DIAMOND HILL
investments

April 7, 2006

Dear Fellow Shareholders,

2005 was an extraordinary year for our business in virtually all respects:

- Excellent investment returns for our clients;
- Strong growth in assets under management from $524 million to $1.5 billion; and
- Solid profits from operations, achieving a 15% operating profit margin.

Our foremost objective is to fulfill our fiduciary duties to our clients. We seek to meet this objective by achieving excellent returns with our investment strategies. While we are pleased that client returns in 2005 essentially met our criteria for success in this area, we remain focused primarily on returns for rolling five-year periods to meet the following criteria:

- Sufficiently above relevant passive benchmarks,
- Ranking in the top quartile of similar strategies, and
- Absolute returns sufficient for the risk associated with the asset class.

Our next objective is to fulfill our fiduciary duties to our owners. Here too, the goal is straightforward: to grow the intrinsic value of the business at a rate sufficient for the risk associated with a business venture like ours. (In last year's letter, we discussed at length the concept of estimating intrinsic value.)

Since the inception of our effort in May 2000, our estimate of the intrinsic value of the business has at least tripled (perhaps growing considerably faster than that), which was sufficient for the risk associated with the business given the circumstances at the time. Today, our business is well established, due to the accomplishments during the past six years. Therefore, achieving a growth rate in intrinsic value that results in its doubling over the next five years should be considered sufficient. Please remember that a company's intrinsic value is frequently not equal to its stock price. We certainly are interested in the stock price, but we cannot directly impact it. However, we can directly impact intrinsic value and hopefully, over time, the stock price will reflect the intrinsic value of our business.

For investors in any business, it is always important to avoid paying a price higher than their estimate of intrinsic value. Doing so can result in an insufficient risk-adjusted return. Over the short term, stock prices change based largely on investor psychology. Over the long run, economics determine an investor's return, specifically:

- The investor's purchase price;
- The growth in the intrinsic value per share;
- Dividends received during the holding period;
- The investor's selling price.

This describes the investment philosophy we utilize in our investment management business.
For our clients, our value proposition is:

- We are experienced investors;
- We use this intrinsic value discipline for our various strategies; and
- We align our interests with our clients through our personal investments in our own mutual funds and private investment partnership.

In previous annual letters, we have discussed our goal of reaching a level of assets under management ("AUM") sufficient for "scale," defined by operating profit margins of 30%. This level of profitability is consistent with industry norms for large firms in our industry, and represents an implicit division of the business economics between employees and shareholders.

In 2005, we achieved a 15% operating profit margin, with less than $1 billion of average AUM. This occurred due to an unusually large percentage of our revenues derived from our private investment partnership's incentive fee. While it is doubtful that in 2006 a similar contribution to the revenue mix comes from this source, growth in overall AUM should result in further margin improvement, with our current goal to reach the 30% threshold in 2007 and beyond.

Our overall growth in AUM and profitability has been led by our funds, Small Cap and Long-Short in particular. The closing of our Small Cap Fund to new investors occurred at year end. Restricting its growth is intended to help assure our ability to achieve our aforementioned five-year return goals. Devoting resources to expand our separately managed accounts ("SMA") business, while starting two new mutual funds, are efforts intended to help grow AUM to $3-5 billion over the next five years.

I would like to thank my colleagues and our Board of Directors for their efforts and support. All of us at Diamond Hill Investment Group will continue our mission to build an excellent investment management firm for clients and owners alike.

Sincerely,

Ric

R. H. Dillon
President and Chief Executive Officer