



## UPDATE ON DIAMOND HILL STRATEGIC INCOME FUND

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## Update on Diamond Hill Strategic Income Fund

The unwinding of leverage in the financial markets has accelerated dramatically in recent days culminating in the New York Fed's intervention on behalf of Bear Stearns (a 0.0% position as of 2/29/08) on Friday. Even firms with high quality assets have been brought to (and in some cases past) the brink of insolvency because their lenders have forced the sale of assets into inhospitable markets. This has led to yet another intense wave of fear with spiking volatility and significant declines in the prices of stocks, corporate bonds, and most other risk-based assets.

It is likely that the economy is in recession, house prices will continue to decline, and defaults on all sorts of credit instruments will accelerate in coming months. Markets, however, are forward looking and they will almost certainly begin to discount (not necessarily good but) better days well before the worst is over in the real economy. We believe that the securities that we are concentrated in – preferred securities, corporate bonds, bank stocks- will do quite well when the markets begin to look beyond the point of maximum uncertainty and fear.

Progress has been made on the factors that we have been looking for to signal a better environment. Financial institutions have recognized or forecasted substantial losses and raised capital to offset a good portion of those losses. The roughly 10% decline in home prices has improved affordability although lower prices and/or lower interest rates will be required to return affordability to the long run average. While the Federal Reserve is faced with an enormously complex and difficult task, it has developed several unique initiatives designed to stabilize the debt markets and to bring down the cost of financing for home owners. Congress now seems well aware of the issues and likely to contribute to a solution if necessary. The risk-adjusted yields on many credit instruments (preferred securities, corporate bonds, leveraged loans, municipal bonds) are now well above the bogies required by many investors with (and this is the key point) either no or very low levels of leverage. The turning point may only require a shift in psychology, the timing and proximate cause of which nobody knows.

As the managers of an unleveraged portfolio with a long-term time horizon, we can step back from the inevitable day-to-day anxiety to better position the portfolio. Since the end of the year, we have decreased our preferred exposure from 43% to 39%. More importantly, within the preferred portfolio, we have sold a number of smaller, lower quality issues and replaced them with new issues such as M&T Capital Trust IV 8.5% (a 1.5% position as of 2/29/08), Xcel Energy 7.6% (a 1.5% position as of 2/29/08), Duke Realty 8.375% (a 1.1% position as of 2/29/08), and PNC Capital Trust 7.75% (a 1.5% position as of 2/29/08). We have increased our corporate bond allocation this year from 26% to 35%. The option adjusted spread of the Merrill Lynch Cash Pay, BB Rated Index is currently 590 basis points, up from 201 basis points one year ago and 458 basis points at the beginning of 2008. We have added positions in such corporate bonds as Freeport-McMoRan 8.25%, Due 04/1/2015 (a 2.7% position as of 2/29/08), Trinity Industries 6.5%, Due 3/15/2014 (a 1.2% position as of 2/29/08), and Xerox 7.625%, Due 6/15/2013 (a 1.5% position as of 2/29/08). Finally, we sold the common stocks of two commercial finance REITs early in the year and added to our positions in the common stocks of US Bancorp (a 1.4% position as of 2/29/08), Wells Fargo (a 1.3% position as of 2/29/08), Wachovia (a 1.2% position as of 2/29/08), Huntington (a 1.4% position as of 2/29/08), and Synovus (a 1.3% position as of 2/29/08). We still have 15% in cash and two callable agency securities.

We appreciate your continued support of the Diamond Hill Strategic Income Fund.



Kent K. Rinker



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### Diamond Hill Investments

Investors should consider the investment objectives, risks, charges, fees and expenses of the Diamond Hill Funds carefully before investing; this and other information including fund performance and a prospectus can be obtained at [www.diamond-hill.com](http://www.diamond-hill.com). Read the prospectus carefully before you invest. Fund Holdings are subject to change without notice. The value of fixed-income securities varies inversely with interest rates; that is, as interest rates rise, the market value of fixed-income securities will decline. Lower quality debt securities involve greater risk of default or price changes due to potential changes in the credit quality of the issuer. Diamond Hill funds are not FDIC insured, may lose value, and have no bank guarantee. Distributed by IFS Fund Distributors, Inc., Member FINRA/SIPC, 303 Broadway, Suite 1100, Cincinnati, Ohio 45202.

**EXHIBIT A**

The table below includes the historical returns for the Diamond Hill Strategic Income Fund.

		<b>Period &amp; Annualized Returns as of 2/29/2008</b>					<b>Total Expense Ratio</b>
<b>Fund / Benchmark</b>		<b>1 Month</b>	<b>1 Year</b>	<b>3 Years</b>	<b>5 Years</b>	<b>Life of Fund</b>	
<b>Strategic Income Fund</b>		<b>Inception Date: 9/30/2002</b>					
<b>Class A</b>	<b>NAV</b>	<b>-2.26%</b>	<b>-4.49%</b>	<b>2.83%</b>	<b>6.64%</b>	<b>7.66%</b>	<b>1.10%</b>
	<b>POP</b>	<b>-5.64%</b>	<b>-7.83%</b>	<b>1.62%</b>	<b>5.89%</b>	<b>6.96%</b>	<b>1.10%</b>
<b>Class C</b>	<b>NAV</b>	<b>-2.40%</b>	<b>-5.22%</b>	<b>2.06%</b>	<b>5.83%</b>	<b>6.96%</b>	<b>1.85%</b>
	<b>POP</b>	<b>-3.37%</b>	<b>-6.11%</b>	<b>2.06%</b>	<b>5.83%</b>	<b>6.96%</b>	<b>1.85%</b>
<b>Class I</b>	<b>NAV</b>	<b>-2.22%</b>	<b>-4.10%</b>	<b>3.26%</b>	<b>6.90%</b>	<b>7.90%</b>	<b>0.71%</b>
Merrill Lynch Domestic Master Index		0.38%	7.98%	5.43%	4.65%	4.88%	--

*The performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Investors should consider the investment objectives, risks, and charges and expenses of the Diamond Hill Funds carefully before investing. This and other information about the Funds is in the prospectus, which can be obtained at [www.diamond-hill.com](http://www.diamond-hill.com). Read the prospectus carefully before you invest. The Funds' current performance may be lower or higher than the performance data quoted. To obtain performance information current to the most recent month-end, please visit [www.diamond-hill.com](http://www.diamond-hill.com) or call 1-888-226-5595.*

**Performance is not guaranteed.** Performance returns assume reinvestment of all distributions. Average annual total returns illustrate the annual compounded returns that would have produced the cumulative total return if the Fund's performance had remained constant throughout the period indicated. Returns for the periods less than one year are not annualized. These total return figures may reflect the waiver of a portion of a Fund's advisory or administrative fees for certain periods. In such instances, and without such waiver of fees, the total returns would have been lower. The maximum sales charge is 3.50%. The investment return and net asset value will fluctuate, so that an investor's shares, when redeemed, may be worth more or less than the original purchase price. Diamond Hill Funds are distributed by IFS Fund Distributors, Inc., Member FINRA/SIPC, 303 Broadway, Suite 1100, Cincinnati, Ohio 45202.

As of April 30, 2009, BHIL Distributors, Inc. (Member FINRA) became distributor for its affiliate, the Diamond Hill Funds.

Information contained herein is intended as a snapshot as of the date of this investment letter and is retained for historical reference only and should not be relied upon for current information. For current fund information, please go to [www.diamond-hill.com](http://www.diamond-hill.com).