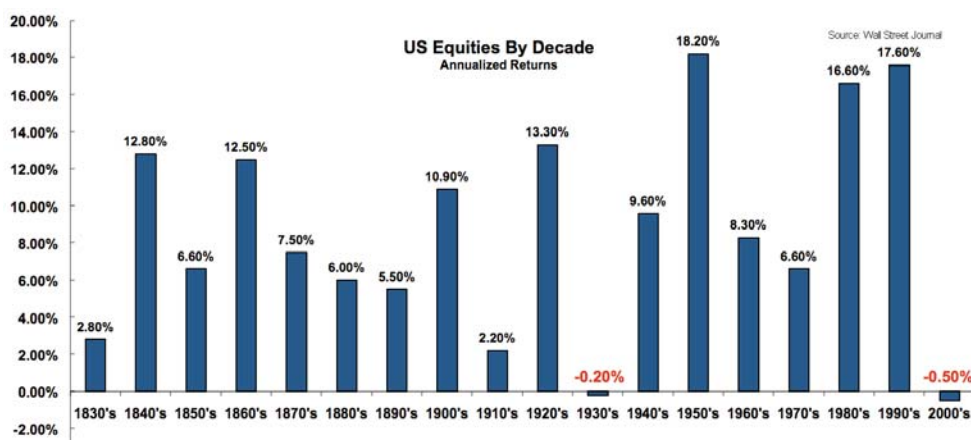


"HAPPY NEW DECADE!"

Simply saying "Happy New Year" seems inadequate as we think about what U.S. investors have endured over the last 10 years, officially the worst calendar decade for the country's stock market. Investors in a broad basket of stocks have seen their equity capital shrink at a rate of $-.50\%$ per year which equates to a cumulative loss of about -5% . This period eclipses the losses endured in the 1930s where stocks declined at a rate of $-.2\%$. In contrast, Berkshire equity portfolios were able to grind out a positive return this past decade, rising in the mid single-digits. Clients who also had a Berkshire bond portfolio likely fared even better. The chart below shows just how unique this past decade was.



Time Magazine recently ran a cover story entitled "The Decade From Hell" with content not limited to the financial system. It cited the contested presidential elections of 2001, 9/11, Anthrax scares, snipers in Washington D.C., Hurricane Katrina, two wars and record energy prices. On the financial front, we started with the crashing of the tech bubble, a deep recession that took the S&P down 50% and corporate malfeasance (think Enron, World Com). The mood of the country, indeed, seemed grim.

And, of course, the decade's misery was punctuated by the financial panic of 2008 where we saw some of the most storied financial institutions fall, shattering confidence. The panic steam rolled into the early months of 2009 and was almost surreal as investors watched market-crashing news events and the destruction of financial value in real time.

Obama gets sworn in?
Stock market
down 3.5%.

Newly appointed Treasury Secretary speaks?
Stock market down 5%.

\$50 billion in Maddoff assets?
Gone.

Job losses?
About 700,000
per month.

Unemployment rate?
Near all time high.

Financial institutions?
Failing and may need
to be nationalized.

Gold?
New highs.

US dollar?
New lows.

Political rancor?
Palpable.

Pessimism?
Maximum.

A formula for a **60% increase in the market**. Crazy. Yet, that's exactly what happened.

Berkshire is a fee-based, SEC registered advisory firm serving the portfolio management needs of high net worth and institutional clients. Over the past 20 years, we have successfully implemented highly focused equity, fixed income and balanced portfolios. Our guiding principle is a belief that success is achieved by combining rigorous, well crafted investment processes with an exceptional level of client service and attention to detail. Asset Management with a Difference...Diligence, Integrity and Focus.

IN THIS REPORT

- The past decade has been the worst on record for US stocks, including the 1930's
- Periods of "maximum pessimism" have often provided the best entry points for investors
- Stock valuations are now substantially lower than at the beginning of the decade likely providing better long run appreciation potential
- Mutual fund flows indicate high aversion to US stocks and a preference for recent winners such as gold and bond funds
- New services are now available through Berkshire Asset Management: 401(k) plans and trust services

As the market started to rally, most analysts didn't give it much of a chance. The prediction was, as equally improbable as the crisis once seemed, a sustained uptrend was equally unlikely. After all, the fundamentals of the economy were dismal. It is often those improbable events that have the highest payoff. However, while fundamentals matter, valuation and sentiment do too. Eventually, bear markets end, sometimes with no true visible catalyst. The mass selling just subsides. In March 2009, stocks were so heavily discounted and viewed as such a long shot, intrepid investors had huge upside betting on even the smallest shred of good news. Sure, there was a legitimate change in the trajectory of the economy but we think valuation and investor sentiment was the larger force behind the rally.

By the end of the year, stocks went on a wild ride from being down 25% to being up 25%.

Is the rally for real? What gives us confidence that the next decade is likely to be better than the last?

Valuation: We start this decade at substantially lower valuation that we began the prior one. Stocks at 15 times earnings provide far better appreciation potential than they do at 30 times earnings like they were at the beginning of the decade. The largest 10 stocks in the S&P 500 trade at an even larger discount with a P/E averaging around 12 or so. In 1999, they traded at a premium to the average stock.

Sentiment: Regardless of the strong rise in the market in 2009, we believe people seem quite leery of the market and are almost reviled by the thought of U.S. equities. We believe there has been a near wholesale abandonment of the asset class or that, at minimum, expectations for U.S. equities are extremely low. At the beginning of the decade people believed so fervently that "over time, U.S. stocks will do 10% a year" it was viewed almost as "gospel." The fundamentals appeared strong, but so were values and expectations.

Now, almost the exact opposite is true. Few believe that U.S. stocks can do 10% per year or, if they do, their behavior does not show it. Mutual fund data clearly shows money is flowing rapidly into bond funds, gold and emerging markets and out of U.S. equity funds. Proposing these as investment 10 years ago would have been quite unorthodox! Gold was so out of favor that international authorities tried to prevent its collapse. But now after it is the best performing asset class over 10 years, no price is too high for investors! This is a very expensive insurance policy against paper currency. The herd once again is flocking to these popular areas and there is no reason to believe this "rear view mirror" approach to investing will provide any better results in the next 10 years.

Fundamentals and Outlook: Despite a sharp rally, stock prices do not fully reflect their true earnings power. Return on shareholder equity remains below average but is improving. Companies have been forced into disciplined cost cutting and asset utilization is likely to rise. This will provide solid earnings leverage even with small changes in demand. Corporate balance sheets are particularly healthy. Risk premiums remain elevated which provides upside potential.

Is the economic picture perfect? Far from it but the U.S. economic engine is highly viable. The fundamental value trade off for U.S. equities is still good enough (and likely to improve) to beat last year's decade handsomely which, for all, will be a welcomed rebound.

In the end, the difference between investors' ultimate results often does not rest in analytical ability, education, access to

information or even investment approach. We continually find the differentiator is often temperament and the ability stick to the basic framework of decision making. This has been no small factor in our success during 2009. During times of underperformance or losses, many will find it tempting to focus on what's gone wrong or chase other areas of the market that may have provided a more favorable short-term outcome. The best managers realize that the path to recovery means optimizing remaining capital by carefully analyzing a range of intelligent choices and positioning the portfolio to capitalize on the next favorable turn of events. This ability to remain steadfast and confident in the wake of crisis, without reversing course, may be what adds the most value over time.

We are excited to announce two new services available through Berkshire.

The first is a full service participant directed 401(k) plan. After we've carefully dissected the fee structure of many competing offerings, we have found many plans are often paying **two to three times more** in fees than necessary (the bulk of them often hidden deep in the fine print). If you have an existing plan, we would be happy to review ways to substantially decrease fees while maintaining a high quality investment line up and excellent technology. Or if you are thinking of starting one for your company, we would be happy to help you explore your options.

The second is the ability to provide trust services through two of our major custodians, namely Schwab and US Trust. Both offer the ability to serve as a full service corporate trustee at a reasonable fee structure.

Please contact us if we may be of assistance in either of these areas.

Commentary Disclosures:

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References to particular securities are intended only to explain the rationale for the portfolio manager's action with respect to such securities. Such references do not include all material information about such securities, including risks, and are not intended to be recommendations to take any action with respect to such securities.