

October 5, 2001

THIS ISSUE

"Never give in, never give in, never, never, never, never-in nothing, great or small, large or petty-never give in except to convictions of honor and good sense."

Sir Winston Churchill

The Stock Market

DEAR CLIENTS:

Summary

"It was a clear morning in the middle of September. If there was one geographical spot in the United States that could justly be called the financial center of the country, it was the junction of Broad and Wall Streets in New York. There was a sudden blinding flash of bluish-white light and a terrific crashing roar, followed by the clatter of falling glass from innumerable windows and by the screams of men and women. A huge bomb had gone off in the street-with such appalling violence that it killed thirty people outright and injured hundreds, wrecked the interior of offices, smashed windows for blocks around, and drove an iron slug through the window of the Bankers' Club on the thirty-fourth floor of the Equitable Building." Is this a news account of the horror of the terrorist attack on September 11, 2001? No, it's an excerpt from Frederick Allen Lewis' book, *Only Yesterday: An Informal History of the 1920's*, describing the terror attack on Wall Street that occurred on *September 16, 1920*. For a more complete look at the 1920 attack, see the September 20, 2001 article by Daniel Gross, "Previous Terror on Wall Street-A Look at a 1920 Bombing," available on TheStreet.com website.

Then, as now, the aim of the terrorists was to strike a crippling blow to the heart of the world financial system. Then, as now, terror struck at a time when the financial markets were already in a downtrend, sending the markets reeling. After taking eleven months from the attack to find and form a bottom in 1921, the market launched into a roaring bull market lasting eight years. The terrorists failed then in their quest to topple the financial markets and we have no doubts they will fail this time. Just as the seeds of panic and terror were sown in these two Septembers, 81 years apart, we believe the seeds of the next bull market are being sown now. Although no one can predict with any certainty how stocks and the market will act over the next 3-6 months, we are confident by sticking with our discipline of buying good businesses at 50 cents on the intrinsic value dollar, the next 12-36 months will be very rewarding.

Farewell To
 A Friend

As we stated above, the U.S. equity market was in a downtrend prior to the terrorist attack on September 11, 2001, with the attack triggering a further sharp sell-off. Total returns are displayed below:

Kirr, Marbach Partners
 Value Fund

General

| | <u>Pre-Attack</u> | | <u>Full Period</u> | |
|-----------------------|-------------------|----------------|--------------------|----------------|
| | <u>Q3</u> | <u>YTD</u> | <u>Q3</u> | <u>YTD</u> |
| | 7/1/01-9/10/01 | 1/1/01-9/10/01 | 7/1/01-9/30/01 | 1/1/01-9/30/01 |
| Standard & Poor's 500 | -10.52% | -16.51% | -14.68% | -20.39% |
| NASDAQ Composite | -21.52% | -31.24% | -30.65% | -39.33% |
| Russell Midcap | -10.79% | -12.54% | -17.86% | -19.47% |

We mentioned in our interim letter to clients dated September 21, 2001 the performance of client equity portfolios had experienced a sharp and what we considered short-term decline. Indeed, the average performance of our equity portfolios went from *solidly* positive at the end of August (year-to-date) to *slightly* negative at the end of September. Although we are never pleased or satisfied to report a negative number, we do not operate in a vacuum and, as you can see from the performance chart on the previous page, it could easily have been *much* worse. We also said we expected the tug-of-war between fear and greed to create massive *short-term* volatility. We still do. For example, from the close of the day prior to the attack (September 10, 2001) to the near-term low (which coincided with the date of our interim letter, September 21, 2001-5 trading days), the S&P 500 declined by 11.6%. From that near-term low, the S&P 500 gained 11.1% over the next 8 trading days.

Allow us to repeat ourselves. We seek to own stock in good businesses with strong management teams, possessing what we see as solid prospects for earnings growth. We look at buying stock in a business as if we are buying the entire business and try to buy stock for the *long-term* that is currently selling for 50 cents on the intrinsic value dollar. Buying 50-cent dollars makes good long-term investment sense. While 50 cent dollars can certainly go to 40 cents over the short-term, if we are right they have an even better chance of becoming 90-cent or 100-cent dollars over the long-term. The stock market is and has always been a forward-looking discounting mechanism. In other words, though the stock market cares about today's headlines, what it *really* cares about are what the headlines will be 6-12 months from today and beyond. Everyone "knows" how bad things are with the current state of the markets, the economy and corporate earnings because it's been beaten into our consciousness on a continual basis. Our challenge is, as it has always been, to tune out the cacophony and focus on the long-term prize. It's never been more difficult than now, but the overall risk/reward parameters are as positive as they have been in recent times.

THE STOCK MARKET

Corporate earnings were collapsing, equity markets around the world were in decline, corporations and individuals had too much debt, unemployment was rising and consumer confidence was fading, threatening the last bastion of strength in the U.S. economy. And this was all *before* the terrorist attacks on September 11, 2001. Thus, things will surely get worse before they get better, but they *will* get better. The economic weakness in the aftermath of the attacks should remove any doubt as to whether or not the U.S. economy is in recession. However, the U.S. economy has experienced six "official" recessions since World War II, all six of which were followed by a recovery. No exceptions. Further, history has shown that the deeper the downturn, the more vigorous the ensuing upturn is likely to be. The Federal Reserve cut interest rates by 100 basis points in the aftermath of the attack (for a total of nine reductions summing to a whopping 400 basis points in nine months), sending the federal funds rate to 2½%, the lowest level since 1962. The Fed governors indicated after the most recent cut on October 2, 2001 they remain prepared to cut rates further, should continued economic weakness warrant it. The Fed has already pumped a massive amount of liquidity into the banking system. Morgan Stanley estimates the Fed's current provision as 15 *times* the amount provided during the huge buildup made in anticipation of a Y2K disruption.

The combination of the U.S. economy's perfect 6-for-6 record in recoveries (all 6 of which were *preceded* by a stock market rally), a Fed clearly willing to put the full force of every monetary tool at its disposal to work and indications of tremendous fiscal stimulus in the works makes it a bit easier to see past the valley. This is not to say we expect the U.S. economy to make a rapid, V-shaped recovery and the major market indices to quickly move back up to their old highs. Nothing could be further from the case. As we said above, corporate earnings were weak prior to the attack, which will now provide "cover" to companies throwing in the towel for 2001. There is a great deal of heavy lifting to be done to boost the economy without touching off a new round of inflation. Layer on top of this the fact the U.S. will be fighting a war of indeterminate length against an unseen foe and the task ahead is formidable. But there will be a

recovery and we believe the companies we own will both weather the current storm and prosper when the upturn arrives.

As we stated in our interim letter, on September 10, 2001 we owned a portfolio comprised of stocks of good businesses, with solid management teams, selling at attractive valuations. We still do today. Although estimating near-term earnings prospects is extremely problematic in this difficult environment, we are still able to trace-out reasonable estimates of “normalized” earnings, looking a year or two out. Based upon these estimates, our portfolio is attractively valued and has solid long-term upside potential. During the recent market downdraft, we sold some of the names we owned that had held-up relatively well and have begun to redeploy this cash into both existing names that have been hit, as well as some new names.

SUMMARY

These are the most trying times our nation has faced in many, many years. As American president Woodrow Wilson said, “We cannot be separated in interest or divided in purpose. We stand together until the end.” We think difficult conditions are where investment managers prove their mettle and worth to their clients. We are up to the challenge and thank you for the opportunity you have given us to manage your funds in this most extraordinary period. We greatly appreciate the trust you have placed in us and will continue to try each day to earn that trust.

FAREWELL TO A FRIEND

Will Raub, from the brokerage firm of Cantor Fitzgerald, started covering our account in late 1985. Will was 22, right out of Sienna College and we could not *possibly* conceive of how he could add any value to our effort. Though not very experienced, he was *extremely* persistent and over the next 16 years he would prove time and again our initial impression was wrong. Will would quickly advance and become a senior member of Cantor and could easily have passed coverage of our account on to a more junior broker. Though we have no doubt he was mightily tempted on occasion,

he never did. We had formed a bond over the years because we both tried to conduct our respective businesses the same way—treating people with whom you do business with dignity and respect and always, always putting your customer’s best interests above your own or your firm’s interests. In the “good old days,” brokers were known as “customer’s men (or women)” because they worked for their customers’ best interests. Period. Unfortunately, there are not very many of them around anymore. We are fortunate to still be covered by some of them. Will was the epitome of the customer’s man and was a true friend of the firm. He did a great job for us and for our clients. Will was killed in the terrorist attack on the World Trade Center on September 11, 2001. He was 38 and left behind his wife, Maureen, 6-year old daughter, Rebecca and 3-month old son, Liam. We miss Will’s laughter, humanity and expertise, but we will never forget.

KIRR, MARBACH PARTNERS VALUE FUND


KM is the investment adviser to the Kirr, Marbach Partners Value Fund (“Value Fund”-NASDAQ-KMVAX), a registered, open-end investment company, more commonly known as a mutual fund. Value Fund is a diversified equity portfolio managed in KM’s traditional, value investment style and commenced operations on December 31, 1998. Please call Craig Kessler, KM’s Director of Marketing at 812-376-9444 or 800-808-9444 if you have questions or would like a Prospectus and account application. You can also visit Value Fund at www.kmpartnersfunds.com. **Read the Prospectus carefully before you invest or send money. The Prospectus contains important information about Value Fund, including charges and expenses. Past performance does not reflect how Value Fund may perform in the future. The investment return and principal value of your investment will fluctuate. When redeemed, your shares may be worth more or less than their original cost. Rafferty Capital Markets, LLC is the Distributor for Value Fund.**


GENERAL

We would like to add your e-mail address to our address book. Please drop an electronic line to Kip Wright, CFA, KM's Senior Client Service Officer at kip@kirmar.com. Many of our clients now prefer using e-mail for routine items. In addition, we sent interim letters to clients on September 11 and September 21, 2001. We hope to never have occasion to respond to an event like this again, but to the extent we ever have something to say between quarterly letters, we are able

to deliver these interim updates electronically (as well as via traditional mail). Since e-mail transmissions are generally not considered secure, in order to safeguard your non-public personal and financial information, our policy is not to transmit information such as account numbers, account balances, performance or passwords via e-mail.

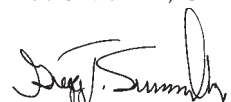
Regards,
Kirr, Marbach & Company, LLC

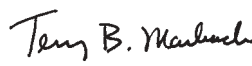

David M. Kirr, CFA


Darrell H. "Kip" H. Wright, CFA



Allan C. Nichols, CFA



Deborah N. Malone



Gregg T. Summerville, CFA


Terry B. Marbach, CFA



Donita C. Compton



Mary A. Schoettelkotte



Mark D. Foster, CFA


Craig A. Kessler


Mary Jo Cusano


Karen S. Sluder


Mickey Kim, CFA


Richard H. Hummel, CFA


Patsy A. Kaisher