



Dear Fellow Value Fund Shareholder:

Through June 30, 2010, the net asset value of the Investor Class of the FAM Value Fund was \$39.16. This represents a decrease of -0.4% from the beginning of the year. For comparison, the S&P 500 Index decreased -6.7% and the Russell 2000 Index declined -2.0%.

2010 Review Year-to-Date

The stock market started the year by continuing 2009's strong rally. At the end of April the S&P 500 Index was up more than 6% for the year. Unfortunately, April proved to be the peak of the first six months. Government debt problems in Europe and renewed fears of a global economic slowdown shifted stock prices into reverse. Since the peak in April, stock prices have declined by more than 15% putting them back in Bear Market territory. The main question being asked today is, "Will the U.S. economy experience a double-dip recession?" No one knows the answer to this and it is out of our control; consequently, we focus on investing in financially superior companies that can still make money in the stock market even if the economy is stagnating.

Portfolio Activity

Given the increase in stock prices earlier in the year, we were net sellers of stocks in the first six months of 2010. We sold partial positions in stocks that we viewed as fairly valued. This list includes Berkshire Hathaway, General Electric, M&T Bank and Martin Marietta Materials. We also sold our entire position in Cognex and International Speedway Corporation.

We did purchase two new ideas – Digital River and Bank of the Ozarks. Digital River is a technology company that provides retailers with a way to sell their software over the Internet. We purchased shares of the company at a little more than two times the cash on the balance sheet. The company has more than \$400 million in cash, minimal debt, and is growing its core sales at a double-digit rate.

Our other purchase was Bank of the Ozarks. This Arkansas bank serves a number of fast growing markets in the Southeast. The CEO, George Gleason, has been leading the company for more than 20 years and has an excellent record. The bank has a very strong capital position, above average profitability, and good credit results.



Performance Detail

Despite the fact that most markets are down year-to-date, one half of our stocks appreciated in the first half of the year. In general, our financial companies performed well with two of our property and casualty insurance companies posting gains, four of our five banks showing a positive return year-to-date, and a 30% gain in our life insurance investment.

Best Performers

The Fund's best performer on a dollar-weighted basis was Berkshire Hathaway (+ 21%) with a gain of more than \$6 million. Berkshire is well known as the investment vehicle of world renowned investor Warren Buffett. The company's operations have performed well and at March 31, 2010, the company had an all-time record book value of \$89,000 per share. In addition to good fundamental performance, the stock was added to the S&P 500 Index which created temporary demand for the stock. We took advantage of this demand and the subsequent increase in price to sell a small portion of our shares.

The second best performer in dollar terms was Protective Life (+31%) for a gain of more than \$3.3 million. Protective's leadership has done a terrific job of managing through the financial crisis and improving the company's financial strength. Over the last 18 months, management has increased the company's capital base by \$1 billion putting the company in a strong financial position. The stock entered the year at a significant discount to our estimate of intrinsic value. As its value has begun to be recognized, the stock has performed well.

The third best performer in dollar terms was Ross Stores (+25%) for a gain of \$3 million. Ross has been an amazing story over the last three years despite the recession and financial crisis. Since the summer of 2007, the stock has appreciated more than 70% compared to a 30% decline in the stock market. The Ross Stores retailing formula of designer clothing at a discount price has been a big hit with consumers.

Worst Performers

The Fund's worst performer on a dollar-weighted basis was money management firm Franklin Resources (-18%) generating a loss of \$3 million. Franklin is a global asset management firm and was impacted by the worldwide decline in stocks. The company is very strong with \$4 billion of cash and significant profits. Given the company's exposure to the stock market we would expect this stock to do well in Bull Markets and poorly in Bear Markets. This is exactly what has happened year-to-date.



The second worst performer in dollar terms was Amsurg (-19%) also with a loss of \$3 million. Amsurg owns and operates ambulatory surgery centers (hence the name) which perform specialized surgeries. While earnings are expected to decline a slight -4%, we can see no fundamental reason for a -19% decline in the stock price year-to-date. With the stock trading at less than ten times trailing earnings and solid cash flow generation, we are holding onto the stock.

The third worst performer in dollar terms was Federated Investors (-23%) with a loss of almost \$2.8 million. Federated is an asset management firm with an excellent franchise in money market funds. The current low interest rate environment is temporarily hurting the money fund business and pressuring Federated's earnings. Over time, higher interest rates should improve the attractiveness of money funds and result in higher profitability for Federated.

Our Investment Strategy

The value of any business is determined by the cash that the business generates and what management does with the cash. Since these are the two main sources of value, we focus our research on these areas and look for companies that have the following characteristics:

High profit margins, significant free cash flow, high returns on invested capital, low levels of debt or other types of leverage, and management with a track record of using capital wisely. We like to purchase this type of company at a low price compared to the company's value.

We invest this way because it provides three important advantages:

- 1) **The risk of permanent loss of capital is greatly reduced.** There are two ways to lose all of your money in an investment. The first is to pay too high a price. For example, in the technology bubble of 2000 people were willing to pay any multiple of earnings to be part of the "new economy." One of the favorites of the day was JDS Uniphase with a stock price of more than \$1,000 a share. Today the company is profitable, but the stock trades for \$9 share. This is a loss of 99% and a permanent loss of capital for those investors.

The second way to have a total loss of capital is to invest in a company with too much leverage or poor asset quality. The recent financial crisis provides numerous examples



of this type of business including AIG, Bear Stearns, Lehman Brothers, and Washington Mutual.

Our approach will avoid these two pitfalls as we invest in strong companies and pay attention to the price that we pay.

- 2) **Financially strong companies can do better than average in poor economic periods.** We like companies with low levels of leverage and significant cash generation because they can do well in *any* economic environment. As demonstrated in the recent downturn which was one of the worst economic environments of the last fifty years, this type of company performed relatively well. During calendar year 2009, all the companies that we own positions in today reported positive earnings per share – every business made a profit and some of our holdings did significantly better than just making a profit. We expect this to be the case in 2010 as well.

Here are two examples of companies that were able to take advantage of the economic turmoil to grow their businesses:

- Bed Bath & Beyond used its financial strength to take advantage of the demise of its most aggressive competitor. Bed Bath & Beyond has continued to open new stores and has a record \$1.8 billion in cash on the balance sheet.
- Brookfield Asset Management took advantage of low prices for assets around the world and expanded their holdings in strategically important railroads, ports, and real estate. These assets will add to the long-term intrinsic value of Brookfield's shares.

- 3) **Companies that generate free cash flow can increase shareholder value in slow economic environments.** Due to the effects of the financial crisis and the large amount of world debt, the consensus view is that economic growth will be below average for the foreseeable future. If this is the case, companies that generate cash flow may still be able to create returns for their shareholders through the wise use of that cash. A company can use its cash to expand the business, reduce debt, pay dividends, or repurchase company stock. All of these actions can increase the intrinsic value per share of stock.



For example, consider one of the Fund’s longtime holdings John Wiley & Sons. We first purchased John Wiley in the summer of 2002 at a price of \$24 per share. Wiley is not a fast growing company. Management usually tells investors to expect sales to grow in the mid-single digits per year. However, the company generates large amounts of cash which has been used to make two significant acquisitions, repurchase stock, and increase the dividend annually. As a result of these actions during an eight year period where real GDP grew at 1.7% per year and the S&P 500 Index returned 2.5% per year, we have earned a 7.3% annual return on our original purchase of John Wiley.

Since economic forecasts are often wrong, no one can be sure what the next six months will bring; nor can they accurately predict the next six years which is more our perspective as we look at longer term horizons. That is why we use our own independent, time-tested and reliable research process to find financially strong, quality businesses that can endure economic cycles and potentially thrive over the long term. History shows that stocks purchased at reasonable valuations have performed well over time and can provide a positive return after inflation — so we will stay the course and strive to protect *and* grow your assets despite what may occur in the short term.

Long-Term Returns

| | Average Annual Total Returns as of June 30, 2010 | | | | Life of Fund (1/2/87) |
|--------------------|--|--------|--------|---------|--------------------------|
| | 1-Year | 3-Year | 5-Year | 10-Year | |
| FAM Value Fund | | | | | |
| (Investor Shares) | 18.20% | -7.11% | -0.58% | 6.40% | 9.73% |
| (Advisor Shares)* | 17.77% | -8.20% | -1.58% | N/A | * |
| S&P 500 Index | 14.34% | -9.84% | -0.81% | -1.61% | 8.81% |
| Russell 2000 Index | 21.48% | -8.60% | 0.37% | 3.00% | 8.26% |

*FAM Value Fund Advisor Shares were launched on July 1, 2003. The return since inception is 2.93%

The performance table does not reflect the deduction of taxes that a shareholder would pay on Fund distributions or the redemption of Fund shares. This information represents past performance of the FAM Value Fund and is not indicative of future results.

FAM Value Fund



Thank you for investing with us in the FAM Value Fund.

Sincerely,

John D. Fox, CFA
Co-Manager

Thomas O. Putnam
Co-Manager