PABRAI INVESTMENT FUNDS

To: All Limited Partners of The Pabrai Investment Funds

From: Mohnish Pabrai, Managing Partner

Date: October 15, 2002

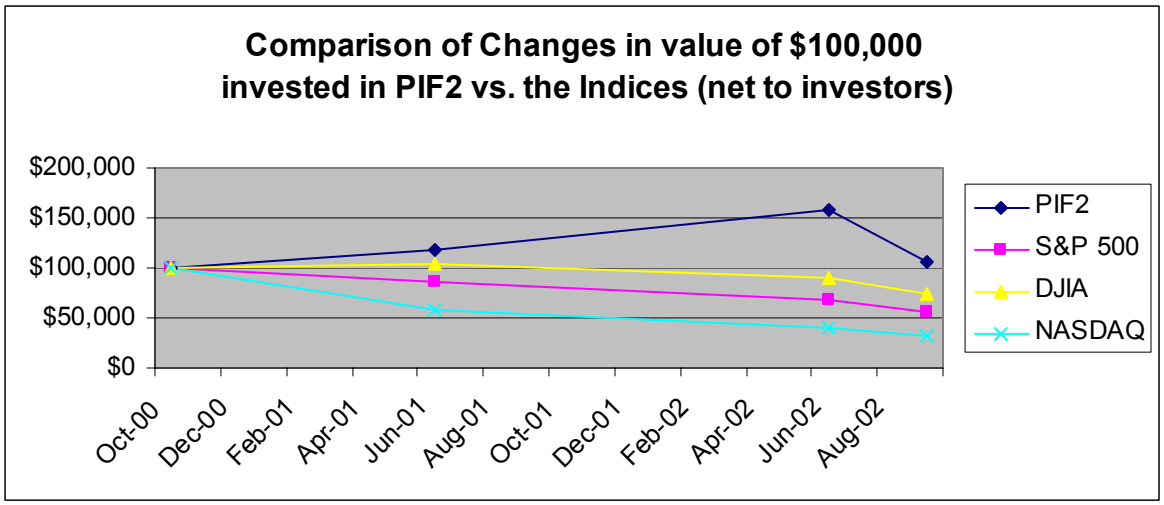
Re: **Updated PIF2 Performance Data**

Dear Partners:

We had $225,000 in new funds added to PIF2 on 10/1/02 by existing partners. Per fund rules, updated NAV numbers are released anytime there are subscriptions or redemptions and at fiscal year end. Here are the updated NAV numbers on PIF2 as of market close on 9/30/02.

PABRAI INVESTMENT FUND 2 Performance Summary:

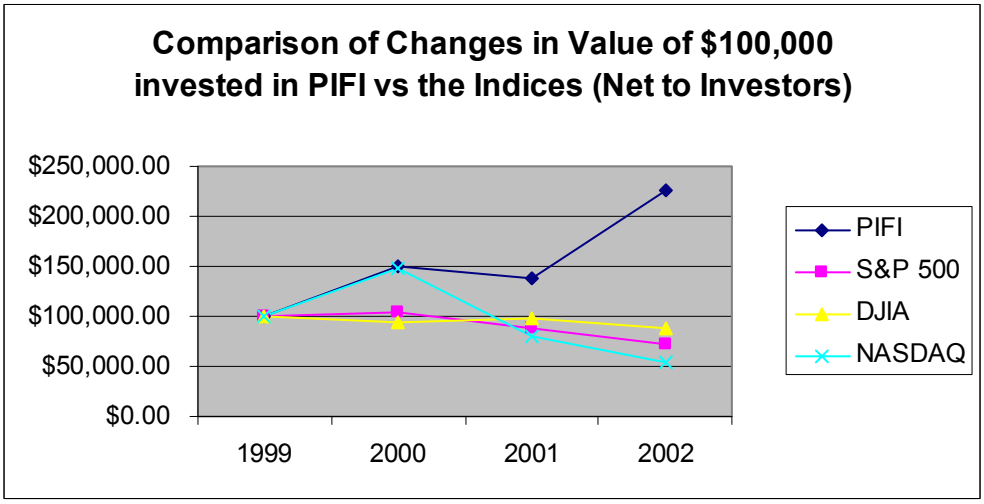
	DJIA	NASDAQ	S&P 500	PIF2 (before exp.)	PIF2 (after exp.)
10/1/00 – 6/30/01	**+4.6%**	**-41.2%**	**-14.8%**	**+20.9%**	**+17.4%**
7/1/01 – 6/30/02	**-14.2%**	**-32.3%**	**-19.1%**	**+42.7%**	**+35.3%**
7/1/02 – 9/30/02	**-17.0%**	**-19.9%**	**-17.6%**	**-33.9%**	**-32.7%**
Year to Date	**-22.6%**	**-39.9%**	**-28.9%**	**-26.5%**	**-26.2%**
Annualized	**-13.7%**	**-43.5%**	**-24.6%**	**+6.8%**	**+3.4%**
Cumulative	**-25.5%**	**-68.1%**	**-43.2%**	**+14.0%**	**+7.0%**



For completeness of the track record I am also including the last published performance numbers PIFI and PIF3.

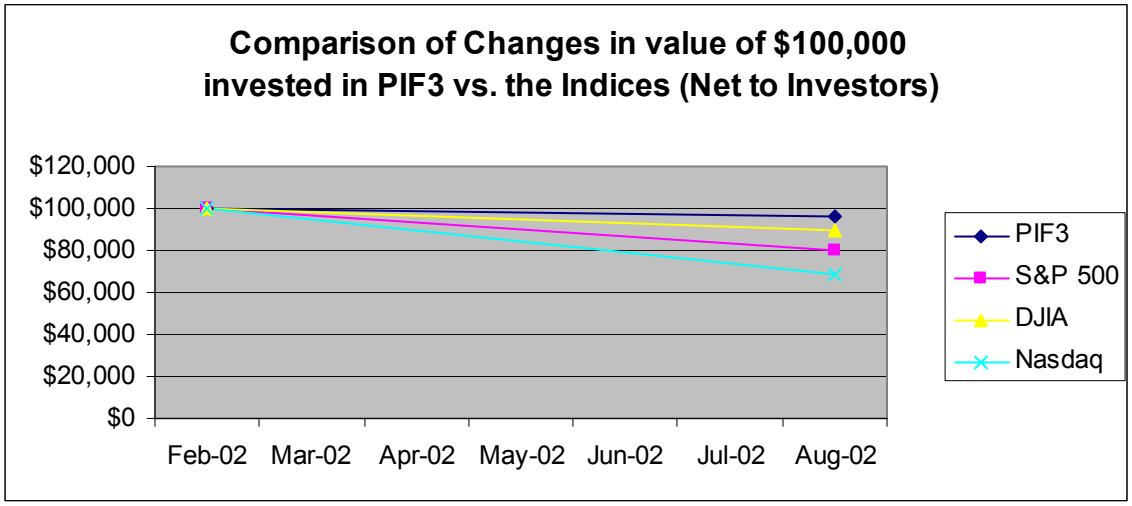
PABRAI INVESTMENT FUND I (closed) Performance Summary:

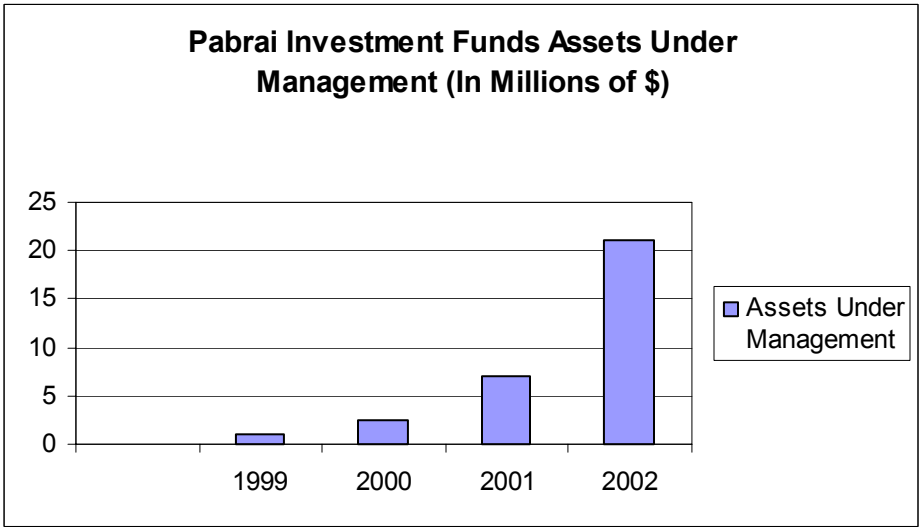
	DJIA	NASDAQ	S&P 500	PIFI (before exp.)	PIFI (after exp.)
7/1/99 - 6/30/00	**-4.7%**	**+47.3%**	**+4.7%**	**+62.5%**	**+50.1%**
7/1/00 – 6/30/01	**+2.2%**	**-45.5%**	**-15.9%**	**-7.7%**	**-8.3%**
7/1/01 – 6/30/02	**-10.0%**	**-32.3%**	**-19.2%**	**+76.6%**	**+63.6%**
Annualized	**-4.3%**	**-18.4%**	**-10.7%**	**+38.3%**	**+31.1%**
Cumulative	**-12.3%**	**-45.7%**	**-28.9%**	**+164.5%**	**+125.4%**



PABRAI INVESTMENT FUND 3 Performance Summary:

	DJIA	NASDAQ	S&P 500	PIF3 (before exp.)	PIF3 (after exp.)
2/1/02 – 7/31/02	**-10.3%**	**-31.5%**	**-19.6%**	**-2.1%**	**-3.5%**
Annualized	**-19.5%**	**-53.0%**	**-35.4%**	**-4.2%**	**-6.9%**
Cumulative	**-10.3%**	**31.5%**	**-19.6%**	**-2.1%**	**-3.5%**





Even the not so diligent reader will notice that PIF2 experienced a significant decline in NAV for the last two months (-21.4%), the last quarter (-32.7%) and year-to-date (-26.2%). The broad market and indices all experienced significant drops during the same periods – down

10-12% in the last two months, down 17-20% in the last quarter and down 22-40% year-to-date.

I'd like to share my perspectives on the numbers:

1. Whenever the broad market and indices undergo big drops over short timeframes, we are likely to drop as well. In fact, due to our concentrated and smaller market caps holdings with relatively thin trading volumes (some have zero trading volume on some days), we are likely to lag the market and experience bigger short-term declines. In the last quarter, we had especially big drops in prices of some of our holdings with the lowest trading volumes. In some of these stocks, a single panicked seller can lead to a big price drops in the short-term.

2. Eventually stock prices do get to trading around their intrinsic value. Our portfolio is presently at an all-time record discount to intrinsic value. By my estimation the market has presently valued PIF2 at about 34% of its conservative intrinsic value. This is the widest discount to intrinsic value I've seen since the inception of the funds. I have no idea *when* this gap will close, but am confident that this gap will eventually shrink substantially – leading to satisfactory long term result for all of us.

3. I'm probably preaching to the choir, but I do hope you evaluate PIF2 or any other fund you're invested in on their long-term track record. The nature of markets, unfortunately, does not insulate us from short-term gyrations. One of funds worth looking at on this front is Sequoia Fund (www.sequoiafund.com) founded by Bill Ruane in 1970. Some of the Berkshire shareholders are probably familiar with Bill Ruane.

   When Buffett terminated his partnership in 1969, his partners had the dilemma of what to do with the money. The only fund manager Buffett suggested that his former partners invest with was Bill Ruane's Sequoia Fund. Ruane and Buffett had worked together at Ben Graham's firm in the early 1950s. It turns out that it was just unbelievably good advice. Sequoia Fund has generated one of the best long-term track records of any mutual fund. In the last 32 years, they've average a 16.55% annualized rate of return. A $10,000 investment in 1970 is worth about $1.4 Million today versus $316,000 for the S&P 500.

However, if you had taken Buffett at his word and invested in the Sequoia Fund in 1970, here is the experience you would have had over the next 5 years:

	Sequoia Fund	**S&P 500**
12/31/70*	12.11%	20.60%
12/31/71	13.64%	14.29%
12/31/72	3.61%	18.98%
12/31/73	-24.80%	-14.72%
12/31/74	-15.48%	-26.52%

* From inception on 7/15/1970

It is amazing that the stellar Graham-trained Ruane/Cunniff team managed to lag the S&P 500 4-years in a row and were down another 15% in the 5th year. Their 5-year record was a total return of -10% versus a net positive return for the S&P 500 of 7.4%.

In 1975, the Sequoia Fund investors had just the last 5 years of data to go by and that was quite lackluster. One could not be faulted for seeking a better fund manager than Ruane in 1975. Of course the next 27 years were just stellar, but it just goes to show how markets can make even outstanding fund managers look terrible for what many might consider long-term.

I am not trying to draw any comparisons between Sequoia Funds and Pabrai Funds or to imply that we expect to lag the S&P 500 for the next several years. Merely want to illustrate the point that when evaluating fund managers, its best to do a look back going as far back as you can and not fixate on quarterly or year-to-date numbers.

4. Over the long haul, I do expect that we'll continue to meet or exceed our stated objectives of beating the three indices over the long haul – leading to a satisfactory result for all of us.

Alignment of Interests

To date, I have always reinvested all its fees back into the partnerships. Dalal Street, the investment manager that I own, has 84,833.03 units of PIF2 and 37,993.95 units of PIFI. Based on last published NAV, this stake is worth $909,410.08 + $856,383.63 =

$1,765,793.71. Thus I have a deep vested interest in the future performance of The Pabrai Funds. When you win, I win. Our interests are completely aligned.

Future investment management fees are only payable to Dalal Street after we are at a all time high for the respective funds (plus 6% annualized from the date of the last high). The PIF2 NAV needs to above about $18/unit (currently at $10.72) before any fees are payable to me. It is thus probably comforting to note that PIF2 will be sporting one of the lowest expense ratios for equity funds. I expect our expense ratio to be below 0.30% annually - which is probably lower than virtually any managed equity mutual fund or hedge fund in the world. It also compares well to the ultra low 0.18% fee for the Vanguard S&P 500 Index fund (VFINX) – especially when you consider that VFINX is an unmanaged index fund with $64 Billion in assets compared to our actively managed $14 Million.

Annual Meeting

The Pabrai Funds annual meeting held on Sept. 14, 2002 was a big success. We had over 80 attendees (up from 46 last year) and an engaging question and answer session. I enjoyed meeting many of the partners that I had never met before and folks enjoyed getting to know each other. For the benefit of partners who were unable to attend, I have put the powerpoint presentation and the transcript of the meeting on our website (http://www.pabraifunds.com) under "Articles & Speeches".

Lots of good data and good questions. I encourage you to view the presentation and read the accompanying transcript. Next year's meeting is scheduled to be on Saturday, Sept. 13, 2003 at 4:00 PM at the same venue:

Carlucci's Restaurant, 6111 North River Road, Rosemont, Illinois 60018
Tel. +1847.518.0990

Please put it on your calendar!

Speech at Northwestern University's Kellogg School of Management

For those who are in the Chicago area, I wanted to let you know that I'm speaking on **Wednesday, Oct. 30, 2002** to the Investment Management Club at Kellogg from **5:00-6:30 PM**. You're welcome to attend. Just utter the magic words, "Friend of Mohnish", at the door and they'll let you in. The price is right – it's free.

Northwestern University
Kellogg School of Management
Donald P. Jacobs Center, Room 101 (right inside the main entrance to Kellogg).
2001 Sheridan Road
Evanston, IL 60208

The topic is "**Latticework: Worldly Wisdom, Mental Models & Investment Success**"

This presentation will explain the basic components of developing a personal investment strategy and present one methodology, The Latticework of Mental Models, for in-depth discussion. With over 90+% of investment managers, mutual funds and hedge funds consistently lagging the broad market indices like the S&P 500, a very strong case has been built on simply investing in index funds and not trying to beat the market.

While indexing is a very valid approach, there are still the other 10% of managers who are able to beat the market and a small minority of them has beaten it by wide margins over long periods of time (Warren Buffett, Charlie Munger, Peter Lynch, John Templeton, Seth Klarman, Marty Whitman, Bill Nygren etc.).

During the evening, I'll delve into Charlie's Munger's notion of the Latticework Mental Models and Worldly Wisdom and contrast it with the nuances of The Efficient Market Theory (EMT) and Modern Portfolio Theory (MPT) - to explain why some of these managers are consistently able to beat the market.

Finally, I will present his opinion on why applying the Latticework of Mental Models in a disciplined manner would enable virtually every individual investor to improve their investment returns noticeably. I've given a similar talk to other groups over the last year and it has been well received. I encourage you to try to attend.

Minimum Investment Amount for New Partners

We added no new partners - keeping the total US-based partners at 82. We are limited to 100 US partners by law. The minimum investment to join the funds as a new partner thus remains unchanged at $400,000. The next opening of 12/1/02. Existing partners can add funds in increments of $25,000 at each opening (with a $25,000 minimum). This does not apply to our offshore investors. PIF3 is setup as an offshore mutual fund limited to non-US accredited investors. The minimum investment for new PIF3 is always $100,000.

Merging PIFI and PIF2

All the PIFI and PIF2 partners should have received their ballots and merger documents by now. We've gotten several of them back from the partners with their votes. Please remember to send them in so they arrive in our offices no later than 10/31/02. The merger, if approved, will lead to a further reduction in our expense ratio starting from 2003. Excluding investment fees (which are not payable until the fund is at a historical all-time high), I expect our expense ratio for the merged fund to be under 0.25% of assets under management.

Thanks for your continued interest, referrals and support.

Warm Regards,

Mohnish Pabrai

Appendix A

PIF2 NAV and Performance Fees and Expenses Since Inception.

Per the Sept. 30, 2002 custodian and bank statement, the value of PIF2 assets is **$14,046,030.** The cash expenses incurred by PIF2 through September are legal, accounting and administrative expenses totaling $58,304.42. The NAV before fees and expenses is **$14,104,334.42 or $11.40/unit.** In other words, PIF2 is up **14.0%** since inception two years ago before fees and expenses - or an annualized rate of **6.8%**

NAV after all expenses is $14,032,747.11 or **$10.70/unit.**

The previous NAV high after fees is $17.43 set on 6/1/02. Since the NAV is below the previous historical high, there is a no fee is payable to Dalal Street (General Partner) at this time. PIF2 is up **7.0%** since inception twenty two months ago AFTER all fees and expenses - or an annualized rate of **3.4%.**

$225,000 in new funds came in on 10/1/02 resulting in 21,028.04 units being issued.

Total units outstanding as of 10/1/02 are **1,332,192.10**

PIF2's Performance BEFORE and AFTER fees and expenses vs. the Indices.

No. of Units	Date	PIF2 NAV Pre-Exp.	PIF2 NAV Post-Exp.	S&P 500	S&P 500	DJIA	DJIA	NASDAQ	NASDAQ
110000	10/1/2000	$10.00	$10.00	$10.00	1436.51	$10.00	10650.92	$10.00	3672.82
330014	6/30/2001	$12.09	$11.74	$8.52	1224.42	$10.46	11140.05	$5.88	2160.54
1027795	6/30/2002	$17.25	$15.89	$6.89	989.82	$8.98	9563.39	$3.98	1463.21
1311203	7/31/2002	$14.73	$13.62	$6.35	911.62	$8.50	9056.72	$3.62	1328.26
1332231	9/30/2002	$11.40	$10.70	$5.68	815.28	$7.45	7939.11	$3.19	1172.06

PIFI's Performance BEFORE and AFTER fees and expenses vs. the Indices.

No. of Shares	Date	PIFI NAV Pre-Fees	PIFI NAV Post-Fees	S&P 500	S&P 500	DJIA	DJIA	NASDAQ	NASDAQ
100000	7/1/99	$10.00	$10.00	$10.00	1391.22	$10.00	11,139.24	$10.00	2692.96
164453	6/30/00	$16.25	$15.05	$10.47	1456.60	$9.53	10,613.49	$14.73	3966.11
230480	6/30/01	$14.97	$13.78	$8.80	1224.42	$9.74	10,847.09	$8.02	2160.54
216027	6/30/02	$26.45	$22.54	$7.11	989.82	$8.77	9,773.40	$5.43	1463.21

PIF3's Performance BEFORE and AFTER fees and expenses vs. the Indices.

No. of Units	Date	PIFI NAV Pre-Fees	PIFI NAV Post-Fees	S&P 500	S&P 500	DJIA	DJIA	NASDAQ	NASDAQ
65100	1/25/2002	$10.00	$10.00	$10.00	1133.28	$10.00	9840.08	$10.00	1937.70
255836	3/29/2002	$11.39	$11.01	$10.12	1147.39	$10.62	10446.55	$9.52	1845.35
289769	7/31/2002	$9.81	$9.64	$8.04	911.62	$8.97	8828.85	$6.85	1328.26

Note: The source for the indices data is Barron's. The DJIA data includes dividends. The S&P 500 and Nasdaq numbers exclude dividends as Barron's does not provide historical dividend data for the S&P 500 and Nasdaq Composite. PIFI and PIF3 performance numbers are dated since The Pabrai Investment Funds only releases performance data annually at fiscal year end for all funds. The only exception is whenever there are subscriptions or redemptions for a given fund. Thus PIFI and PIF2 performance is updated and PIF3 is not.

Past performance is not indicative of future results. Returns are presented net of all fees and expenses, include the reinvestment of income and are calculated using a simple rate of return. The securities discussed do not represent all securities recommended for the Funds. It is also not a recommendation to buy or sell and one should not presume they will be profitable.

Please be aware that our past newsletters may discuss specific securities that have performed well without necessarily addressing those that have underperformed within our Fund(s). Readers should not infer that all investment decisions within the Funds were profitable.