The *Value* Investor™

The Century Management Newsletter
Value Investing Since 1974

October 2009 Issue

As we begin the fourth quarter, we would like to update you on our year-to-date results, as well as share with you some of our overall thoughts and current investment strategy. Let's begin with our performance. From the low on March 9, 2009, through September 30, 2009, our CM Value I composite (a proxy for our average account) has appreciated 62.20%. On a year-to-date basis through September 30, the CM Value I composite has appreciated 19.01%. This has been a meaningful change from how the year began. As a matter of fact, except for the stock market recovery that took place at the bottom of 1932, this has been the most significant six month recovery in market history.

So where does this leave us today? The answer to this question seems to be divided into several schools of thought among professional investors. **One school of thought is that the market has come up too much too soon with little underlying fundamental support from the companies themselves and/or the economy as a whole, and thus we are being set up for a significant pull back in market prices. A second school of thought is that there is a "new normal" going forward which will consist of slow, subpar, economic growth and a fair amount of market volatility. A third school of thought is that the economy is currently recovering in a meaningful way and that individual companies have made the necessary adjustments to not only weather the storm, but to also thrive in the future and to continue to appreciate full speed ahead at least through the first or second quarter of 2010.**

As we outlined in our various communications to you over the past year, we believe that the sell-off in stock market prices was far overdone relative to supporting company fundamentals, and that there was enough stimulus being put into the financial system to regain price stability and investor confidence. We mentioned that as credit began to loosen from the chokehold that occurred from October 2008 through March 2009, P/E multiples would likely expand and stock prices would soon follow even if fundamentals did not improve right away. Furthermore, back in February we said that the average stock was selling in the bottom quartile of its historical valuations and their low prices were not likely to stay there very long. Last, we pointed out that the stock market has a history of appreciating 31% on average in the year following a bear market bottom, and at the extremes as much as 45%.

As we evaluate today's prices relative to company fundamentals, interest rates, and inflation, and take into account potential growth and economic drivers, we believe the average stock in the U.S. market is now approaching the upper-end of its fair value zone. (*Fair value is the midpoint between the buy and sell point.*) **With regards to**

our portfolios here at Century Management, we believe our equities are just now beginning to enter their fair value zones. Thus, when you add our increasing cash position to our equities, all things being equal, we believe our portfolios hold more fundamental value with less risk than compared to the average stock in the U.S. market today.

Century Management 40-Year Study

To help you understand our perspective, we would like to share with you the most recent results of a study we have been conducting for the past 40 years. **As we have said in the past when referencing this study, while it does not give us the information we need to know to invest in individual stocks, it does help us to understand the type of market and overall economic environment in which we are operating**. On a weekly basis, we monitor the relationship between the Moody's Baa (investment grade) corporate bond yields and the median (midpoint) P/E of the 1,700 stocks found in the Value Line Investment Survey® ("Index"). Over time, we have found this Index to be an excellent proxy for the average stock and the U.S. equity market as a whole. Since stocks and bonds are always in competition for investor dollars, monitoring this relationship helps us to arrive at what we believe to be the best fair value P/E ratio for the overall market given the current interest rate environment. Once this fair value P/E has been established, we can then determine whether the U.S. equity market as a whole is selling at a discount or a premium (*i.e. whether it's cheap or expensive*).

Currently, the Moody's Baa corporate bond yield is 6.17%, roughly 18% below its 65-year average of 7.50%. In the world of bonds, this is a big percentage difference. (**See the long and short-term history of the Moody's Baa bond yield on Charts 1a and 1b on page 3)**. Back in October 2008, the Moody's Baa bond yield reached 9.49%, creating the largest spread over 10-year U.S. Treasury bonds in more than 50 years (**See Chart 8 "The Spread" on page 10**). Given that we have had such extremes in the credit markets over the past year, we feel that it is important to "normalize" this bond yield so that we can remove the high and low extremes of the market from our valuation study.

Normalizing this bond yield, instead of using the yields at their extremes, helps prevent us from using P/E ratios and other valuation standards and assumptions that might not be sustainable in the future. For example, if we were to use today's Baa bond yield of 6.17%, this would be equivalent to a buy point P/E of 16.21 (100 divided by 6.17% yield = 16.21 buy point P/E). In other words, relative to this interest rate, this P/E ratio would be considered to be at a bargain level. However, this lower yield (higher P/E) might not be sustainable. For example, if interest rates rise or there is an increase in inflation, bond prices would go down which would drive yields higher, and as bond yields increase P/E ratios would fall. Therefore, by using a normalized Baa bond yield of 7.50%, we get an equivalent buy point P/E of 13.33, or **17.8% less** than the non-adjusted bond yield. Normalizing today's bond yield is a more conservative approach.

This inverse relationship between bond yields and P/E ratios is critically important to understand since this has a huge impact on stock prices. For example, during the credit crisis late last year the Baa yield shot up to 9.49%, thus driving the equivalent buy point P/E ratio down to 10.5. Is it any wonder then that the median P/E for the Value Line Index® actually hit 10.1, a 19-year low, in December? While normalizing the Baa bond yield is a more conservative approach, we believe it will serve us well over the long run.

Moody's Baa Bond Yield

Chart 1a
65-Year History

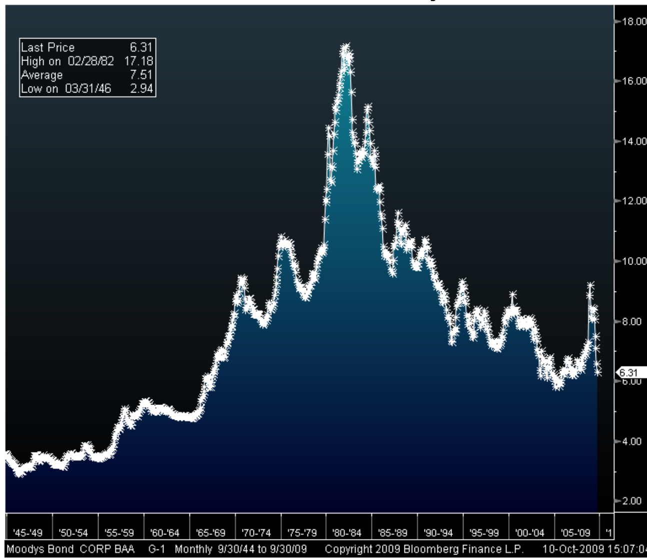
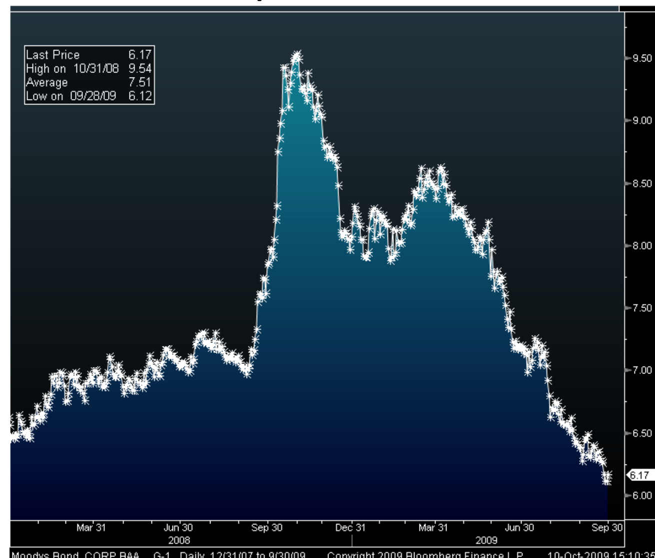


Chart 1b
Close-up of Last 21 Months



<u>**Chart 1a**</u>
From September 1944 through September 2009
High Yield: 17.18% (02/28/82)
Average Yield: 7.51%
Low Yield: 2.94% (03/31/45)

<u>**Chart 1b**</u>
From January 2008 through September 2009
High Yield: 9.54% (10/31/08)
Average Yield: 7.51%
Low Yield: 6.12% (09/28/09)

Source: Bloomberg Finance L.P.

Now that we have normalized the bond yield, we can proceed in determining whether the U.S. equity market as a whole, as represented by the median P/E of the 1,700 stocks in the Value Line Index®, is selling at a discount or premium to fair value. For details of this process, we should turn our attention to **Chart 2 (on page 4)**.

In **Row 1**, we list the "normalized" Baa bond yield of 7.50%. In **Row 2**, we convert this yield into a **buy point P/E** (100 divided by 7.50% yield = 13.33 buy point P/E). When you can buy a stock with an equivalent P/E (or lower) to that of a similar credit quality bond, the stock is usually a better deal because most stocks have earnings that grow over time, whereas a bond has interest payments that are fixed and therefore do not grow over time. **In other words, with a stock you get both the earnings yield and the growth.**

Historically, our study shows that the Value Line® median P/E does not reach **fair value** until it is 25% above the buy point P/E; this is shown in **Row 3**. In **Row 4,** we show the weekly Value Line® median P/E closest to the market low in March, along with the end of the 2009 second and third quarters. **Row 5** shows the **discount or premium** in which the median Value Line® stock (Row 4) traded relative to its equivalent fair value (Row 3), in a more "normalized" interest rate environment.

Chart 2 (on page 4) shows just how cheap the average stock was selling relative to its fair value back in March 2009, and how only seven months later it is now selling at a premium.

Chart 2

Row	The Median P/E for the Value Line Index(R) of 1,700 Stocks (Our Proxy for the U.S. Equity Market as a Whole)	03/13/09	06/30/09	09/30/09
1	NORMALIZED Moody's Baa Corporate Bond Yield	7.50%	7.50%	7.50%
2	NORMALIZED Baa Corporate Bond Yield Equivalent **Buy Point P/E**	13.33	13.33	13.33
3	Add **25%** to the Buy Point P/E to Arrive at the Baa Bond Yield Equivalent **Fair Value P/E**	16.67	16.67	16.67
4	**Median Value Line® P/E Ratio**	10.3	14.8	17.5
5	**Value Line(R) Median P/E Discount / Premium to the Baa Equivalent Fair Value P/E**	**-38.20%**	**-11.20%**	**5.00%**

*7.50% is the average Moody's Baa corporate bond yield over the past 65 years. We reference this above as the "normalized" corporate bond yield. Baa bonds are considered investment grade quality. The Value Line(R) median P/E represents the median P/E from the Value Line Investment Survey(R) of 1,700 stocks and includes two quarters of forward looking earnings and two quarters of trailing earnings. The Value Line(R) median P/E shown in the 6/30/09 and the 09/30/09 columns was for the weekly Value Line(R) issue dated 07/03/09 and 10/02/09 respectively. Source: Value Line(R) and Bloomberg Finance, L.P.

Our 40-year study shows that over the past 30 years, bear markets typically reached an average "worst case" bottom when the median P/E sold at an 11% discount from its actual (not normalized) Baa equivalent buy point P/E. This bear market went below this average, finally hitting bottom with a 13.5% discount from its Baa equivalent buy point P/E (not shown on Chart 2). Stocks were truly on sale at bargain basement prices.

Though we do not believe it is likely, it is statistically possible to once again have the median P/E of the Value Line Index® trade below its equivalent buy point P/E. **If we use today's actual Baa bond yield of 6.17%, the potential risk level or decline is approximately 20% for the median stock in this index given today's fundamentals, interest rates, and inflation. However, if we use the normalized Baa bond yield of 7.50%, the potential risk level or decline is approximately 34%.**

Our study also shows that the Value Line® median P/E typically trades between 10% and 15% above fair value. Therefore, to determine the sell point (*i.e. full value*) of the "average stock", we add 10% to 15% to the **Baa equivalent fair value P/E** of 16.67 to arrive at a potential **sell point P/E** of 18.3 to 19.2 (rounded). This means that from today's **actual median P/E** of 17.5, the 1,700 stocks in the Value Line Index® have a chance to appreciate approximately 5% to 10% before we would consider them fully valued. We believe this should be a reasonable upside range for the average U.S stock over the next 12 to 18 months.

To summarize, we believe the median stock in the 1,700 stock Value Line Index®, our proxy for the U.S. equity market, is presently at the upper-end of its fair value, approaching its

sell point, and now has approximately 2 to 3.5 units of risk for every 1 unit of upside based on the measurements in our 40-year study.

(Importantly, while not mentioned earlier, if earnings or the rate of earnings growth are better than expected, this could provide the average stock with additional upside to the numbers we have shown. This may not be too difficult to imagine as the previous two quarters have proved better than expected. However, this works both ways. A disappointment in earnings or the rate of earnings growth could have the opposite effect.)

Century Management Portfolios

Now that we have discussed the U.S. equity market and have a better understanding of the environment in which we are operating, let's turn our focus to the Century Management portfolios. **We believe there is likely to be good upside in your total portfolio from here, especially when we review each company on a stock-by-stock basis using our fundamental analysis.** As our individual stocks (not the market at-large) trade between what we believe to be their fair values and maximum sell points (*the high end of what we believe their fundamental values can justify over a four to five year time horizon*), they are being trimmed and will eventually be sold in full. Generally speaking, on a risk adjusted basis, this takes place when bonds or cash provide us with a better return—in other words, when a stock's price is well above what its fundamentals (sales, earnings growth, etc.) can justify. Therefore, as the price moves higher into the sell zone, there is significantly more downside risk than upside potential for the foreseeable future. Selling at these price points is an integral part of our disciplined selling strategy.

Sometimes there are no immediate replacements (stocks or bonds selling at bargain basement prices) for these sold securities. When this is the case, the proceeds will stay in cash or cash equivalent positions until a new bargain buying opportunity comes our way.

With more and more articles, managers, and mutual funds taking on bullish viewpoints, along with ever increasing investor confidence and momentum in the midst of this 60% plus price recovery, there will be more temporary pressure to stay fully invested and to participate in this somewhat psychologically generated rising tide that is currently lifting many boats. **However, we would be remiss if we did not continue to exercise our sell discipline.**

Chart 3 (on page 6) and **Chart 4 (on page 7)** show how we have been executing our sell discipline and raising cash as stocks begin to reach their various sell points. **Chart 3** shows the Moody's Baa corporate bond yield and its equivalent buy point P/E (**Rows 1 and 2**). **Row 3** shows the Baa equivalent fair value P/E. **Row 4** shows the FY1 P/E for the equities in our CM Value I composite. **Row 5** shows whether our stocks are selling at a discount or premium given the current interest rate environment.

At the bottom of the market on March 9, 2009, our stocks were selling at a 41.9% discount to their normalized Baa equivalent **fair value P/E** and more than 27% below their normalized Baa equivalent **buy point P/E**. Having been oversold and trading at such significant discounts

to their fair values and buy points, it is now easy to see why our stocks have performed so well over the past six months, especially when compared to bonds and cash. As of September 30, 2009, our stocks are selling at a 1.3% discount to their Baa equivalent fair value P/E relative to normalized interest rates (see Row 5 on Chart 3). **In other words, we believe our portfolios continue to have upside potential (*i.e. value*). If we use the historical parameters discussed earlier to project our upside potential over the next 12 to 18 months, we still see the possibility for a 10% to 15% return from here, not counting dividends which would add roughly 2% to these numbers.** Again, this assumes the current low interest rate, low inflation, and improving individual stock fundamentals environment that we have today. Of course this is always subject to change and is not guaranteed, but it is what we believe the potential to be during this time frame.

Chart 3

Row	CM Value I Composite	03/09/09	06/30/09	9/30/2009
1	NORMALIZED* Moody's Baa Corporate Bond Yield	7.50%	7.50%	7.50%
2	NORMALIZED Baa Corporate Bond Yield Equivalent **Buy Point P/E**	13.33	13.33	13.33
3	Add **25%** to the Buy Point P/E to Arrive at the Baa Bond Yield Equivalent **Fair Value P/E**	16.67	16.67	16.67
4	**CM Value 1 Composite FY1 P/E Ratio****	9.68	14.54	16.45
5	**CM Value 1 Composite (Equities Only) Discount / Premium to the Baa Equivalent Fair Value P/E**	**-41.92%**	**-12.76%**	**-1.30%**

*7.50% is the average Moody's Baa corporate bond yield over the past 65 years. We reference this above as the "normalized" corporate bond yield. Baa bonds are considered investment grade quality. **The FY1 P/E ratio uses the future 1 year estimated earnings in its calculation. Source: Bloomberg Finance, L.P. and Century Management

Chart 4 (on page 7) shows how our allocation between stocks, bonds, and cash is now slowly transitioning to a larger cash position as stocks begin to reach our various sell targets. It is important to remember that we are not making a macro call to increase cash; rather, we are letting our value discipline guide us to what we believe is cheap and what is becoming a little more pricey. We mention pricey rather than expensive because as we average out of various positions, often there remains more upside potential; this is why most positions are not sold in full all at once. Still, we do need to be mindful when a stock passes what we believe to be its fair value (*the midpoint between the buy and sell point*). Once a stock passes fair value, increasingly there is more downside risk and less upside potential. This is why we typically average out, or sell in stages, as the price continues to appreciate to our maximum sell target.

Chart 4

CM Value 1 Composite Asset Mix	03/09/09	06/30/09	9/30/2009
Cash & Equivalent	17.56%	19.73%	23.46%
Stocks	82.22%	79.54%	75.43%
Bonds	0.22%	0.73%	1.11%
Total	100.00%	100.00%	100.00%

Chart 4 represents the CM Value 1 composite (*i.e. a proxy for the average account)*. Note that each individual account will vary from this composite due to various factors such as start dates, deposit and withdrawal amounts and dates, and custom trading notes specific to individual client needs. In addition, it highlights three points in time: the market low on March 9, 2009, as well as the end of the second and third 2009 calendar quarters. Source: Century Management

Chart 5

CM Value I Composite GICS Sector Breakdown
September 30, 2009

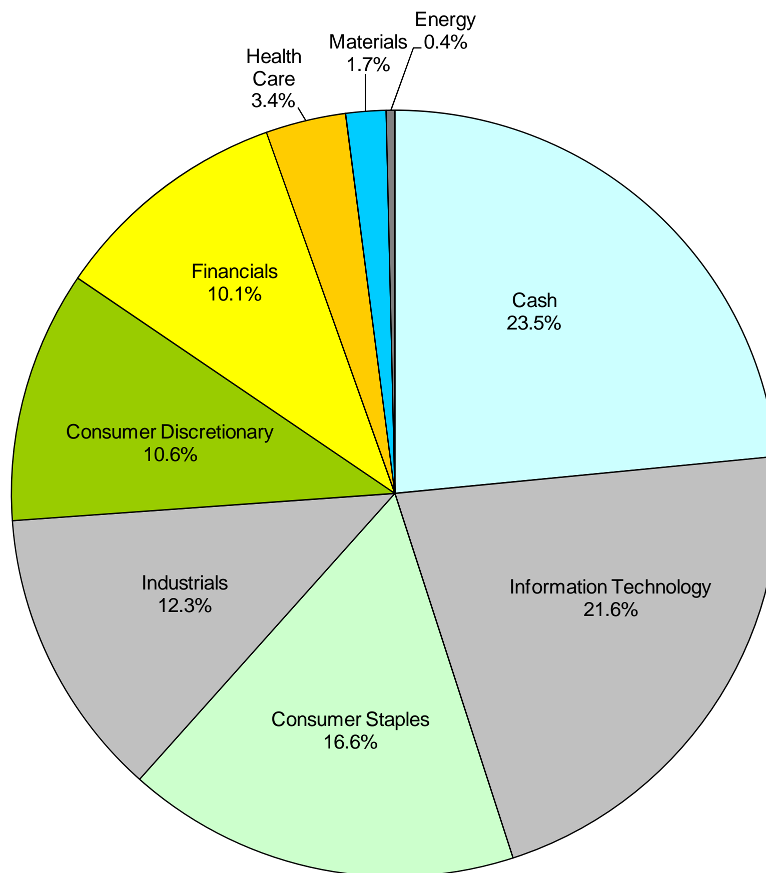


Chart 5 (on page 7) shows how our portfolios are diversified today. Cash is our largest weighting, representing 23.46% of the typical portfolio. Technology is our second largest weighting, which includes quality names such as **Microsoft, Intel, Applied Materials, Dell, Texas Instruments, Paychex,** and **Automatic Data Processing**. Consumer staples is our third largest weighting, which includes blue chip holdings like **Coke, Colgate-Palmolive, General Mills, Procter & Gamble, Wal-Mart,** and **Walgreen's**. Our investment in the industrial sector includes **3M, Emerson Electric, FedEx, United Parcel Service, General Electric,** and **Avery Dennison**. Our leading consumer discretionary names include **Walt Disney, News Corporation,** and **Comcast**. In the financial sector we own industry stalwarts such as **American Express, Marsh & McLennan,** and **Wells Fargo**.

Currently, more than half of our typical portfolio is invested in large, blue chip quality companies, and roughly a quarter of the average portfolio is in cash. This means that less than 25% of the average portfolio is invested in small to mid-cap stocks. Over time, it is highly likely that our weighting in small to mid-cap stocks will increase significantly when the opportunities present themselves.

Over the past 35 years, roughly two thirds of our investments have been in smaller companies. These "little jewels", as we like to call them, usually give our portfolios those above average returns that are not always found in the larger companies. However, at today's prices, many of the large-cap stocks that we have in our portfolios are priced at bargain levels, and thus we have invested accordingly.

While we are generally concerned with the economic problems that are facing this economy, such as over-capacity, high-debt levels, high unemployment, falling real estate values, and a lower demand for goods and services, these problems can be solved over time. **Rather, our main area of focus is on the individual companies that make up our portfolios and on finding the new values that will eventually deliver tomorrow's returns.**

Last, we are continuing to manage for reward as well as for the risk that is on-going in today's market. With improving company fundamentals and a recovering economy, albeit a slow one, we believe we are very well positioned today. While our portfolios are now building cash and are not likely to appreciate in a straight line, we do believe that three to four years from now they should be higher than they are today.

Century Management on Bonds

Over the past year we have had a great deal of interest from clients regarding our bond portfolios. Investing primarily in U.S. corporate bonds, Treasury bonds, Treasury notes, and cash, our bond portfolios have been performing very well in this environment.

Chart 6 (on page 9) shows our CM Fixed Income composite's 2009 year-to-date performance, as well as our rolling 1 through 5 year annualized returns net of fees. (*The composite is a proxy for our typical bond portfolio.)*

Chart 6

Net of Fees	CM Fixed Income Composite	Barclays US Aggregate Bond Index	CM Fixed Income Composite Outperformance Over Benchmark
2009 YTD Through 9-30-09	**9.02%**	5.72%	3.30%
1 Year Ending 9-30-09	**14.72%**	10.56%	4.16%
2 Years Ending 9-30-09	**10.95%**	7.05%	3.90%
3 Years Ending 9-30-09	**9.01%**	6.41%	2.60%
4 Years Ending 9-30-09	**8.68%**	5.72%	2.96%
5 Years Ending 9-30-09	**7.54%**	5.13%	2.41%
Years 1 through 5 are time weighted annualized returns. Source: Century Management			

Applying the same value discipline to bonds as we use with our equity investments, we have been taking advantage of the many value opportunities that have been presented; thus, we have moved from cash into U.S. Treasuries and U.S. corporate bonds. To gain a full appreciation and understanding of the environment, and therefore the opportunities we have had, it is important to review the past two years. As we completed the third quarter of 2007, our CM Fixed Income composite held 42.28% of the portfolio in cash, 35.26% in long-term U.S. Treasury bonds, 16.68% in U.S. Treasury notes, and only 1.59% in corporate bonds. (See **Chart 7** for quarter- over-quarter changes).

Chart 7

CM Fixed Income Composite									
Allocation Breakdown	**09/30/07**	**12/31/07**	**03/31/08**	**06/30/08**	**09/30/08**	**12/31/08**	**03/31/09**	**06/30/09**	**09/30/09**
Cash & Equivalents	**42.28%**	**72.00%**	**59.41%**	**45.64%**	**36.75%**	**25.95%**	**23.14%**	**23.75%**	**27.84%**
U.S. Treasury Bonds (Long-Term)	35.26%	5.97%	8.74%	8.52%	2.54%	0.30%	1.62%	7.35%	**6.52%**
U.S. Treasury Notes	16.68%	14.70%	11.84%	11.07%	10.91%	6.50%	6.10%	3.79%	**3.08%**
U.S. Corporate Bonds	**1.59%**	**1.36%**	**10.84%**	**27.38%**	**43.58%**	**59.96%**	**61.81%**	**59.30%**	**57.39%**
Municipal Bonds	1.33%	3.46%	9.17%	7.39%	6.22%	7.29%	7.06%	5.54%	**4.89%**
Other	2.86%	2.51%	0.00%	0.00%	0.00%	0.00%	0.27%	0.27%	**0.28%**
Total	**100.00%**	**100.00%**	**100.00%**	**100.00%**	**100.00%**	**100.00%**	**100.00%**	**100.00%**	**100.00%**
Source: Century Management									

However, as 2007 came to an end, our cash position increased to 72% as we sold, for a very good profit, approximately 83% of our position in the long-term U.S. Treasury bonds. Shortly thereafter, with roughly 72% of our Fixed Income composite in cash, the spread between the Moody's Baa corporate bond yield over the 10-year U.S. Treasury bond yield (known as **"the spread"**) began to widen out to 350 basis points* or 3.5%—a value zone.

(*As mentioned earlier in this update, the Moody's rating of Baa for corporate bonds is the industry's rating for the average investment grade corporate bond.)* As such, we began our first round of buying into corporate bonds. (See **Chart 8**)

***Basis Point Defined**: A unit that is equal to 1/100th of 1%. For example, a 1% change = 100 basis points, and 0.01% = 1 basis point.

Chart 8

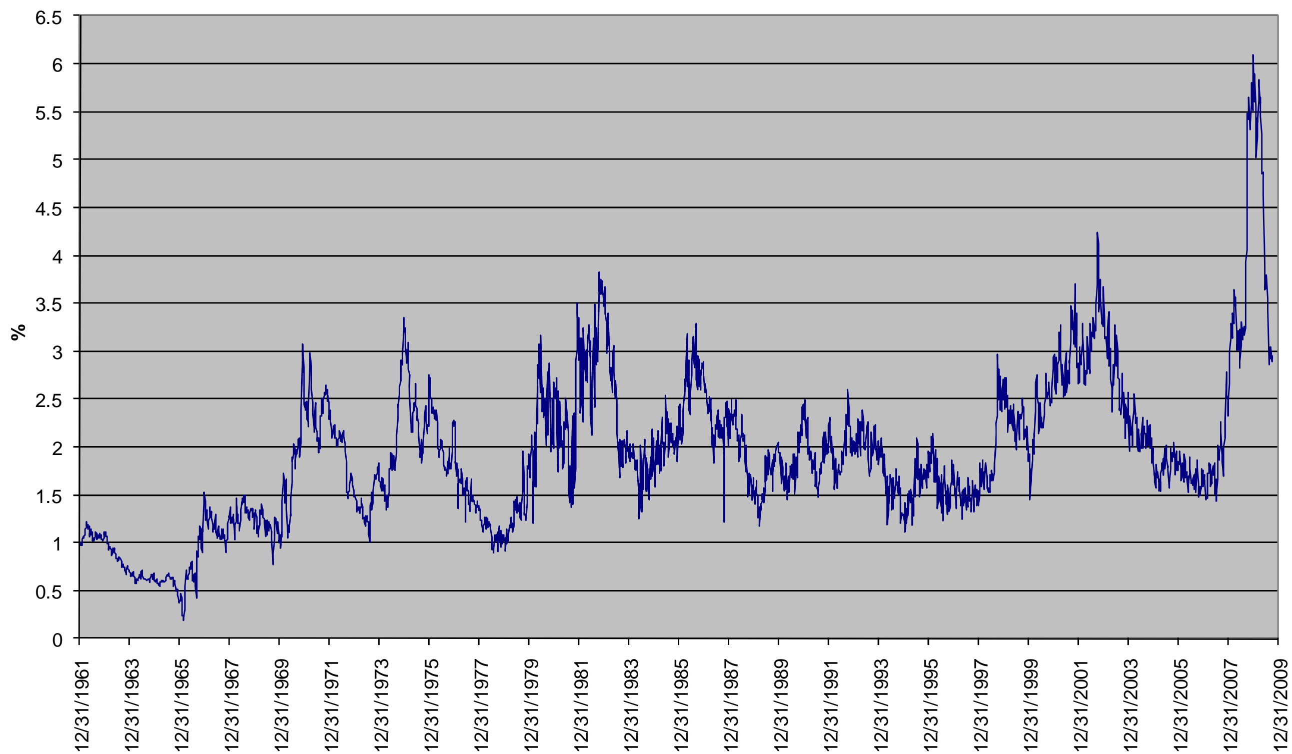


Chart 8 shows that on a historical basis, Baa corporate bond yields do not typically trade at a 350 basis point (*i.e. 3.5%*) spread over 10-year U.S. Treasury bond yields. According to Bloomberg, since 1962, the average spread has only been 193 basis points. Therefore, when this Baa spread widened in such a dramatic fashion over a very short period of time, it was truly a meaningful event. In only two other periods going back to 1962 did the spread (*i.e. risk premium*) for investment grade corporate bonds become so large; they were the periods of 1980-1982 and 2001-2002. Moreover, it has only been on a handful of occasions over the past 47 years that investors could get more than a 300 basis point spread over the 10-year U.S. Treasury bond. So when we began buying corporate bonds in March 2008, we felt confident that we were buying them at value prices.

By mid-2008, the Moody's Baa corporate bond spread had narrowed back to only 282 basis points above the 10-year U.S. Treasury bond. **Chart 7 (on page 9)** shows that as of **June 30, 2008**, the CM Fixed Income composite invested in 45.64% cash, 27.38% corporate bonds (up from 1.36% just six months prior), 11.07% U.S. Treasury notes, and 8.52% long-term U.S. Treasury bonds. At that time we were somewhat concerned that we had not bought enough corporate bonds to take full advantage of the 350 basis point spread just a few months earlier. However, according to our investment analysis, we found the best values to be limited to just a few sectors, like consumer discretionary and finance. We felt that the corporate bonds in most other sectors, such as energy, industrial, and utilities, were still at or above their fair values and not worth the risk premiums they were trading for over Treasuries. Believing in diversification and not wanting to overweight our bond holdings to any one sector, nor pay-up for bonds just to "chase yield", we stuck to our discipline and remained in approximately 45% cash.

Being lightly invested turned out to be a good thing; the bond market went from bad to unbelievably bad in the fourth quarter of 2008 as the **Baa spread widened out to 617 basis points! The yield on investment grade corporate bonds finally peaked at 9.49%, the highest yield since 1994. It was at this time that credit markets virtually froze and no security was spared. All sectors of the bond market became extremely cheap, including the highest quality corporate bonds. Only U.S. Treasuries gave investors a positive return during this time. We took advantage of this opportunity and sold virtually all of our remaining position in long-term U.S. Treasury bonds and reinvested the majority of the proceeds into a basket of corporate bonds. As of December 31, 2008, U.S. corporate bonds represented roughly 60% of the CM Fixed Income composite (See Chart 7 on page 9).**

The heavy weighting to corporate bonds (most of which are investment grade) has held steady though 2009. However, in June 2009, we did get another opportunity to increase our position in long-term U.S. Treasury bonds at bargain prices.

As of September 30, 2009, our CM Fixed Income composite holds 57.39% in U.S corporate bonds, 27.84% in cash, 6.52% in long-term U.S. Treasury bonds, 3.08% in U.S. Treasury notes, 4.89% in municipal bonds, and 0.28% in other fixed income securities.

Chart 9 (on page 12) breaks down the weighted averages of the CM Fixed Income composite as of September 30, 2009. On average, the portfolio shows an "investment grade" rating from both Moody's and Standard and Poors. The average bond has a 10.6 year maturity, but due to the interest payments that are generated, this brings the average duration down to 7.6 years. The average coupon is 5.93% and the average yield to maturity (including cash) is 5.60%.

Today, bonds are trading in their fair value zones and we believe they still offer solid return potential over the next three to five years.

Chart 9

CM Fixed Income Composite Weighted Averages 09/30/09	
Average Yield to Maturity (includes cash)	5.60%
Average Maturity (in years)	10.6
Average Coupon (%)	5.93%
Average Duration (in years)	7.6
Average Moody's Credit Rating	A3
Average S&P Credit Rating	A-
Source: Bloomberg Finance, L.P. and IDC	

- **Yield to Maturity (YTM):** *The rate of return anticipated on a bond if it is held until the maturity date. YTM is considered a long-term bond yield expressed as an annual rate. The calculation of YTM takes into account the current market price, par value, coupon interest rate and time to maturity. It is also assumed that all coupons are reinvested at the same rate. Sometimes this is simply referred to as "yield" for short.*
- **Maturity:** *The length of time until the principal amount of a bond must be repaid.*
- **Coupon:** *The interest rate stated on a bond when it's issued. The coupon is typically paid semiannually.*
- **Duration:** *A measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices. The bigger the duration number, the greater the interest-rate risk or reward for bond prices.*

Conclusion

In the coming years, you can expect us to continue to buy stocks and bonds for total return and long-term growth. However, when we see that these assets are above our fundamental buy points, and the ratio of upside potential versus the downside risk is not in our favor, we will invest in cash and cash equivalent holdings irrespective of the short-term yield.

In closing, we would like to leave you with a thought from Benjamin Graham (1894-1976), the “father of value investing”.

“A final retrospective thought. When the young author entered Wall Street in June 1914 no one had any inkling of what the next half-century had in store….Yet if we confine our attention to American investment experience, there is some comfort to be gleaned from the last 57 years. Through all their vicissitudes and casualties, as earthshaking as they were unforeseen, it remained true that sound investment principles produced generally sound results. We must act on the assumption that they will continue to do so.”

Chart 10

Major Events During and After Benjamin Graham's Life

Year	Event
1914	World War I (1914-1918)
1929	Great Depression (1929-1932)
1939	World War II Begins in Europe (1939-1945)
1941	Pearl Harbor Attacked
1945	U.S. Government Debt to GDP was 112% (As of September 2009 it is 84%)
1950	Korean War Begins
1962	Cuban Missile Crisis
1963	President Kennedy Assassinated
1968	Vietnam War (1959-1975)
1973	Arab Oil Embargo-Oil Prices Go From $2 to $10 Per Barrel
1974	Major Bear Market in Stocks / Price Controls / President Nixon Resigns
1980	18% to 19% Federal Funds Rates
1981	16% to 18% 30-Year Mortgage Rates
1987	U.S. Stock Market Crash / Dow Drops 22.48% In One Day
1991	Gulf War Begins
2000	Beginning of Three Year Stock Market Decline / NASDAQ Eventually Declines 78%
2001	Terrorist Attack on World Trade Center (9/11) / Afghanistan War Begins
2003	Iraq War Begins
2008	Major Stock Market Decline / Credit Crisis / National Real Estate Decline
Plus 12 Recessions Since 1948	

One of the most profound lessons to be taken from Graham's writing is that no one could have predicted these events, just as no one can predict the major events of tomorrow. Economist John Maynard Keynes said, "The inevitable never happens. It is the unexpected always." Successful investing does not depend on being able to predict the future, but rather on using sound investment principles, since they will generally produce sound investment results. You have our commitment that we will continue to use sound investment principles in the management of your portfolios.

September 2009 was the official 35 year anniversary of Century Management. We would like to thank you, our friends, and clients for your continued trust and confidence in our company. As our commitment to you, we continue to invest 100% of our own investable assets in the same securities that are found in your portfolios, including cash.

If you have any questions regarding your account, a managed bond portfolio, or if you feel you could benefit by having us complete a financial plan for you, please give your service representative a call at 1-800-664-4888.

Sincerely,

The Century Management Team

Please Visit Our Website

To review our 2009 Value Investor™ newsletters and client communications, be sure to visit our website at: **www.centman.com**

If you are viewing this letter via your email, click the active links below for direct access to our website:

- **July 2009 CM Value Investor Newsletter**
- **March 2009 CM Value Investor Newsletter**
- **February 2009 Recorded Call with Arnold and Scott Van Den Berg**
- **Century Management Website Home Page**

Disclosures

Certain statements included herein contain forward-looking statements, comments, beliefs, assumptions, and opinions that are based on CM's current expectations, estimates, projections, assumptions and beliefs. Words such as "expects," "anticipates," "believes," "estimates," and any variation of such words or other similar expressions are intended to identify such forward-looking statements.

These statements, beliefs, comments, opinions and assumptions are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult if not impossible to predict with certainty. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in, or implied by, such forward-looking statements.

Clients are cautioned not to place undue reliance on these forward-looking statements, which reflect CM's judgment only as of the date hereof. CM disclaims any responsibility to update its views, as well as any of these forward-looking statements to reflect new information, future events or otherwise.

Factual material is obtained from sources believed to be reliable and is provided without warranties of any kind. Past performance is no guarantee of future results.

If you should have any questions regarding the contents of this update, please contact your CM service representative at 1-800-664-4888.

The Century Management Team

"To no force in the universe belongs such power as minds united in one purpose."

~ Prentice Mulford

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We would like to thank the entire Century Management team for their review and individual contributions to this letter.

Since 1974

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