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"Patience is bitter, but its fruit is sweet." – Aristotle

April 6, 2016

Dear Clients:

Kings Island amusement park says "riders (on Banshee) will scream their way through 4,124 feet of track and seven stomach-churning inversions at speeds up to 68 mph on the world's longest steel inverted roller coaster." While Banshee riders get on and off at about the same place, many exit feeling like their insides have been rearranged.

Investors had plenty of reasons to have their confidence shaken in the first quarter, as headlines blared U.S. stocks had their worst start to the year in history. The possibility of an economic hard landing in China and further devaluation of the yuan, oil free-falling 50% and weak manufacturing data led to fears of a global recession.

As usual, this brought market pundits trying to make a name for themselves by calling the next crash out of the woodwork. RBS, a major global bank, advised its clients to "sell everything," predicting a "fairly cataclysmic year ahead." This being a presidential election year, candidates also one-upped each other portraying how bad things are and, of course, how they are the only one able to fix the situation.

Oil stabilized, though inventories remain elevated. Manufacturing activity strengthened, probably aided by a slightly weaker dollar. Employment continued to expand. In response to the global turmoil, the Federal Reserve adopted a "dovish" stance regarding future interest rate increases.

With the S&P 500 experiencing a harrowing plunge of 11% between New Year's Day and February 11 and subsequent slingshot recovery of 13% to the end of March (finishing the quarter essentially flat), investors endured their own Banshee ride.

We understand and share your frustration regarding our recent underperformance. As we'll explain, we believe there are valid reasons to be optimistic the tide will reverse, hopefully sooner rather than later. In addition, despite the strong rally from the middle of February through the end of the first quarter, investor sentiment remains very pessimistic. From a contrarian point of view, this is great news.

Periods ending March 31, 2016
(Total Returns-Annualized*)

	Russell 3000 Index	S&P 500 Index
3-months	0.97%	1.35%
One-year*	-0.34%	1.78%
Two-years*	5.82%	7.12%
Three-years*	11.15%	11.82%
Five-years*	11.01%	11.58%
Ten-Years*	6.90%	7.01%

The Stock Market

Although the first quarter was excruciating for investors, it provided excellent examples of some timeless investing lessons.

The stock market is inherently volatile. J.P. Morgan Asset Management calculated the average intra-year drop (peak-to-trough) in individual years from 1980-2015 was a whopping 14.2% (Exhibit A). However, these drops ***seldom led to yearly losses***, with 27 of the 36 years ending with positive returns. You may not have realized it at the time, but if you're invested in stocks, this is what you signed-up for.

While the average annual return for U.S. stocks has been about 10% since 1926, actual yearly returns have almost never been "average." It's somewhat of a conundrum; even though the annual average is 10%, it's not safe to assume 10% is a reasonable expectation for any given year. According to Vanguard, from 1926-2014, the average annual stock return was 10.2%, but actual returns fell in the ***range of 8%-12% in only 6 of 89 years*** (Exhibit B).

Time in the market is more important than timing the market. You'd like to sell ahead of drops and buy ahead of rallies. Successful market timing requires you to get ***both*** the sell and subsequent buy correct. This is not only futile, but devastating to long-term returns.

Exhibit A

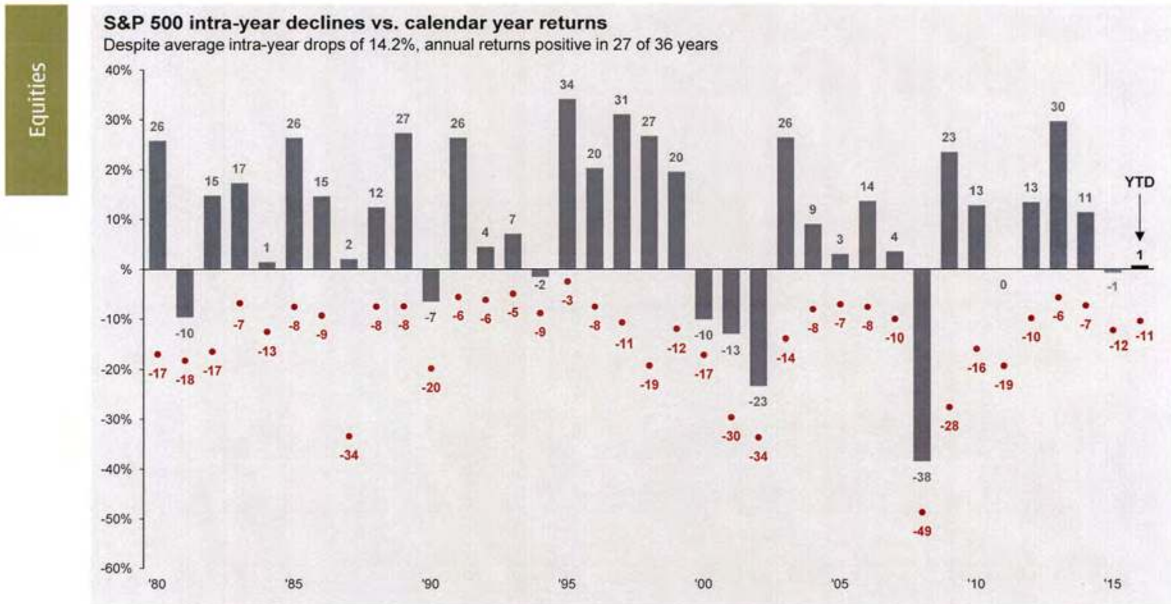
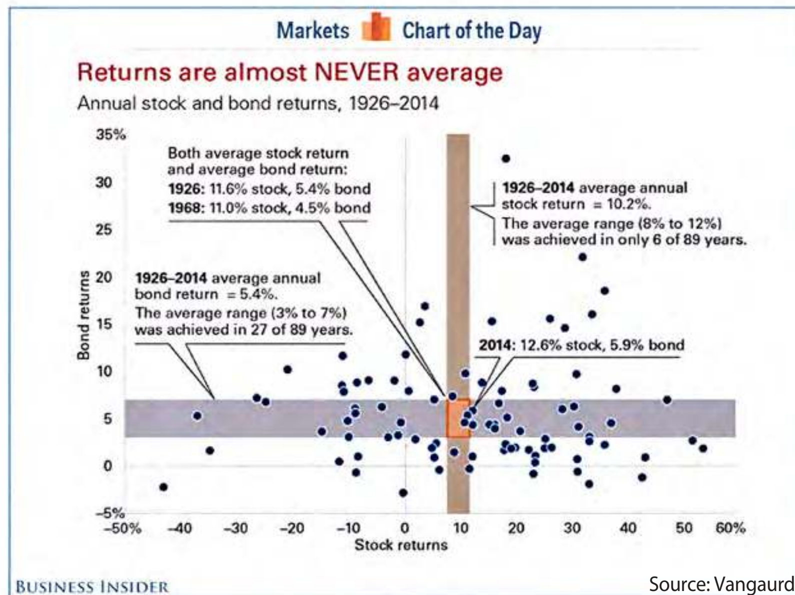


Exhibit B



According to Crandall, Pierce, if you invested $100 in the S&P 500 on the first day of 1991 and didn't touch it, you would have had $618.96 at the end of 2015. However, if you missed just the ***single best trading day*** in each of those 25 years, you would have had just $247.85 (Exhibit C).

Bad news can be your friend, if you let it. As Warren Buffett said in the New York Times at the darkest point of the global financial crisis, "bad news is an investor's best friend. It lets you buy a slice of America's future at a marked-down price."

Successful investors focus on ***process, not outcome***. You can't tell if a short-term outcome was the result of a "good" or "bad" process. However, a sound process should lead to a good long-term outcome.

Investing is a probabilistic endeavor. We are long-term owners of businesses and expect to hold positions for five or more years. Our process involves exploring the market's nooks and crannies to find underfollowed, unloved or misunderstood companies with common characteristics we believe increase our odds of success, over the long-haul:

Low Valuation. We research stocks as if we were buying the entire business. We estimate earnings the business should generate over time. We like to buy stocks trading at a significant discount to our evaluation of the intrinsic value of the business.

High-quality business. Many times a stock is cheap for good reasons. Just because you see a discarded cigar butt with a couple puffs left on the sidewalk doesn't mean you should pick it up. Similarly, we like companies with solid growth prospects and a sustainable competitive advantage.

Strong, shareholder-oriented management. We are big believers in "eating our own cooking." Similarly, we like it when the management team owns a significant amount of its own stock and allocates its resources to benefit shareholders.

Low financial risk. We avoid companies with excessive debt or risk obsolescence.

We also stay away from what's currently "hot" and sectors we don't understand. Despite our best efforts, we've made mistakes (and will again). So, we diversify our holdings and limit the size of individual positions.

Given our disappointing absolute and relative performance going back to 2014, it's reasonable to question whether A) our process is still sound and B) there is good reason to expect performance to turn.

We've been "value" investors since our business was founded 41 years ago. It seems like a long time ago, but this same process led to our winning a prestigious Lipper award in both 2013 and 2014.

We understand you can't spend awards, but want to highlight two points.

First, returns from value investing are necessarily "lumpy." By definition, value investors are buying stocks that are out of favor. We can control the price we pay, but have absolutely no control over when other investors will recognize the company's improved prospects and start to favor the stock.

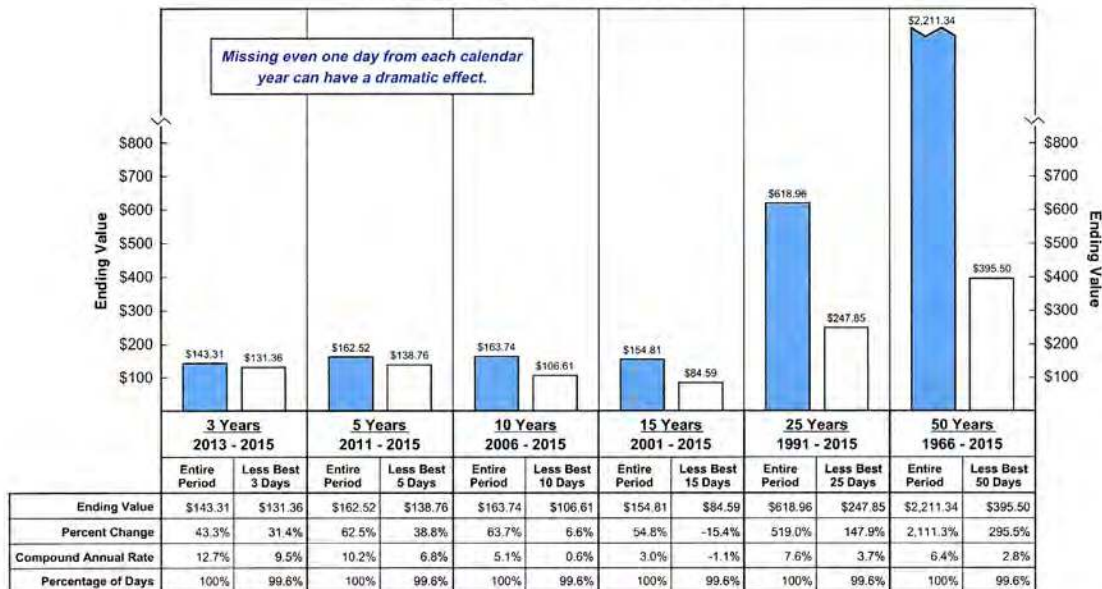
Second, value investing requires patience and a thick skin to withstand the inevitable periods of underperformance. Academic studies have shown time and again "value" investing outperforms "growth." If this is the case, why isn't everybody a value investor? It's human nature. The majority of investors simply aren't wired to have the discipline, patience and fortitude required.

This is all well and good, but why do we expect the performance pendulum to swing back from growth to value? The reasons are A) growth and value have typically run in cycles (lasting several years) and B) growth has been very much "in style" since the current bull market began (and become expensive).

As you can see in the graph from Strategas Research Partners (Exhibit D), the outperformance of growth relative to value has reached the point where, historically speaking, the pendulum has started to swing back to value. Note the last time this occurred was at the height of the bubble in technology/growth stocks in 1999-2000. Fundamentals and valuation do eventually matter. When that happens, value investors will be rewarded for their patience. **In other words, we're optimistic value investors will again have their time in the sun.**

Interest Rates and the Bond Market

The bond market had a similarly rocky first quarter. The yield on the 10-Year U.S. Treasury Bond started 2016 at 2.27%, declined to 1.66% on fears of global economic weakness and closed the quarter at 1.77%. Corporate bond yields were impacted not only by wide swings in U.S. government yields, but also by a similar panic that gripped stocks. Bonds in commodity-based sectors such as energy and mining were particularly hard hit,



	3 Years 2013 - 2015		5 Years 2011 - 2015		10 Years 2006 - 2015		15 Years 2001 - 2015		25 Years 1991 - 2015		50 Years 1966 - 2015	
	Entire Period	Less Best 3 Days	Entire Period	Less Best 5 Days	Entire Period	Less Best 10 Days	Entire Period	Less Best 15 Days	Entire Period	Less Best 25 Days	Entire Period	Less Best 50 Days
Ending Value	$143.31	$131.36	$162.52	$138.76	$163.74	$106.61	$154.81	$84.59	$618.96	$247.85	$2,211.34	$395.50
Percent Change	43.3%	31.4%	62.5%	38.8%	63.7%	6.6%	54.8%	-15.4%	519.0%	147.9%	2,111.3%	295.5%
Compound Annual Rate	12.7%	9.5%	10.2%	6.8%	5.1%	0.6%	3.0%	-1.1%	7.6%	3.7%	6.4%	2.8%
Percentage of Days	100%	99.6%	100%	99.6%	100%	99.6%	100%	99.6%	100%	99.6%	100%	99.6%

Example: For the 3 years 2013 - 2015, $100 invested grew to $143.31. If the best day is removed from each of the 3 calendar years, the ending value would be $131.36.

Data: Capital Appreciation; $100 invested at period inception.

Sources: Standard & Poor's Corporation; *Copyright © 2016 Crandall, Pierce & Company • All rights reserved.*

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Exhibit D

VALUE INVESTING POISED FOR A REBOUND

Source: Strategas Research Partners

as plummeting commodity prices threatened issuers' ability to service their sometimes massive debt. While some of these bonds have recovered, we expect several will eventually end up in default.

We continue to use the bond side of the portfolio as a defensive tool, to buffer the potential downside of equities and provide some stable income.

Summary

As stated at the beginning of this letter, we certainly understand our weak absolute and relative performance going back to 2014 has been very frustrating. We are heavily invested alongside you, so our experience has been the same. We don't know when the performance pendulum will swing from growth to value, but history shows it eventually will. We do know the market won't ring a bell when it's about to happen, so we need to "be there" when it does.

Ours is a most humbling business. We try to generate strong performance every day and for all periods. Unfortunately, that's just not how the real investment world works. We have to remind ourselves not to get too high when performance is strong, nor too low when it's weak. As KM approaches its 41st birthday, we thank you for the trust and confidence you've placed in us. We assure you we take the responsibility of investing your precious assets very seriously.

Regulatory Update

Kirr, Marbach & Company, LLC (KM) is registered with the U.S. Securities and Exchange Commission ("SEC"), which requires advisers to file Forms ADV-Part 1 and 2A ("Brochure")/2B ("Brochure Supplements") electronically on the Investment Adviser Registration Depository (www.iard.com). Form ADV-Part 2A is a narrative disclosure of an adviser's business, written in "plain English." The SEC mandated the headings, specific topics to be covered and the order of presentation. We have enclosed a copy of KM's ADV-Part 2A "Brochure" for each client account.

As a SEC-registered investment adviser, KM is subject to periodic examination by the SEC, which can occur at any time. In the aftermath of the Bernie Madoff scandal, the SEC has determined that it's a good idea for their examiners to independently verify records provided by registrants (like us). This being the case, it is possible during our next examination that the examiners will contact clients to confirm account balances, holdings or other information. We do not know if this will become a standard part of routine examinations, but wanted to alert clients ahead of time.

Related to the above, the SEC adopted an amendment to Advisers Act Rule 206(4)-2 ("Custody Rule"). This rule requires KM to 1) make "due inquiry" of Custodians to confirm periodic statements have been sent directly to clients and 2) on statements KM provides to clients, "urge" clients to compare the statement from KM with the statement from the Custodian. In addition, ***unless we have written authorization from a client to instruct the Custodian to make distributions of cash or securities from the client's account or transfer cash or securities between a client's accounts, the client should instruct their Custodian directly***. This rule creates some additional burdens, but is for your own protection.

Regards,

Kirr, Marbach & Company, LLC

KIM: Buffett tells shareholders 'America's never been greater'

Mickey Kim
March 12, 2016

INVESTING
Mickey Kim

Fans of Berkshire Hathaway CEO Warren Buffett eagerly await the last Saturday in February for his annual letter to shareholders. As usual, this year's letter contained both timely commentary and timeless investment wisdom, delivered with wit, simplicity and humility (http://www.berkshirehathaway.com/letters/2015ltr.pdf).

I recently wrote of the "bull market" for apocalyptic forecasts, featuring market pundits competing in a high-stakes arms race to call the next market meltdown. Similarly, Buffett noted in this election year, "candidates can't stop speaking about our country's problems (which, of course, only they can solve)." Further, "as a result of this negative drumbeat, many Americans now believe that their children will not live as well as they themselves do.

"That view is dead wrong: The babies being born in America today are the luckiest crop in history," Buffett wrote. "America's economic magic remains alive and well. Today's politicians need not shed tears for tomorrow's children."

Politicians should also learn from Buffett's refreshing willingness to humbly admit mistakes, without sugarcoating. He admitted to "serious mistakes I made in my job of capital allocation." Further, "we are now paying the price for my misjudgments" and "I will commit more errors; you can count on that."

Buffett's investment mantra has always been: "Be fearful when others are greedy, and be greedy when others are fearful." As a net buyer of stocks since he was 11 years old, when stocks go down, he views it as good news—no different than when hamburgers or Coca-Cola or anything else he buys all the time goes on sale.

Think of buying a stock as if you're buying the entire company (which Berkshire often does). A successful long-term investor tries to buy when the stock price reflects a significant discount to the company's intrinsic value. While stock prices can swing wildly, company values are generally more stable. That's why Buffett believes a "stock going down is a good thing, unless the company itself is losing value."

Declines in short-term price quotations shouldn't really concern investors, but can cause people to do things they wouldn't do otherwise. He said that, if you're considering buying a farm, you shouldn't be

looking at the next six months and trying to decide whether now is the time to buy. "Look at what the asset is likely to produce over time and what you have to pay for it," he said. "If you can buy it cheaper, so much the better. For people to try and time stocks is crazy."

Buffett noted some of his biggest winners initially went down in price, with Berkshire itself going down 50 percent three different times during his 51 years in control. He said, "You can't predict what stocks will do in the short run, but you can predict that American business will do well, over time." Therefore, "a great strategy is just to buy stocks consistently and not worry too much about whether they go up or down in any given month or year."

"For 240 years it's been a terrible mistake to bet against America, and now is no time to start. America's golden goose of commerce and innovation will continue to lay more and larger eggs," he said. In sum, "America's never been greater."•

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The New York Times

The Opinion Pages | OP-ED CONTRIBUTOR

Buy American. I Am.

By WARREN E. BUFFETT OCT. 16, 2008

Omaha

THE financial world is a mess, both in the United States and abroad. Its problems, moreover, have been leaking into the general economy, and the leaks are now turning into a gusher. In the near term, unemployment will rise, business activity will falter and headlines will continue to be scary.

So ... I've been buying American stocks. This is my personal account I'm talking about, in which I previously owned nothing but United States government bonds. (This description leaves aside my Berkshire Hathaway holdings, which are all committed to philanthropy.) If prices keep looking attractive, my non-Berkshire net worth will soon be 100 percent in United States equities.

Why?

A simple rule dictates my buying: Be fearful when others are greedy, and be greedy when others are fearful. And most certainly, fear is now widespread, gripping even seasoned investors. To be sure, investors are right to be wary of

highly leveraged entities or businesses in weak competitive positions. But fears regarding the long-term prosperity of the nation's many sound companies make no sense. These businesses will indeed suffer earnings hiccups, as they always have. But most major companies will be setting new profit records 5, 10 and 20 years from now.

Let me be clear on one point: I can't predict the short-term movements of the stock market. I haven't the faintest idea as to whether stocks will be higher or lower a month — or a year — from now. What is likely, however, is that the market will move higher, perhaps substantially so, well before either sentiment or the economy turns up. So if you wait for the robins, spring will be over.

A little history here: During the Depression, the Dow hit its low, 41, on July 8, 1932. Economic conditions, though, kept deteriorating until Franklin D. Roosevelt took office in March 1933. By that time, the market had already advanced 30 percent. Or think back to the early days of World War II, when things were going badly for the United States in Europe and the Pacific. The market hit bottom in April 1942, well before Allied fortunes turned. Again, in the early 1980s, the time to buy stocks was when inflation raged and the economy was in the tank. In short, bad news is an investor's best friend. It lets you buy a slice of America's future at a marked-down price.

Over the long term, the stock market news will be good. In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497.

You might think it would have been impossible for an investor to lose money during a century marked by such an extraordinary gain. But some investors did. The hapless ones bought stocks only when they felt comfort in doing so and then proceeded to sell when the headlines made them queasy.

Today people who hold cash equivalents feel comfortable. They shouldn't. They have opted for a terrible long-term asset, one that pays virtually nothing and is certain to depreciate in value. Indeed, the policies that government will follow in its efforts to alleviate the current crisis will probably prove inflationary and therefore accelerate declines in the real value of cash accounts.

Equities will almost certainly outperform cash over the next decade, probably by a substantial degree. Those investors who cling now to cash are betting they can efficiently time their move away from it later. In waiting for the comfort of good news, they are ignoring Wayne Gretzky's advice: "I skate to where the puck is going to be, not to where it has been."

I don't like to opine on the stock market, and again I emphasize that I have no idea what the market will do in the short term. Nevertheless, I'll follow the lead of a restaurant that opened in an empty bank building and then advertised: "Put your mouth where your money was." Today my money and my mouth both say equities.

Warren E. Buffett is the chief executive of Berkshire Hathaway, a diversified holding company.

A version of this op-ed appears in print on , on page A33 of the New York edition with the headline: Buy American. I Am.

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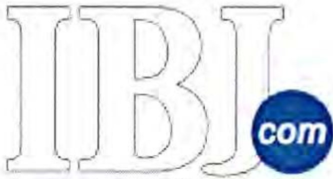

KIM: We're in a bull market for apocalyptic forecasts

Mickey Kim
February 13, 2016

INVESTING
Mickey Kim

Stocks have plummeted at the start of 2016. The financial crisis and concurrent, excruciating bear market are still fresh in investors' minds. Understandably, nobody wants to suffer through a repeat of being sucked into a market vortex.

Unfortunately, there is no shortage of market pundits and others whose modus operandi is to play/prey on investors' fears by painting a picture of impending doom and gloom, whether supported by the facts or, in most cases, not.

It's human nature to be frightened under this scenario. In a recent market update, Liz Ann Sonders of Charles Schwab noted that economist Daniel Kahneman won the Nobel Prize for showing that people respond more forcefully to loss than gain. According to Kahneman, "Organisms that treat threats as more urgent than opportunities have a better chance to survive and reproduce."

With today's 24/7 media bombardment, when stocks hit a rough patch (like now), it's easy to see how investors' loss aversion can lead to panic and trigger short-term decisions harmful to attaining long-term goals. Trying to avert losses often leads to averting gains. Because we've been hard-wired with this survival instinct since prehistoric times, the best investors can hope for is to be able to acknowledge and understand this behavioral bias.

Motley Fool columnist Morgan Housel recently wrote "Why We're Terrified of Typical," which stated we are prone to being too attracted to the thought of rare things while forgetting the law of averages. Housel pointed out two primary factors that combined to make this problem worse over the past decade: the terrible financial crisis and the market for investing commentary's becoming hotly competitive.

According to Housel, "The power of a financial crisis is fresh in our minds and the prize for predicting the next financial crisis in a hypercompetitive media market is enormous." This has led to an arms race among market pundits to call the next market meltdown. Housel says the paradox is, "The entire reason we pay so much attention to the 2008 financial crisis is because it was rare, but paying so much attention to it makes us overweight the odds of it happening again."

In sum, "In both medicine and investing, you may want someone who obsesses over outliers, but there's a difference in respecting outliers and seeing them around every corner."

Carl Richards wrote "Let Go of Irrational Fears" for The New York Times. When talking about the chances of something bad happening, people tend to fall into three groups. The "Numbers Don't Matter" group dismisses statistics altogether and trusts their gut. The "Odds Look Great" group focuses on good news. If there's only a 10 percent chance something bad will happen, they stick their worry in a closet. Alternatively, the "We're Doomed" group obsesses over bad things that have a tiny probability of occurring, like dying from Ebola.

Richards advises, "Whether we're taking about our money, our health or our safety, we've got to get past that fear of the thing that has a tiny chance of happening. This fear blinds us to making the most of the remaining 90, 95 or 99 percent. Once we've done everything we can reasonably do to be safe, once we've accounted for everything within our control, we need to learn to let go of the rest."•

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KIM: Herd mentality dangerous for coaches and investors

Mickey Kim
January 30, 2016

Mickey Kim

Economist John Maynard Keynes said a successful investor must be "eccentric, unconventional, and rash in the eyes of average opinion." The difficulty is, "If he is successful, that will only confirm the general belief in his rashness; and if in the short run he is unsuccessful, which is very likely, he will not receive much mercy."

Thus, investors are often reluctant to act on their own information and go against the comfort of the herd, fearing damage to their reputations as sound decision-makers. Keynes famously said, "Worldly wisdom teaches that it is better for reputation to fail conventionally than to succeed unconventionally." Keynes wrote these words in 1936 but could have been talking about the Green Bay Packers, Coach Mike McCarthy and one of the most exhilarating games in NFL history. The Packers traveled to Arizona for a Jan. 16 playoff game against the Cardinals (which had annihilated the Packers 38-8 three weeks prior).

A seven-point underdog, the Packers trailed 20-13 with no timeouts and less than a minute to play when they faced an impossible fourth and 20 from their own four-yard line. Quarterback Aaron Rodgers heaved the ball, which teammate Jeff Janis improbably caught at the Arizona 36-yard line.

With the ball back at the Arizona 41, there was time for one final desperation play. Rodgers fired the ball into the end zone, which was again miraculously caught by Janis. The Packers trailed 20-19 with 0:00 on the clock.

McCarthy had the choice of A) attempting a game-tying 33-yard extra-point kick to send the game into overtime or B) going for a two-point conversion that would win the game. This was no different from any investing decision. Both are probabilistic endeavors. You assign probabilities to various possible outcomes. The process-oriented coach or investor takes the action with the highest chance of success.

McCarthy had seconds to decide which was greater—the chances of 1) Rodgers gaining the two yards needed for the immediate win or 2) making the kick to tie AND winning in overtime.

Nate Silver's website (www.FiveThirtyEight.com) uses statistical analysis to tell compelling stories about sports, elections, politics, economics and science. Since 2001, NFL teams have converted 47.2 percent of their two-point tries (431 of 913). Kickers made 94.3 percent of extra-point kicks in this first season from 33 yards (1,131 of 1,199). Since 2001, the visiting team has won 45.5 percent of overtime

games (110 of 242).

Using just league averages, these three numbers determine which option would have given the Packers the best chance to win. Going for two points and the win would have succeeded 47.2 percent of the time. Attempting the kick AND winning in overtime would have succeeded 42.9 percent of the time (94.3 percent of extra-point kicks times 45.5 percent visitor overtime wins). Thus, going for two points would have been superior by 4.3 percentage points (47.2 percent minus 42.9 percent).

Alas, McCarthy elected to kick the extra point. The Cardinals got the first possession of overtime and drove 80 yards in two plays for the winning touchdown. Rodgers never touched the ball again.

Herd mentality can afflict NFL coaches and investors. Don't buy on euphoria or sell on panic, just because the crowd is. As Silver says, "This isn't about passions and it isn't about statistical mumbo-jumbo. It's about arithmetic."•

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