





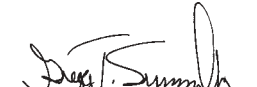
Please contact Craig Kessler at 812-376-9444, 800-808-9444 or craig@kirmar.com if you have questions or would like a Prospectus and account application. You can also visit Value Fund at www.kmpartnersfunds.com. **Read the Prospectus carefully before you invest or send money. The Prospectus contains important information about Value Fund, including charges and expenses. The performance data quoted represents past performance and assumes the reinvestment of capital gains and income distributions. Performance also reflects fee waivers in effect. In the absence of fee waivers, total return would be reduced. 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.**

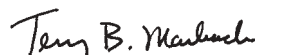

David M. Kirr, CFA


Darrell H. "Kip" H. Wright, CFA


Allan C. Nichols, CFA

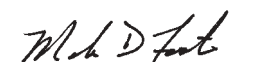

Deborah N. Malone

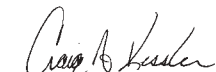

Gregg T. Summerville, CFA


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

SECURITIES AND EXCHANGE COMMISSION-FORM ADV-PART II

Form ADV-Parts I and II describe an investment adviser's business and practices. Federally registered advisers, like us, are required to file an annual updating amendment to Form ADV-Part I electronically with the Investment Adviser Registration Depository (IARD). We made our annual amendment filing in March. The SEC is contemplating changes to Form ADV-Part II, but has not implemented any changes at this time. Advisers are to amend Part II as needed, but are not required to file amendments with the SEC. As a matter of practice, we have provided each client account with a copy of our annual amended Form ADV-Part II for the past several years and do so again this year.

Regards,

Kirr, Marbach & Company, LLC

KIRR, MARBACH & COMPANY, LLC

KM & Co

Investment Managers
www.kirmar.com

David M. Kirr, CFA
Mickey Kim, CFA

Gregg T. Summerville, CFA
Darrell H. "Kip" Wright, CFA

Mark D. Foster, CFA
Terry B. Marbach, CFA

April 5, 2002

THIS ISSUE

"Don't judge each day by the harvest you reap but by the seeds that you plant."

Robert Louis Stevenson

"It is better to keep your mouth shut and appear stupid than to open it and remove all doubt."

Mark Twain

"Success is a lousy teacher. It seduces smart people into thinking they can't lose."

Bill Gates,
founder of Microsoft

The Stock Market

DEAR CLIENTS:

Why Enron Matters/
The Covenant of Trust

Most major U.S. equity market indices (except NASDAQ) ended the first quarter of 2002 close to year-end 2001 levels, though the investment sea was quite choppy during the quarter. The market stumbled out of the starting blocks in January and February as investors grappled with uncertain prospects for near-term economic recovery and a crisis of confidence brought on by almost daily revelations of wrongdoing by Enron senior management and their (not so) independent

CPA firm, Arthur Andersen. We will discuss this topic and its implications for investors in further detail. The S&P 500 rallied to recover almost all the decline in March and actually finished the quarter with a slight positive total return. This was due to strengthening economic indicators and the Fed's pronouncement the U.S. economy has recovered to the point where the risks of further weakness and increasing inflation are now in balance.

The Value of
Value Investing/
The False Promise of
Asset Allocation

Summary

Periods ending 3/31/2002 (Total Returns-Cumulative-Bloomberg)

	S&P 500	NASDAQ	Russell Midcap
3-Months	+0.3%	-5.3%	+4.2%
One-year	+0.2%	+0.6%	+9.9%
Two-years	-21.5%	-59.4%	-3.3%
Three-years	-7.4%	-24.4%	+26.5%

KM's Newest Partner
Kip Wright, CFA

Kirr, Marbach
Partners Value Fund

SEC Form ADV-Part II

Given the massive destruction of wealth that has occurred since the early spring of 2000, preservation of capital continues to be the name of the game. You may recall from our most recent quarterly letter, Warren Buffet's expectation of longer-term

annual returns is in the neighborhood of 7% (net of transaction costs and fees). Given this backdrop, and at the risk of violating Mr. Twain's rule, if we can produce a mid-to high-single digit total return in 2002, we'll look pretty good.

THE STOCK MARKET

The S&P 500's +0.3% total return for the first quarter might lead one to believe it was a tranquil quarter for the stock market. Nothing could be further from the truth. "Enron flu" quickly infected the other independent power producers before "jumping species" to the telecommunications sector and any other company suspected of using aggressive accounting practices, ranging from Tyco International Ltd. to Krispy Kreme Doughnuts, Inc. Unfortunately, the maelstrom also negatively impacted a small number of our holdings, particularly those in the telecom sector. We believed (and still do) the companies we own in this sector are long-term survivors and the stocks were (and are) extremely attractively valued. What we found was other investors' primal fear of not owning the "next Enron" *massively* trumped valuation, over the short-term. As Mr. Buffet also said in his article, the stock market functions as a voting machine in the short-run, but acts as a weighing machine in the long run. In other words, "fear and greed play important roles when votes are being cast, but they don't register on the scale."

As we have stated, the market had a tremendous recovery from its low on September 21, 2001 and is no longer attractively valued, as a whole. Last fall, we thought investors' outlook for the economy was overly pessimistic, creating a great investment opportunity. The economic cards turned over since then have been even better than we expected and our clients have been rewarded accordingly. Human nature as it is, economic expectations have now been rapidly ratcheted upward, creating more risk. Though we are still finding value on a selective, stock-by-stock basis, we are having difficulty uncovering investment themes or groups with exceptional value. Because of the slim pickings in the equity market and the uninspiring value in the bond market, client cash positions have increased. We want to remind clients the relative abundance or dearth of attractive investment opportunities dictate portfolio cash positions.

With the Fed signaling their campaign to boost the economy with an unprecedented 11 interest rate reductions covering 475 basis in 2001 has arrested the decline

for now and set the stage for recovery, interest rates are likely to increase as the economy strengthens, restraining the market's P/E. If the market multiple can no longer expand, the math says earnings must then increase faster than expected for stock prices to rise. The risk in the stock market is valuations are extended, even assuming fairly aggressive earnings growth expectations (particularly for the last half of 2002). This leaves very little room for error.

WHY ENRON MATTERS/ THE COVENANT OF TRUST

In many ways, Enron is the "poster child" of everything wrong about the go-go stock market of the late 1990s. Enron's rapid and spectacularly visible implosion has provided copious fodder for market pundits and comedians alike, but the potential implications go far beyond its appeal to the public's prurient interest. If the circumstances surrounding Enron's collapse could be seen as an isolated instance of management incompetence or outright fraud, investors might be able to shrug it off as just a "one-off" bad situation. Our concern is investors, regulators and politicians may come to view Enron's problems as endemic, not isolated.

As with many of life's endeavors, investing is based on trust. Investors in American capital markets trust the Street is fair, corporate management is honest and certified financial statements can be relied upon to give an unbiased and accurate portrayal of a company's operations and finances. Much has been written about the "democratization" of the financial markets in the 1990s, as John and Jane Q. Public became portfolio managers actively trading their 401-Ks and online brokerage accounts. All was right with the world, until the music stopped, exposing cracks in this "Covenant of Trust." The Street received a black eye when it was revealed how and why major brokerage firms (such as CS First Boston) favored certain of their customers with allocations of "hot" IPOs. A second blemish appeared when it became apparent some of the high profile analyst *wunderkinds* (such as former Internet guru Henry Blodget of Merrill Lynch) were spending more time shilling for the

superior to growth over a long period of time and any attempt to diversify away from value dilutes value's advantage.

We argued proponents of asset allocation were making the mistake of thinking "value" and "growth" are two mutually exclusive universes of stocks. As the Goldman Sachs report said, the distinction between value and growth is one of emphasis. As both disciplines attempt to exploit a mismatch between price and prospects, it is misleading to say a growth stock can't be a value stock, and vice-versa. We referred to a white paper published by pension and investment consultant Ennis Knupp + Associates, whose business is to offer advice on asset allocation. This paper can be accessed at www.ennisknupp.com/satellites/WholeStockPortfolio.pdf or we'd be happy to send you a copy. Briefly, by diversifying among many styles/sectors, the portfolio begins to take on the characteristics of the overall market. As you would expect, *gross* investment returns also begin to mimic the overall market. However, this strategy of "closet indexing" is bound to underperform on a net basis because you end up with an indexed portfolio, but with active management fees and transaction costs. Further, **achieving superior long-term performance requires you learn to live without it over the short-term.** In other words, though a skilled manager's returns may not correlate well with "the market" over the short-term, they will hopefully outperform over the long-term.

Putting this all together, value investing has shown to be superior to growth investing over a long period of time. However, value and growth move in cycles and value will suffer through periods of underperformance, which at times can become extreme (as it did from 1995-1999). The key questions an investor has to ask herself when confronted with whether or not asset allocation makes sense are: "What am I trying to accomplish with my investment portfolio?" and "Am I willing to live through short-term periods of underperformance in order to reach my long-term goals?" We submit if your goal is to approximate market returns on a gross basis and you cannot tolerate short-term underperformance, then diversifying away from value and its proven long-term superiority is appropriate. If, however, your goal is to earn above-average returns over the long-term and you are willing and able to endure short-term underper-

formance, keeping all or most of your eggs in the value basket allows value's long-term advantage to compound for you.

SUMMARY

Each of us gives you our most humble thanks for your faith and trust in us. As we approach our 27th anniversary on May 1, 2002, we are reminded everyday that without you, we wouldn't have a business. We are truly blessed. As you know, we're always interested in growing our business. Over the years, referrals from clients have been one of our best sources of new business. If you know of anyone who might be interested in talking to an investment manager who has generated good, long-term returns by investing in 50-cent dollars, please let us know or have them contact Craig Kessler, Director of Marketing at 812-376-9444, 800-808-9444 or craig@kirmar.com. Thanks again.

KM'S NEWEST PARTNER KIP WRIGHT, CFA

In recognition of Kip's major contributions to the success of our business as a senior client service officer, Kip was named a Managing Director and invited to become a Member of Kirr, Marbach & Company, LLC, effective January 1, 2002. Kip joins David Kirr, CFA, Gregg Summerville, CFA, Mark Foster, CFA and Mickey Kim, CFA as Members of KM. Congratulations, Kip!

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.

companies they followed and their firm's investment banking department than performing actual securities analysis. The honesty of corporate management was called into question as a number of instances were reported of CEOs (such as Gary Winnick of Global Crossing) reaping *obscene* amounts of wealth while employees and shareholders were left holding a worthless bag. Doubt was cast on the integrity of "certified" financial statements and CPA firms when it was understood how conflicts of interest arose between auditor and client, severely impairing the ability of the auditor to perform its critically important role of watch dog (such as between Arthur Andersen and Enron).

The purpose of reciting this litany is not to "pile on" or just report on the numerous recent "car crashes." There is a *cumulative* effect from all of these seemingly disparate events, all of which circle back to the erosion of what we refer to as the Covenant of Trust. We've already witnessed some of the short-term fallout, but as always, the key question is what the impact will be over the *longer term*. It seems reasonable reported earnings will be lower than they would have otherwise been as auditors, under the microscope of audit committees and regulators, become increasingly willing to challenge their clients' accounting practices. Some Wall Street firms have already changed their stock rating systems to reflect the "new" reality that, by definition, 90-95% of stocks *cannot* be above average and "buys." We expect the credit rating agencies, stung by criticism for rating Enron debt as investment grade right up to the bankruptcy filing, to be very quick to cut credit ratings and much slower to raise ratings. The possible effect on the psyche of investors is more difficult to predict. We've developed an "equity culture" in the U.S. over the past decade and that won't change overnight. The S&P 500 enjoyed an average annual total return of 28.5% from 1995-1999, so success came easy to many novice investors. However, given the destruction of wealth since 2000, it's not difficult to see how investors could become disillusioned with the market, particularly if they come to believe the game is rigged against them. If this comes to pass, we can envision a scenario where individual investors become net sellers of equities and employees begin clamoring for defined benefit retirement plans, rather than 401-Ks. As the marginal buyer determines stock prices, this would be a significant obstacle for the market to overcome.

We hope there will be a silver lining in this dark cloud of greed and self-dealing. We hope a new era dawns characterized by **Accountability** and **Rational Expectations**. Senior management works for the owners of the business, the shareholders, and should view the public shareholders as their partners, not their patsies. CEOs will be held accountable for every aspect of their business. In the future, it is doubtful a CEO will attempt to invoke former Enron CEO Kenneth Lay's "I know nothing" defense. Accounting standards will be tightened and CPA firms held accountable for certifying their clients are adhering to these standards. Part of the SEC's charge is to assure a level playing field for investors and they will be held accountable for making it so. The root cause of many of these problems was the market and economy were doing so well in the second half of the 90s, many assumed the good times would keep right on rolling. The expectations of investors, investment managers, senior management and the Street spiraled ever higher. It's a virtual mathematical impossibility for investment returns to compound at 28.5% and corporate profits to compound at 20% plus, given 4-5% GDP growth, but pressure to deliver "the number" is intense and people tried. A little lie to make this quarter's number became a bigger lie to make the next quarter, which led to outright fraud on down the road. While we're all for aiming high, and do it everyday, unrealistic expectations can lead to aberrant behavior.

THE VALUE OF VALUE INVESTING/THE FALSE PROMISE OF ASSET ALLOCATION

The investment firm of Goldman Sachs recently published an informative research report, "The Value of Value Investing," which discusses the differences and similarities between value and growth investing, the long-term superiority of returns from value investing and a hypothesis for the underperformance of growth. You can access the entire report at www.gs.com/funds/WHATNEWS/newsdesk.html or we'll be happy to send you a copy. The report begins by saying growth investing dominated the investing landscape so thoroughly in the late 1990s the five-year

period ending in 2000 marked the greatest underperformance for value investing since 1927. We can attest it certainly felt like it. This forced even longstanding value managers to either close their firms or abandon their discipline. The report goes on to describe the distinction between value and growth as one of *emphasis*. While both schools of investment agree the value of an investment is a direct function of its cash flows, value investors stress **proven** cash flows; growth investors focus on **future** cash flows.

"Value investors place less faith in future estimates, favoring stocks with lower valuations relative to current assets and cash flows—those in which investors have modest expectations of future growth. Value investors look among such low-expectation stocks for those companies with secure business franchise, a strong balance sheet and demonstrated cash flows, all of which increase their potential to deliver superior returns.

"Growth investors seek out those companies with the highest growth potential, via new products and/or expanding markets. The price of such promising growth companies will be higher relative to existing assets and cash flows, of course, and so they represent high expectation stocks. Growth investors moderate the risk of these higher valuations by seeking out companies with excellent management, competitive dominance and recurring revenue.

"Fundamentally speaking, both growth and value investors seek excess returns by uncovering a mismatch between price and prospects. That's why we can say that the labels 'Value' and 'Growth' are somewhat misleading—because great investments by definition incorporate a favorable balance of both price and prospects. Take prospects. It might seem intuitive that growth stocks have outperformed value stocks, because growth companies typically outgrow value companies. And yet, the returns from investing passively in growth stocks have lagged the returns from investing in the lower-expectation value stocks over extended periods. Over time, on average, price has proved to be a more powerful influence on investment outcomes than prospects (emphasis added)."

The report goes on to cite an updated study conducted by Eugene Fama of the University of Chicago and Kenneth French of the Massachusetts Institute of Technology. Their methodology focused on the return differential between the least and most expensive third of the market, as defined by a stock's price relative to book value. **The study found that over the past 75 years, value outperformed growth by almost 3.5% per year on a compounded basis.** The excess returns to a value strategy, *while cyclical*, were prevalent over long stretches of market history. Although 3.5% compounded may not sound like a very big deal, the implication is if you assume a value investor and a growth investor start with the same initial investment, **in 20 1/2 years the value investor would have twice as much money as the growth investor (i.e. a decidedly big deal).**

In our letter to clients dated July 6, 2001, we stated the conventional wisdom had become investors should have their equity assets spread over a wide range of investment styles (i.e. value/growth) and market capitalizations. The reasoning is "you don't want all of your eggs in one style/market cap basket" and, over time, weakness in one style box will be offset by strength in another. On the surface, this argument seems to make some sense. However, we explained in our world, we try to construct a well-diversified portfolio of 45-55 stocks, selling at 50 cents on the intrinsic value dollar. Portfolio diversification makes absolute good sense to us, which is why client equity portfolios typically contain 45-55 stocks. However, in our admittedly old school way of looking at the world, it *doesn't* make much sense to further diversify this portfolio of underpriced stocks by adding overpriced stocks to the mix. Though some of the stocks we buy don't pan-out, our performance record over the past nearly *27 years* indicates we're right much more often than not. The conclusion of the study by Fama and French of *75 years* of return data referenced above is consistent with what we've been saying and practicing all along; value investing is