

LETTER TO SHAREHOLDERS

January 28, 2008

Dear Shareholder:

Overview

The adage, “Be careful what you wish for,” comes to mind as we look back at the end of 2007 and what has transpired thus far in 2008. The stock market posted negative returns across all indices in the last quarter of the year and has continued that trend up through the authoring of this letter. The S&P 500 Index peaked last October and has declined 16.0% since then, while the Russell 2000 Index of small-cap stocks peaked in July and has since declined 20.8%.¹ *The New York Times* recently reported that “2007 was the worst year for financial stocks since 1970.”² It has been a tale of two markets. Whether or not one owned financials (and to a lesser extent underperforming consumer stocks) dictated performance. FPA Crescent returned -0.4% in the quarter and +6.8% for the year-to-date period, successfully beating its benchmark and most major market averages. You will find comparative performance at the end of this letter.

We spend significant time penning our quarterly letters and, as much as we hope that they are widely read, we realize that they will never make a bestseller list. We assume that just 10% of the recipients read our missives but feel, should we have even just one reader, we need to write the letter so that you may better understand our investment process as well as to engage in the quarterly exercise of self-examination of recent decisions and current outlook. Such communication has greater importance in turbulent times or periods of underperformance. Although recent relative performance has been reasonably good, it has been a rocky road for the equity markets. As money managers with a long-term perspective and a willingness to hold cash and yet have the audacity to not call ourselves market timers, we may sometimes appear enigmatic. In turn, we sometimes find ourselves confounded by our shareholders who express a long-term orientation, yet add capital when performance looks relatively good and redeem when the opposite invariably occurs. In advance of discussing what we are doing today, we thought we would present a chronology of what we observed as likely to come to pass which has indeed done so and that our discipline has remained consistent throughout, then greater comfort may be taken that your capital has been entrusted to capable hands. The concerns we raised and alarms we sounded caused us to preach conservatism going back to 2005. To that end, we have reprinted excerpts from shareholder letters going back to 2005 for your review. In some cases following the excerpt, we parenthetically address our current point of view.

1st Quarter 2005

“We have shunned owning financials but believe we are now at an inflection point where shorting them appears to be more timely, and have gradually been increasing our short exposure to the sector. Complacent borrowers have taken on more financial leverage than they have a right to by any prudent measure. Complacent lenders, fourteen years since the consumer was last weakened in a recession, have aided and abetted borrowers’ spendthrift. We have been gradually increasing our short exposure, which represents more than 10% of our short book at this time.”

2nd Quarter 2005

“The housing market continues to outstrip the returns of the stock market and, as we have previously stated and believe, continues to be the engine of the U.S. economy...any weakness in the housing market will provide investment opportunity.”

“The consumer continues to impressively hang in there, thanks to low interest rates, rising home prices and easy lending standards. How long will this be is the question of the day...in 2007...\$1 trillion of the nation’s mortgage debt – or about 12% of it – switch(es) to adjustable payments. As interest-only debt (fixed for a teaser period) becomes adjustable, payment shock for the borrower will likely materialize, leaving many borrowers unable to repay their loans as scheduled.”

¹As of January 23, 2008.

²*The New York Times* 1/2/2008.

“...volatility has fallen to an all-time low. We envisage a period of increased volatility in the future. We will not scamper onto a limb to prophesy timing, direction or magnitude, but will confidently state that at some point in time the stock market will decline enough to allow us to invest our cash hoard. Since we cannot assess the timing of such opportunity, we wait patiently with the hopes that our own investment time horizon matches that of our investors. We look at the world as binary – either we invest in the stocks of businesses we believe offer the potential for high rates of return, or we keep it safe. If the Fund had a mattress, we would use that.”

4th Quarter 2005

“Small-capitalization stocks have become relatively expensive, having moved from more than a 40% discount to their large-capitalization brethren to the 10% premium today. We see little advantage to owning smaller, less liquid securities in your portfolio when they trade at a premium and your portfolio reflects this current reality and the weighted-average market capitalization of the securities held has increased to \$4.491 billion from \$3.242 billion a year ago, and \$893 million at its nadir in the Spring of 2000.” (We have continued investing in larger-capitalization companies as that is where the better value appeared. At this time, the weighted average market capitalization of FPA Crescent is \$36.548 billion.)

“Should our projection of mid-single-digit market rates of returns come to pass with greater volatility that is closer to its historic norm, we would then expect to see the gradual diminution in the size of many funds and the obsolescence of others.”

“We cast a wary eye as we hike the economic terrain looking for signs of weakness from the fearless overextended consumer with far more house than income. The housing market may be the linchpin of this fragile economic state.”

“We posit that many homeowners are currently purchasing unaffordable shelter, but have convinced themselves otherwise by maintaining the expectation that home prices will continue to rise, their incomes will at least remain constant, and that they will have the ability to refinance their mortgage while interest rates remain low. Mortgage lenders, with their innovative mortgage products, have proven more than accommodating in aiding and abetting homeowners’ quest for greater affordability, to wit: piggyback loans, i.e., second trust deeds that allow people to qualify for first mortgages; option ARMS that give the borrower the choice as to whether they would like to pay their mortgage in a given month; low documentation loans; and most recently, 40-year amortization products. Maybe we should take comfort in knowing that the National Association of Realtors says that there’s no housing bubble.”

1st Quarter 2006

“We have a laundry list of concerns – not long on optimism here. Margins for most companies are above normal, which leads people to think they are buying values on current earnings, which we believe is not true. Valuations based on normal earnings are high.... A range of data is pointing to spreading weakness in the housing markets. Volatility in the financial markets is near all-time lows. Volatility is now even lower than the previous low before the Long-Term Capital blowup in 1998. Bullishness is one standard deviation from the mean. Most importantly for us, our screens are turning up a small number of stocks and, of these, few meet the required standards. We firmly believe that our value standards are there to be followed, even if it temporarily means that cash builds.”

2nd Quarter 2006

“...the size of the (corporate) CDS (Credit Default Swap) market is now upwards of four times as large as the corporate bond market. We do not know how this leverage in the system unwinds in the future but we have our reservations.” (The system is beginning to be stress-tested. For example, ACA Capital has \$60 billion of swaps that they have already received forbearance on twice. The company has less than \$450 million in cash, as of year-end 2007. It appears that the holders of these CDS do not want to force the issue but this should and

will require them to take charges that reflect this reality. A portion of Merrill Lynch's recent write-offs took into account their belief that ACA would not prove to be a viable counterparty.)

3rd Quarter 2006

"As investment managers, we do not think we are so different from manufacturers. Investment ideas are our stock in trade, as opposed to widgets. Sadly, there aren't a lot of those coming out of our plant these days. We trust the reason is not that our equipment is broken. Opportunities certainly exist in the market. There is always something to do; however, we do not believe that there is enough to populate a portfolio in its entirety."

"With the last consumer recession having occurred in 1991, its impact has receded further from the minds of many investors and young portfolio managers, the chance of losing money seems all too remote, but not to us."

"The business of trading public and private companies continues to be one where liquidity is as easy to come by as rain was to Noah....Today's excess liquidity will probably one day dry up. Leverage funds will likely implode."

"As we become more invested, bear in mind that we frequently invest early. Do not be surprised to see stocks we purchase decline before they increase. As long as fundamentals remain intact, we will likely increase our position. We view such declines as temporary. Temporary means not permanent. It does not mean quick."

4th Quarter 2006

"We can imagine, although do not portend, that a crack in the façade of the investment banks could be the linchpin that creates future opportunity."

2nd Quarter 2007

"We have a four letter word in our portfolio, C-A-S-H. As we have previously stated, cash is a by-product of our investment process, not a macro call. There certainly exists the opportunity to make money in this market, just not at the level of risk we like to consciously accept. Cash and its derivative, downside protection, are viewed as unnecessarily punitive in the current bull-market environment."

"Maybe the subprime losses can be contained without too much damage to the underlying economy, but we doubt it."

"We believe the best part of the credit cycle is behind us. We own neither banks nor thrifts as a result."

3rd Quarter 2007

"We do not believe that, with home prices declining nationally for the first time since the 1930s and the expected negative impact on consumer spending, the price of oil at a high, the price of gold at a high, and the U.S. dollar at a low, the stock market should also be hitting new highs."

"We do not expect this to end well." (Making reference to the build-up of debt held by the U.S. government and consumer.)

"We maintain, though, that a severe U.S. downturn will be felt overseas." (Contrary to what many believe to have been an uncoupling of the U.S. economy from the rest of the world.)

What has recently occurred to negatively impact the stock market has fallen well within our expectations, as you have read. We suspect that before this is over, the market will see lower levels as we believe this is the worst credit crisis to impact our country since World War II and navigating the economic fall-out will prove challenging. At times, we would not be surprised to read headlines expressing excitement that the worst is behind us and clear skies lie ahead, only to be subverted by continued after-shocks of unwinding the biggest housing bubble in U.S. history, and the related roles that irresponsible financial institutions played as lenders,

insurers, and traders of a sundry of asset classes. We thus continue to exercise caution even as we have begun to increase our invested position.

Risk

As many financial institutions awakened to find that their capital had fallen below regulatory thresholds due to loan and trading losses as well as business impairment charges, the sovereign funds of our wealthy and “friendly” trading partners have stepped up and injected capital. These are the investment operations of countries that heretofore have not been allowed to invest in businesses that could potentially harm our state. You may recall that the U.S. government would not allow Unocal to fall into the hands of the Chinese state-run oil company in 2005 or that Dubai was not allowed to purchase management contracts to service six of our ports in 2006. But now that we have found trouble, or trouble has found us, we happily put aside such jingoistic thoughts and, for a combined \$39.1 billion entry fee, have allowed Singapore to become partners with UBS and Merrill Lynch, Abu Dhabi, Kuwait, and Saudi Arabia with Citigroup, China with Bear Stearns and Morgan Stanley, and so on. We are not pushovers though; it has taken \$133 billion of cumulative write-downs by banks and securities firms since the beginning of 2007 to change national opinion.³

Another potential problem that could negatively impact global financial institutions is their exposure to Credit Default Swaps (CDS) – at best a form of insurance dependent on the insurer making good and, at worst, a derivative bet on the change in high-yield and/or corporate bond spreads. We considered purchasing CDS on subprime mortgages back in early 2006, but we stayed away from the trade as we were concerned that if things were as bad as we thought they could conceivably be in a worst-case scenario, there would be excessive counter-party risk. We thought we might end up absorbing the negative carry for an extended period and the day that we would be proven correct and went to cash the check, it would bounce. It would be like our homeowner insurance carrier not paying to rebuild our home that just burned to the ground.

To date, that hasn’t materialized and a number of Wall Street fortunes have been created as a result of the bear bet made on subprime mortgages and to a lesser degree, corporate bonds. The last time we looked a couple of years ago, the size of the corporate CDS market was four times the size of the entire corporate bond market and the system has never been stress-tested. We are not sure what the notional size of the mortgage CDS market is today but it is huge, and the counterparty’s ability to pay in the event of default is suspect. This could create the next round of write-downs for financial institutions here and abroad, and the capital that would then have to be raised to keep these companies afloat could make the exposure to subprime and structured finance look like a rounding error and the current credit crisis appear somewhat liquid.

We are not calling for a CDS debacle, but we bring it to your attention as we believe that risk and risk management are consistently misunderstood. No less an arbiter of risk than the publishers of *Risk* magazine in their January 2008 issue awarded the French bank Société Générale the honor of Equity Derivatives House of the Year. They bestowed too soon, for in this same month, Société Générale announced that one of their junior 31-year old traders placed ill-advised bets on stock index futures and lost the bank \$7.2 billion. Imagine what a senior trader could do.

Commercial and credit card loans are two other risk areas that face lenders and we do not believe that the associated risk has been adequately discounted in current stock prices. Stephanie Pomboy at MacroMavens recently pointed out “that a record 93% of loans used in CMBS (Commercial Mortgage-Backed Securities) issued in the 3rd quarter were Interest Only....As it invariably would, this “aggressive” behavior has already led to a surge in delinquencies. Bank loan charge-offs for commercial mortgages are now rising faster than they are in residential mortgages. And, they are doing so at a time when banks’ exposure to this segment is, conveniently, the highest (at 14% of total bank loans) since data began to be collected thirteen years ago.”⁴ Meanwhile, credit card delinquencies have been trending higher and, although still below their past peaks, they are at all-time highs in dollars, almost two times what they were in the last consumer recession in 1991 and 30% greater than where they were during the 2001 recession.⁵

³Lou Chen, Vivien. “Greenspan Says U.S. Housing Market May be ‘Starting to Bottom’.” *Bloomberg* 1/24/2008

⁴Pomboy, Stephanie The Next Disaster. (11/1/2007). *MacroMavens*.

⁵Pomboy, Stephanie The Next Disaster. (11/1/2007). *MacroMavens*.

Economy

Much of our economic outlook is tied to our lengthy discussion of the financial sector. So goes the industry's collective capital base and ability and desire to lend, so will go our economy. Much of the economic crosscurrents we face are new to us – all of us. Neither economist, nor market prognosticator alive has seen home prices decline nationally, let alone with debt on household balance sheets at all-time highs – important considerations where consumption accounts for 70% of our Gross Domestic Product. So we imagine that we are not alone, as we admit that we lack clarity as we look into the future. Our partner, Bob Rodriguez, recently penned an excellent summary of the issues facing us in an essay entitled, aptly enough, Credit Crisis. We suggest that should you desire a clear view to the challenges we face, you visit our website and read his excellently laid out arguments.

http://www.fpfunds.com/news_01222008_credit.asp

The credit constriction that currently has a chokehold on worldwide liquidity outside of the sovereign funds has yet to run its course. The Federal Reserve has cut the Fed Funds rate from 4.25% to 3.50% in four months. We do not believe that a 1.75% drop in rates will incentivize lenders to extend credit. Banks are fighting to raise capital in the face of rising losses from bad loans, derivatives, structured product, etc., and are more concerned with shoring up their balance sheets than they are with growing them. The Fed can drop rates but they cannot force capital constrained banks to lend and overleveraged consumers to borrow. In that the stock market has been moving in concert with the 10-year Treasury yield, we would argue that the Fed faces the dilemma that their aggressive monetary actions to date are pushing on a string. And yet, they face the issue that, if they move too aggressively, they might fuel further inflation. For those of us who drive, fly, shop, eat, and receive healthcare, we realize that the headline rates of inflation seem instinctually low.

There are three key economic variables we are watching very closely today. They include the monthly change in industrial production, the change in monthly retail sales, and the new weekly claims for unemployment insurance. Thus far, industrial production has moderated over the last couple of months, but is not signaling a recession. The weekly change in unemployment claims, which can be volatile, is also moderating and not yet signaling a recession. On the other hand, retail sales have clearly slowed over the last few months and are among a couple of economic indicators that are pointing to a contraction of economic activity. We will continue to monitor these indicators, and others, to help guide us allocating your capital.

Investments: Equity

A business's valuation will move up and down, but always with less volatility than a company's stock price. Once we become comfortable with our analysis and have conviction, then we care more about how the market will value a business a few years out than where it trades in the interim. By avoiding companies with excessive financial leverage, we at least hope to minimize that volatility and make sure that the prospects of bankruptcy are almost zero.

We continue to maintain that corporate earnings are overstated, thereby making Price/Earnings (P/E) ratios understated. Corporate operating margins remain near their all-time highs. Any reversion to the mean negatively impacts corporate earnings. The S&P 500's P/E is additionally understated if you were to exclude the P/Es of energy and financial service companies. The energy sector continues to operate with above trend earnings, although as we have discussed in great detail, we believe that this will continue to be the case. Financial service companies' P/Es appear quite inexpensive if you were to consider the recent write-downs as anomalies. Market pundits tend to exclude non-recurring charges. The problem is that sometimes those pesky write-offs that were supposed to only happen once, happen again, and again. We also continue to believe that financial companies have been over-earning for years and that the "normal" level of earnings will prove less than recent experience. This could take up to two P/E points out of the S&P 500.

We like to shop amongst the downtrodden and have, in fact, dedicated an analyst to pursuing investment opportunities in financial services companies, particularly lenders. The KBW Bank ETF declined 37% from

its peak a year ago but has since rallied so that the index decline is 27.5%, though we expect additional fall-out in the sector.⁶ We have begun to invest in a few new companies but we have not jumped in with both feet as we believe we have yet to hit bottom. Although we cannot pick when the depths of despair will be reached, we feel that time is on our side as we expect tens of billions of dollars of additional bank write-downs and that stocks will not bottom until we are further down the path of recognition. With so many institutions raising capital to buttress dangerously low reserves, the one question we keep asking ourselves is what is the denominator, i.e., how many shares will have to be issued, diluting current shareholders, so that the organization remains viable?

Although we believe more downside exists, our longer-term time horizon, combined with inexpensive prices on normalized earnings, dictates our acquiring some shares in the consumer sector. We believe that our invested position will increase over the course of 2008 as additional bad news provides investment opportunity. We will scale in over price and time. We do not expect to make money on each tranche purchased but do expect to make good money on our average cost. Investor patience can at times be tested by large cash positions, only to be replaced by the patience required to hold a position that was started too early, as defined by stock price movement, rather than business value.

As one example of what we are doing, we have increased our investment in Group 1 Automotive, the third largest automobile retailer in the U.S., as the stock has declined and, at the same time, reduced a portion of our offsetting short exposure. We continue to believe that Group 1's earnings per share, normalized for a reasonably good economy, are \$4 today, and growing. Passenger automobile sales declined 2.8% in 2007 to 16.1 million units and are currently estimated to decline another 4.3% in 2008 to 15.4 million, still 11.5% less than the 17.4 million peak in 2000.⁷ However, these numbers include both retail and fleet sales, with the latter representing a disproportionate amount in the recent year, which means that retail sales are actually lower than they appear. We think we are already more than halfway to the recession declines seen in 1991, and adjusted for Group 1's better-than-average brand mix (~60% Asian manufacturers) even closer to a bottom. We do not believe we have reached bottom, but we believe that the upside that we can see over the next five years more than offsets the downside we believe exists.

We took a position in Covidien, the medical-device company that was spun out from Tyco, when the stock came under pressure and traded down to an attractive valuation. The company has strong market share positions in segments that are stable with consistent demand and an oligopolistic nature. For example, in endo-mechanical devices, Johnson & Johnson and Covidien capture close to 100% share, in pulse oximetry, Covidien has 60% share of the market, and so on. We like that the medical device markets where Covidien operates are less volatile vs. higher tech markets like stents. The management team and the employees are highly incentivized to maximize shareholder value since they own close to 7% of the outstanding stock via stock and options, more than a \$1 billion vested interest. The CEO and several other members on the management team also purchased additional shares after the spin-off at prices higher than our average purchase cost, showing their strong conviction in the business. We believe that Covidien had been weighed down as part of Tyco and, in the future, that selling synergies, bolt-on acquisitions, and cost-saving opportunities will contribute to an increase in revenues and reduced costs. The risk profile in this company is low with consistent revenue growth and more than 95% of sales from disposable products, strong and stable cash flow generation and a solid balance sheet. We believe the downside is limited from our average purchase price and that should the CEO, Rich Meelia, and his team execute according to plan, which they are highly incentivized to do, our upside is significant.

We have a mea culpa regarding a consumer investment that cost our portfolio dearly in 2007. Circuit City (CC) declined approximately 72% from our average cost to end the year at \$4.20 (it has since rebounded to \$5.24).⁸ CC is the second largest independent, consumer electronics retailer in the United States with more than \$11 billion in sales from approximately 650 stores. The company also has 800 smaller stores in Canada that generate approximately \$500 million additional sales.

⁶KBW Bank ETF (KBE). Peak: \$60.41, 2/20/2007. Trough: \$38.22, 1/18/2008. Current: \$43.74, 1/28/2008.

⁷Wards

⁸Price as of 1/28/2008.

We were initially attracted to Circuit City because the company offered the opportunity to substantially improve their profit margins and generate excellent earnings growth as those margins expanded. CC's valuation looked inexpensive when measured by its sales and "normalized" profitability. We also believed that the stock had good downside protection because the company's balance sheet appeared fortified with more than \$300 million of cash, net of debt. At the time of our purchase, CC's operating profit margin was roughly 1% and we believed that the company could achieve at least a 3% margin once management improved the operating performance of the company.

To achieve higher profit margins and earnings, a new CC management team began, a couple of years ago, to roll out modern information technology systems to better manage merchandise, stores and labor. Management changed many operating processes and store procedures in 2007 as part of this improvement process. All store personnel were retrained to become more knowledgeable about the consumer electronic products sold in the stores. The company reclassified several different job descriptions, and in the process terminated some higher-cost personnel that were essentially performing entry-level work. Store managers were required to have their stores in compliance with the new directives within a six-month period of time. If the store was not in compliance, new store management was brought in to improve results.

In retrospect there were too many changes made in such a short period of time. The company bit off more than it could chew, and the operating results suffered as the store personnel struggled in their execution of management's changes which led to salesperson productivity declining way beyond expectations. Sales productivity improved during November and December but has a long way to go before we would be satisfied. From our channel checks, it appears that customers believe that the service level has improved in many of Circuit City stores. That's a good start.

We still maintain that a 3% operating margin is attainable (Best Buy's operating margin is 5.5%). At that level, the implied EPS for the company is approximately \$1.40, with no growth in sales. With modest sales growth of mid to high single digits over the next few years, CC's earning power could approach \$1.75. Should CC be able to turnaround its operations and achieve these metrics, we would not be surprised to see the stock trade significantly higher and turn this position into a winner for us. Though the company has many challenges to overcome before it approaches that level of profitability, we believe it is still attainable, even in a challenging economic environment.

Investments: High-Yield/Distressed

We argue that corporate bond yields for the more levered companies have been held artificially low due to the proliferation of derivatives specifically, Collateralized Loan Obligations (CLO) and Credit Default Swaps (CDS). The ability to take loans, put them into baskets and, in turn, parse them into distinct tranches, and then sell them to those who would not otherwise be buyers of the underlying collateral, explains in too brief a fashion a CLO but portrays the alchemy of structured finance. The more than \$220 billion that has been raised for CLOs just since the beginning of 2005 has created ephemeral demand for high-yield bonds.⁹ All things being equal, an increase in demand begets a lower yield. Should you wish to buy a high-yield bond but fret that a bankruptcy would be too much to bear, you can purchase insurance from a panoply of investment and commercial banks, and insurance companies happy to provide credit protection in the form of CDS. An investor with the ability to insure is a buyer willing to accept a lower bond yield. Bond demand has been reduced by the recent closure of the CLO market and the questions surrounding the economic viability of the counterparties providing the CDS protection.

High-yield bond spreads have widened, as a result, and look more attractive. The option-adjusted spread of the Merrill Lynch U.S. High Yield Index widened from its historic low of 242 basis points (bps) reached in June 2007 to a current 703 bps.¹⁰ While the default rate was 0.9% in 2007, Moody's currently predicts an increase to 5.3% by year-end 2008. We have begun to increase our investments in high yield but here too, we believe that better entry points will surface as default rates rise.

⁹S&P Leveraged Commentary & Data

¹⁰Bloomberg. 1/28/2008.

Closing

We doubt that all risks we have discussed have been adequately discounted in the stock market. It was less than a year ago that people thought that subprime loans would prove not to be an issue as they could easily be absorbed in our \$14-trillion economy. That has not proven to be the case. We also realize, though, that the stock market usually bottoms before the economy. We just do not think we are there yet, as busts tend to follow booms.

Respectfully submitted,

A handwritten signature in black ink that reads "Steven Romick". The script is cursive and fluid, with the first letters of "Steven" and "Romick" being capitalized and prominent.

Steven Romick



FPA Crescent Fund

December 31, 2007

Portfolio Characteristics

	FPA Crescent	Russell 2500	S&P 500	Lehman Bros. Gov't/Credit
<u>Stocks</u>				
Price/Earnings TTM	12.3x	21.5x	16.9x	
Price/Earnings 2007 est.	11.2x	16.5x	15.2x	
Price/Book	1.6x	2.3x	2.8x	
Dividend Yield	1.5%	1.4%	2.0%	
Average Weighted Market Cap (billion)	\$36.5	\$3.0	\$109.5	
Median Market Cap (billion)	\$3.9	\$0.8	\$13.0	
<u>Bonds</u>				
Duration (years)	1.6			5.4
Maturity (years)	2.3			8.1
Yield	4.8%			4.5%

Portfolio Analysis

10 Largest Holdings (excluding U.S. Treasuries)		Portfolio Composition	
ConocoPhillips	6.3%	<u>Asset Class</u>	
ENSCO International	5.1%	Common Stocks, Long	55.7%
Assurant	3.9%	Common Stocks, Short	-4.6%
Reliant Energy	3.0%	Preferred Stocks	0.9%
Koninklijke Phillips Electronics N.V.	2.7%	Bonds & Notes	12.3%
Covidien	2.7%	Cash & Other	35.8%
Rowan Companies	2.2%	Total	<u>100.0%</u>
Magna International	2.1%	<u>Geographic</u>	
Chevron	2.0%	U.S.	52.4%
Sally Beauty Holdings 10.5% 2016	1.8%	Europe	6.1%
Total	<u>31.7%</u>	Other	4.5%

Performance Statistics

	FPA Crescent	60% R2500/ 40% LBGC	Russell 2500	S&P 500
<u>Statistics</u>				
Gain in Up Months - Cumulative	297.2%	279.0%	425.8%	363.1%
Upside Participation		106.5%	69.8%	81.8%
Loss in Down Months - Cumulative	-116.4%	-133.3%	-241.4%	-203.5%
Downside Participation		87.3%	48.2%	57.2%
Up Month - Average	2.6%	2.4%	3.8%	3.2%
Down Month - Average	-1.9%	-2.3%	-3.8%	-3.3%
Delta between Up/Down months - Average	4.5%	4.7%	7.6%	6.5%
Worst Month	-10.7%	-10.5%	-18.9%	-14.5%
Best Month	12.6%	9.7%	14.4%	9.8%
Standard Deviation	2.87	2.84	4.71	3.96
Sharpe Ratio (using 5% risk-free rate)	2.64	1.74	1.43	1.38
<u>Performance</u>				
Quarter	-0.4%	-1.3%	-4.3%	-3.3%
Calendar YTD	6.8%	3.9%	1.4%	5.5%
1 Year - Trailing	6.8%	3.9%	1.4%	5.5%
3 Years - Trailing	10.0%	7.0%	8.4%	8.6%
5 Years - Trailing	13.1%	12.1%	17.0%	12.8%
10 Years - Trailing	10.1%	8.3%	9.0%	5.9%
From Inception ^a	12.6%	9.9%	11.7%	10.5%

(Please see reverse.)

HISTORICAL PERFORMANCE

	FPA Crescent	60% R2500/ 40% LBGC	Russell 2500	S&P 500
2007	6.8%	3.9%	1.4%	5.5%
2006	12.4%	11.2%	16.2%	15.8%
2005	10.8%	6.0%	8.1%	4.9%
2004	10.2%	12.7%	18.3%	10.9%
2003	26.2%	28.1%	45.5%	28.7%
2002	3.7%	-6.6%	-17.8%	-22.1%
2001	36.1%	4.8%	1.2%	-11.9%
2000	3.6%	7.9%	4.3%	-9.1%
1999	-6.3%	13.3%	24.2%	21.0%
1998	2.8%	4.9%	0.4%	28.6%
1997	22.0%	18.5%	24.4%	33.4%
1996	22.9%	12.6%	19.0%	23.0%
1995	26.0%	26.7%	31.7%	37.6%
1994	4.3%	-2.0%	-1.1%	1.3%
1993 ^a	9.6%	8.2%	10.1%	5.3%

Objective, Strategy and Rankings

Objective

The Fund's investment objective is to provide a total return consistent with reasonable risk through a combination of income and capital appreciation by investing in a combination of equity securities and fixed income obligations. We strive to achieve equity rates of return with less risk than the stock market.

Strategy

To invest across a company's capital structure to meet our objective. This includes investing in Common and Preferred Stocks, Convertible Bonds, High-Yield Bonds, and Bank Debt. There is an occasional use of Government Bonds.

Downside Protection

FPA Crescent's ratio of positive to negative monthly performance is, on average from inception,^a 6% better than the equity indexes. FPA Crescent has, on average from inception,^a captured 76% of the upside monthly performance but just 53% of the downside when compared to the equity indexes.

Volatility

FPA Crescent has exhibited much less volatility as measured by its Standard Deviation from inception.^a On average, the Fund's Standard Deviation is 34% lower than the equity indexes. FPA Crescent has a much lower delta in its average monthly performance, i.e., the difference between the average positive and negative month when compared to the equity indexes.

FPA Crescent has had only one year of negative performance since inception,^a a loss of 6%. Compare that to the following indexes:

	60% R2500/40% LBGC	R2500	S&P 500
Number loss years since inception ^a	2	2	3
Worst annual loss	7%	18%	22%

Performance

FPA Crescent has beaten the stock indexes for the inception-to-date time period.^a Lipper has recognized FPA Crescent as the #2 balanced fund for 10 years (out of 245), for the period ended December 31, 2007.

Conclusion

FPA Crescent has met its objective since inception having achieved higher absolute rates of return than the indexes and a dramatically higher Sharpe Ratio.^a

NOTES

^a Inception date is June 2, 1993. Returns from inception are annualized. The annualized performance of the Russell 2500 and Lehman Brothers Government/Credit Indexes begins 6/1/93.

Past performance is not necessarily indicative of future results. The performance data represents past performance, and investment return and principal value will fluctuate so that FPA Crescent Fund shares, when redeemed, may be worth more or less than their original cost. All returns assume the reinvestment of dividends and distributions. There are no assurances that the Fund will meet its stated objectives. A portfolio's holdings and allocations are subject to change because it is actively managed and should not be considered recommendations to buy individual securities. Distributed by FPA Fund Distributors, Inc., a subsidiary of First Pacific Advisors, LLC.

Balanced Benchmark is a hypothetical combination of unmanaged indices comprised of 60% Russell 2500 Index and 40% Lehman Brothers Government/Credit Index, reflecting the Fund's neutral mix of 60% stocks and 40% bonds.

Russell 2500 Index is an unmanaged index comprised of 2,500 stocks of U.S. companies with small market capitalizations.

Lehman Brother Government/Credit Index is an unmanaged index of investment grade bonds, including U.S. Government Treasury bonds, corporate bonds, and yankee bonds.

S&P 500 Index includes a representative sample of 500 leading companies in leading industries of the U.S. economy. The index focuses on the large-cap segment of the market, with over 80% coverage of U.S. equities, but is also considered a proxy for the total market.