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Jonathan Smith & Co.
INVESTMENT COUNSEL

Everyone loves it when movies, books, careers, and long lives finish well. It's hard to accept it when they don't. Finishing well isn't easy. For instance it took nearly 50 years for Walt Disney's original animation art collection to finish well. Back in 1960, Walt himself handpicked 250 pieces of original animation art - backgrounds, preliminary paintings, and sketches. He boxed them up, and shipped them off to Japan for a touring exhibition which was set to coincide with the debut of the film "Sleeping Beauty."

Mitsukoshi, a department store in Tokyo, got first crack at the exhibit and from there it traveled to 16 other stores in Japan. The collection must have been stunning: scenes from "Sleeping Beauty," "Flowers and Trees" (1932) and "Three Little Pigs" (1933). Also included were backgrounds from the "Nutcracker Suite" and "Rite of Spring" sequences in the 1940 film "Fantasia."

When the whirlwind tour finally landed and the country was all aglow from having enjoyed the exhibition (and the movie), Walt donated all the artwork to the National Museum of Modern Art (NMOMA) in Tokyo. What looked like a wonderful Disney ending wasn't. The NMOMA, it seemed, felt the Disney artwork wasn't a "good fit" for its permanent collection. So they lined up nearby Chiba University to accept the donation, figuring the pieces would enhance their visual arts program. There was still no happy ending. Chiba's academic focus, it turned out, was medicine, science and math, not art. Perhaps they couldn't picture Walt's "Three Little Pigs" hanging in the biology lab.

So, it turns out the whole exhibit got shoved in the back of a janitor's closet - literally. And there, for 44 years it sat, until four years ago when somebody opened the janitor's closet, tripped over a cardboard box, pulled a string to turn on the bare light bulb, and said "what the heck is *that* stuff?" When the Chiba University powers that be finally sorted it out, they boxed up this veritable Rip Van Winkle of an art collection, and shipped it *back* across the ocean to Disney. Were they seeking atonement for almost a half century of artful neglect? No! They were asking Disney to repair and

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restore the pieces! A group of Disney technicians set out on a year's worth of restoration work on "Sleeping Beauty" and the other 249 pieces. When Beauty looked as good as Walt would have wanted, they boxed her up once more, along with the other 249 pieces *plus 300 more,* and shipped the whole bundle back to Tokyo.

Just as Walt originally intended, over the course of two years, seven museums proudly delighted millions of Japanese children, their parents, and their grandparents before the tour finally came to a temporary rest at the Tokyo Museum of Contemporary Art. It would only take one more transpacific flight before Walt got his 'happily ever after.' Since Chiba was still the owner, Disney promised it would give the university hi-resolution digital copies of *all* the artwork *and* $1 million worth of scholarships *if* Chiba promised to ship the collection back, once more, to Disney. Nearly fifty years and twenty thousand frequent flier miles later, the artwork is safely home.

Superior investment results really matter; they are our imperative. But there's something else that matters which, if we miss it, will mean we haven't done our job well even if the results are superior. That 'something' is helping clients finish well. Over the last six months, two of our clients finished well: one in September and one in March. Each lived into their late eighties. Each enjoyed meaningful relationships with family and close friends. Each exhibited gratitude for all that life had given them, despite numerous challenges and setbacks.

Neither client outlived their assets and both left what they owned to those they loved. We got to serve them, love them, help them cross the finish line, and lay them to rest. The family of the first client asked me to be a pallbearer. The cousin of the second, after calling me repeatedly with health updates at the client's request, finally asked what line of work I was in. When I replied that I was her investment advisor, the family member said, "from the way she spoke of you I thought you were her rabbi." In this profession, it doesn't get more sacred than that.

Another dear friend recently finished one chapter of life well and started another. Team member extraordinaire Eileen Armenante retired from Jonathan Smith & Co. on April 1st, after serving us and our clients for many years. Nine quick years ago, Eileen brought to us her pair of "northern eyes," as she called them: the ability to both see and understand our value proposition from the client's perspective. Eileen gave us unique insight on our written words, our advertisements, our day to day operations; in other words, everything that we do.

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I'll never forget, during the transition of a new client, as the assets were being transferred from the old custodian to the new, how Eileen went back and poured over three years of statements, trying to make sense out of them. A true guardian, Eileen was convinced that something didn't add up. She realized that not only was the former advisor charging twice the management fee the client had agreed to, but he had added an extra month of fees when the account had closed. Few people care as much about the last three years of a widow's brokerage statement as Eileen. We could fill an entire commentary with all that Eileen did for our clients and her team. Much of it went unseen, but all of it mattered, and was greatly appreciated. She finished well in every respect.

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To say that the stock market's performance and our investment performance over the last three months has been disappointing, depressing, and frustrating is an understatement. By all measures, 2008 has been an ugly year.

Financial panic got going in earnest with one of the worst Januarys in memory. By the end of the first quarter, many global markets fell in the double digits (or close to it). In the U.S. market, we saw the near collapse of the investment bank Bear Stearns due primarily to a crisis of confidence (a "run on the bank") rather than a change in Bear's business value. It was clear to many that Bear Stearns was worth much more than the $2 per share JPMorgan originally agreed to purchase it for. Superb deal for JPMorgan. Bad deal for Bear Stearns. But in this environment, we've seen a movement from a wild tolerance for risk to zero tolerance for risk. The pendulum has swung. And, as is often the case when people are panicked, most prices fell, regardless of the quality of a business. It's precisely the kind of market where opportunism and patience meet.

The monetary and fiscal authorities moved with amazing speed, with the Federal Reserve cutting the prime rate to 5.25%, and the administration and Congress coming up with a fiscal stimulus package around $150 billion dollars. The Fed, in our view, deserves applause for the way they have acted to create new ways to keep the financial and credit markets stable. In a time where some credit markets have stopped functioning, the Fed stepped in to help those markets re-establish equilibrium. This is in the best interest of all investors. We need properly functioning credit markets to keep our other markets (stock market included) functioning. The key point is that the monetary and fiscal policy makers are focused and engaged, and Ben Bernanke has demonstrated he will do what is necessary to stabilize the markets and restore confidence. Will all of this be

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successful? We think so. This does not mean that we will not have a recession or that financial markets will not continue to be volatile.

Despite all the turbulence, the market's performance has been (and is) perfectly normal. Pleasant? No. Normal? Yes. It's times like these that let us practice what we preach, holding stocks whose prices have fallen, but whose intrinsic values have not. In fact, it's not just holding, but having the willingness to buy more shares of businesses whose prices have fallen and which represent excellent long term opportunities for those who can remain patient.

I know many people are focused on the question of whether we will go into a recession or not. If we go into a recession, history says we will come out of it. We have had only two significant recessions in the past 25 years that at most lasted about 17 months. Stock valuations are as low as they've been at any time since 2002 and may already fully reflect a recession. So, why not invest for the 95% of the time the economy is growing, rather than the 5% it is not?

At the core, we know that for our clients to profit from this market will require that we focus on what the business values of our companies are today *and will be* in the future rather than on the value that a panicked market ascribes to them. If someone offers me $50 per square foot for my home I would reject the offer out of hand and would not lose a wink of sleep over it. If someone offers to buy one of our holdings for 50% less than we think it's worth, our response is exactly the same: thanks, but no thanks. But if they're willing to sell to us for that price today, we will gladly buy it. The business values we use drive our investment decisions, however, we don't know when those values will be realized, which is why we hold fast during uncertain and choppy times. Patience (or what we like to call "time arbitrage") is, in our experience, the single greatest trait common to those with superior long term investment performance.

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