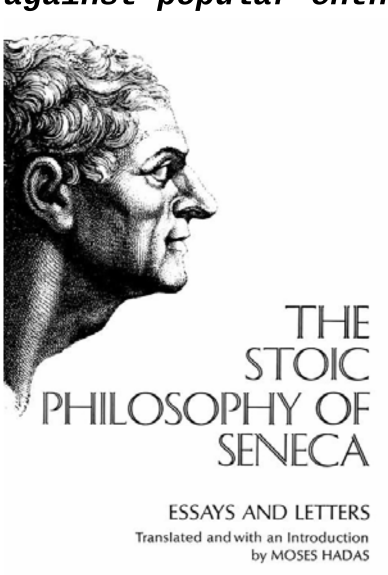
Knightsbridge Asset Management, LLC

November 1, 2005

Third Quarter Commentary

"We are not allowed, I maintain, to travel a straight road……………our parentage draws us into wrong. No one confines his mistakes to himself as people sprinkle folly among their neighbors, and receive it from them in turn. For this reason, in an individual, you find the vices of nations, because the nation has given them to the individual. Each man, in corrupting others, corrupts himself; he imbibes and then imparts………and the worst in every separate person becomes concentrated in one mass. We should, therefore, have a guardian, as it were, to pluck us continually by the ear and dispel rumors and protest against popular enthusiasms."



-Lucius Annaeus Seneca, 4 BC – 65 AD
-Roman philosopher, dramatist and statesman
-Moral Epistles, Epistle XCIV
-Translation by Richard Gummere
-Loeb Classical Library, Vol. III
-www.stoics.com

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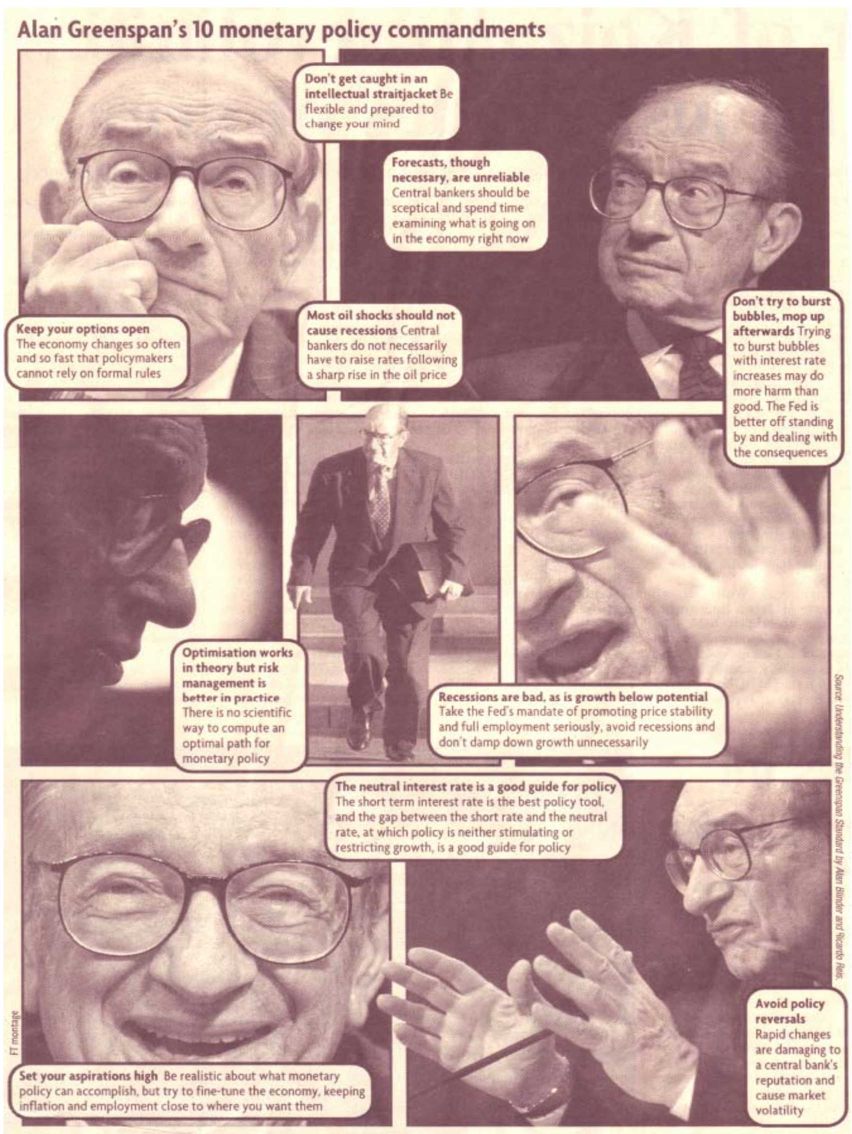
Some things just never change. We would suggest that a substantial part of the Federal Reserve Chairman's job is to "protest against popular enthusiasms", a job ill-suited to politicians or the judiciary. The Fed's form of protest is simple…………the manipulation of short-term interest rates………for the good of the economy………long-term. In other words, to lean against the popular economic winds………to be an economic alter-ego………a sort of Jiminy Cricket-like father-figure, resting on our shoulders, "plucking us by the ear"………encouraging our collective economic behavior to be something other than what it is inclined to be. Either we spend too freely, stimulating unsustainable economic activity and price level, or we are too economically reticent and tentative, causing unhealthy economic contraction.

The appointment of Benjamin Bernanke to succeed Alan Greenspan come January closes a remarkable eighteen year tenure for the venerable Fed Chairman. Suffice it to say that although Mr. Greenspan had his detractors, the overwhelming majority have been both seduced by his intellect and astounded by his abilities to successfully navigate myriad crises such as the market crash in '87, the '94 Mexican peso collapse and O.C. municipal bankruptcy, the '97 and '98 Asian currency meltdowns, the



Russian ruble default, the collapse of Long Term Capital Management, Y2K (we remember predictions of airplanes falling from the sky), 9-11 and the subsequent closing of the NYSE, and sundry other mini-crises of lesser stature. Mr. Greenspan’s philosophy was something like let the free markets do what they will and the Fed will deal with the cleanup. Others have felt that the Fed should have been more activist in attempting to prevent distortions………bubbles, if you will.

By all accounts, Mr. Bernanke is brilliant. Having scored 1590 out of 1600 on the SAT, we are left wondering which question he missed. After graduating summa cum laude from Harvard, he got his PhD in economics from MIT. Apparently the weather in Boston was not much worse than Dillon, South Carolina from whence he came, or maybe he just didn’t notice because he was too busy studying. Nevertheless, we are impressed that he was a notable saxophone player in high school, and are certain his command of the blues genre will come in handy during all those insufferable Humphrey-Hawkins testimonies he must necessarily give on Capitol Hill to all the limelight-seeking politicians clamoring for air-time.

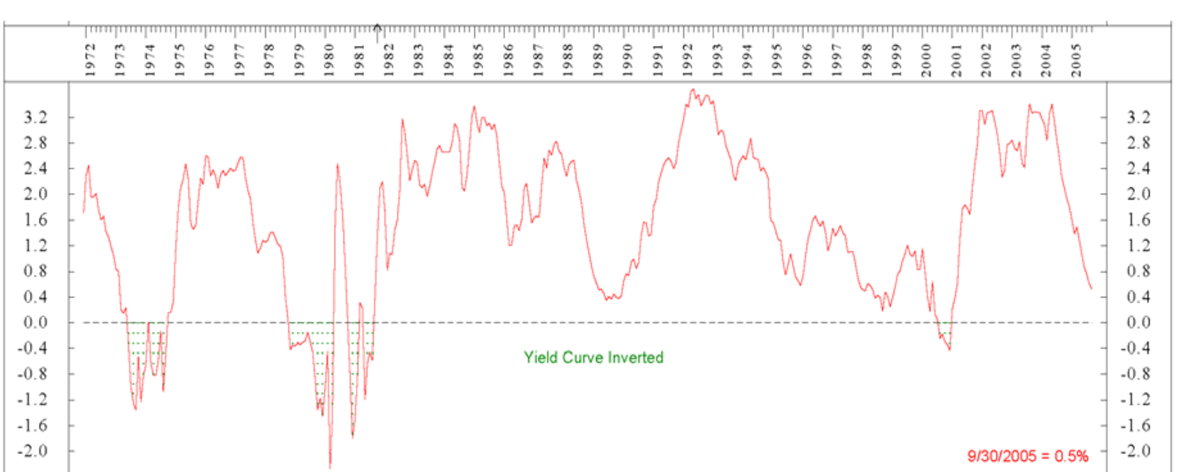
Mr. Bernanke’s background is mostly academic, having been an economics professor at Stanford and most recently Princeton. He is best known for his work in the arcane area of “inflation targeting”, the polar opposite of “inflation fighting”. Inflation targeting is all about how to create some inflation when ‘ya ain’t got none, even if it means doing an airdrop of hundred dollar bills over Newport Center (which we hope would be the case since that’s where we live). This subject was of particular concern to the Japanese, as the Chinese deflationary winds had to blow over Japan before they reached the United States. So by 2002-2003, even the U.S. was starting to worry as interest rates plunged and the PPI (Producer Price Index) started to flash negative numbers. Deflation would sound the death knell for all elected politicians, so needless to say there was much hand-wringing on the Potomac.

For the above mentioned reasons, many observers think Mr. Bernanke will be less of an inflation fighter than Mr.

Greenspan. The bond market confirmed this by tanking upon the announcement of Mr. Bernanke as Mr. Greenspan's replacement. Nor has it recovered since. We do not believe there was a better choice, but the simple fact is that a known commodity is being replaced with an unknown commodity, and there is some level of nervousness associated with this. Financial markets were comfortable with the old Jiminy-Cricket, whose credentials as a "protester against popular enthusiasms" were well established.

Futures markets are predicting the discount rate will go to 4.50% from the current 4.00%. If so, a quarter point increase in December and again early next year would allow Mr. Bernanke to observe what by then would be fourteen consecutive increases in the Federal Reserve discount rate leaving the early portion of his stewardship to addressing the question of how long and how far any decline in rates should be.

All of this raises the question of whether recession can be avoided in the context of an inverted yield curve………or a nearly inverted yield curve………an unusual situation where the shortest-term interest rates are equal to or higher than longer-term interest rates.

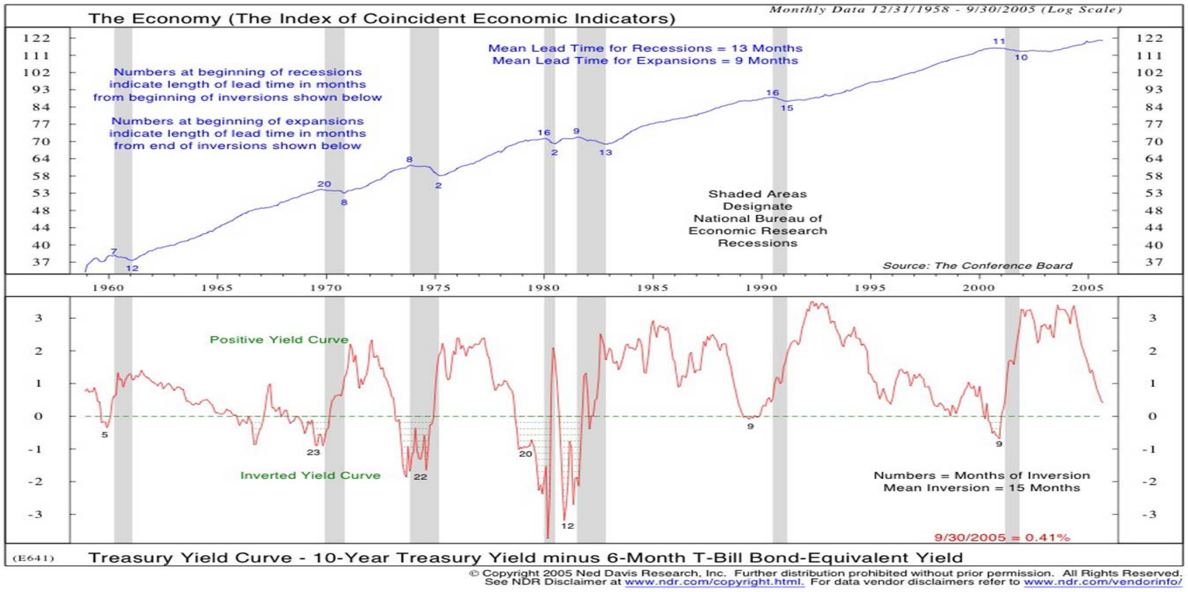


(B542) Yield Curve (10-Year Treasury Note Yield minus Six-Month T-Bill Yield)

We quote Univ. of Calif., San Diego Professor James Hamilton:

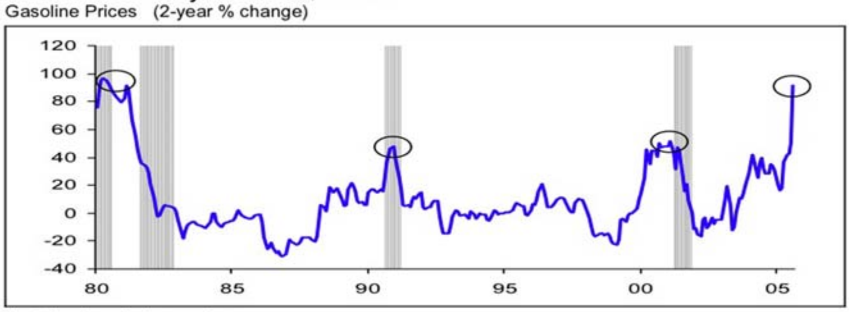
"One of the best-established predictive relations in macroeconomics is the observation that, when the difference in yields between long and short-term interest rates is low or negative, future GDP (gross domestic product) growth tends to be slow or negative." We're pulling for "slow".

We are mindful that the past seven episodes of a flattening or inverting yield curve produced recessions in seven cases of the eight occurrences as seen here.



Also, in four of the previous five episodes, rising oil price momentum has been another negative leading to a cyclical bear market and a subsequent economic recession. The following chart shows that each of the last three recessions was preceded by an outsized rise in gasoline prices.

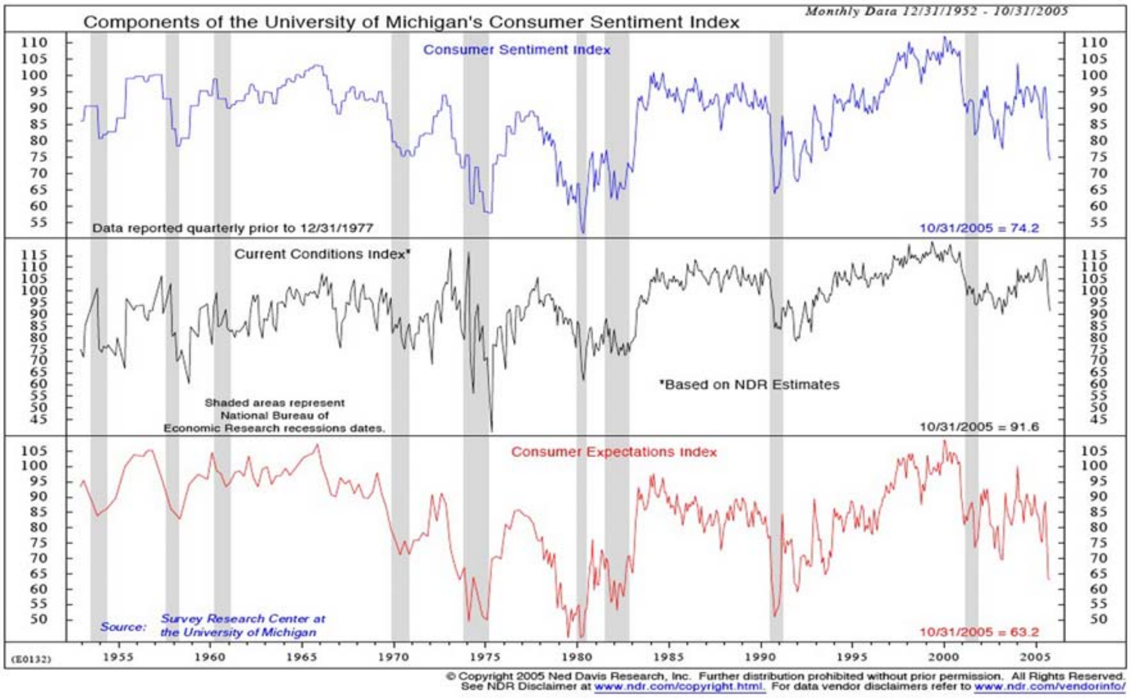
Is A Recession Really Out of the Question?
Gasoline Prices (2-year % change)



Shaded regions signify recessions
Source: Department of Energy, NBER, Merrill Lynch

At the risk of "piling-on", we note that the presidential approval rating of 39% in the latest NBC/Wall Street Journal poll is low by historical standards, lower than any poll in the 16 years of Reagan and Clinton administrations, and reflective of the current consumer malaise. Consumer insecurity, even in the face of surprisingly strong 3.8% real GDP growth last quarter, portends a modest Christmas selling season. Moreover, a Consumer Expectations reading of 63 is low for a not-yet recessionary environment. In fact the past two stock market bottoms (September 1990 and

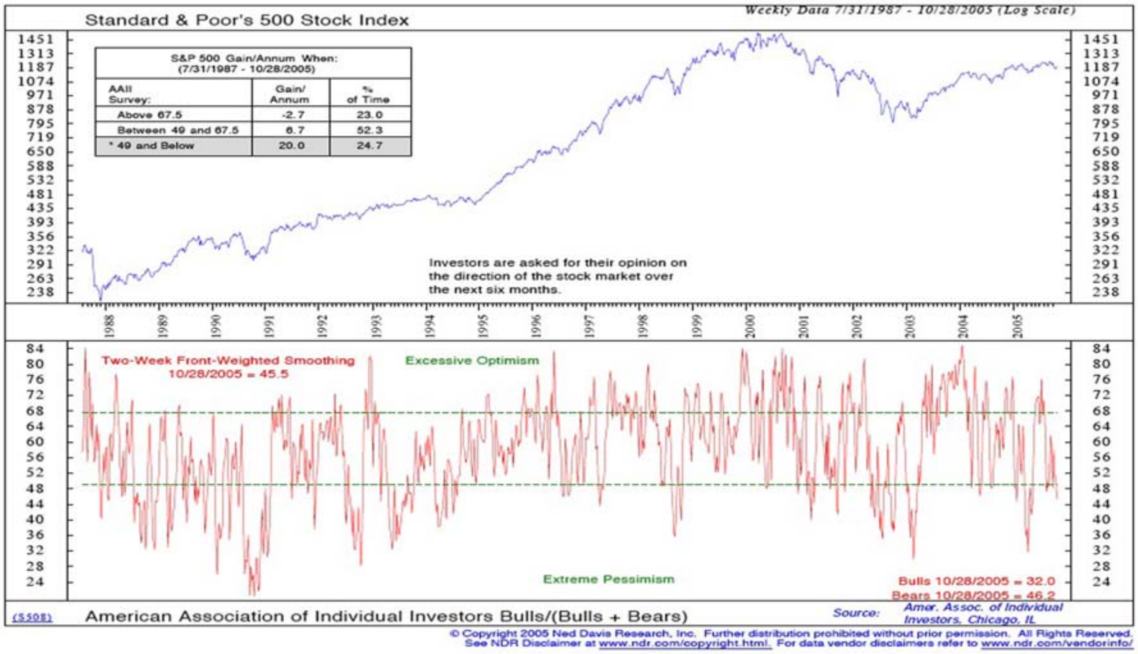
October 2002) were accompanied by *initial* plunges in consumer confidence to the 75 level and below.



Although high gasoline and heating oil prices, vulnerabilities exposed by Katrina and Wilma, a seeming lack of rapid progress in Iraq, and well publicized problems at General Motors, Delphi, and the airline industry may be responsible for the consumer funk, recent data suggests oil related prices are falling somewhat, the weather is improving, Kirk Kerkorian may shake up a moribund GM, and there is even hope for extricating ourselves from the morass in Iraq.

All is not downbeat, even though some of the foregoing would suggest such, and even though reinforced by October stock and bond market action.

In fact, recent measures of market sentiment point more toward the possibility of a stock market bottom being put in place. As seen below, the bullish percentage is only 32% in the American Association of Individual Investors poll, and has reached a level of bearishness that, in the past, has portended 20% per annum gains from the S&P 500.



There is no question that the market is anticipating slower GDP growth and a diminution of earnings growth rates. Whether the recent October declines are sufficient to discount the short-term economic damage from higher interest rates has yet to be proven, with evidence mixed. The U.S. has evolved increasingly to a service economy which lends resilience, and interest rate moves by the Fed have had diminishing effect, which is a doubly-edged sword. On one hand, GDP swings are more muted, making it more difficult to go into a recession. On the other hand, the Fed may have to dole out stronger medicine to accomplish its objectives and remain true to "protest against popular enthusiasms."

Very truly yours,

Alan T. Beimfohr **John G. Prichard,CFA**