PROFESSIONAL FINANCIAL MANAGEMENT, INC.

945 Technology Blvd., Suite #102, Bozeman, MT 59718

January 12, 2011

Dear Client,

Happy New Year! Enclosed are your fourth quarter 2010 and 2010 annual reports along with our privacy statement. We are doing things a little different this year in that we will be sending information required for 2010 tax preparation in a separate mailing - we found this information was being passed over when combined with your report information so hopefully you will find this as an improvement!

The past year offered an interesting mix of positive and negative news as investors around the world eagerly anticipated signs of economic recovery and financial stabilization. While most financial markets logged positive returns for a second straight year, investors had to endure a host of troubling news and pessimistic market predictions (a concern we've focused on throughout the year). US markets were down through the first eight months of this year. But diversified, long-term investors were rewarded with attractive market returns, as the S&P 500 closed the year up 15.06%, with most of the gain coming in the fourth quarter.

Stocks performed well in the US and most developed countries, especially across size and value risk factors. Fixed income returns were positive as well despite assertions that bond prices were in a dangerous "bubble". All this happened in the face of ongoing concerns over a possible double dip recession, rising government indebtedness, and inflation. Markets in thirty-seven out forty-five countries tracked by MSCI achieved positive return in both local currency and US Dollar terms. Despite continued weakness in residential housing and commercial property, real estate securities around the world outperformed the broad equity market. Best of all, your diversification across the size and value risk dimensions in your portfolio provided (as it usually does) higher returns than the broad market.

In fact, our client portfolios are nearing their highs reached in October of 2007. We say this with caution, not to return your focus to your "number" (getting "back" to something that was unrealistically high makes little sense), but because we believe our overall strategy, despite the ups and downs of the stock market, has performed as expected over the past decade and that should provide you a good dose of confidence going forward.

What can be expected in 2011? As always, we have no way of knowing. Jason Zweig who writes the Intelligent Investor column in the Wall Street Journal summed it up in a recent article when he said "what happens in the future is the realm of surprises; no one, no matter how expert, can reliably foresee what will happen and how people will react to it". This is not to say, however, that there is absolutely no way to get a reading on the market. One measure we have found particularly useful these last few years is the PE10, a fairly reliable market valuation measure. Right now it signals a moderately overvalued U.S. Stock market, but one we feel is still a better current investment opportunity than cash or bonds.

Where does this leave the "Bond" Market? Bonds are still, in our opinion, overvalued and due for a decline if (when!) prevailing interest rates rise. Our move this past July out of longer duration, riskier fixed income positions into shorter duration bonds, higher quality bonds was made as a defensive move for that reason. The protection of principal as rates rise will far outweigh any small additional incremental return gained by staying in riskier bonds – as we see bond yields return to "normal" however, we will move back to a more traditional allocation.

What changes can be expected going forward? No changes will be made with regard to our basic strategy. However, using the above shift in bond strategy as an example, we do make slight changes or modifications where appropriate. It's important to understand that these changes do not constitute market timing (jumping completely in and out of the market based on perception of market valuations – a strategy that is doomed to fail). Rather, these are considered" tactical" portfolio adjustments. Tactical adjustments are changes "on the margin" of a portfolio and are based on longer term trends. Our continued review of the most current investment and tax research provides us new information to use for your benefit (i.e., use of the PE10, fair value of TIPS bonds, etc.). A more recent example came from a recent study demonstrating that value and small cap stocks almost invariably "lead the way" out of market declines, and as such, we are using this information to implement a moderate increase to our weightings in these asset classes. So far, our tactical adjustments have produced moderately increased returns and reductions in risk over a strict "buy and hold" strategy, and we expect that to continue.

In summary, we watch your money as carefully as our own, continually strive to improve our portfolio management, and attempt to bring you the best combination of risk and return reasonably possible.

As always, we welcome your questions, thoughts, concerns and feedback and look forward to serving you in the months (and years!) ahead.

With warm regards,

Doug Babcock

Bob Frey