

Investment Management of Virginia, LLC

Third Quarter, 2009

Summary: Slow Motion Economic Recovery

Given its strong third quarter performance, the stock market has started to discount an economic recovery. While we believe that an economic recovery will occur, the rebound likely will be sub-par because the economy faces multiple structural, fundamental and policy headwinds. However, that profile is not necessarily bad for the equity markets. In fact, we may be in a situation similar to the early 1990's, which was characterized by slow but sustainable growth, low inflation, and healthy equity market appreciation.

Our independent evaluation of 121 economic indicators reveals that 54% of the measures we track are demonstrating improvements in economic activity, a marked increase since earlier in the year and a positive for the equity markets. Credit markets also have normalized. Low interest rates for good credits, as well as the steepening yield curve, indicate that credit markets once again are allowing companies to access capital.

Technical market indicators suggest that the market is overbought in the near-term. However, the trend clearly is upwardly sloping for now. We expect a "rotational correction" in the markets as long as the underlying fundamentals are progressing positively. In addition, we believe that investor sentiment is neither overly bullish nor overly bearish at these levels.

Finally, valuation and earnings trends remain favorable for equity markets. Earnings estimates for 2010 have turned higher after declining for the past six quarters. Based on valuation methodologies other than price/earnings, the markets still appear to offer some of the lowest valuations since the mid 1990s.

Slow Motion Economic Recovery

During the third quarter, many reports gauging economic activity improved significantly, and the equity markets delivered another quarter of positive growth. Through September 30, the S&P 500 was up 19.3% on a year-to-date basis, having risen 15.6% during the quarter just ended.

Dr. Ed Yardeni outlined the economic conditions leading to the strong equity market performance:

"So far, the economic recovery is playing out according to the usual script. The economy usually gets out of recession once inventory liquidation has run its course. This happens when production is slashed faster than sales fall during the recession. Sales stop declining, and then start rebounding usually in response to stimulative monetary and fiscal policies. During the recession, businesses also slash employment and capital spending. Such cost cutting tends to boost profit margins. It doesn't take much of a rebound in sales to trigger a revival in corporate profits, which then stimulates a cyclical upswing in business hiring and spending. Easier credit conditions and rising home affordability lift housing sales. Incentives usually take auto sales out of reverse and put them into drive."

(Dr. Ed Yardeni, <http://www.yardeni.com/>)

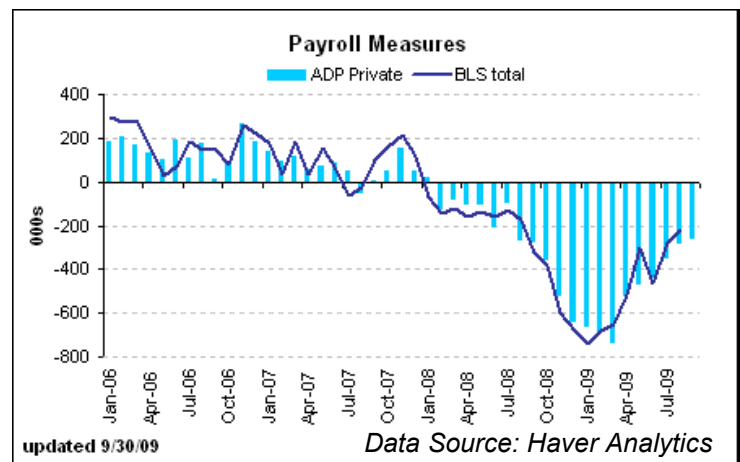
Equity markets typically lead economic recoveries, as may be happening currently. As the cycle progresses, household wealth begins to stabilize on the heels of improved housing, higher equity values, increased savings, and reduced debt. Consumer confidence begins to rebuild. Early indications do, in fact, point to positive GDP growth for the quarter just ended, with estimates hovering in the +3.0% to +3.5% range.

Nonetheless, we believe that the economy faces multiple structural, fundamental, and policy headwinds that portend sub-par growth for upcoming quarters. To be clear, we believe that the current recovery will continue, but, near-term, we do not

expect to see the strong growth rates in the economy experienced prior to last year's financial crisis.

Economic Trends

Our independent evaluation of 121 economic indicators reveals that 54% of the measures we track are demonstrating improvements in economic activity, a marked increase since earlier in the year. The Institute for Supply Management's manufacturing index rose for the eighth consecutive month in August, consistent with manufacturing growth and an economic recovery. Housing appears to be stabilizing as reflected in the Case-Shiller home price index, which registered its third monthly gain. Existing home sales increased a record 7.2% last month, rising for the fifth time in six months; and, new home sales jumped 9.6% in July, following a similar gain in June. Aided by the "Cash-for-Clunkers" program, auto sales improved to a seasonally adjusted rate of 14.1 million units in August. Both durable goods orders and shipments appear to have stabilized and show indications of improvement. Though unemployment, which tends to lag a recovery, remains high, the ADP employment

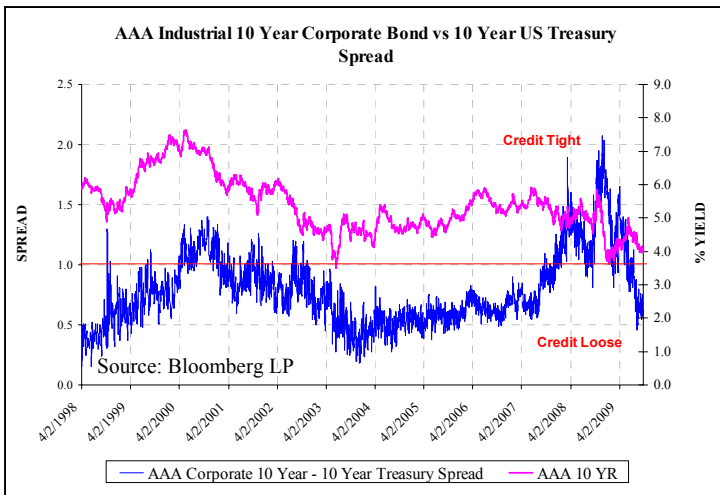


payroll measures, along with the Bureau of Labor Statistics' jobs count total, both indicate meaningful improvements since the beginning of this year. Collectively, these trends support the notion of an economic recovery.

Financial Conditions

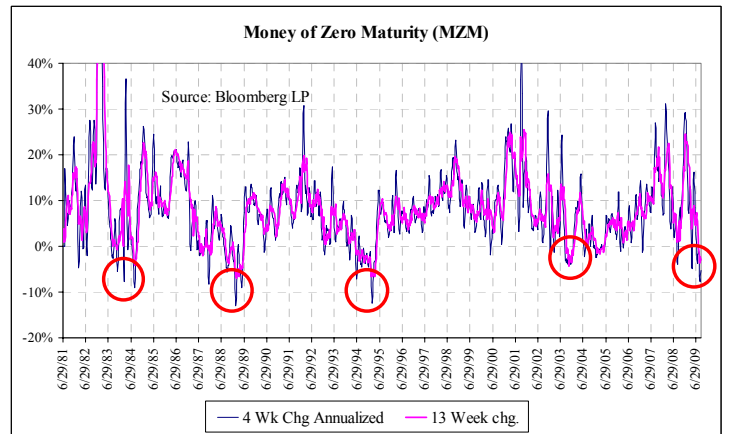
Credit and debt markets, which are over five times the size of the US equity market, represent the backbone of our finance-based economy. Without credit, the economy cannot function properly. It wasn't until Lehman Brothers declared bankruptcy, exactly one year ago, that the equity markets realized the importance of the credit markets. Few people in the world had any idea of the damage that could occur in "safe" money-market funds when Lehman failed. However, Lehman Brothers short-term corporate paper was held in many money funds throughout the world. Concerns mounted that a number of these money funds would "break the buck" and trade below par. This trend created a potential "run on the bank" panic. Immediately, The Federal Reserve stepped in to insure money funds. Congress, however, took its time before passing the Troubled Asset Relief Program (TARP). In a panic, credit collapsed worldwide. Almost immediately, corporations began hoarding cash, slashing costs, and curtailing capital spending projects. Interest rates on corporate borrowing soared, and for many institutions cash for operations became scarce.

With the help of numerous Federal Reserve and Treasury programs, the corporate credit markets have normalized over the past twelve months.



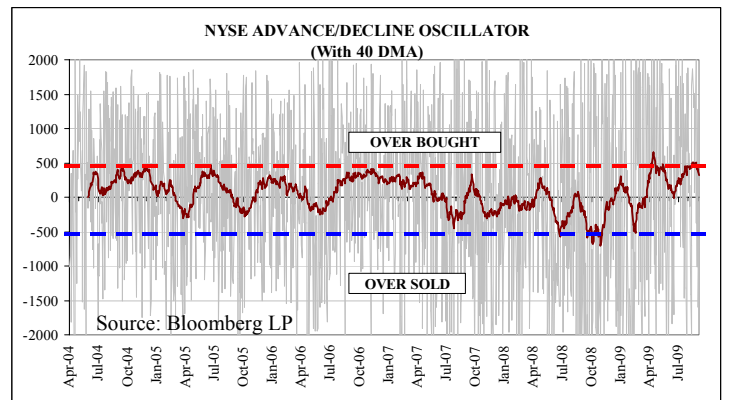
Monetary Trends

Since the back half of 2007, Federal authorities, as well as Central Banks around the world, have executed multiple conventional and unconventional programs geared toward stimulating monetary expansion. At several points, money growth measured at a 20% to 30%+ annualized rate. In fact, the Fed doubled the U.S. adjusted monetary base, raising it by nearly a trillion dollars, and simultaneously cut the Fed Funds Target rate range to 0% - 0.25%. While the Fed Funds target remains in that range, the Fed is removing or reducing a number of the programs designed to provide credit and stimulate the economy. It appears that the monetary stimulus is working and, if left unchecked, would lead to inflation. Similarly, money growth, measured by MZM (money of zero maturity), has turned negative. Typically, declining money growth would be a negative; however, available cash on the sidelines remains at very high levels. In sum, monetary trends appear neutral to modestly supportive for the equity markets.



Technical Market Trends

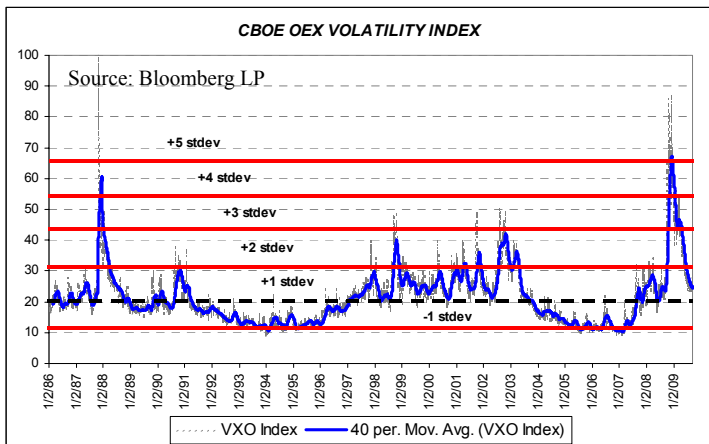
Most of our technical indicators reflect "overbought" conditions for the equity markets – and have done so for a while. In the short-term, we would not rule out a market correction. In fact, we believe that the market has been experiencing a "rotational" correction throughout the summer months leading into the fall. A rotational correction occurs when stocks that have lagged the market rally (often high quality stocks that held up relatively better during the severe downdraft) begin to rise as investor dollars rotate out of stocks that have participated fully in the rally and become extended or fully priced. Another technical crosscurrent may be found among the many investors who held high levels of cash or fixed income throughout the equity market rally since the March lows of this year; fearing that they may miss out on further gains, they may now be looking, selectively, to raise equity exposure. Historical precedents indicate that the current "overbought" conditions may be corrected by short, shallow corrections or rotational corrections, as long as the underlying fundamentals are progressing positively. Accordingly, we believe the technical market trends remain neutral.



Sentiment Indicators

Investor sentiment indicators have a very long history of being very good "contrary" indicators, especially at extremes. Most of these measures have short to intermediate-term implications and provide valuable insight into investor behavior. An assessment of the American Association of Individual Investors' (AAII) "Bullish" measure indicates that investors currently have regained confidence in the investment markets without being overly bullish. It is important to note that during the week of the March 2009 low (S&P 500 = 666), bullishness measured only 19 on an index scale of 0-100, a data point that was consistent with established market lows over the past twenty years. Another indicator we review is the "VIX" or Volatility Index, which

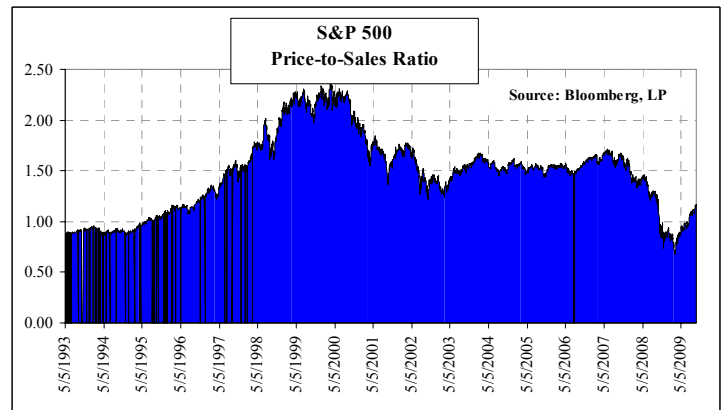
measures expected volatility in the market. In March, the VIX was at a record high level, but it has since retraced to more normal levels. We believe that investor sentiment is neither overly bullish nor overly bearish at these levels.



Equity Market Earnings & Valuation

We believe that the equity markets will provide long-term investment opportunity for investors as long as economic and company fundamentals continue to show improvements. Our proprietary work indicates a 95% correlation between the direction of forward earnings revisions and the direction of the equity markets. Corporate earnings and earnings revisions have been improving steadily. Early in this market rally, many in the media applied a 15x market multiple on trailing earnings and concluded that the market was overvalued. However, past recessions have demonstrated that markets lead recoveries and are “forward looking”, reflecting improving odds for earnings advances ahead of the actual improvements. Consequently, price-to-earnings multiples always appear high at market bottoms. On a short-term basis, the market has advanced nearly 55% from the March lows, and the forward price/earnings ratio appears relatively high. Corporations may have to demonstrate material, positive improvements in earnings for equities to advance from

these levels. We would point out, however, that based on other methodologies, e.g., price-to-cash flow and price-to-sales, which are less skewed during recessions, the markets still appear to offer some of the lowest valuations since the mid 1990s.



Conclusion

Currently, three of the six market components we have examined provide positive/supportive indications; the other three read neutral. Taken on the whole, we view these trends as constructive. Nonetheless, after the stunning 50% rise, which has been led by distressed and over-sold, stocks, it may be time for the market to progress with different players taking the lead. Looking ahead, investors likely will gravitate toward companies that generate real sales and earnings growth – or ones, which by virtue of sound balance sheet management, can acquire these objectives on the cheap. As economic activity improves, household wealth expands, and consumer confidence improves. Again, based on current measures, we are looking for a return to tepid growth. However, that profile is not necessarily bad for the markets. In fact, we may be in a situation similar to the early 1990’s, which was characterized by slow but sustainable growth (below par), low inflation, and healthy equity market appreciation.

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