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THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

A Deep-Value Approach to Fixed Income Investing

TOM SIDEREWICZ is the Portfolio Manager for the CM Advisors Fixed Income Fund (CMFIX) at Century Management. Based on its five-year annualized return of 8.19% for the period ended March 31, 2011, and out of 162 funds in Morningstar's Multisector bond category, Morningstar® has rated CMFIX four stars. In 2000, Mr. Siderewicz joined Century Management in Austin, Texas, where he worked in a variety of capacities, including Equity Analyst, Fixed Income Analyst, Fixed Income Portfolio Manager and member of the investment committee. In aggregate, he has more than 20 years of experience in the financial industry specializing in fixed income. Mr. Siderewicz began his professional employment as a Financial Consultant with Merrill Lynch. After spending the early part of his career as an Institutional Bond Broker at various regional financial institutions, including Masterson Moreland Sauer Whisman, he worked as an Institutional Fixed Income Trader for Charles Schwab. He graduated with a B.A. in economics from California State University, Long Beach, in 1990, and he holds the Chartered Financial Analyst designation.

SECTOR — GENERAL INVESTING

TWST: Please start with a brief history of Century Management and an overview of your operations.

Mr. Siderewicz: Century Management was started in 1974 by Arnold Van Den Berg, who is still the Chairman of the Board and very active in the day-to-day research and management of the company. Historically, we've been a value-oriented shop with a focus on small-cap value, although we've always invested in all asset classes across the board, including fixed income, large caps, wherever we feel there is value. Our client base historically has been high net worth individuals and retirees, although we do manage money for institutions, family offices and pension funds. The firm's overall philosophy is deep value. It comes from the Graham & Dodd school of thought. Therefore, on both the equity and fixed income side we're looking for undervalued securities, or buying securities as prices decline enough so that there is value in the security at the time we buy it. This way we don't have to make a lot of future projections. What we're really looking for is a price that reflects a tremendous reduction in risk. And when we find it, it also gives us a greater upside potential.

TWST: What are the firm's assets under management?

Mr. Siderewicz: Right now, we're right around $2 billion in assets under management.

TWST: You spoke about being a value-oriented firm. Is there anything you would add in describing the overall investment philosophy and strategy?

Mr. Siderewicz: Like I said, it's a deep value philosophy. When we look at any asset, we'll appraise the asset and determine its intrinsic value. We want to buy assets when they are selling at deep discounts to their intrinsic value. This allows us to establish a margin of safety so that if we're wrong in our appraisal, we still have a chance of showing a positive return, or at the very least, less of a loss. Typically when it comes to equities, we try to buy them when they are trading approximately 50% below our appraised intrinsic value. However, when it comes to small-cap securities, many times we get them down as low as 60% or 70% below intrinsic value. Especially in a market like we saw couple of years ago, we really saw some deep discounts, it seemed like everything was on sale. By focusing on a deep discount to today's intrinsic value, it allows us to make our returns off from the bottom. We feel that when you're buying securities with a margin of safety, i.e., at a deep discount to intrinsic value, you're going to reduce the risk in the overall portfolio, as well as increase the return potential.

TWST: Please tell us about the fixed income fund.

Mr. Siderewicz: The CM Advisors Fixed Income Fund was started in March of 2006. On a firm-wide basis, our separate account business has always invested in fixed income securities, as we've always had clients that wanted balanced accounts or straight fixed income accounts. So it seemed only natural to start a mutual fund for clients that had smaller accounts. This way they could still have a cost-effective vehicle in which to get fixed income exposure. Furthermore, it is really difficult for smaller- to medium-sized accounts to buy small individual pieces of a bond and still get favorable pricing. So the CM Advisors Fixed Income Fund is another vehicle that our separate account clients and now non-separate account clients can use in their asset allocation. Plus, for anyone buying this Fund, they can rest assured that we are using our core, deep-value philosophy in the management of the fund on a day-to-day basis.

TWST: What kinds of opportunities are you finding in today's market?

Mr. Siderewicz: In fixed income, right now, obviously with the yields being as low as they are, I'm finding that you have to be a little bit more opportunistic than just a buy-and-hold mentality. There have been opportunities periodically on the longer end of the curve. We think the short end of the curve is grossly overpriced, but the longer end of the curve, the long-term Treasury or longer term corporate bonds, those yields ebb and flow with the economy. The long-term Treasury is highly correlated to nominal GDP. So in this kind of environment we are seeing fits and starts. For example, when we have a strong quarter, yields drift up a little, and then when we have a weak quarter or two, yields will come right back down. Today we're trying to be a bit more opportunistic out on the longer end of the yield curve, because we think the long end of the yield curve is a better value than the shorter-term maturities. It's not going to really run away from here, but it is going to ebb and flow with nominal GDP and the strength of the economy. Other than that, we've been very defensive. Today, we have approximately 45% of the fund in cash. We are just waiting for what we would call good opportunities, i.e., deep values where we can buy and still get a margin of safety on our investment.

TWST: What are some of your current holdings?

Mr. Siderewicz: In our current portfolio, we have roughly 35% to 40% in intermediate corporate bonds with maturities ranging from six to 11 years. Although corporate spreads have tightened dramatically since the 2009 market, when they were historically wide, we still think there is some room for corporate spreads to tighten from here. We think if you look at it additively, and say BBB long corporate paper is trading at roughly just under 6%, then you've got a spread of about 134 basis points (1.34%) over Treasuries. We think it could still tighten a little bit, but most of the spread tightening is probably behind us. However, if you look at corporate yields, the spread in yield over Treasuries as a percentage of the Treasury yield; by this measure the amount of risk premium you're getting on corporate bonds is still historically fairly high. We do think corporate bonds right now are a good place to be as far as they're not overvalued just yet.

As for Treasuries, like I said, we've been in and out of long bonds or longer-term Treasuries, not because we have a trading mentality — in fact, our fund turnover is really very low — but as I said, with the ebbs and flows of the economy, you're getting those long rates drifting up and then things slow down and then the rates come back down. So we've been trying to take advantage of the long bond or longer-term Treasuries as they drift up toward the 4.75%-ish level. We made investments in long Treasuries about the time of our last interview with you, February to April of last year, and got in around 4.75%, and that worked out really well because the long bond dropped in the midyear slowdown we had in 2010, dropping all the way down to 3.65%. This is the level where we sold our position. I think it got as low as 3.50%. That turned out to be a nice play for us. Recently, in the last couple of months, we've seen long Treasuries back up at 4.75% and once again, we have reestablished a portion of our long-term Treasury position.

TWST: With the corporate bonds, what are your investment parameters? Investment grade only?

Mr. Siderewicz: The fund can do anything; we could be 100% high yield, 100% cash, we could be in mortgages, we could be in TIPS, or anything in between. We have a wide-open mandate in our prospectus; however, our goal is for the fund to have an overall investment grade weighting more times than not. As such, it is highly unlikely that we will ever be 100% in any one asset class. Right now, most of our corporate bonds are in the BBB area. Although we have a few that are A and AA quality, and approximately less than 5% of our corporate bonds are below investment grade. But our mix of corporate bonds averages BBB quality, with an average of eight- to 10-year maturities. When we bought those names, by historical standards they were really cheap. We bought a lot of this paper in the fourth quarter of 2008 through the first quarter of 2009, and they've performed quite nicely. And as I mentioned earlier, we still think there is price and room for spreads to tighten a little further.

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TWST: What are your thoughts on the potential for rising interest rates and inflation going forward, and how would that affect a fixed income portfolio like yours?

Mr. Siderewicz: Where you're going to get most of the rate move, we would think it would be on the short end of the yield curve. Eventually, when the Fed starts to tighten policy — which we think winding down QE2 by June 30 will definitely be a step in the tightening direction — you're going to see the rates on the short end of the curve, which are artificially low right now due to the Fed policy, come up. And then you'll probably see a flattening of the yield curve. Historically, if you go back to the Fed's tightening cycles, when they're on a sustained tightening basis you almost always end up with a very flat yield curve at the end of the tightening cycle. You can go back to 2006 or 2007, when they last tightened. They got the Fed funds rate up to 5.25%, and I think the long bond peaked out at 5.40%. So it's 15 basis points of spread differential versus 450 basis points right now. We would expect the next move to be one in the direction of tightening by the Fed, and we would expect this tightening to produce somewhat of a flatter yield curve than we see right now.

On the inflation front, we're going to post some uptick in the headline CPI rate that includes food and energy, just because of what energy prices and food prices at the commodity level have done recently. But we don't expect the core rate to show much of an uptick. The reason for this is that wages are not moving. With a weak labor market, employees don't have pricing power; we don't think too many people are pounding the table for a raise. So you're not really seeing wages keep up with what we're seeing in the headline CPI with the energy prices and food prices. Those extra dollars that you put in your gas tank has to come from somewhere; it's going to come out of discretionary spending, and that should keep the core rate somewhat tame. If you look at the core measures of inflation, it's made up with a heavy weighing on services and service pricing. And if you look at service inflation, based on the report we got last week, those price increases seem rather tame compared to what we've seen historically and what we're seeing now on the commodity front.

TWST: Do you pay attention to any other macroeconomic or market trends/dynamics?

Mr. Siderewicz: Obviously, the industrial production capacity utilization is important, and we look at that as to how much spare capacity does the economy have. If it has a lot of spare capacity, you have what they refer to as an output gap, which is hard to track in real time. But by looking at the capacity utilization in both manufacturing capacity and also on the labor side — and you're trying to understand just how much room and spare capacity the economy has — it is a view that leads to inflation. The more spare capacity the less inflation pressure there is. If factory utilization is up in the mid-80s, then we think companies have a little bit more pricing power. But where it is now and as weak as it has been, I don't think companies have the pricing power to pass through much of their commodity input costs to the consumer. We are definitely keeping a close eye on those sorts of measures. And when they come out, we try and dig down beneath the headline numbers to see what the underlying trends may be.

TWST: Do you have any particular advice for investors in terms of how they should incorporate fixed income into their overall investment strategy, or advice in terms of evaluating particular investments?

Mr. Siderewicz: Our advice has always been to pay attention to price. We believe what Ben Graham said is true: the price you pay determines your return. Therefore, the most closely watched fundamental in our opinion is price. My advice to investors is that when you see prices going down in an asset class and yields going up in bonds — bond prices going down — that is when you start thinking about moving some money into that asset class. And you don't have to do it all at one time, but if you see big-cap U.S. stocks really getting beat up, you might want to increase your allocation to big-cap U.S. stocks. Same with any other asset class. If you see interest rates going up dramatically and it's on the evening news that inflation is going to go crazy and bond yields are going to go through the roof, that's a good time to sprinkle some money into that asset class. If the prices go lower, then add some more money to it. We're big fans of averaging down in price, so if you pay one price, you start a position, and the price goes lower, well then that is a better price, i.e., a better value, so you just buy a little bit more.

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I see too many investors doing what we call "chasing yield" or "chasing returns," and they seem to allocate money to investments that have already done fairly well in price and have already moved up on the hopes that it will continue. The problem with doing this is that you are increasing your risk, because you're paying a higher price and at the same time you're also reducing your potential return. If the price has already moved up "X" percent, then that's just "X" percent less it will move up in future.

TWST: Would you talk about performance for the fixed income fund and more broadly, for the firm as a whole?

Mr. Siderewicz: Fixed income-wise, inception (3-24-06) through April 15, 2011, the CM Advisors Fixed Income Fund is up an annualized 8.03%. On a rolling five-year basis ending April 15, 2011, it is up 8.55%, and for the rolling three-year return ending April 15, 2011, it is up 6.99%. The one-year return ending April 15, 2011 is 6.65%.

Performance				
	1 Year	3 Years	5 Years	Inception
CM Advisors Fixed Income Fund	6.65%	6.99%	8.55%	8.03%
Barclays US Aggregate Bond Index	5.36%	5.55%	6.26%	5.91%
All periods ended April 15, 2011. Inception date for the Fund is March 24, 2006. All returns for the Fund are annualized and net of fees.				

TWST: What do you use as a benchmark?

Mr. Siderewicz: The Barclays Capital U.S. Aggregate Bond index, which was formally the Lehman Aggregate. Since inception and over the past five years we have done a good job versus the benchmark. For example, since inception ending April 15, 2011, the benchmark is up 5.91%. For the rolling five-year return ending April 15, 2011, it is up 6.26%. For the rolling three-year return ending April 15, 2011, it is up 5.55%. For the one year ending April 15, 2011, it is up 5.36%.

TWST: Is there anything else you'd like to add?

Mr. Siderewicz: I would add a little bit more to my advice to other investors. I gave you the overview of what my thoughts are for any asset class, but in fixed income in particular right now it's a unique situation. With yields being as low as they are, most people when they think of investing for fixed income, they look at the yield and they think that's the return that they're going to get. And for the most part, that is correct if someone is going to hold on until maturity. But what you really want to look for, if you are looking to invest in bonds, is for a manager that manages on a total-return basis, because most of the return in bonds right now is going to come from the price appreciation or depreciation, not yields. This is because the yields are so low that it's really hard for the yield to be a meaningful percentage of the overall return. For example, if you've got a 3.5% yield on a 10-year bond, the yield only has to move up 50 basis points and one year's yield is basically wiped out by the price change of the bond. If yields move down by 50 basis points then the total return would double the yield for the year. So the price action is very important in fixed income investing right now.

TWST: Thank you. (MN)

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The Fund's expense ratio for the fiscal year ended February 28, 2011 was 0.90%. The Fund's expense ratio as a percentage of the Fund's average daily net assets as of March 31, 2011 was 0.83%. This expense ratio may fluctuate based upon a number of factors, including changes in the Fund's net assets.

Investment in the Fund is subject to investment risks, including, without limitation, market risk, income risk, lower-rated securities risk, interest rate risk, management style risk, regional and sector risk, maturity risk, mortgage risk, other investment companies risk and credit risk. For more information about the Fund, including the Fund's objectives, charges, expenses and risks (including more information about the risks listed above), please read the prospectus.

An investor should consider the investment objectives, risks, and charges and expenses of the Fund carefully before investing. The prospectus contains this and other information about the Fund. A copy of the prospectus is available by calling 1-800-664-4888 or writing the advisor at 805 Las Cimas Parkway, Suite 430, Austin, Texas 78746. You may also call the Fund directly at 1-888-859-5856. The prospectus should be read carefully before investing. The information presented on this page is not an offer to sell or a solicitation of an offer to purchase the Fund.