
J.L. BAINBRIDGE

& COMPANY, INC.

◆PROFESSIONAL MONEY MANAGEMENT◆

2008 MID-YEAR REPORT

INVESTMENT RESULTS


For the first half of 2008 J. L. Bainbridge & Company, Inc. achieved a -13.6% rate of return on all monies managed in its equity investment program. In conjunction with returns in its equity program for 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006 and 2007 returns of 10.2%, 38.4%, 20.3%, 23.2%, 29.9%, 5.6%, 16.9%, -3.2%, -8.5%, 13.8%, 14.6%, 5.1%, 13.3% and 3.8% respectively, a January 1, 1994 investment of \$250,000 has grown to a June 30, 2008 value of \$1,117,763. This equates to an increase of 347% over the past fourteen and one half years or 11.2% compounded annually. These results assume reinvestment of dividends and are after transaction costs and our management fee.

INVESTMENT REVIEW

Our negative return for the first half of 2008 is the result of a sharp stock market decline that

occurred primarily during the month of June due to the price of oil reaching \$140 a barrel and the fear of recession. While we fully understand how difficult the temporary decline of ones retirement savings is to our clients, the only good advice we can give is to hold stocks of quality companies with strong long-term earnings growth which provide confidence they will not only recover but will appreciate to new highs. In July the majority of the companies carefully selected for investment will report quarterly earnings which we expect will dispel the gloom and concern that the slow economy and high energy prices will cause lower earnings growth for our holdings.

Relative to the price of oil, clearly some industries such as auto, retail, recreation and travel are being severely impacted. In addition the bursting of the housing bubble is creating havoc in financial, home construction and related industries. However we do not own any companies in these industries, and for those companies with some products such as 3M's roofing granules and



United Technology's Carrier residential air conditioners, booming international markets are more than making-up the minor impact on earnings from these domestic product lines. 3M and United Technology generate more than fifty percent of their business from outside America and are growing rapidly in Eastern Europe, South America, Russia and Asia including China and India. The same is true for other companies in our portfolio and we remain confident they will continue to post impressive growth.

INVESTMENT STRATEGY

Investment success is achieved by owning companies with double digit earnings per share increases year after year that will inevitably lead to long-term double digit appreciation in their stock price. On the other hand, poor investment results are caused by owning companies that are not growing. Nothing demonstrates this point better than the fact General Motor's stock hit a fifty-three year low last week. Thus anyone currently holding GM's stock that was purchased anytime since 1958 has a loss.

Since 1981 our investment program has focused on owning companies with a proven record of annual earnings growth coupled with substantial cash flow and little debt. In addition one has to constantly monitor these companies and be on the lookout for changes that jeopardize future prospects. Pharmaceutical companies are an example of an industry with decades of success that have fallen on hard times due to government and insurance company intervention and the failure to develop new products to replace those

losing patent protection. Hence three to four years ago we sold Merck and Pfizer. Earlier this year we reached the conclusion that due to high gas prices, the decline in home values and the fact there are too many new stores being opened, retail prospects have deteriorated, and we sold PetSmart and Target. The proceeds were reinvested into Boeing, Caterpillar, Eaton, Goodrich, Precision Castparts and Regal-Beloit which are all companies that derive a growing and significant amount of business from international markets around the world.

While these companies are increasing earnings at double digit rates, their stocks have declined recently due to recession fears and high oil prices. For example, Boeing and Goodrich declined because domestic airlines announced they were reducing the number of flights and retiring older less fuel efficient aircraft. This led some analysts to conclude Boeing could see orders deferred or cancelled and Goodrich could sell fewer replacement parts. Actually Boeing's \$300 billion backlog is widely dispersed geographically around the globe with less than ten percent from domestic carriers. Goodrich, which supplies parts and systems for aircraft maintenance, has very limited presence on the older planes being taken out of service. However, Goodrich's parts and systems have a large presence on every major aircraft, both commercial and military, currently in production and under development. Considering Boeing and Airbus have orders on hand to produce one thousand planes annually for the next five or more years, Goodrich's prospects are well defined for the decades these planes will be in service and require periodic maintenance. Accordingly we project both of

these companies will grow earnings consistently at least in the low teens compounded annually for many years.

These are just two examples of short-term emotional irrational selling that is not relative to the factual situation. Recession fears are again in the headlines with growing concern that emerging markets may be headed for a slowdown. Relative to the USA we continue to expect a recession will not occur and in the event it does, the recession would be mild and short in duration for the following reasons:

- The globalization of trade is causing an explosion of exports from the USA which will exceed one trillion dollars this year and is growing 15% annually.
- The Federal Reserve's aggressive interest rate cuts and infusion of money into the banking and investment industries.
- The fiscal stimulus package that will put \$150 billion of cash in consumer's pockets.

Relative to emerging markets there may be an economic slowdown, but not in the building of infrastructure, such as airports, railways, roads, mining, energy, water, housing, etc., because these are long-term projects essential to the development of their economies. Importantly, they are being funded by governments with more than adequate financial wherewithal to pay for these projects for decades. The companies we have selected for investment have the high quality innovative products needed for the completion of these projects. Caterpillar's first quarter report illustrates this point in that while USA business

was flat due to weakness in residential housing, earnings increased 18% due to international growth, which comprised 58% of total sales, with sales outside North America increasing 30%.

CONCLUSION

Over the past thirty years numerous market declines have occurred and in each the media pounded the table that the present decline is the worst ever and will cause an economic catastrophe. The common element of these declines is they all ended and the market recovered and moved to new highs. Today's economic problems are relatively minor, when compared to previous periods of economic uncertainty, and confined to the industries listed earlier in this report. For example in the early 1980s there was a deep recession with inflation and interest rates well in excess of 10%. Regarding the outlook for the market over the next several years, today's extreme pessimism and low price to earnings ratio for the companies in general and especially those in our portfolio are the same as prevailed in 1981 when the great bull market of the 1980s and 1990s began. The average PE for our portfolio is 13.4 and 11.8 for projected 2008 and 2009 earnings respectively and the potential return over the next eighteen months is 69%. Consequently, today is the time to be optimistic about future investment returns, and we are very confident the next major bull market is just around the corner.

It should not be assumed that past results will be achieved in the future or that a loss could not be incurred. Furthermore it should not be assumed that future results will exceed market indexes.

ENHANCING CLIENTS' LIVES

At J.L. Bainbridge & Company, Inc. our business is dedicated to “enhancing clients’ lives” by providing long term professional money management service totally focused on helping clients finance their children’s education, build and preserve the resources for an enhanced retirement and achieve a meaningful higher standard of living.

The foundation of J.L. Bainbridge & Company, Inc.’s business philosophy is based on the full understanding that our future and success is completely dependent on client satisfaction and delivering to clients a consistent long term investment service of the highest level of quality, competence and integrity.

Our commitment to “enhancing clients’ lives” is a guiding light that governs our professional daily activities and demands every decision and action be assessed as to exposure to investment risk as well as the long term benefit to clients.

J.L. BAINBRIDGE

& COMPANY, INC.

Managing more than \$350 million for over 900 clients nationwide.
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