2nd Qtr 2000

EDMP, INC. Quarterly Review

PRESIDENT'S MESSAGE

How's Business ?

Our second quarter of year 2000 was, relative to many other investors' portfolios, a solid one. Even though we gave back a small portion of the gains we enjoyed during the first quarter, we are still in positive territory for the year in the majority of our portfolios.

Although it is still too early to call, the year 2000 could possibly mark the end of the longest and greatest bull market in history. This should be of great concern to the large group of investors that for the last year or two have thrown caution to the wind with their *don't worry, pay any price* mentalities. Perhaps, this year's results will serve as a cruel reminder that in the longer run, valuations do truly matter.

EDMP clients, on the other hand, should have an entirely different perspective. Frankly, as President of EDMP, I am quite proud of our dedicated professionals for their tenacity and dedication to sound investing principles and practices. While most money managers succumbed to the enticing siren's song of easy riches, our team stuck to our knitting with most gratifying long run results. With prudence as our beacon, we never forgot that the protection of our clients' money was and remains our most sacred responsibility. In the fall of 1992 we wrote our EDMP brochure and proudly report that we have yet to find a single reason to change our philosophy in even the slightest way. If you haven't recently read our brochure, I strongly recommend it. For your convenience, the following excerpt entitled "Portfolio Strategies" is reproduced as follows:

Objective: The primary objective of our firm's investment policy is first and foremost to protect our clients' money. With this objective in mind, our credo is:

"To Win You Must Not Lose."

Therefore, great emphasis is placed on reducing the risk associated with the investments in our clients' portfolios.

Strategy: Our strategy is both simple and logical. First, no more than 5% of our clients' money will be committed to any single idea, company, or industry. Our goal is to build a diversified portfolio of at least 20 different companies in at least 20 different industries. Therefore, a mature, fully invested portfolio may contain 40 or more diverse selections.

In simple terms, we invest in companies, not in the stock market. In the long run, if a company prospers and grows, its market price will rationally reflect that fact. The effect of our core strategy is to produce reliable, above average long-term returns through both market appreciation and growth of dividend income.

Furthermore, to the maximum extent possible, we seek those companies that have proven to be relatively unaffected by the economy or business cycles. Last, we strive to identify and invest in the highest quality companies our minds can conceive, at values low compared to historical norms.

The above strategy reflects the primary theme we offer for this quarter's newsletter, i.e. investing in companies (sound businesses) rather than the stock market. This is in stark contrast to the practices of most investors who to their long-term detriment are driven by and react to the irrational short-term movements in stock prices. Their obsession with stock price and its inherent volatility paints what would be a rather humorous picture if it were not so important. Warren Buffett once said that: "The dumbest reason in the world to buy a stock is because it's going up." As a corollary, may I add that the dumbest reason in the world to sell a stock is because it's going down.

Those investors who make investing (or should I say speculative) decisions solely on price movement never learned these important principles. Consequently, they never experienced the comfort and the long-term investing success of their more rational counterparts.

As a side bar, it continues to amaze and mystify us that people find it so hard to learn from history. Even though the historical evidence overwhelmingly favors prudent long-term investing strategies, many if not most investors relentlessly persist in chasing stock prices. Sadly, this is the primary reason that most investors/speculators suffer with poor long-term results. Recent history exemplifies this concept most profoundly.

Well, you may sensibly ask, if you can't trust stock prices, then what can you trust? The answer is simple and those of you who have been clients of ours for a while hopefully already know the answer. Smart and successful investors place their trust in the long-term future of the companies they own.

At EDMP, we strive to be permanent owners/shareholders of the companies in which we invest. Through research and analysis we have learned many important lessons, facts and principles about investing in general and the "stock market" more specifically. A few of the more important ones are listed below.

We have learned that:

- Stock prices do not always reflect the true value of a good business or a bad one.
- It's more important to know what your business is truly worth, than what a few investors may be willing to pay today.
- If you don't buy a company (stock) with the express purpose of selling today, then today's price is irrelevant.
- The long-term business opportunities and the financial stability of your company are profoundly more important than this quarter's results. (Even a Coca-Cola, Wal-Mart, or Intel can have a bad quarter or even year).
- When volatility is high, as it is today, the value of the business behind the stock could not possibly vary as much as the stock price movement indicates.

There are many more principles we could list, but the important point is this, true investors realize that there is an actual business behind the stock. One of the primary reasons we look for good, solid and experienced management is for their ability to guide our companies though the inevitable challenges of running a business, especially a large one.

So it all comes down to **how's business**, not just today, but for the foreseeable future? We invest in a company because we believe it has future growth potential, solid management and a strong balance sheet. The key, however, lies in the growth potential and is therefore where we place most of our effort. Although forecasting the future potential of a business is vital to success, it's also very difficult to do. Consequently, it's a process more related to hand-grenades than to rifle shots. In other words, it's about seeing a trend and assuming a reasonable plus or minus deviation from your expected forecast. This is why we illustrate a value corridor on our fundamental forecasting charts.

Most importantly, forecasting is a relentless exercise. Since it's a virtual given that rapid change is the norm and not the exception, the forecaster must never let his or her guard down for even a moment.

As our valued clients, this is predominantly and precisely what you pay us for. We, on the other hand, view this as our solemn duty and most important responsibility to you.

Try as we may, try as we might, and work as hard as we do with as much logic as we can apply, and still rarely are we perfectly correct. Fortunately, we do hit our plus or minus corridor for error most of the time. Occasionally, we miss our target badly, almost always a result of being blindsided by an unforeseeable event or circumstance. This is why we diversify, because the unknowable cannot be known.

The beauty, however, of a well diversified and balanced portfolio, as we dutifully create, is that you don't need a perfect batting average to reach your goals. Unfortunately, some people either don't realize this or forget it under the duress of an occasional misstep. Believe it or not, we have had clients with a portfolio of 20 companies with nineteen of them exceeding our objectives. Human nature being what it is will blind them to the fabulous 19 and they will focus on number 20, the dud. The total portfolio is performing above expectations and they can only see the company that is down. In reality, a few bad choices, regardless of who is managing the account is a given.

There are simply too many variables and too much to know to either achieve or expect perfection. This is the nature of the beast and is unavoidable. The important point is that a sound strategy and prudently implemented discipline, as we follow, negates mistakes to irrelevance. It's critical to have a clear picture of the whole portfolio and refrain from obsessing on a single part. Perhaps this is why some people prefer mutual funds to a custom designed portfolio. Even though a fund has numerous disadvantages, ignorance is bliss. The devil is in the details and mutual funds don't provide any.

One final point on forecasting needs emphasis. We are discussing the forecasting of the operating results of the businesses, in other words, their earnings potential. Nothing in what we have said relates to forecasting stock prices. Trying to guess where the price of a "stock" may go in the short run is an exercise in futility. As the famed investor Bernard Barauch so aptly put it, "forecasting stock prices can only be done by liars." On the other hand, forecasting the growth of a business on an operating basis can be much more reliably accomplished.

In the beginning of this letter we commented that 2000 could possibly mark the end of the longest and greatest bull market in history. We would like to clarify our position and more importantly point out how this would relate to your portfolios.

One of the more important characteristics of this bull market is unprecedented overvaluation. We have never participated in this insanity. Instead, we carefully selected good businesses that were selling at sensible valuations relative to their future earnings potential. This fact is a primary reason we are so dramatically outperforming most managers during this now difficult environment. More importantly, thanks to our prudence, we are also outperforming with significantly less risk.

As a caveat, it would be possible, though unlikely, that our "cheaply priced" companies could fall a little in a widespread bear market. However, remember, time is the friend of the investor and the enemy of the speculator. Logic would dictate that all we would have to do is keep a cool head because our companies will most certainly return to intrinsic value, which is at prices that are actually higher then many of our holdings sell at today. The same is true for the many companies selling dramatically above their intrinsic value, the difference being that these overvalued companies' prices are significantly above their intrinsic value.

One of the common characteristics of the end of a bull market is high volatility. This scares most investors, as it should. So far, this year has been plagued with high volatility. Simply stated, when people get scared they tend to behave irrationally. None of you should be scared because your portfolios are comprised of sound growing businesses, the majority of which are at sensible or even low valuations. The few companies we hold that are highly priced have been appropriately pared back as discussed in our last letter. The principle is this, a true long-term investor accepts periods of high volatility as an unavoidable cross they must bear. Fundamentally, you cannot be a long-term investor without being prepared and willing to ride through some volatility.

A final thought on the ending of bull markets is very important. Many people, even today, are still traumatized by the great bear market of 1929 and the twenty-five dismal years of bad performance that followed.

Today, things are materially different than they were then. In 1929 we had no Federal Reserve, no SEC and the Securities Acts of 1933 and 1934, unlimited margin and we were mostly isolated from world markets. Modern investors have more information, knowledge and financial protection. Consequently, subsequent bear markets have ended quickly with new and stronger bull markets to follow.

In reality, what most people mistakenly refer to as the largest and greatest bull market of recent time has been a series of rolling bull and bear markets from one sector or class to another. The main characteristic of these bull markets has been overvaluation. The bear markets that followed were merely the return to more sensible and economically based valuations. Since the majority of companies you own are already either at value or in some cases downright cheap, we have little or nothing to worry about. Even better, as discussed in last quarter's letter, we have adequate cash reserves to exploit opportunities as they unfold.

It was hard to be a rational and prudent manager that paid strict attention to valuation, prudence and risk during these wild and wooly times. Therefore, it is most gratifying, and we are most proud that EDMP, Inc. has achieved Nelson's "World's Best Managers" status for the past five year period. (Details can be found on our Website www.EDMPinc.com). We are more proud of the lack of risk we took to achieve our results than we are of the results themselves. We hope you share our pride.

In closing, we believe we are very well positioned for the future. We also believe the long-term future will be very good, short bear market interruptions not withstanding. Getting you, our valued clients, to see what we see is a goal we are committed to. Evidence of this can be found on our website with several new enhancements we have made for your benefit. If you have not logged on in a while, please do.

It remains our privilege to serve you. And, as always, remember; Earnings Determine Market Price, always have, always will.

Sincerely,

Charles C. Carnevale
President