ROMC FUND

2008

ANNUAL REPORT

For the twelve months ended December 31, 2008

ROMC Fund service providers

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ROMC Fund results

Calendar year	Owners' return
2007 *	9.1%
2008	5.7%
Overall	15.3%

Total return is shown in Canadian dollars, net of expenses

* From October 1 to December 31, 2007

Glossary of financial terms: Revised & somewhat cheeky

CEO	Chief Embezzlement Officer
CFO	Corporate Fraud Officer
Broker	What my broker has made me
Financial Planner	A guy whose phone has been disconnected
Bull Market	A random market movement causing an investor to mistake himself for a financial genius
Bear Market	A long period when the kids get no allowance, the wife gets no jewelry and the husband gets no sex
Market Correction	The day after you buy stocks
Standard & Poor	Your life in a nutshell
Cash Flow	The movement your money makes as it disappears down the toilet
Profit	An archaic word no longer in use

Source: MSN groups - Berkshire Hathaway Shareholders

To the owners of ROMC Fund:

In 2008, our per-security net asset value increased $0.62, or 5.7%. Since inception, a little over one year ago, our net asset value per-security (our market value) has increased from $10 to $11.53, an annual growth rate of 12.1%.

The result, while not spectacular, meets the all-important test of increasing after-tax net worth by more than the rate of inflation, as illustrated below[1]:

	Owners'			
Calendar year	pre-tax return	after-tax return	Inflation	Relative results
		(1)	(2)	(1) - (2)
2007 * ----------------------------	9.1%	7.0%	0.1%	6.9%
2008 -----------------------------	5.7%	4.4%	1.2%	3.2%
Overall	15.3%	11.7%	1.3%	10.4%

Owners' return is shown in Canadian dollars, net of expenses.

* From October 1 to December 31, 2007

Time in, not timing

If you read the papers, you'll know by now that a number of financial industry forecasters claim to have predicted the recent demise of equities. Some stories suggest these savants knew the latest bear market would start as early as the fourth quarter of 2007. As luck would have it, the stock market did begin a material decline on October 10th of that year—just 9 days after our launch. If timing is everything, you would be wise to consider your manager's forecasting abilities when making decisions about ROMC. I don't have any special insights into the future and I don't think there is any advantage in trying to guess a market top or bottom. I do see a distinct advantage in finding and acquiring interests in good businesses that are also good investments and leaving them alone. It's time in, not timing. To make my point, let's review our own experience. From its start on October 1, 2007 ROMC has held, on average, more than 100% of its net worth in common stocks. During our brief history, stock markets around the world have declined substantially – our own S&P/TSX Composite Index having lost 34%[2]. At the same time, ROMC's market value has increased 15%.

[1] After-tax return is a rough estimate and may not represent an individual shareholder of ROMC Fund. Everyone's tax situation is unique. Inflation = Change in consumer price index; source: Bank of Canada (www.bankofcanada.ca)

[2] Source: www.standardandpoors.com

Would a prognostication of index prices, confidently provided by a title-endowed 'expert', have helped us attain better results? Not as far as I can see.

Getting a fair deal

In 2008, by my calculation, our investees' own business values increased by more than their market values. Since ROMC's inception, however, the two appear to be moving in tandem. This is good news. As long-term investors, we can only hope to achieve the same market results as our investees' own economic results. Notice the words "long-term". Over a short period, market prices can differ widely from sensible economic fundamentals, depending on the market's mood – which oscillates between euphoria and as Woody Allen put it, "despair and utter hopelessness." (No points for where we sit today.) To have prices and economics tracking closely over such a short period of time is remarkable and suggests we are getting a fair deal.

	Market value 31/12/08	% of Assets
Insurance (Cost $2,313,144)	**$3,236,678**	**60%**

Insurance remains our largest area of concentration. Last year, I described the two critical factors that determine success in an insurance operation – underwriting discipline and investment acumen. I also mentioned that our insurance investees demonstrated a high level of both. That was doubly true in 2008. On an underwriting and investment basis, they proved their superiority yet again. Now the distance between their competitors and them, while already wide, looks like the Grand Canyon.

Our insurance investments do not offer much in the way of cash dividends. The aggregate dividend yield, based on the year-end market value of our investees, is just 1%. That's okay. Their value is measured by the quality of the managers handling our capital as owners. And our managers may well be the best in the business. They are also major owners, which makes them our partners. Capable, honest and on our side – that's the dividend.

In last year's letter, I told you not to expect much from our insurance holdings in 2008. I was wrong. This year, I repeat my warning. There has been an absence of natural (and unnatural) disasters over the last few years. Probabilities suggest this will not continue indefinitely. In addition, it is hard to believe that interest rates, at less than 3% on long-term government bonds, will generate much current income on our investees' significant bond holdings.

	Market value 31/12/08	% of Assets
Healthcare (Cost $1,778,847)	**$1,699,520**	**31%**

When I first discussed my rationale for investing in the pharmaceutical industry, I described an arbitrage of sorts between what our investees were reporting in earnings on a GAAP basis and what they were actually earning in cash. This difference all but disappeared last year due to a material increase in our investees' reported earnings. In 2007, cash earnings were 169% of reported earnings.

In 2008, cash earnings were 112% of reported earnings. Dividends accounted for 96% of reported earnings last year vs. 109% in 2007, and dividends increased over the year.

	Market value 31/12/08	% of Assets
Media & communication (Cost $885,442)	**$972,952**	**18%**

This is an industry particularly sensitive to the economic cycle. When advertising makes up the bulk of your revenue, tough times can have a devastating impact on your top line. Add to the mix the current mood of shareholders, as reflected in stock prices, and this industry looks to be spiralling into oblivion. That is silly. It may well be a bumpy ride, but our results over an extended period of time should prove satisfactory.

What occurred in the pharmaceutical industry over the last few years also occurred in media. That is, little use of common sense when acquiring competitors. This recklessness has come home to roost in the form of asset write-downs. Reported earnings are being devastated on two fronts: Cyclical weakness and the evaporation of goodwill. Cash earnings have not been as affected which suggests some economic value exists.

	Market value 31/12/08	% of Assets
Merchandising (Cost $290,976)	**$335,202**	**6%**

Our retail investees continue to surprise me. I would not have thought that they could grow during a year in which, if you believe the news, half the planet declared bankruptcy. Our investees not only increased their overall sales, they did so on a same-store basis. (For those not employed as shopkeepers, "same-store sales" only counts revenue from stores at least one year old.)

I feel I should continue to caution you on our retailers' near-term prospects. ROMC has been lucky so far (better lucky than good, I'm told). Our investees will not escape a material slowdown in consumer spending and 2009 looks to be braking hard.

	Market value 31/12/08	% of Assets
Liabilities	**($883,248)**	**-16%**

You have doubtless heard stories of investment funds that, through the use of leverage, met their demise. In a common scene, enterprising 'hedge-fund' managers accepted $1 from investors and magically turned it into $30 of investments; their bankers and brokers only too happy to participate in 21st century alchemy. After collateralizing, securitizing and swapping this lead, which for a brief moment glittered like gold, managers came to the crushing realization that no matter how many post-graduate 'geniuses' the financial industry lured away from meaningful employment, alchemy makes for better bedtime stories than investment strategies. In the not-so-orderly exit from exposures, bankers – of course – took precedent. And so, intrepid investors failed to recoup much, if any, of their lead. It only takes -3.3% to wipe out shareholders in a $30 to $1 leverage ratio. (So what happens when results are -33%?)

While on my horse, I should mention that we too got caught up in the quest for gold. In fact, during October and November, your manager threw caution to the wind in an all-out frenzy to extend ROMC beyond its means. Well, you can hardly blame me. After all the years I have been filling some of your ears with the myth of a cheap stock market, we actually found ourselves in one. And I figured it might be time to stop talking and start walking. So, I hiked up ROMC's leverage ratio to: (Are you seated?) $1.16 to $1.

Checks and balances

ROMC has an important job: Allocate owners' capital, at opportune times, to businesses whose growth exceeds that of the general economy and which are run for the benefit of owners. Simple and not easy: Many seemingly attractive businesses are run by management, on behalf of management and for management. Huge salaries, bonuses, perks, patsy boards, unsustainable pension arrangements, re-priced stock options and termination settlements that could keep a small country running are handed out as the norm today for average, if not below average, operating performance. Owners don't stand a chance in the vast majority of management-controlled businesses. Did you know that 2007 compensation for the average publicly-listed company CEO was USD 18.8 million?[3]

Fortunately, ROMC has avoided much of this nonsense. At year-end, 72% of our capital was invested in businesses run by controlling shareholder-managers who are paid a relative pittance for the privilege of making us money. Their average total pay in 2007 was just over USD 800 thousand – just 4% of the average public company CEO! And our investees delivered a weighted average return on owner's capital of 26% that year, when the average public company (using the S&P 500 Index) delivered 13%[4].

You were quick to calculate that 28% of our capital must be invested in management-controlled businesses. Yes, and I hope they have been well chosen. But just in case, we've allocated our capital to those who pay out all of their surplus earnings in the form of dividends. At year-end, ROMC's management-controlled investments had a weighted average dividend yield of 10.5%.

Since we do not control our investees, these checks and balances help to ensure our survival.

[3] Source: Enough., John Bogle, pg. 131

[4] Source: www.standardandpoors.com

Expenses

ROMC operating expenses for 2008

Administration	$15,091
Commissions & interest	$30,369
Manager's remuneration	$106,569
	$152,028

If we were to add back operating expenses, ROMC's 2008 gross asset value per-security increased $0.68, or 6.2%.

Closing comments

ROMC's results have been positive thus far in great measure due to the quality of its owners. I'll give you an example. In October, I announced a special valuation in order to allow (read beg) new and existing owners to increase their participation in ROMC at what was, in my opinion, an opportune time. Some of you took me up on it and ROMC grew more than 40% that day. The market return on that new capital was entirely responsible for the 6% result for the year. In fact, from October 15th (special valuation day) to December 31st ROMC's reported result was 16%, much of it due to where we allocated new capital. Without it, our result for the year would have been zero.

More important is the fact that at a time when the world was reported to be falling apart and stock markets were in a tailspin, ROMC's owners marched resolutely into it all. That was impressive. I am fortunate to be partnered with such rational people – it makes me feel like the fellow who took his father's advice after asking him the secret to a happy family life. "That's an easy one," his dad told him, "marry up."

March 27, 2009 David McLean