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2009 started out with the Dow around 8,700. Ten weeks later, the Dow was 6,500 and the globe was on the brink of a Depression. The market snapped back after the March low and the Dow rallied to close the year near 10,500 fueled by the healing global economy. It was a long and trying year but it wound up being a very good one. For the year, the S&P gained 23.5% and the Dow gained 18.8%. On average in all our accounts, our equities gained approximately 29%. Together we stayed focused, disciplined and fought the urge to panic. The reward was a very good year.

We learned very valuable lessons in 2009 that will become assets for us in the future. One key lesson that emerged as our theme of the year came from a quote from Tolstoy, "**The strongest of all warriors are these two – patience and time.**" For our year end letter, we thought we'd recount some of those points for you from our weekly emails...

1/2/09 Don't wait until you feel better to invest – counter-intuitive thinking

We said *"Over the past 9 recessions, once the market bottomed the next 12 months saw gains in a range of 31% to 59%. The average gain following a bottom was 39%. We believe this recession's bottom was in November when the Dow touched 7,500. A 39% gain would take the Dow to 10,500 later this year."*

(While we were wrong about the final bottom, the Dow did manage to close the year at 10,428)

We also said, *"Every recession feels terrible...and in every recession in the past, the right thing for stock investors to do was to stay in the market and ride the storm out. The danger for investors is to cash out after the damage is done and vow to only get back in when they feel better. By the time you feel better about the economy the market will be dramatically higher."*

1/16/09 TARP is going to work

In discussing the government bailout of the banks, we said, *"The media loves to tell you 'We've poured \$350 billion into the banks and we'll never get that money back.' That simply isn't true. Not only will the government injection of capital give these institutions time to heal, we believe the government will get repaid on their preferreds with interest and profit from the warrants on the common stock."* Amazingly, here a year later, 6 of 7 big banks have fully repaid their TARP investment with interest. Plus the government has reaped big profits on the warrants.

1/30/09 Buying AFLAC during the panic

We added a significant position in AFLAC in most of our client accounts after the shares fell from \$45 at the start of the year to \$23 by the end of January. AFLAC has a great long-term track record of growing revenues, earnings and the dividend and they are active buyers of their stock. We said at that time, *"We cannot predict what the stock will do over the next few weeks. When we make a purchase like AFLAC, our focus is on what the stock can do for you over the next 3-5 years...not the next 3-5 weeks."* This philosophy tested our patience as AFL fell another 50% over the

following month but it ended the year at \$46+ doubling our money in a relatively short amount of time plus paying us a 4.9% dividend yield vs. our cost.

2/20/09 Turn off the TV

We reminded you that the media is not your friend as an investor... *"In this environment patience is our best virtue. The negativity and gloom is extremely high. The media isn't helping as they seemingly glorify the "collapse of the American Dream", etc. We met with clients this week and they commented on just how depressing the news is. Our suggestion...just turn the news off. Watch a good movie or listen to some nice music but don't obsess nightly over the "doom of the day". Give this economy some time to heal. Don't stay glued to CNBC or FOX or your computer looking at stock quotes and listening to the extreme negativity. It serves no purpose other than potentially leading us to make irrational decisions with our capital. With the advent of the internet and cable news, Americans have become addicted to immediate access to information. As investors this short-term mentality rarely serves us well."*

3/6/09 The market makes the bottom – the beach ball effect

We wrote our most important weekly email on Friday, March 6th which turned out to be the day the market made its bottom around 6,500. We said, *"It is like a beach ball being pushed under water. The deeper you push it the greater the pressure is to release it. The deeper it goes, the faster it snaps back. The same is true for stocks. Mild corrections in stock prices are typically met with tame rallies. History shows that severe, extreme bear markets are usually met with snap back recoveries that are dramatic and fast. It is going to take a long time to get back to 14,000 on the Dow but the move to 8,000 or 9,000 could come extremely quickly."*

Warren Buffett famously said, *"Be greedy when others are fearful and fearful when others are greedy."* That quote was very appropriate for March 6, 2009 and just 60 days later, the Dow had rallied from 6500 to 8500.

3/27/09 Should we take investment advice from Glen Beck or experienced money managers?

One more comment about the media... *"We have written numerous times about the media stoking fear – i.e. "bad news sells", etc. and I think we've been right to encourage you to temper what you hear from the media. A few clients have mentioned to us recently they are scared to death about the market because of what they are hearing Glen Beck, Rush Limbaugh and others say. These commentators are saying Obama's budget is going to bankrupt our nation, China will stop buying our bonds and the market is about to plunge."*

*Rather than listening to what Glen Beck is **saying** to make our investment decisions, we'd prefer to watch what Warren Buffett, Chris Davis, Longleaf Partners, Fairholme and others are **doing** with their investment portfolios. They aren't running to the exits based on the Obama budget."*

4/3/09 Great insight from Chris Davis on investor behavior

Chris Davis is the third generation of the Davis family to run the Davis New York Venture Fund – one of the largest US equity funds. He said, *"Over time stock prices are driven by the value created by the business but in the short-term, they are frequently driven by emotions. Investor behavior tends to be destructive – when things are going up, they want to buy into what has already worked. When things are going bad, they want to get out – after prices have already fallen. **Investors tend to do in the present what they wish they had done two years ago.** The trick is to look forward two years and ask, 'When I look back in 2011, what will I wish I had done in April 2009?'"*

5/22/09 Reiterating our investment philosophy

In May, we reiterated our investment philosophy saying, *"We repeatedly say to you that we don't obsess over the next 3-5 weeks and rather make our investment decisions for you based on the next 3-5 years. We try to be careful and deliberate in how we invest your very hard-earned money. Our model is pretty simple – to put your money into great businesses as fractional **owners** of those businesses not to try to be short-term **traders** of their stocks. Too much trading is a product of thinking you can out smart the market. We've learned we cannot out smart the market on a trading basis so we have chosen the patient, calmer, more rational approach of being long-term **owners** of companies."*

6/5/09 Bull markets climb walls of worry

We said, “There is a great old saying about the market – “Bull markets climb walls of worry”. The market doesn’t stay at its low until all the worries have abated. History shows that the market starts to go up just when things look the worst. 2009 is a classic example of this. In early March when the talk of nationalizing banks was still around, the market started to go up. We went from 6,500 to 7,200 and pundits said, “It will go back and retest”. It didn’t. It went to 8,000. Talking heads then said “That is it...too much, too fast, the economy is too full of problems to go any higher” and....it went to 8,500. Last week at 8,500, almost to man the market experts were calling for a big correction and a possible retest of the 6500 level. The market went up 300 points this week.”

7/10/09 Focus on cash flow

Emphasizing the importance of cash flow, we said, “The value of any financial asset is the present value of its future cash flows. A business must eventually return cash to its owners to be of value. Small business owners understand this point intimately, as their livelihood is based on the cash that comes in the door versus the cash that goes out. Ask a small business owner about his reported earnings and you’ll likely get a quizzical look. Ask him about the cash flows and you’ll get the story. Greatmark is intently focused on cash flows. We tend to own businesses that produce significant excess cash flow and they use that cash flow to buy back stock, pay a growing dividend and make smart acquisitions. We think of owning stocks like actually owning the businesses themselves.”

8/21/09 Avoid the advice to trade frequently

Reiterating our belief in patient long-term investing vs. short-term trading, we said, “The market sold off hard on Monday and the bears on TV were saying, “That’s it, the rally is over, prepare for 10-15% downward moves...” The bears have been calling for this correction for months. In late May the old adage of “Sell in May and go away” was being touted by market experts. And yet, the rally has persisted. We remind you that many of the pundits on TV are market strategists for major brokerage firms. They come on TV and promote taking profits, trimming winners, raising cash, hedging portfolios, etc. Brokerage firm strategists are always advising trading – either working money into stocks or trimming back portfolios. While that advice is prudent at times, let us never forget they get paid to get clients to trade their accounts.”

9/25/09 The bear case is always more convincing because it deals in the present

The bear case is always more articulate and compelling and rational because it deals in the present. But the market always looks to the future. 2009 is a classic example of this – the market started higher despite worsening economic news. The market was seeing the recovery to come long before the pundits who kept trying to talk the market down. Bill Miller at Legg Mason had a great recap of the mindset of a market bottom and how the “experts” react at each step.

- First, it is said the fiscal and monetary stimulus are not sufficient and will not work.
(we’ve heard that all year)
- When the market starts up and economic forecasts begin to be revised up, the refrain is that it is only inventory restocking and once it is over, we’ll have a double dip. *(we’re hearing that a lot now)*
- Once the economy begins to improve, the worry is that profits won’t recover enough to sustain stocks.
(“experts” today keep saying profits won’t emerge)
- When profits do recover, they will say the recovery will be jobless
(“jobless recovery” is the trendy forecast today)
- When jobs are created, the fear will be it cannot be sustained. *(probably what we’ll hear late this year)*

11/6/09 Corporate cash at record levels – major deals being done

We reported to you that cash on corporate balance sheets had reached 11% of total assets up from 9.8% at the start of the year. Businesses are stockpiling cash at historic levels. This bodes well for future merger deals and corporate expansion. Indeed, the week of November 6th saw two big deals announced – Stanley Works buying Black & Decker and Warren Buffett’s Berkshire Hathaway spending \$26 billion to buy BurlingtonNorthern. In early December, Exxon agreed to buy XTO Energy for \$30 billion. We expect to see a huge wave of mergers in 2010 especially in the cash-rich technology and healthcare sectors. The big will get bigger and the strong will get stronger.

11/13/09 Money isn't going into stocks, it is going into gold and bond funds

In what may prove to be a classic “*chasing what has worked*” scenario, investors have poured money into gold and bond funds in 2009. Through the end of September, investors had put more than \$300 billion in bond funds and only \$15 billion into equity funds. All that money crowding into bonds cannot be a good thing long-term. As for gold, we measured the flow of money into exchange traded funds and the #1 fund this year for new money was the gold fund which attracted \$12 billion while the S&P 500 index ETF had \$32 billion *withdrawn*. If the herd and masses are pouring into bonds and gold and taking money out of stocks, we are glad to be invested in stocks. Usually what the herd does winds up being wrong. Stay tuned.

12/4/09 The importance of dividends

*“We spend a lot of time talking to you about stock buybacks, fortress balance sheets and the importance of growing dividends. Many of the companies we own have consistently raised their dividends and many have raised them **this** year which is remarkable given what we’ve been through. That steadily increasing source of cash is one of the real benefits of investing in high quality stocks. And, as we’ve mentioned to you a number of times, many of our stocks still have dividend yields of 3% or more. The Wall Street Journal this week published a study of investing returns over the past 80 years. During that time, dividends have produced a remarkable 43% of the total return earned from stocks. From 1926-2009, stocks returned 9.8% a year. Of that, dividends have averaged 4.1% a year and appreciation has been 5.4% a year.”*

12/11/09 Despite the big rally, leading “experts” are still very bearish

“As the market goes higher, fewer and fewer people seem to believe it. Perversely, that is a very positive sign. Sir John Templeton once said, “The time of maximum pessimism is the best time to buy, and the time of maximum optimism is the best time to sell.” Just this week, leading market strategist Meredith Whitney said on CNBC, “I am more bearish today than I have ever been.” Given the volumes of data that we have shared with you that show the economy is improving and given the steep yield curve, record global stimulus and rising stock market we find it hard to believe that she is more bearish today than she was back when the world appeared to be headed over the economic cliff this winter – but she is.” (we think that is a good thing for us)

12/18/09 Positive cycle feeds on itself

We suffered through a negative cycle starting last fall as bad news fed on itself, scared consumers who pulled back, which lowered demand and created more bad news. But we are now starting to see the positive news begin to feed on itself – consumers feel a bit better, spending rose about 3% during this Christmas season, businesses are starting to hire temporary workers and some full-time workers. We said, *“As companies start to hire, consumer confidence will grow even more. The more confident we feel, the more we will begin to spend – to replace an old home computer, to buy a new TV, to replace an old washer/dryer, etc. The more the consumer spends, the more corporate demand picks up (to produce those goods) and the more hiring takes place and this positive cycle feeds on itself.”*

We hope this review has been helpful to you. There are very valuable lessons in these summaries for us as your partners going forward. As the saying goes, *“Those that don't learn from history are doomed to repeat it”*. We hope to be good students so we can turn these lessons into assets for the future.

2009 was a wild ride but we fought through the extreme negativity and won the battle. We still have work to do to get back all of the losses of 2008 and we recognize that more bumps are in the road ahead of us. We do not expect smooth sailing through 2010. Huge challenges remain in front of us as a nation. Perhaps the greatest challenge we face remains the war on terror which almost dealt us a blow on Christmas day. We also face the seemingly certain confrontation brewing with Iran over their nuclear ambitions. Oil remains a wild card especially if events erupt in the Middle East. The fear of an asset bubble developing in China also remains a concern.

But as we have said on numerous occasions, there are always fears we have to face as investors. We will always have enemies who wish to do America harm. It is a sad reality of this life. But we are very strong believers in the power and freedom that comes from capitalism. All across this world, human beings awake every day hoping to

make their life a little bit better and capitalism is the only proven way in the history of mankind where man can improve his earthly destiny. Man cannot depend on government to meet all his needs. We are seeing rumblings of that on the streets of Iran where the citizens are realizing they cannot depend on a government that has turned to tyranny. The nature of man cries out for capitalism and freedom and the ability to grow and expand. In that, we are most encouraged. People all over this planet use Johnson & Johnson products every day, drink Coca-Cola, talk on Nokia phones, use the internet powered by Cisco Systems, Intel and Microsoft. Their health is improved by the products of Amgen and Medtronic and like you they hope to use these products to make their lives a little bit better.

We are bullish. We think we have a great formula for investing. We seek to own and partner with great businesses with a long-term and patient horizon. We are **owners** of great companies **not** flippers of stocks. That strategy was rewarded in 2009 and we think it will be for years to come. Happy New Year and thank you for being our partner.

Greatmark Investment Partners

Richard Illges & Jeff Adams

