroleum (NYSE: CMZ, TORONTO: CMT) – Compton’s shares have been absolutely demolished by the market. They are now trading for under \$1, and rumors are swirling. Natural Gas pricing has dropped to a level less than half of what it was just 12 months ago, and there is real risk that Compton might not survive for very long given their sizable debt load. Unlike other investments where I have said that a reduced price does not indicate a lower value, such is not the case with Compton. There is substantial risk here given the economy (and more importantly, low natural gas prices). With this said we are holding our shares and potentially adding if the conditions warrant. Despite the high risk, there are many situations that could unfold and lead Compton’s stock back above \$10 in short order. Time will tell, but this will remain a very small holding until the situation becomes more predictable.

Nicholas Financial (NASDAQ: NICK) – The combination of low trading volume, a hated business model, apathy by investors, and tax loss selling pushed Nicholas shares down tremendously during the quarter. Unlike Compton, I do not believe that risks have increased substantially here, and I am getting more excited about our investment in Nicholas. The company is in a good position with its lenders all things considered, and is still profitable. The CEO has been a small buyer of the stock, and the shares traded for less than half of liquidation value at the end of year. At the end of December, I opted to liquidate almost all of our holdings in Progressive Corp and put the money (plus idle cash) to work in Nicholas shares making it our second largest holding in aggregate across all accounts. I have also posted an [updated report](#) on the site that discusses the investment case here and refreshes some figures.

Are the Ravens Leaving the Tower?

As my clients and friends know, I am a big fan of capitalism generally. I am also a (big) fan of America and our financial system, but I will not hesitate to point out the way under-regulated greed and misaligned incentives have helped push our country far closer to the abyss than I would have ever imagined.

I think during good times people forget why banks exist, why the paper that our government prints our money on has value, and why we trust strangers when we buy things from faraway places. Essentially people forget why it is that our economy functions the way it does taking it for granted because it works. There are many unspoken rules and assumptions that allow our form of capitalism to function, and recently many of the rules have been challenged, threatened, and, in degree, nearly broken. These recent transgressions have posed some questions in peoples’ minds about how stable our economic system is, and, more fundamentally, how stable the world economy is. While I will not argue that we have reached some economic utopia where perfection has been achieved, I will reiterate that our economic system has shown a great ability to raise the average standard of living better than any other. Increasing economic efficiency and providing a fairly transparent market for skills, products, and services will of course present the world

with its share of relative winners and losers, but the key advantage of our pseudo-capitalism is that *on average* society is, and will be, better off.

There are, however, prerequisites to our market based system functioning properly:

- Education levels must be consistently strong in our population
- Rule of law must be evenly and rationally applied
- Corruption must be vigilantly hunted down and suppressed as much as possible
- Reasonable policies must be made and maintained to insure that our collective national assets are used equitably for the benefit of all
- Finally, many industries need to have a lightweight yet comprehensive form of government regulation insuring compliance to certain standards, which are not easily regulated by normal market forces (pollution, insurance, banking oversight, etc)

Recently there has been a lot of talk. “Has American-style capitalism failed?” To some extent, this kind of question is axiomatic: Our economy is what it is, and recently it has failed in many respects indicating that the answer to this question is “yes.” *However, the underlying problems of the recent events have a lot more to do with the underpinnings and prerequisites of capitalism than with capitalism itself.*

Of the prerequisites for Capitalism, America is ahead of most societies (though we are far from perfect), but regarding education, we are behind and getting worse. Capitalism is just a form of economic order that allows the populace to move capital to areas that they collectively value the most. Adam Smith termed this the *Invisible Hand*. However, without a strong base of education, there will be many economic actors who will not have the sense of where they should steer their piece of the economic pie. A society lacking proper education will no longer be as viable a place to do business; there will be less innovation, less productivity, and less real wealth creation. This will also, over time, erode the other key tenants of our society (good laws, lack of corruption, etc).

With the rise of China, India, and a smattering of other formerly “Third World” countries, it is easy to see that we are indeed losing our prominence on the world stage. While some may see this as a sign of trouble for us, I see it only as opportunity. Our economic style and way of life has helped to influence all these countries in a major way (for right and wrong), and our future is now tied with theirs through trade, technology, and our largest companies. We also have much to (re)learn from our companions across the seas. At times I think we are so immersed in competition with our neighbors overseas that we miss *why* they are so successful. China and India have undertaken massive efforts to increase the education levels of their citizenry and improve their laws and regulations. Bill Gates cited the best University in the world for recruiting to be in India, and he said #2 on the list was not even close. These countries have moved past their old fronts as cheap places for labor. More and more they are being perceived (rightly) by businesses as places where genuine talent and intellect can be found.

As I think through the myriad of issues that our country faces, I am reminded of a trip I recently took to Europe during which I visited the Tower of London. On my tour of the Tower grounds I learned that there are ravens that live there, and an old legend says that if there are ever fewer than six ravens on the Tower grounds, the kingdom will fall. Now just for good measure, the ever pragmatic Brits make sure they keep a few extra ravens on the grounds, and to be extra careful they clip their wings and keep the ravens fat and happy so leaving is the last thing on their minds. As I think of the current economic situation and constant questioning of whether our form of capitalism is really the best for all, or worse, whether it even works, I am left with the question: “*Are our ravens leaving the tower?*” Could we be watching the downfall of our American society?

For the Invisible Hand of Capitalism to function properly, it is crucial that education is strong. There will always be a division of wealth and power in a free society, and natural talents and hard work will separate, but a system of capitalism and democracy relies on everyone having a similar shot at success. If too many people are not prepared for the harsh competition for resources that occurs in a capitalistic system, the division of wealth and overall wealth creation will both move in the wrong direction.

Some may not immediately see the issue of having too large a distribution of wealth, but a favorite quote of mine captures this issue in beautiful simplicity:

“Any [economic] system produces winners and losers. If the gap between them gets too great, the losers will organize themselves politically and seek to recast the existing system...” – **Henry Kissinger** (in the *Economist*)

Or put in a blunt and perhaps less elegant way, here is a reference for the younger generation:

“Hungry people don’t stay hungry for long.” – **Rage Against the Machine** (from the song “New Millennium Homes”)

If we as a society can come to grips with the above, and remember what it takes to make our economic system succeed, I think our outlook for America will be bright. Education needs to be (re)valued by our society, and our economic system needs to be reinvigorated with support and understanding from the populace. Our economic bicycle has encountered two flat tires, and we need to fix them fast, but we do not need to switch to a unicycle.

I apologize if this letter was a bit different than my normal fare, but I hope you found it valuable. While I promise not to make a habit out of providing social and political commentary, I thought this season of potential change was a good time to discuss a few things more fundamental to society and wealth creation than my usual mumblings about cheap stocks or economics. We as a society are very wealthy, but our wealth lies in things that are hard to see and measure; they lie in the prerequisites for capitalism, not in our nice cars and big houses - although those things are a nice byproduct!

To close, I am confident that America’s ravens will be here for some time, but our work will not be easy or pleasant. I have placed my money where my mouth is as Remick Capital portfolios are essentially 100% invested into North American stocks (and bonds), and I look forward to telling those who think Americans will not turn the economic situation around, “I told you so,” when this is all behind us.

I leave you with a quote from the late J.P. Morgan:

“Remember, my son, that any man who is a bear on the future of this country will go broke.”

As always, my money will be invested right alongside yours so you can be sure that I will work diligently to make sure our investments will be profitable ones, regardless of the market conditions. I appreciate the trust you have placed in Remick Capital as your Investment Advisor; I will work hard to make our relationship as profitable as possible.

If you ever have any questions about this report, your investments, or anything financially related in general, please do not hesitate to call me.

Sincerely,



Benjamin Hacker
Principal,
Remick Capital, LLC
(503) 702-2712
www.remickcapital.com

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