Knightsbridge Asset Management
division of Canterbury Capital Services, Inc.

July 29, 1997

SECOND QUARTER COMMENTARY

"Plainly, nobody will be afraid who believes nothing can happen to him...fear is felt by those who believe something is likely to happen to them...people do not believe this when they are, or think they are, in the midst of great prosperity, and are in consequence insolent, contemptuous and reckless."

Aristotle, 384-322 B.C.
Greek Philosopher
Rhetoric, 1382 b29

"What, me worry?"

Alfred E. Neuman
American Cultural Icon
Mad Magazine

Contemptuous of caution, neophyte investors have been emboldened by recent successes in a seemingly one-way market environment. The degree of recklessness can be gauged by the simple fact that margin debt as a percentage of GDP (gross domestic product) is at all-time highs, having roughly doubled in the past four years. "Margin" represents money borrowed to purchase securities. Since GDP is a growing number itself, margin debt might similarly grow and the ratio would remain unchanged......that the ratio itself has doubled is astounding. Only in this environment, where the mantra of Alfred E. Neuman has been given the new-found respect Rodney Dangerfield sought perennially, could such an occurrence go largely ignored.

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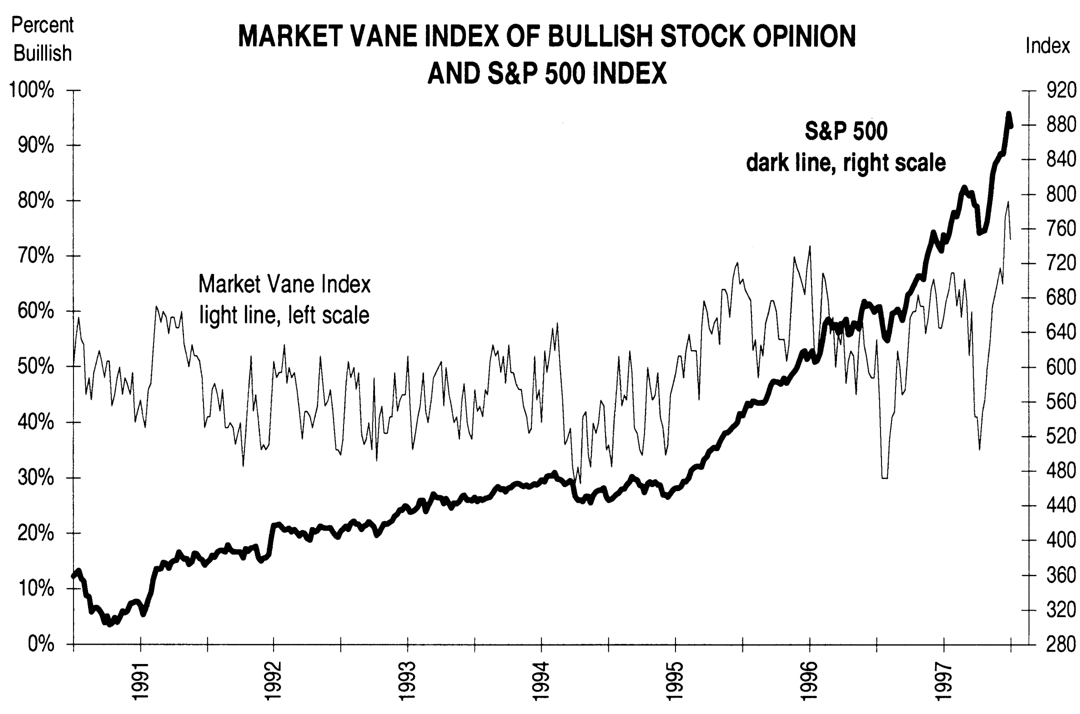
Just when it looked like the market was tracing out a much needed correction, a sudden reversal sent the DJIA (Dow Jones Industrial Average) up 20% in 2 months......and to new highs. Having been investing other peoples' money for a quarter-century, I did a quick memory scan attempting to recall the last time such had happened. No luck there. But, in fact, it turns out this was the third time since 1920 that this has happened. It is also the first time since November 1928 that a 20% move in two months produced a new high (and we all know what happened in October 1929!). Moreover, as powerful as the Japanese bull market was ending in 1989 at 39,000 on the NIKKEI, its 15 year gain was not as large as this current one in the U.S. We might add that the Japanese market is currently about 20,000 on the NIKKEI, down from 39,000 eight years ago. In just the last two years the wealth created by our market is approaching 50 % of GDP in size and is larger than the wealth creation at the 1929 stock market peak (the 1929 market top was not exceeded again until 1954). In fact, the S&P 500 average has now produced a 17% average annual return for the past 15 years, an unsurpassed statistic going back as far as data exist on this, 180 years.

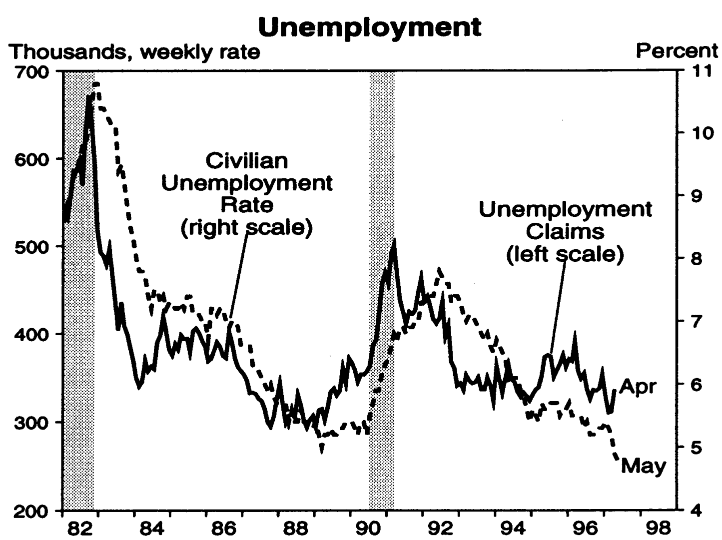
That bullishness has gone berserk is demonstrated by the Market Vane Index of Bullish Stock Opinion as of June 30th. It registered 79% bulls and 21% bears. As one may observe from the chart below, there has never been more than 71% bulls at any time in the past eight years, and possibly quite a bit longer than that.



Source: Market Vane Corp.

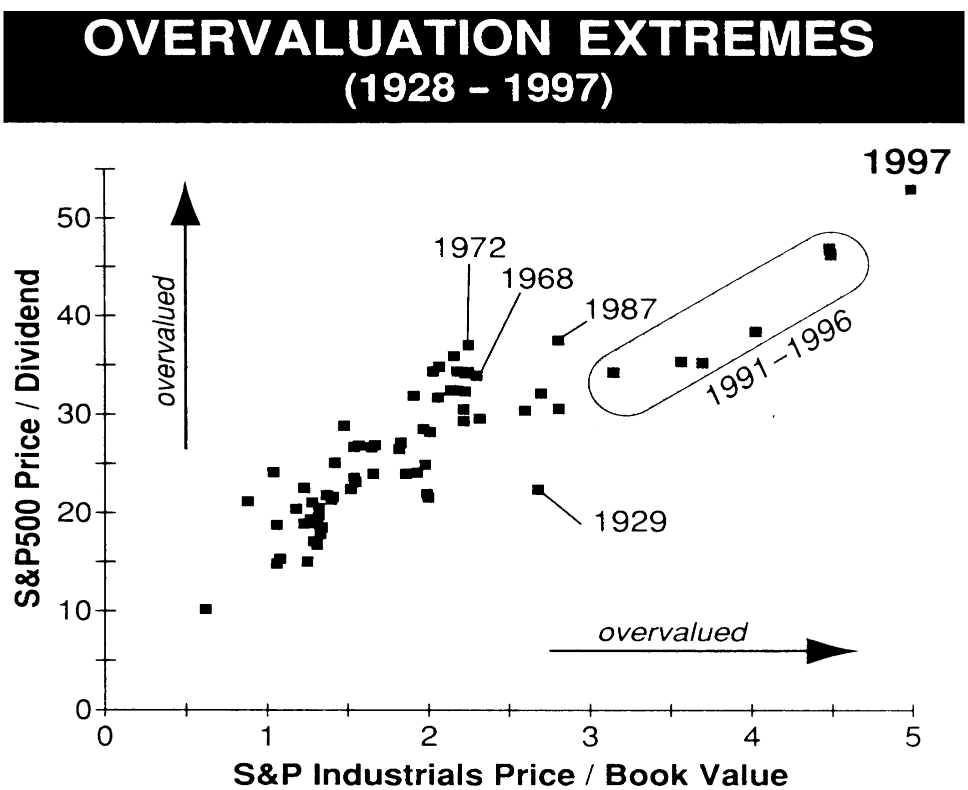
We have always adhered to the principle that maintaining a contrary opinion posture is the best way to simultaneously enhance investment return potential while minimizing risk. Measuring the extremes of sentiment is an important component of such an approach. There is only one portfolio manager alive today who was managing money in 1929. That is Phil Carret, now 100 years old. Phil Carret is bearish. We are bearish. Other money managers are bearish too but fearful of reducing equity exposure for fear of losing their professional money management jobs, just like Jeff Vinik, ex-manager of Fidelity's Magellan Fund. Forces conspire to keep one fully invested......this way one is always right in a bull market and has plenty of company when the time comes to lick the wounds inflicted by the bear. A contrarian by necessity is an iconoclast who leans against the prevailing winds and acts against the grain of popular opinion. However, contrary opinions are only of value at extremes of sentiment. We appear to be at such a juncture at the present.

The ebullience of the current market environment has been against a backdrop of unusually favorable economic statistics. For example, the unemployment report for May of this year showed a jobless rate of 4.8%, a 24-year low.



Since unemployment has dropped from 7.8% in 1992 to 4.8% in 1997, one might logically conclude that whatever rate of economic growth occurred to produce that drop is ultimately unsustainable. Since 4.8% unemployment cannot go lower than 0.5% (0.5% are in prison) any economic growth that is labor force growth dependent beyond population growth is ultimately cut off. In the next seven years if unemployment kept dropping at the rate it has dropped the past five years, 0.6% per year, unemployment would become zero. Therefore we are certain that the rate of economic growth of the past 5 years is totally unsustainable for the next five years. First quarter GDP growth was a gigantic 5.9%. A non-inflationary rate is thought to be 2-2 ½ %. Current signs of economic sluggishness notwithstanding, it is to be expected that the Federal Reserve will be acting again to reign in economic growth with higher interest rates. And higher interest rates mean a rough environment for stocks, as earnings growth must fight declining price/earnings ratios in the battle for stock valuation. Even without Fed action, recent rates of GDP growth are unsustainable, simply because there is ultimately an inadequate labor pool to accommodate its continuation. Moreover, if current GDP growth is unsustainable, then so is current corporate earnings growth. The problem here is that recent corporate earnings growth rates are being inappropriately extrapolated into the future to justify high price/earnings ratios. This results in a potentially dangerous combination of high P/E ratios on peak earnings.

How extreme is the current overvaluation? The following chart shows prior market extremes compared to 1997.



InvesTech Research (Data: Ned Davis Research)

Yes, this is a scary chart. Almost as scary as the following Lou Harris Poll results from last year. Although this is a repeat of data from a prior quarterly letter, it bears repeating.

Fund Investors – Expectations
Lou Harris Poll - 1996

85%	expect same or better performance of the equity market as in the last 10 years
78%	expect no setback of -20% or more
41%	expect no single year of -10% in the next few years

(But consider this: Since 1900 there was on average every 2.5 years a decline of the Dow Jones of a minimum -20% from one years high to next years low.)

Evidence again that the wisdom of Aristotle is long forgotten but that the slogan of pop-icon Alfred E. Neuman is alive and well......"What, me worry?"

We have sold half of our position in Earthgrains in the low 60's having bought it a year ago in the low 30's. We thought this spin-off from Anheuser-Busch was under-valued as to assets, cash flow and potential earnings. Earthgrains also stood to benefit from the merger of the #1 and #3 companies in their industry (they were #2) as well as a drop in wheat prices. Wheat prices have dropped... wheat futures, once over $6.00 per bushel have dropped to the $3.50 per bushel area recently. With the good news now out, we've taken some chips off the table.

For those accounts that owned IBM from the spring of 1993, we have sold half of that position at 91 (182 pre-split). It's been a great ride from 44 to 182. Additionally, we sold Morgan Stanley Emerging Markets Debt Fund at 14-14 ¼ . We purchased that at 11 ¼ in the fall of 1995 and it yielded 14% as we held it, and then on top of that paid a $3.24 extra dividend in early January. Now the yield is 10% instead of 14% yet T-bill yields are still in the 5.0% range as they were in 1995. What changed was the market's view of sovereign credit risk. In 1995, it was thought that emerging market sovereign yields should be priced 900 basis points (9%) above comparable U.S. Treasury paper......now the thinking has shifted in the belief that 500 basis points (5%) is adequately compensatory for these risks. Maybe so, but we'll let somebody else play that game. We are now in an aggregate cash position of 43% across the board. Newer accounts are in higher cash positions. This is the highest cash equivalent position we have had since mid-1987. We have further battened down the hatches in expectation of inclement market weather. We thank you for your trust, patience, understanding and wisdom.

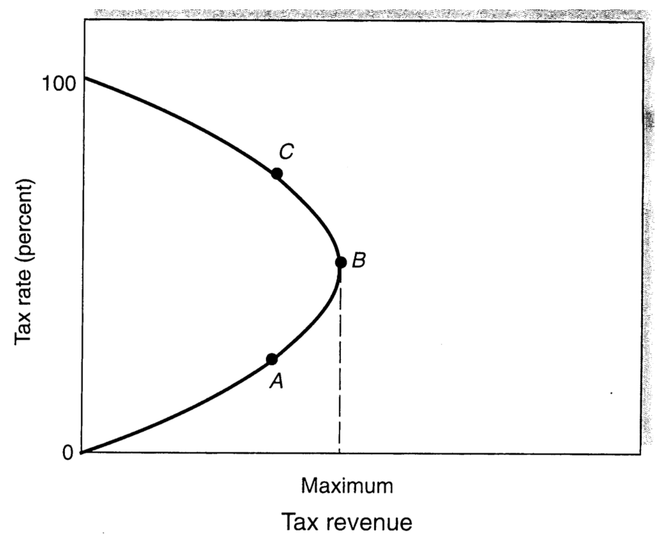
Very Truly Yours,

Alan T. Beimfohr

Arthur B. Laffer

The Laffer Curve

Since taxation affects the amount of the activity being taxed, a change in tax rates will not lead to a proportional change in tax revenues. As the Laffer curve indicates, beyond some point (*B*), an increase in tax rates may actually cause tax revenues to fall. Since large tax rate increases will lead to only a small expansion in tax revenue as *B* is approached, there is no presumption that point *B* is an ideal rate of taxation.



Economist Arthur Laffer has popularized the idea that higher tax rates can sometimes shrink the tax base so much that tax revenues will decline despite the higher tax rates. As the result of Laffer's efforts, the curve illustrating the relationship between tax rates and tax revenues is now called the **Laffer curve.**

July 21, 1997

Alan T. Beimfohr
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Dear Alan,

You and Robinson have really developed an impressive group of people. I was especially please that I could even get a few laughs at some of my tired old jokes. I'm enclosing a couple of papers that I hope are enjoyable to you. I also would love a chance at a rematch and maybe even an extended series of future get togethers. Working with you and your group would for me be the best of all worlds.

Warmest Personal Regards,

Arthur B. Laffer

ABL/st