



January 4, 2007

2006 Review & Analysis

We had another fantastic year with the average account increasing 11.5%, net of all fees. However, if we only evaluate those funds that we were able to invest for the full year (January 1 to December 31), then our average return jumps to an impressive 17.3%, net of all fees. This is even an improvement over last year's respectable 16.6% return.

As will be discussed later, we held the majority of our funds in cash waiting for the right opportunities and then moving heavily on those opportunities while they lasted before retreating back to the safe haven of cash. As always, we consider timing to be crucial for our long-term growth and do not want to be invested in stock simply because everyone else is. As conservative investors, we want to be 70% confident that our investments will positively perform. If we fall below that comfort level, then we prudently move our holdings back into cash.

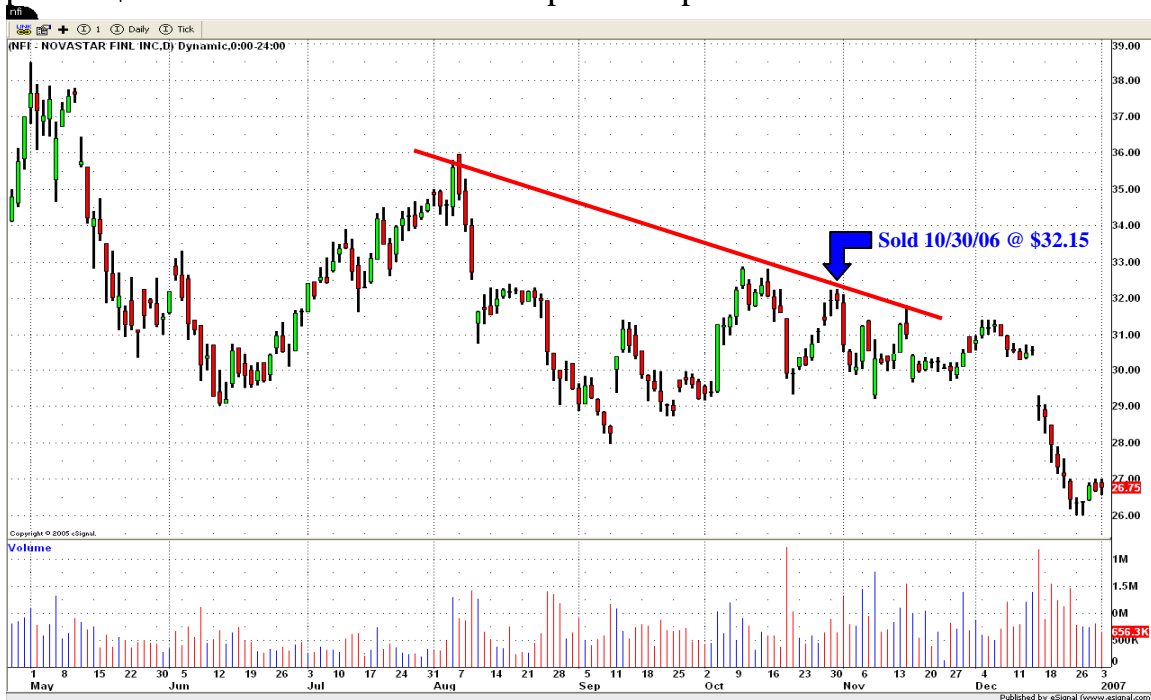
We upgraded our proprietary systems at the end of 2006 to more efficiently find opportunities. It has been well said that "investing is part art and part science." There is no magic formula for determining winners and losers. If there were, mathematicians would be stock gurus. However, computers greatly enable us to filter through the vast amount of information identifying potential opportunities. We then scrutinize those potential opportunities based on multiple criteria. If we decide to go forward on an opportunity, we next determine the best time to buy along with an exit strategy.

Selected Holdings Highlights:

We closed out our holdings in Nortel (NT) in May 2006. While we had hoped that they would be able to overcome their accounting woes we grew weary of waiting for their turnaround. Seeing better opportunities for our assets, we swallowed our losses and moved on to much brighter opportunities.

Our Novastar (NFI) investments performed exceptionally well. Our average return included a 13% capital gain and a 10% dividend yield. We purchased the majority of this stock in December 2005 at \$28. We were especially attracted to its quarterly dividend of \$1.40 (a 20% annual yield). Although many pundits predicted a dividend reduction in 2006, we were confident of NFI's abilities and purchased an extraordinary opportunity. During the early part of 2006, the stock increased to a high of \$38. Since there were still three more dividends to pay out, we decided to hold the stock unless it exceeded \$40. During the summer the stock declined and then attempted another run but only made it to \$36. Although we were still thrilled with the exceptionally high dividend yield, we started questioning NFI's ability to maintain the dividend into 2007. While NFI continued to post solid earnings, we began to realize that their cash flow was failing to

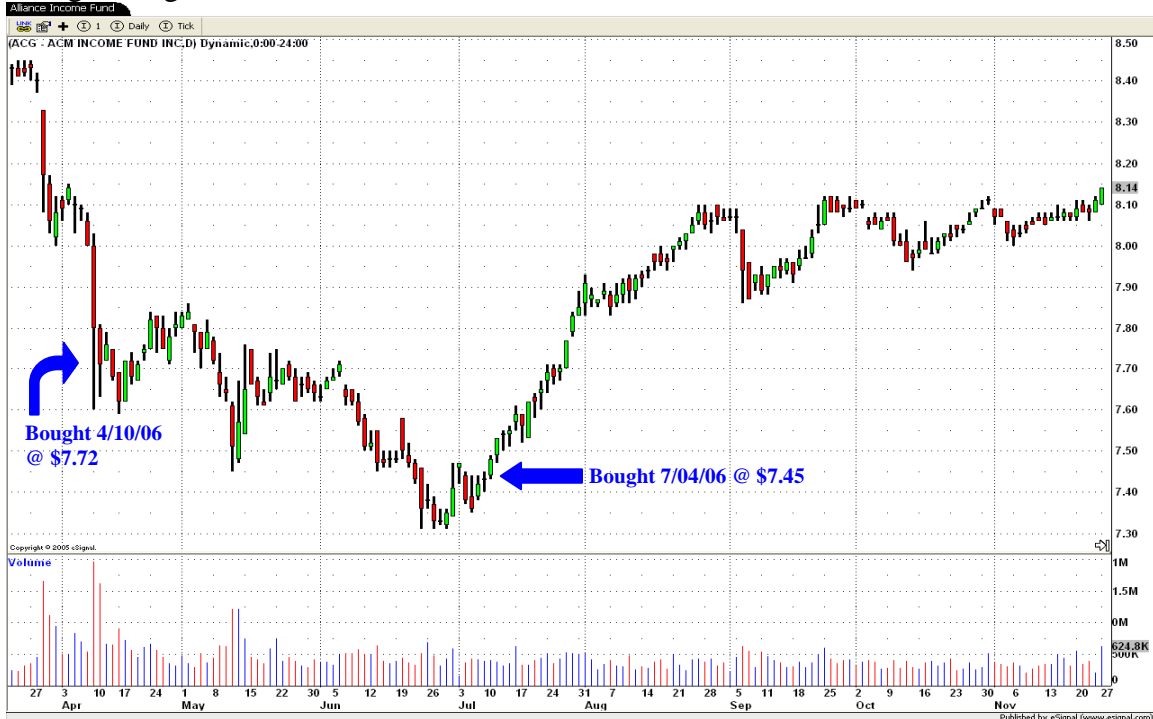
keep pace. Thus our concern that the dividend could not be maintained began to mount. In early fall NFI's management made the unusual move to publicly commit to two more dividends payments in 2006. While this caused the stock to begin another run, when it failed to reach \$33 we realized that we may be looking at the end and began looking for the best exit price. We drew a trend line (the red line on the chart below) that helped us to determine that \$32 would be the best and probably last time to sell the stock while still maintaining a capital gain and securing our dividend gains. Thus we sold at an average price of \$32.15 on October 30th and the expected drop in the stock soon evolved.



We still actively track NFI. While we don't have a crystal ball, we are anticipating a reduction in their dividend payout. If this happens we predict a standard investor panic will ensue with a huge price drop. If this happens we will swoop in and buy up the opportunities.

Our other staple for the year was the Alliance Income Fund (ACG). This closed-end fund is highly leveraged and is primarily invested in U.S. government bonds. This fund, like all bonds, performs inversely to interest rates. In March, ACG announced a dividend reduction which caused a major decline in the stock price. Adding to ACG's woes was the Federal Reserve's decision to continue raising rates throughout the summer. This caused the stock to plummet as investors fled bonds (please refer to the chart on the next page). Looking at ACG's decline, we again saw a great opportunity. We made purchases at \$7.45 and \$7.62. We felt very confident that the Federal Reserve would not raise rates further at their August 2006 meeting and began to heavily buy up the stock before the opportunity was lost. By the time the Federal Reserve met for their August meeting, we had already seen a 6% increase in our holdings as other investors began to realize what we had perceived back in June. Additionally, when the Federal Reserve paused their rate increases in August, we finally relaxed and let ACG run its course. We knew from history that the Fed, and its predecessor, going all the way back to 1914 had never

resumed rate increases after a pause. Therefore, we anticipate ACG to continue strengthening into 2007.



As we look at 2007, we hope that the bulls will continue to dominate. The three big “wild cards” for this year will be real estate, the dollar, and the war on terror. If real estate takes a hard hit, there will be tremendous pressure on the Federal Reserve to reduce rates in order to avoid a recession. Unfortunately, and quite puzzling to us, the dollar continues weakening. Thus the Federal Reserve would be in a very difficult situation of choosing rate cuts to “save” the U.S. economy or rate increases (thereby strengthening the dollar) to make sure China and foreign investors keep buying U.S. debt and not panicking about our long-term solvency. To make things even more interesting is Iran, North Korea, and the continuing conflict in Iraq. But alas, while this may all seem overwhelming, the reason for pointing all this out is that 2006 started off with a bull market and very similar uncertainties. We are eternal optimists and enjoy the challenge of creating wealth for our clients.

We hope you have found this analysis informative and meaningful. As always, we are actively seeking prospective investments and reacting quickly to the changing market environments. May you have a blessed 2007.

Sincerely,

Jonathan Davey, CPA MBA
President