

January 4, 2006



## 2005 Fourth Quarter and Year in Review

Our investments yielded very respectable returns even though the market indexes were flat for the year. The DOW ended up in negative territory while the NASDAQ grew at only 1.37% and the S&P500 at 3.02%. However, the average of all our clients' accounts increased by **11.7%** net of all fees. Additionally, dividends were earned in December that will not be paid until January 2006. If we factor in those dividends, our dividend adjusted average return shoots up to **13.8%** net of all fees.

This is exceptional due to the fact that we were mostly in cash for approximately four months during the year. Although we prefer to be fully invested, by staying in cash until a good opportunity presents itself, we can reduce risk and still achieve desired results for our clients.

In the first quarter of 2005, the DOW hit a high and then began to severely correct. We heeded its warning and closed out positions in Yahoo and Cornerstone Realty. We took a loss on Yahoo and a gain on Cornerstone (adjusted for dividends). Our holdings in Alliance Capital Fund looked overvalued so they were sold and we took our gains. Shortly after selling Alliance, the fund dropped on a huge correction.

Feeling uncomfortable with the equity market, we turned our sights to the bond market. We began making significant purchases back into Alliance because we now felt that they were undervalued. Our target purchase price of Alliance was \$8.00. We continued making purchases throughout the second quarter each time the fund dropped down to our target price. By August the fund had increased by 5% and was paying a monthly dividend of .67%. Based on patterns we had observed over the previous two years, we anticipated another sell off. Therefore we unloaded our entire position just before the price dropped back down to \$8.00 again. Although we wanted to get back into the fund when it dropped back to our original target price, better opportunities had arisen and we focused on them.

During the third quarter, our holdings in Thoratec and Ameritrade really took off. However, in October, they both dropped below their 50day moving-average on heavy volume. Historically, that is a very bad sign and with the entire stock market taking a beating, we decided to cash in our holdings. We broke even on Thoratec and scored a 29% gain on Ameritrade.

Our latest opportunity arose in early December. The mortgage industry had been severely pummeled with rising rates and a slowing demand. Many mortgage stocks lost nearly 50% of their value during 2005. It was this environment that we began tracking Novastar Financial in earnest. Their dividend yield was up to a whopping 20% due to the fall in their stock price. Many pundits were forecasting further declines and questions about their ability to continue paying their dividend added to the uncertainty. After we meticulously studied their financial statements, chart pattern, projections, and industry



norms, we felt that the stock price would probably not decline much further. Additionally we felt confident that Novastar had the capacity to continue to pay their dividend of \$5.60 per share. Therefore, we made a substantial purchase in early December. In late December, Novastar announced that they would in fact continue paying their \$5.60 dividend and their stock price jumped 10%. While we considered selling out and cashing in on the 10% rise, we were not so sure that the stock price would come back down and allow us to get back in with a 20% dividend yield. Therefore we held our position and, barring any surprises, will reap a 20% annual yield on our investment.

I hope you have found this analysis informative and meaningful. If you have been happy with your returns, we would challenge you to refer at least one new client to us this year. In the investment world, referrals are the best way to grow a business. As always, we are actively seeking prospective investments and will react quickly to the changing market environments.

Happy New Year!

Sincerely,

A handwritten signature in blue ink, appearing to read "Jonathan Davey", is written over a horizontal line.

Jonathan Davey, CPA MBA  
President