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INVESTMENT STRATEGY OUTLOOK – SMALL CAP EQUITY

Quarter Ended September 30, 2007

October 1, 2007

The September quarter was difficult for our small cap portfolios as they declined approximately 6%, compared to the 3.1% decline in the benchmark Russell 2000 Index and the 6.3% decline in the Russell 2000 Value Index. Calendar year-to-date, the small cap portfolios were up approximately 5% and the Russell 2000 Index was up 3.16%.

A number of factors impacted the third quarter. In response to turbulent credit conditions and perhaps a weakening economy, the Federal Reserve Board first lowered the discount rate by 50 basis points in August, then another 50 in September, when they also dropped the federal funds rate by 50 basis points. The thought of 1998 and the Long Term Capital Management crisis likely weighed heavily on their decision. The Fed's action was a booster shot for growth stocks nine years ago and it has been recently, too. Most of the growth stock indices were strong in September, continuing a move away from value stocks this year. While this relative movement was a factor in our third quarter results, we also simply had more than our share of poorly performing stocks.

We are confident that the underperforming companies in the portfolio will improve, but there is no way to gauge how long the market will favor growth. It is *déjà vu* to see investors bidding up the stocks of companies that are "hitting their numbers" even though the multiples in many cases are already very high. It is reminiscent of the 1995-1999 period, and it remains to be seen whether there will be significant fund flows from value pools to growth pools. After the mortgage debacle and credit scare in July and August, it is amazing, and somewhat frustrating, to observe that the market seems little concerned about these warning shots across the bow. Perhaps faith in Bernanke (rates) and the government (borrower bailouts) is enough to justify this attitude. Even the derivative difficulties seemed to have passed without a lot of damage. So far.

We still believe in Economics 101. Excesses and imbalances tend to swing the other way over time. We are beginning to see the pendulum swing back in the housing and mortgage markets. Credit quality may also be on the verge of meaningfully deteriorating. The dollar has been extremely weak. Last quarter's letter articulates our position on some of these issues in more detail, but suffice it to say, we remain somewhat cautious about a few of the macro issues, as well as the overall stock market. Valuations also do not appear to incorporate much bad news. The companies in our portfolio, on the other hand, are sound, well-financed all-terrain vehicles that we feel will perform nicely, at least on a relative basis, over a long-term time frame. They are not Ferraris, however, so if we are entering a growth and momentum environment, the portfolio is likely to underperform.

Before delving into a couple of relatively new holdings, a sentence or two about some of the difficult stocks in the quarter is appropriate. MPS Group and Korn Ferry are both fundamentally sound companies with great balance sheets, but the stocks have come under more severe pressure than we anticipated, related to fears of a weakening economy and a tougher labor market. Although we recognize the macro environment could continue to hurt these companies in the short run, the stocks have declined to very attractive levels and we have been adding to our positions.

Similar macro fears have impacted a number of other holdings, including Acuity Brands, HNI Corporation, Family Dollar, Harte-Hanks and the transportation group. While we may make a modest change in our transportation lineup, we feel good about the financial strength and long-term success of each of these companies. Our contrarian instincts proved deficient, at least in the short run, with our recent purchases of Beacon Roofing Supply and Watsco. Both sell "aftermarket" home supplies -- roofing materials and HVAC (heating, ventilation and air conditioning) equipment. While there is a certain inevitability to the demand for their products, our belief that most of the bad news was already in the stocks proved wrong. Today's valuation for both of these companies is compelling. Additionally, we may have misjudged either the quality of the management or the true nature of some of the project work at Navigant Consulting. That stock is under review.

It is never pleasant to air dirty laundry. While this was a tough quarter, it is certainly possible, and even probable, that we will have additional poor quarters from time to time -- and even tough years. We do hope our clients are mindful of our superior long-term record and the fact that we employ a disciplined approach to investing that has not changed in 27 years. We feel the companies in our portfolio today are attractive. In fact, there are only three of the 42 stocks with a higher P/E (price-to-earnings) ratio than the Russell 2000, based on 2008 estimates. Other valuation measures show a similar relative attractiveness.

Our custom is to address macroeconomic and other broader topical issues following the December and June quarters, and discuss individual companies in more detail following the March and September quarters.

Ethan Allen Interiors

Description

Ethan Allen Interiors (ETH) is a vertically integrated designer, manufacturer and marketer of branded furniture and home accent products through one of the largest networks of home furnishing retail stores. The company's main product lines are case goods (44%), upholstered products (38%) and higher-margined home accessories (18%). Wholesale manufacturing (48% of revenues, 15% margins) produces 60% of the company's product through nine manufacturing plants based in the United States, with the remainder of goods being imported. Retail stores account for the remaining 52% of revenues and generate 2.2% margins, due in large measure to the company's store reinvestments.

Good Business

- Ethan Allen has established a durable business model with an increasingly diverse product set sold at "everyday best prices" by trained professional interior designers.
- Approximately 80% of the company's merchandise has been introduced or refined within the last 3 years. The average order approximates $1,200 to $1,800 with available non-recourse financing.

- Over the past 6 years the company's ROIC (return on invested capital) has averaged 16%.
- The company retains an A- rated balance sheet with a leverage ratio of 1.3.
- Ethan Allen controls its own destiny with a single brand and a proprietary retail distribution channel.

Valuation

- Ethan Allen's forward P/E (price-to-earnings) ratio of 12 compares favorably to the company's 10-year average of 15 (range 10-19), and that of its competitors, at 18.
- Over the past 5 years the company's EV/sales (enterprise value-to-sales) multiple has averaged 1.3, ranging from 1.1 to 1.7. The shares currently trade at more than one standard deviation below the company's 5-year average.
- Over the past 10 years, Ethan Allen has traded for an average of 8.2 times trailing 12-months' EBIDTA (earnings before interest, taxes, depreciation and amortization), ranging from a low of 6 times to high of 14 times. The shares presently trade at 7.4 times.

Management

- Farooq Kathwari has been President and Chief Executive Officer since 1988, although his affiliation with Ethan Allen dates back to the early 1970s. Mr. Kathwari has made good strategic decisions that have distanced the company from the pack. He owns nearly 9% of the company outright -- and with options, approximately 14.7%.
- Jeffery Hoyt serves as the company's Chief Financial Officer, having formerly worked for KPMG.
- Craig Stout is Vice President of Case Goods Merchandising, and has been with Ethan Allen since 1972.
- Ed Teplitz has served as Vice President of the Retail division since May of 2003. Teplitz joined the company in 2001 as VP of Finance, later becoming CFO. Prior to joining the corporate division, Ed was an Ethan Allen licensee in Pittsburgh, Pennsylvania and Cleveland, Ohio.

Investment Thesis

Ethan Allen has carved out a defendable niche in the upper middle-to-lower high-end segment of the furniture industry, where a stylistically diverse, high quality product is delivered through a knowledgeable and trained professional sales force. The company appears to be effectively addressing their manufacturing footprint, incorporating appropriate low cost production with timely delivery of standard and tailored solutions. Retail store efficiency continues to lag. The stock is very depressed, reflecting housing and economic worries. As these issues subside over the next few years and the company's retail stores improve, the stock should be rewarding.

AMN Healthcare Services

Description

AMN Healthcare Services (AHS) is the leading provider of traveling nurse, physician and allied (nonprofessional medical) staffing services in the United States. The company recruits healthcare professionals, and supplies hospitals, other healthcare facilities and physician practice groups with trained workers. The traveling nurse industry is roughly $2.5 billion, with

AMN Healthcare controlling close to 40%. The *locum tenens* (physician staffing) market is about $1.6 billion and AMN Healthcare has the largest share at roughly 17%. Customers use staffing services to cost-effectively manage short- and long-term shortages. Healthcare professionals are attracted to the "travel temp" lifestyle by its flexibility and skill-enhancing opportunities.

Good Business

- AMN Healthcare has leading brands in multiple markets and geographies.
- The company enjoys economies of scale.
- Revenue can be viewed as generally recurring, as assignments are usually multiple weeks, and visibility to the next assignment is typically very good.
- The company earns its cost of capital, and ROIC should expand over the next few years.
- While the company cannot really influence prevailing wage rates, they can manage the spread between bill and pay rates, thus they have reasonably good control of their destiny.
- The business is easy to understand.
- The balance sheet is appropriately levered (37% debt-to-capital; EBIT/Interest expense of 4.7).

Valuation

- The P/E ratio of 18 is on the low end of the range since the company went public in 2001. The 5-year range is 17-28.
- The 2007 estimated EV/EBITDA ratio of 9.5 compares to the 5-year average of 13.
- The price-to-sales ratio is .56 in a 5-year range of 0.55-1.34.
- AMN Healthcare is attractively priced relative to other health care and business services stocks and the market.
- The stock is 40-50% undervalued, based on our discounted cash flow analysis.

Management

- Susan Nowakowski, 42, has been Chief Executive Officer since 2005. She joined the company in 1990 and previously served as Chief Operating Officer and Executive VP of Business Development, and CFO.
- David Dreyer, 51, has been Chief Financial Officer since 2004. He was previously with Sicor, a manufacturer of pharmaceuticals that was acquired by Teva, and began his career with Arthur Anderson.

Investment Thesis

The demand for nursing and physician services is likely to remain strong over the next decade. Strong demographic trends and the desire for a flexible work environment bode well for the future. The AMN Healthcare business model provides real benefits to both recruited professionals and end customers. Scale and brand awareness should work in the company's favor. The stock had over-ambitious expectations when it went public in 2001, but today, trades at an attractive level for long-term investors.

Thank you for your confidence in Fiduciary Management, Inc.

Fiduciary Management Inc.
Small 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	20.42	19.57	2.49	125	1.88	$ 587.2	$ 1,458.2	40.27%
2002	-4.78	-5.46	-20.48	154	1.47	$ 649.7	$ 1,731.0	37.53%
2003	27.18	26.22	47.25	167	1.93	$ 1,206.9	$ 2,927.0	41.23%
2004	20.92	20.02	18.33	181	1.00	$ 1,486.6	$ 3,085.8	48.18%
2005	11.12	10.26	4.55	186	0.69	$ 1,605.8	$ 3,174.4	50.59%
2006	18.46	17.56	18.37	147	0.73	$ 1,606.8	$ 3,589.4	44.77%
2007	-0.92	-1.72	-1.57	161	0.85	$ 1,520.2	$ 3,960.4	38.39%
2008	-21.06	-21.69	-33.79	145	1.16	$ 1,212.4	$ 4,062.5	29.84%
2009	35.72	34.56	27.17	165	0.97	$ 2,004.6	$ 7,008.9	28.60%
2010	23.45	22.43	26.85	170	0.48	$ 2,477.7	$ 9,816.0	25.24%
Q1 2011	7.18	6.96	7.94	182	0.19	$ 2,699.2	$ 11,338.0	23.81%
Q2 2011	1.16	0.96	-1.61	179	0.11	$ 2,718.9	$ 11,819.6	23.00%
Q3 2011	-16.12	-16.29	-21.87	178	0.31	$ 2,188.9	$ 10,357.9	21.13%

*Benchmark: Russell 2000 Index®

Effective January 2012, 2004 – 2011 gross and net composite returns and dispersion 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 Small Cap Equity composite has been examined for the periods 12/31/1993 - 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 Small Cap Equity Composite was created in January 1980. These accounts primarily invest in small to medium capitalization US equities.

The FMI Small Cap Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts, with a market value greater than $500,000 as of month end. A small percentage of composite assets (typically ranging from 0-5%) historically has been invested in unmanaged fixed income securities at the direction of account holders. From December 31, 1993 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 Small Cap Equity Composite portfolios is as follows:

Up to $25,000,000	0.90%
$25,000,001-$50,000,000	0.85%
$50,000,001-$100,000,000	0.75%
$100,000,001 and above	0.65%

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 Russell 2000 Index® measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000® Index representing approximately 8% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. The Small Cap Equity composite uses the Russell 2000 Index® as its primary index comparison.