CAMBIAR INVESTORS

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Overview

The first quarter of the decade of the 2010s resembled more the 1990s and not the "lost" decade of the 2000s that just passed, with stocks marching steadily upwards and impervious to negative international news. U.S. equity indexes led the world with the S&P 500 Index rising by 5.4% and the more tech-heavy Nasdaq Composite Index by 5.9% in the quarter. Smaller cap U.S. stocks performed exceptionally well with the Russell 2000 Index rising 8.9%. It is clear that the U.S. economy has turned the corner and is seeing strength build in a number of areas, with even the housing market showing some evidence of stabilization. Retail sales have picked up demonstrably, railcar and truck loadings are up by 10-20%, and business capital spending has clearly begun to rise, albeit off very depressed levels.

Events beyond the shores of the U.S. were not as constructive. During the quarter, the prospect emerged of a major sovereign default by Eurozone member Greece absent substantial intervention and external assistance. This roiled currency markets and saw the U.S. dollar rise by up to 8% into the month of April versus the Euro. Net – U.S. dollar-denominated assets substantially outperformed the rest of the world, and problems afar appear for the moment to be afar. After a short selloff in January and February in which the S&P 500 Index briefly lost approximately 9% and the MSCI World Index over 11% in U.S. $ terms, markets came roaring back and shrugged off the potential impact of sovereign debt difficulties. Since the broad market low in March 2009, buying the dips has proven highly effective.

It is reasonable to assume that at some juncture in 2010, markets may need a more prolonged digestion period than the 5-10 day selloffs we have experienced since last March. Beyond this vague forecast, we don't dare hazard exactly how the balance of 2010 will play out. Economic growth and business confidence appears to have transitioned from tepid levels last fall to far more robust measures. The logical challenge to the bull market would be a material back up in interest rates, but this does not appear to be in the cards for some time to come. Valuations remain attractive in many areas but are not commandingly so across the board, especially in certain cyclically geared sectors which have become popular "recovery plays".

In keeping with our communication at the end of 2009, we will publish various macro-thematic pieces on our website as white papers; however we will confine the quarterly investment discussion to more useable industry-specific observations and commentary. We plan to publish a broad discussion on sovereign debt dynamics shortly.

Technology Discussion

We venture into a thematic discussion of technology at the ten year anniversary of the peak of the tech-heavy Nasdaq Composite Index. In March of 2000, the Nasdaq briefly reached a value slightly over 5,000; it sits today at less than half that level. It catapulted to unreasonably lofty heights partly on pure speculation and partly on a sense of wonder that led investors to divorce themselves from "normal" stock valuation analysis. This was obviously an expensive mistake, but the emotive considerations are understandable. No other sector inspires quite the same degree of boundless possibilities in terms of devices and uses as technology does. New products and devices can achieve broad market penetration at rates that would be completely implausible in other economic sectors. Many of the competitive dynamics that normally apply to other industries, such as the benefits of scale, capitalization, and entrenched market shares often work much differently.

One highly visibly example of the peculiar dynamics of technology is competitive displacement. In a typical cost-focused manufacturing business, a dominant market share coupled with cost leadership would virtually guarantee decades of sustained competitive advantage and profitability to entrenched companies. But in technology, the ability to shift the paradigm associated with a particular device or tool stands such an academic analysis squarely on its head. Market dominance can be gained or lost with unusual speed.

Ten years ago, the Finnish telecommunications giant Nokia stood without peer in the world of digital cellular communications. Their phones worked better, the batteries lasted longer, the designs were cooler, and the company had achieved a remarkable degree of cost supremacy globally through substantial scale advantages. Nokia sported an impressive operating margin of over 20%, which for large scale electronic hardware business is extremely unusual. That big margin and the huge and growing revenue base supported a far larger R&D budget than any peer could support towards the next generation of cellphones. That next generation

of cellphones clearly included ones with a broader array of capabilities than the rudimentary address book software and a few odd ringtones that the vintage 2000 Nokia phones came with. To this end Nokia invested heavily in a "smartphone" operating system called Symbian which sought to embed a broader degree of operating capabilities in future phones. So - a dominant market position, unmatched profitability and resources, and a clear view toward the future - what could possibly go wrong?

Ten years later, a lot is going wrong. Somehow the Symbian venture just never had enough clarity as to what kind of device and software environment it needed to create. The core innards of a cellphone are a largely commodified set of design specifications, and a handful of companies that do software well and that can bring other applications into the sphere of the mobile telephone can graft that capability onto the commodified cellphone guts. The most notable success is Apple, which has bundled an iPod and a smartphone into just one device, and is deleting Nokia out of the consciousness of their core consumer base. A paradigm shift from a basic cellphone to a broader software-enabled "smartphone", has wiped away the core advantages Nokia clearly possessed. From an investment perspective, one needed to recognize both how rapidly a smartphone with the right blend of software and hardware capabilities could envelop the marketplace, and how vulnerable the old guard would be.

About a year ago, I got my hands on the first popular iteration of an "eReader" in the form of an Amazon Kindle. As compared to a notebook PC, there is a good deal less technology embedded in this device, but for the narrow purpose of its design - to read text - one does not need a lot of computational power. It's a brilliant idea that had a lot of potential for innovation and disruption. But the history of technology is littered with brilliant ideas whose first inventors fail commercially as others simply barge them out of the way with more robust offerings. The Kindle looks like it will be part of that list - more functional, more broadly integrated and more smartphone-like eReaders ought to leapfrog the Kindle. And this is what is happening since the release of Apple's iPad which stands at a unique crossroad between a phone, an ebook, a mobile PC, and other consumer electronic devices. Nobody really knows yet what to call it - a "Super eReader"? Plenty of praise has been heaped upon this contraption already in the popular press, and I'll heap some of my own on to it - it is wicked cool and wicked dangerous to the established order.

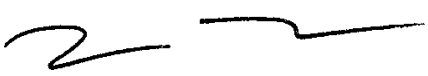
The most dangerous technological developments to investors are "alpha" technologies. These are devices or systems that have a frequent habit of cheaply subsuming other device categories much the way a Swiss Army Knife incorporates a multitude of tools. Smartphones are one such alpha device. A medium quality 2010 smartphone subsumes a digital camera, a computer email system, an mp3 player, an electronic organizer, a pager, and of course, offers immense utility as a mobile phone. In so doing, it quietly devours these adjacent industrial ecosystems and is highly value destructive from an investor's perspective. The roughly 15 year old internet has been an alpha medium (as opposed to a physical device) and is rapidly subsuming all manner of older forms of media, such as newspapers, television, filmed entertainment, and other periodicals, and as well as the enterprises that produce and distribute such media. The printed word still retained value up to 18 months ago in the form of books, where a good substitute technology did not yet exist. No longer is that the case. It is challenging to see the humble paper-based book holding up to the onslaught of digital equivalents it will face in eReader and Super-eReader forms.

Not all that far down the road, it is not so far-fetched to see the whole PC-based technology ecology threatened by some form of Super eReader, whether made by Apple or other companies. Whatever version winds up on top, it has all the earmarks of a highly disruptive alpha technology device, and one that may be broadly value destructive to adjacent technology ecosystems. In this case, it would incorporate PC and smartphone functions into one small and easily portable package. And the PC is vulnerable, not for a lack of functionality, but for a surplus of it. A 2010 vintage PC is an exercise in technological overkill. It has the computational power of a 1990's multi-million dollar mainframe system, staggering graphical capacity, and with visual display costs deflating rapidly, a screen that can be as big as one wants. Yet a PC's main use in offices and in homes is as an email terminal, a repository of music and photos, as a typewriter, web browser, and an organizer - none of these applications exploit the billions of instructions per second that a $1,000 PC can process. For a modest cost, the PC offers such high utility that there has not been much reason to consider alternatives. The 2010 vintage iPad might not yet be the device that displaces the very PCs that displaced so many other contraptions that preceded them, but it is awfully threatening, and this device too will keep evolving rapidly through a highly competitive and iterative process. It may incorporate a few others that can't yet be well anticipated, such as interactive textbooks that integrate conventional books and animations and speech (one can imagine some kind of hybrid between a book and a lecture or video entertainment). Soon, the cost of embedding a Super-eReader with the raw silicon power of a 2010 vintage PC will be trivial, and as this is already more than most persons can realistically use, PC

makers go on to flounder in superfluity. You just have to wonder, in a very 1990s sort of way, exactly how far this could go? All one would have to do is dock the Super eReader onto a cradle that connects to a screen and a keyboard, and a PC, a home entertainment system, a library, and a gaming console all come to life.

When an alpha technology device or category emerges, investors need to process quickly the apparent winners and losers. It's the established order that has the most to lose. Witness the fates of IBM, Digital Equipment, Sperry, Burroughs, Sun Microsystems, and Tandem Computer at the dawn of the PC era. Only IBM still survives by having transformed itself into a services-driven company. PCs are today the largest of all technology categories by revenue, profit, and capitalization if one added up these items for giants such as Microsoft, Intel, Dell, Hewlett Packard, and many others. It is not implausible to see these highly profitable giants standing in 2010 where Nokia resided 10 years ago: blessed with all the advantages of scale, profitability, and resources, riding a crest of demand and impressive profitability, yet poised to be bowled over by forces they just cannot control. The winners of an alpha technology displacement are not so easy to identify, as early movers don't always retain core advantages (witness Amazon's Kindle, for instance). The early winner circa 2010 looks like Apple (AAPL), but will it face a deflationary onslaught from copycats? It is hard to say, and Apple's corporate governance as it relates to shareholders leaves much to be desired. To the extent that one can identify key suppliers of value-added components and systems, this may be the safest way to proceed. We are invested in Corning (GLW) a leading supplier of glass screens, and Applied Materials (AMAT) which supplies chipmakers with vital technologies needed to create next generation technologies, and are presently evaluating a number of other core technology possibilities where substitution to alternatives would prove difficult. It is worth noting that Cambiar has held equity investments in Microsoft and Intel over the past year; however we believe we have seen the future and it may prove uncomfortable for the old guard. As a result, we would anticipate appropriate adjustments to such positions in the future.

Thank you for your continued confidence in us.



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About the Author

Brian Barish is the President and Director of Research of Cambiar Investors and is responsible for the oversight of all investment functions at the firm. Mr. Barish has over 21 years of investment experience. His primary analytical responsibilities include company coverage within technology, autos, tobacco and aerospace & defense. Prior to joining Cambiar in 1997, Mr. Barish served as Director of Emerging Markets Research for Lazard Freres & Co., a New York based investment bank. He also worked as a securities analyst with Bear, Stearns & Co. and Arnhold & S. Bleichroeder, a New York based research firm. Mr. Barish received a BA in Economics and Philosophy from the University of California, Berkeley, and holds the Chartered Financial Analyst designation.

Cambiar Investors

Cambiar Investors, based in Denver, Colorado, is 100% employee owned with over $5 billion in assets under management (as of 3.31.10). Cambiar's investment process focuses on unbiased fundamental research. Our concentrated, opportunistic approach has demonstrated the ability to outperform in a variety of market environments. Cambiar's investment philosophy is implemented across four strategies: Large Cap, Small Cap, International Equity, and Global Multi-Cap Value.

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