FIDUCIARY MANAGEMENT, INC.
Investment Counsel

100 East Wisconsin Avenue, Suite 2200
Milwaukee, Wisconsin 53202
414-226-4545

INVESTMENT STRATEGY OUTLOOK – LARGE CAP EQUITY

Quarter Ended September 30, 2008

<u>*October 1, 2008*</u>

Fiduciary Management, Inc. large cap portfolios were down approximately 4.5% in the September quarter compared to a decline of 8.4% for the Standard & Poor's 500 Index. Stocks that contributed to the difficult quarter included BP and Tyco Electronics. Our significant underweight position in energy was a plus in the quarter, but BP still hurt. Fears about the economy and the automotive markets appeared to negatively affect Tyco Electronics. We remain committed to these ideas. Kimberly Clark and Berkshire Hathaway were up nicely in the quarter, reflecting a flight to defensive stocks (Kimberly) and solid balance sheets (Berkshire). The past several quarters have been very volatile and difficult for stocks as investors grapple with a number of uncommon issues. The large cap portfolios, while down, have held their value better than the market in this tumultuous period. Lower prices have also enabled us to take advantage of some good values, two of which we will discuss shortly.

The aftermath of the bursting of the speculative housing bubble turned downright ugly in the September quarter. It's difficult to use the word *chaotic* in an investment letter, but unfortunately, it describes the recent credit and equity markets. The S&P 500, for example, was down 8.8% and up 5.4% on the last two days of the quarter. As recently as three months ago, it appeared that the credit crunch was more a media phrase than an economic reality, and manageable within the normal boundaries of our financial system. A rapid spreading of fear and diminished liquidity resulted in a bona fide credit crisis, which has culminated, so far, in the $613 billion bankruptcy of Lehman (largest ever), the "rescue" of Fannie Mae, Freddie Mac and AIG, the shotgun marriage of Merrill Lynch to Bank of America, and the Fed engineered takeovers of Washington Mutual and Wachovia. Goldman Sachs and Morgan Stanley recently obtained equity infusions and rushed to obtain a commercial bank charter. (Wal-Mart has been trying for five years to get one; Goldman Sachs and Morgan Stanley got theirs in a day!)

As this letter is written (October 1), the $700 billion "bailout" bill remains hung up in Congress, but it looks like something will be passed shortly. As the program was initially crafted, we had serious reservations. Based on what we know now, it looks somewhat more palatable; however, the government could still end up buying a tremendous amount of paper with dubious value, which of course would result in a heavy burden on taxpayers. The optimists believe a large buyer will stabilize asset prices, which eventually could even lead to a profit for the Treasury. We are not holding our collective breaths. Aside from this program, taxpayers are already taking the brunt of the cost of the $30 billion Bear Stearns takeover, the $85 billion AIG seizure and the $200 billion Fannie Mae and Freddie Mac nationalizations.

Dozens of articles will be written in coming weeks about the financial crisis, the bailouts and who is to blame. The media has already framed this as a failure of the free market system, with the solution, of course, being more regulation. Several new programs and agencies have already been created and more will undoubtedly follow. These programs come with bureaucracy, expense, and the usual government inefficiency and we can't help but fear that the cure may be worse than the disease. While rapid developments in high finance over the past decade have certainly exposed some holes in the regulatory system, the root of this problem appears to be a breakdown of existing oversight and gross negligence on the part of Congress with respect to the government sponsored enterprises (Fannie Mae and Freddie Mac).

Allowing Fannie and Freddie to essentially underwrite, subsidize and invest in mortgages with the implied backing of the Federal government created the mother-of-all moral hazards. These organizations became obsolete years ago, as a large, well-financed and competitive private mortgage industry had developed. Rather than dismantle these institutions, Congress watched them expand, all the while feeding off their political largess. Under the banner of providing "affordable housing" their charters effectively expanded and the risks escalated dramatically. Efforts to rein them in were stymied. Wall Street then did what it does best – exploited an opportunity. With Fannie's and Freddie's imprimatur, the great Wall Street debt machine took flight. Aided by a feckless Fed (1% Fed Funds rate) and greed that resulted in a mad dash for yield and fees, underwriting became an afterthought. Huge leverage and impossible complexity compounded the issue and resulted in an enormous problem that now requires various government bailouts.

While some may accuse us of oversimplifying the issues, much of the crisis flows from the mortgage moral hazard described above. Adjunct developments, such as managing counter party risk in the $60 trillion credit derivative swaps market, ensuring liquidity in money market funds, and bolstering FDIC funding are all serious issues with no easy solutions. We've addressed a couple of these problems in previous letters and more will certainly be said in coming pieces. Our historical letters can be found at www.fiduciarymgt.com.

Regardless of what role the government takes during this crisis, it will likely take years to sort out. A significant deleveraging is under way and this won't be good for growth, although it may be needed to restore balance sheets and get the economy poised for the next up cycle. The Bernanke Fed is adamant about avoiding deflation, which often accompanies deleveraging. The Fed Chairman is acutely aware of the Japanese experience over the past seventeen years and doesn't want it repeated here. Going overboard to avoid deflation, however, could result in the opposite: a dollar crisis and inflation (most likely stagflation), which would be tough on valuations.

Financial crises, while not common, have occurred many times in our history. We've survived all of them and there is little doubt we will get through this one, too. We remain optimistic about the long-term prospects of equity investing. Poor returns usually follow periods of outsized gains and the opposite is also true. Most of the indices have had a difficult run for the better part of a decade. We think the next decade will be better.

As is our custom, we have highlighted a couple of our large cap investments below.

Sysco Corporation (SYY)

Business Description

Sysco is the largest provider of foodservice products in the U.S. and Canada, distributing more than 300,000 products to 400,000 restaurants, schools, hotels, healthcare institutions, and other foodservice customers. Restaurants account for two-thirds of Sysco's annual sales, with independents contributing 60% of restaurant sales and chains making up the rest.

Good Business

- Sysco holds a dominant position in its industry and is the largest foodservice distributor in the U.S. with approximately 15% market share. The company benefits handsomely from significant economies of scale, which allows it to earn an operating margin roughly three times that of its closest competitor.
- Sysco provides products that are necessities for daily life, and operates a business that is easy to understand.
- Sysco has a long history of extremely consistent revenues and earnings.
- The company generates strong returns on invested capital (ROIC), with a 5- and 10-year average ROIC of 22.4% and 21.0%, respectively.
- Sysco is conservatively financed and its debt is AA-rated by Standard & Poor's.

Valuation

- Sysco's current enterprise value-to-sales multiple is 0.54x, which is approximately 30% below its 10-year average multiple of 0.76x.
- Sysco's enterprise value is 8.7x estimated fiscal year 2009 earnings before interest, taxes, depreciation and amortization (EBITDA). This compares to its 10-year average multiple of 13.1x EBITDA.
- Between 2000 and 2007, transactions announced for 12 comparable companies were executed at mean and median enterprise value-to-EBITDA multiples of 10.1x and 11.0x, respectively.

Management

- Sysco's top ten executive managers have been with the company for an average of 21 years. Insiders own about 1.0% of diluted shares outstanding.
- Executive management is compensated based on three key operating metrics: earnings per share growth, return on equity (ROE), and operating company performance.
- Rick Schnieders, CEO, has been with the company since 1982, serving in several different roles before becoming CEO in 2003.

Investment Thesis

A multitude of factors has provided the opportunity to buy a strong, high ROIC franchise at an attractive valuation. Sysco is battling poor demand in the restaurant industry, food and fuel cost inflation and a slow progression of its supply chain initiatives. These factors are masking the true value of the company. Sysco continues to dominate the foodservice distribution industry and is led by an experienced management team. The valuation is near a record low.

American Express, Inc. (AXP)

Company Description

American Express ("AXP") is the largest closed loop network credit card company with over $700 billion of "billed" charge card spending and $76.5 billion of total managed credit card loans. With over 90 million cards in force worldwide, AXP generates about half its revenue from merchant fees. It is a global company with a powerful brand.

Good Business

- AXP's network is highly durable and generates significant recurring fee revenues.
- The company's super prime customer base consistently generates spending volumes per card four to five times greater than the industry average with below-average loss rates.
- AXP generates an ROE in excess of 30%. Over two-thirds of capital generated is returned to shareholders.
- AXP's balance sheet is conservatively levered. The investment portfolio is clean.

Valuation

- Over the past ten years, AXP's price-to-earnings (P/E) multiple has averaged 20x, ranging from its current low of 12 to a high of 30x. The company's median multiple is 19x.
- Over the next three to five years, AXP's normalized earnings per share (EPS) could range between $4.90 and $5.40. Even capitalized at a below-average 15x, the upside is substantial.

Management

- AXP's management team is highly regarded within the industry.
- Kenneth Chenault has been Chairman and CEO since April 2001. Previously, Chenault was President of TRS (now US Card Services) since August 1989.
- Daniel Henry has been the company's CFO since October 2007.
- Al Kelly has served as President of the Global Consumer Group since July 2007. Messrs. Henry and Kelly both have numerous years of experience at the company prior to their current roles.

Investment Thesis

American Express has a durable business model, largely driven by merchant fees and net interest income. AXP's business is characterized by high barriers to entry, low capital intensity, modest leverage, and high returns on incremental capital. The current consumer slowdown, however, will lead to higher charge-offs, but AXP should weather the cycle better than its competitors. Moreover, with a strong capital base, AXP has sufficient resources to manage both credit and liquidity issues. Trading at a discount to the market and its historical average, AXP is an attractive investment opportunity over the next three to five years.

Thank you for your support of Fiduciary Management, Inc.

Fiduciary Management Inc.
Large Cap Equity Composite
12/31/2000 - 09/30/2011

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
2001	20.47	19.70	-11.89	1	0.00	$ 3.6	$ 1,458.2	0.25%
2002	-13.33	-14.11	-22.10	8	0.17	$ 14.0	$ 1,731.0	0.81%
2003	34.29	33.15	28.68	4	0.86	$ 20.8	$ 2,927.0	0.71%
2004	19.32	18.46	10.88	10	0.46	$ 48.9	$ 3,085.8	1.58%
2005	10.22	9.57	4.91	28	0.29	$ 192.2	$ 3,174.4	6.05%
2006	17.91	17.15	15.79	49	0.30	$ 491.0	$ 3,589.4	13.68%
2007	5.05	4.34	5.49	86	0.48	$ 1,000.2	$ 3,960.4	25.26%
2008	-26.38	-26.91	-37.00	130	0.63	$ 1,969.3	$ 4,062.5	48.48%
2009	30.92	30.09	26.46	252	1.22	$ 3,820.3	$ 7,008.9	54.51%
2010	12.52	11.81	15.06	394	0.31	$ 5,923.2	$ 9,816.0	60.34%
Q1 2011	5.01	4.85	5.92	436	0.12	$ 6,717.9	$ 11,338.0	59.25%
Q2 2011	2.07	1.91	0.10	459	0.11	$ 7,701.2	$ 11,819.6	65.16%
Q3 2011	-13.91	-14.04	-13.87	485	0.18	$ 6,989.5	$ 10,357.9	67.48%

*Benchmark: S&P 500 Index®

Effective January 2012, 2004 – 2011 gross and net composite returns were restated due to an error.
Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Inc. (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 09/30/2011. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Large Cap Equity composite has been examined for the periods 12/31/2000 - 09/30/2011. The verification and performance examination reports are available upon request.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $10.3 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The FMI Large Cap Equity Composite was created in December 2000. These accounts primarily invest in medium to large capitalization US equities.

The FMI Large Cap Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts. From December 31, 2000 thru September 30, 2002 all accounts included were managed for at least one quarter, from October 1, 2002 to present all accounts were managed for at least one month. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes.
Dispersion is calculated using the standard deviation of all accounts in the composite for the entire period.

Currently, the advisory fee structure for the FMI Large Cap Equity Composite portfolios is as follows:

Up to $25,000,000	0.65%
$25,000,001-$50,000,000	0.55%
$50,000,001-$100,000,000	0.45%
$100,000,001 and above	0.40%

The firm generally requires a minimum of $3 million in assets to establish a discretionary account. High Net Worth individuals may establish an account with a minimum of $1,000,000, however, the firm reserves the right to charge a minimum dollar fee for High Net Worth individuals depending on the client servicing involved. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request.
Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The S&P 500 Index® is widely regarded as the best single gauge of the U.S. equities market. This index includes 500 leading companies in leading industries of the U.S. economy. Although the S&P 500® focuses on the large cap segment of the market, with approximately 75% coverage of U.S. equities, it is also an ideal proxy for the total market.
The Large Cap Equity composite uses the S&P 500 Index® as its primary index comparison.