



Alan Greenspan, who has now slipped comfortably (and lucratively) into the role of wise man, is to be honored by New York University's Stern School of Business, which will name a chair in economics in his honor. Despite Greenspan's reputation lately sliding precipitously along with the economy and markets he kept afloat with cheap money every time they were disrupted or he thought they might be disrupted (recall Y2K?), he still commands six-figure fees for speaking engagements and is a senior advisor to the likes of Pimco and Deutsche Bank. To his credit, Greenspan after the global financial system came close to collapse, conceded that he had been wrong about how markets worked—quite a concession for an ideologue like him—he generally has deflected criticism. But how can someone who loved his carefully crafted image as a financial hero not also accept his portion of shame when those markets ravage the world? Never mind. Greenspan, like some retired sports superstar, never has to pay for a meal. The NYU chair testifies to that. Or does it? The press release announcing the new chair celebrates the generous donor, John Paulson, who is giving the business school \$20 million to endow both the Greenspan chair and another, in Paulson's name. This isn't Paulson's first grand gesture toward Greenspan, whom he hired to advise Paulson & Company after the Fed Chairman retired. The black humor behind all this is that Paulson could not consider as chump change the \$20 million gift to NYU had he not bet back in 2007 and 2008 that Greenspan's "What-Me-Worry?" approach to the housing market would turn into catastrophe. Without the Maestro's encouragement that adjustable rate mortgages, derivatives and other financial innovations were excellent ideas, Paulson could never have earned personally \$10 million a day in each of those years. Perhaps Paulson likes to have Greenspan around so he can ask him what his market view is and then do the opposite?

-Gray Emerson Cardiff

## At Mid-Year

Now that the first half of 2010 is behind us, we can sum up in two words how the market has fared through June 30th: Not good, particularly compared to what happened in 2009. Turn back the calendar to last year. After a terrible first ten weeks, the market in early March began a steep recovery. The Dow at mid-year was up 3.8%, the S&P 1.7%, the Nasdaq 16.4% and the Wilshire 5000 3.7%. An equally-weighted portfolio of *Sound Advice* holdings had notched an 18.7% rise, which would pick up momentum as the year progressed.

But not this year. This time the market also reversed direction but after a good start, and ran downhill from April till the end of the second quarter. The Dow as of June 30th had lost 6.3%, the S&P 7.6%, the Nasdaq 7.1% and the pan-market Wilshire 5000 6.5%. *Sound Advice* had lost 5.9% over the same period.

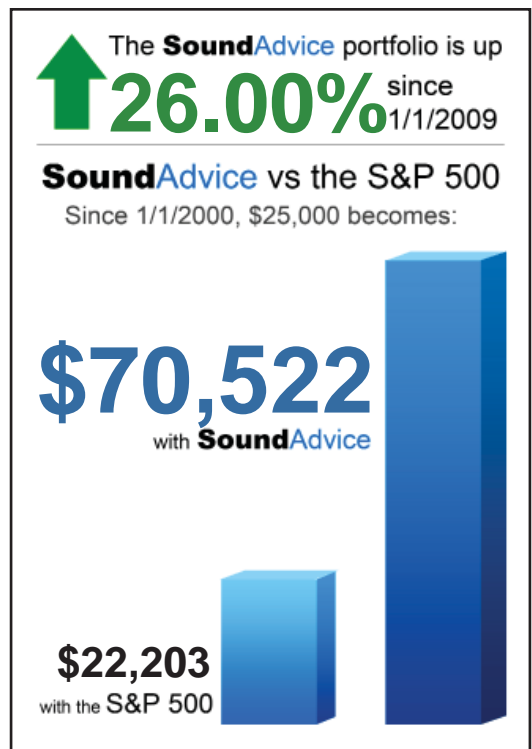
These aren't terrible numbers, but if you measure from the April 23rd highwater mark for equities, the benchmarks fell on average 15%. Over the same period, the *Sound Advice* portfolio dropped 13.3%.

2008, the so-called *annus horribilis*, is fresh enough in investors' memory to make them anxious that any significant decline in prices would be only the first shoe, which discourages taking advantage of falling prices. Perhaps that explains why being bearish lately has been so much in vogue.

Looking at market sectors, the worst performers during the 2010 decline were agriculture (-35%), mortgage finance (-34%), alternative fuels (-33%) and consumer electronics (-32%), while the best were gold mining (19.3%), residential REITs (4.3%) and brewers (3.1%). In short, anything that depends on renewed consumer confidence and a growing economy suffered, while things that are either essential like housing (but not owner-occupied housing), beer, or during a time of anxiety make it easier to sleep at night like gold (perhaps beer too) fared better.

The losers, frankly, are of more interest as recovery stories. During difficult periods, we try to remember that you make your best profits during declines, presuming you are wired to buy into weakness.

Transocean was down 44%



in the first half. The story is too well known to recount, but we encourage anyone who can tolerate the anxiety to consider these shares. Unless BP, the well owner, can demonstrate that Transocean, with whom it contracted and promised to indemnify for just the sorts of nightmarish events that have occurred, Transocean has only modest liabilities. Based on everything reported to date, BP appears to have acted recklessly and on occasion disregarded Transocean employees' warnings.

**Boston Scientific** (-35.6%) unlike RIG is hardly blameless for its problems, and yet we are confident that the market too has woefully undervalued this maker of stents, heart-rhythm devices and other medical tools. We're still reeling in disbelief that Boston Scientific failed to file simple paperwork about a benign change in how it manufactured defibrillators and then decided preemptively to recall all of its defibrillators. Not only did that overreaction give competitors an edge they exploited during the three months Boston Scientific waited for FDA approval but it also made physicians and investors wonder about Boston Scientific's ability to put one foot in front of the other. Boston Scientific still is the dominant seller of drug-coated stents, has a new line of stents coming to market soon, has a well-recognized hearth-rhythm monitoring device business and continues to develop other promising medical devices and procedures. Above all, BSX is among the most despised companies, which saddles its shares with a significant pessimism discount. Long-term we think BSX has immense recovery potential. Indeed, we're waiting for the quarterly conference call (July 21st) to see if there is initial evidence that better times are coming.

**Tetra Tech** (-27.8%), which specializes in water remediation and other environmental issues, derives just over two thirds of its revenues from government projects, not a good thing when government budgets at all levels are stretched thin. Another major client in good times, new construction, is also a drag lately. Nonetheless, TTEK is too good at what it does to be avoided. It has enough cash flow that it can make strategic, mostly small, acquisitions to broaden both its geographic reach (Europe and Asia are ripe for what Tetra Tech does) and its business mix (wind power and nuclear projects are relatively new areas). TTEK's future is very bright, which makes it a bargain for patient buyers.

**ProShares UltraShort 20+ Years ETF** (-26.3%), has had a rough time. The European sovereign debt crises have boosted the dollar and dollar-denominated government debt. Fears that European, American and Chinese economic expansion might stall banished any concerns about inflation and provided even more tailwind for bond prices. We could dump this bet on rising interest rates, and quote Keynes about the market being able to remain irrational longer than we can remain solvent, but we think that any hint that the global economy and especially the U.S. economy is recovering will kill the rally in Treasuries and give this ETF room to recoup its losses.

The best performance came from a mix of sectors. Not surprisingly the two best were sold before the market went south. **Perrigo**, which manufactures and distributes OTC and some prescription drugs, enjoyed a 27.4% rise. It was sold in the March issue. Last month, we sold **Odyssey Healthcare**, the hospice services company which is being bought by Gentiva after the deal was announced and soared 70.4%. Other gainers still in the portfolio include **Fastenal** (20.5%), a hardware vendor that caters to construction and manufacturing, and **Liberty Global** (18.7%) a cable company focused in Europe, South America and Asia. The **Ford Convertible Preferred** (10.6%) reinstated its dividend and paid the previous five quarters' distributions that were in arrears plus interest on that amount, remains the best way to own Ford. **USAA Precious Metals & Minerals Fund** (10.9%) also was a plus, but lagged its benchmark over the last quarter because it is overweighted toward mid-sized, efficient producers, while the market favored recently the biggest miners like Newmont and Barrick.

As you know, *Sound Advice* remains bullish about the direction of the U.S. economy and consequently about where stock prices are headed. Despite the slide since April, we expect our portfolio, populated mostly by undervalued, out-of-favor companies with strong balance sheets, will continue to give us relative outperformance. It's not too much to ask not just for relative outperformance but for positive results too. Let's see what the second half of the year has to say about hope. SA

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## Sector Funds

During the market's strong run through mid-April, retail investors showed their ambivalence about stocks by avoiding putting new money into funds. On the whole, they preferred bond funds. After the market tumbled, that reluctance to trust equities apparently has been rewarded. However, as we assert on the previous page, a pessimistic market mood can provide an excellent environment for buyers. As we prepare to put the July issue to bed, a week before we publish, equities have had a few tasty days that have wiped some of the last eight weeks' bad taste away. Whether this is the turn remains to be seen. Even if this is a reversal, undoubtedly there will be other declines. Provided they happen while our buy signal remains intact, we have no problem buying when others are selling shares. The same should be true for fund investors whether they look to the broadly diversified funds we reviewed in the May issue, or in the sector funds we discuss below.

Though funds account for more than a quarter of the Sound Advice portfolio, they can be overlooked for the very reason they appeal to many investors: diversification. Fund portfolios filled with scores of stocks defy simple explanations for their price changes, and even when a fund is focused on a single sector such as energy or REITs or when the fund is relatively concentrated, changes in the manager's outlook are difficult to detect unless his or her portfolio gets picked apart, which is what we'll devote this issue to. For those subscribers who prefer stocks over funds, what our fund managers currently favor could be a useful starting point for further research.

As a group the eight managed funds (six mutual funds, one closed-end (CEF) and one exchange traded fund (ETF)) are down 1.8% for the year, better than common market benchmarks and for that matter better than indexes for their respective sectors. We remain optimistic about how these managers will do in the future. We cover five in this issue.

### Fidelity Select Natural Gas Fund

We introduced **Fidelity Select Natural Gas Fund (FSNGX)** last September to replace a general energy fund managed by Icon. There were two reasons. First, we had concluded that despite Icon's reputation as value-oriented, its selection process

included what amounts to a momentum factor that might work in up markets but did not in sideways or down markets. Second, we believed that among the various subsectors within the energy industry natural gas was the most depressed and thus the most likely to rebound given our assumption that as the global economy exited a deep recession demand for energy would increase. Though FSNGX until March was more than meeting our expectations, its portfolio has

Fidelity Select Natural Gas Top 10 Positions	
Plains Exploration & Production	9.86%
Anadarko Petroleum	9.75%
Chesapeake Energy	8.84%
Southwestern Energy	5.14%
Denbury Resources	4.69%
Range Resources	4.67%
Massey Energy	3.51%
Petrohawk Energy	2.98%
Ultra Petroleum	2.75%
Nabors Industries	2.64%
	54.8%

been hit by two problems. First, energy in general has suffered as the durability of a global economic recovery came into doubt thanks to European debt problems, the consequent weakness of the Euro, slowing in recovery in the U.S. and questions about whether China might tamp down its own economic growth. But these are issues for all energy funds.

What has affected FSNGX specifically is the second problem: Over the last year, James McElligott, the fund manager, introduced a new exploration and development company into its portfolio, Anadarko Petroleum, which at the time was an excellent choice. Indeed, Anadarko as of the most recent filing with the SEC (Feb 28, 2010) had become the fund's second largest position (9.2% of the portfolio) and was performing excellently until April 20th, when BP's Macondo well in the Gulf of Mexico failed and began to spew oil and natural gas into the Gulf of Mexico. BP has two non-operating partners, Mistui (10% share) and Anadarko (25% share). Unlike Transocean, which was contracted by BP to operate the drilling platform and is contractually insulated

from liabilities resulting from the disaster (except for harm to its own employees and pollution caused by materials on the platform), Anadarko, even though it made no operational decisions, could be vulnerable to a proportionate share of the costs, which presently are unknowable but certainly will exceed the \$20 billion BP has committed to an escrow account to cover claims. We say “could be,” because Anadarko asserts that BP was grossly negligent in how it operated the well. Were that charge substantiated, Anadarko would escape most of the damage. As we have learned while following the impact of the Gulf catastrophe on Transocean, handicapping the twists and turns as they hit share prices is impossible on the short-term. From everything we’ve seen so far, BP repeatedly emerges as taking risky decisions, which individually might have been justifiable but when combined reflect recklessness. The damage, however, has been done to Anadarko shares and to FSNGX, which have been cut in half since April 20th.

The fund manager, at least as of May 30th when Fidelity made its monthly report to shareholders, had not reduced its Anadarko position, though as Anadarko has continued to fall, his stoicism might dwindle. Since the fund made its last filing to the SEC, Anadarko itself accounted for a 2.4% loss for the fund.

McElligott has not made any radical changes, selling a few small positions and initialing others of similar size. Addition of Exxon Mobil (1.8% of the portfolio) reflects completion of Exxon’s acquisition of XTO Energy, a natural gas producer the fund owned. The underlying rationale for owning FSNGX remains intact: as the U.S. economy recovers, demand for energy will rise. That natural gas is seen as cleaner than coal for generating electricity can only enhance demand.

**Davis Financial Services Fund**

**The Davis Financial Services Fund (DFIBX)** owns a relatively compact portfolio that as of March 31st held 32 positions, the 20 largest of which account for more than 90% of its invested assets. There have been few changes over the last 12 months, mostly trimming of existing positions, particularly Transatlantic Holdings, a reinsurance company, that last year was the largest position (11.3% of the portfolio) by 19%, and even larger cuts in smaller positions in medical-liability

insurance provider FPIC Insurance (more than cut in half from 1.8%), JP Morgan (more than a third from 0.9%). Even what is now the largest position in the portfolio, American Express, was reduced by 169,500 shares but rose from 6.1% to 10.6% of the portfolio thanks to price appreciation. New positions mostly were outside the U.S. (two Brazilian and one Swiss institution). The largest buy was \$18 million (2.6% of portfolio) of Dunn & Bradstreet, the business data publisher, which lately has been trading close to where it stood before the March 9, 2009 market low.

The fund managers do like to feather their portfolio with non-financial assets, though sometimes it’s not obvious. Lately the portfolio’s seventh largest position (5.5%) is Canadian Natural Resources, an energy company active in North America, Africa and the North Sea. The third largest position (7.9%) is in Loew’s, a holding company that gets just 40% of its profits from CNA Insurance (90% ownership), but gets most of the rest of its revenues and profits from its 70% ownership of Boardwalk Energy, a pipeline company, its 51% ownership of Diamond Offshore, a marine drilling company, its 100% ownership of HighMount, an exploration and development company focused

Davis Financial Fund Top 10 Positions	
American Express	10.63%
Transatlantic Holdings	8.65%
Loews Corp.	7.93%
Wells Fargo	6.69%
State Bank of India	6.26%
Oaktree Capital Group	5.50%
Canadian Natural Resources	5.46%
Bank of New York Mellon	5.11%
Markel Corp	4.29%
Julius Baer Group	3.91%
	64.4%

on natural gas, and fees earned for managing 18 hotel properties.

**CGM Real Estate Fund**

**CGM Real Estate Fund (CGMRX)** is 4% to the good this year, which should not be surprising since Real Estate Investment Trusts (REITs) are in the black. It should also not be surprising because, as *Morningstar* notes, Ken Heebner’s real estate fund has the top performance record for every interval

**CGM Real Estate Fund Top 10 Positions**

Digital Realty Trust	7.19%
Simon Property Group	6.70%
Host Hotels & Resorts	6.31%
Teck Resources	6.28%
SL Green Realty Corp	6.04%
Alexandria Real Estate	5.79%
LaSalle Hotel Properties	5.73%
Cliffs Natural Resources	5.59%
DiamondRock Hospitality	5.54%
Freeport-McMoRan	5.43%
	60.59%

measured beyond the last three years. What is surprising is that the fund has not done better. As we noted earlier this year, Heebner has returned to a portfolio strategy used to great success earlier in the decade when CGMRX ran circles around other REIT funds: he again has introduced shares of mining companies, arguing that because mining companies own land, they were appropriate for a real estate fund.

Heebner works with a very concentrated portfolio, which as of the most recent filing (March 31st) numbered 19 positions. Mining stocks account for 26.5% of the portfolio, up since the previous filing at the end of 2009 when they accounted for 21%. The portfolio now, after dropping Southern Copper, which was a 5.5% holding, and adding Alpha Natural Resources, Cliff Natural Resources and BHP Billiton, skews toward diversified miners. However, this is fine tuning. The real message is that Heebner is going deeper into mining stocks, and if you are viewing CGMRX as purely a REIT play rather than a REIT play as interpreted by Ken Heebner, this might not be the fund for you.

This time around, at least so far, Heebner's strategy has hurt performance. For example, RWR, a REIT ETF, is up 6.9% over the same period, and it appears that Heebner's return to natural resources is the culprit: the quintet of mining stocks on average have lost 4.5%. Whether Heebner since March 31st has reduced or increased exposure to mining stocks is an interesting question, since he is apt to make abrupt but significant changes to the portfolio, and what the fund holds today could bear little resemblance to what appears in the latest SEC report.

If we look at what he has done with more traditional real estate positions, the largest sector is lodging (19.3%) followed by office and light industrial (11.8%) with retail (11.3%) close behind. Significant sector changes have occurred in retail, reduced by a third, and self-storage (Public Storage is the only holding),

**Hambrecht & Quist Life Sciences Fund Top 10 Positions**

Celgene Corporation	5.10%
Amgen Inc.	3.80%
Teva Pharmaceutical	3.80%
Gilead Sciences	3.70%
United Therapeutics	2.80%
Illumina, Inc.	2.50%
Cephalon	2.50%
Vertex Pharmaceuticals	2.10%
AMAG Pharmaceuticals	2.10%
Align Technology	2.00%
	30.4%

more than doubled to 5.1% of the portfolio. The single largest position remains Digital Realty (7.2%), which concentrates on properties dedicated to data storage and communication facilities.

### Hambrecht & Quist Life Sciences Fund

**Hambrecht & Quist Life Sciences Fund (HQL—NYSE)**, reintroduced to the *Sound Advice* portfolio last December to diversify our healthcare holdings away from that sprawling industry's more traditional sectors, is a closed-end fund (CEF) focused on biotech companies. HQL as well as its sibling CEF, H&Q Healthcare Investors, have another facet that distinguishes them from most other biotech funds: management can invest in non-publicly traded companies, mostly startups, that gives shareholders exposure—whether for good or bad—to untested companies with potential either to soar or to vanish. This year to date HQL is down 3.3%. The thematic headwinds for HQL are that not only is the market skeptical about how healthcare reform will play out (more of a problem for established firms, especially for insurers) but also skittish venture capital for new and not-yet-mature biotech firms restrains the entire industry.

HQL's portfolio has had some significant shifts at the top. If we compare the current top-10 positions with how they stood when we recommended the

CEF last December, we see Daniel Omstead, the fund manager, has reduced two positions: Illumina, a diagnostic company, by almost a fifth to 2.5% of the portfolio and Vertex Pharmaceuticals, a biologics company focused on developing drugs for viral infections, by more than a third to 2.1%. Positions in Gilead, which develops drugs for treatment of HIV/AIDS, cardiovascular and respiratory conditions and diseases of the liver (98% increase in shares), and AMAG, which is active in developing treatments for anemia and also works in imaging, more than doubled.

Omstead observes that though the publicly traded portion of the portfolio kept pace with its benchmark, the restricted shares did not, which is consistent with the nervousness of an unsettled market that is leery of anything that is not a well established company. This is the third time we've owned HQL, and our experience has been that the restricted positions in young and juvenile companies have contributed to its market-beating performance. The fund currently trades at an 18% discount from the net asset value of its holdings

**If there is one truth about successful investing, it is this: if you are in this for long-term, significant profits, you should never be in synch with received opinion. The consensus, though it might be right at the moment, eventually turns out to be wrong. Or as Ben Graham put it, the market in the short-run is a voting machine that registers popularity. In the long run, it is a weighing machine that registers value.**

when compared to the typical telcom fund's hyper-active 287% turnover rate, is glacial. It's not just that Gabelli is patient in an impatient business, he is also insistent on value. GABTX's positions on average trade significantly below the telecom and media industries' benchmark valuations. Though GABTX's positions cumulatively trade at significant discounts when compared to sector averages (Price to Sales and Price to Cash Flow are 58.5% and 54.1% of sector averages), growth of cash flow is half-again higher than peer companies' performance. That's a very powerful parlay.

Note that Gabelli takes "global" seriously. More than 55% sit outside the U.S. (Europe 33%, Asia 13%, Latin America 10%). Just under a quarter of assets are in emerging markets, which over time should be the most dynamic regions.

What interests us about telecom is that investors tend to view such companies more as utilities, that is, and dismiss them as not capable of rapid growth but nice dividend payers. To an extent that is true. However, telecom marches to cyclical trends. In recessions revenues decline across this industry. In expansions, they increase. The wireless business, for instance, even in a weak economy is exploding with smart-phones that allow users to tap into all that is on the Internet—but at prices higher than for simple voice or text messaging. About a third of GABTX's portfolio is in wireless communications companies. Even those wireline telecom companies, which truly are stodgy and will continue to lose business to wireless competitors, benefit in a recovering economy, though not as much as will the wireless players.

The past months' gloom has challenged *Sound Advice's* bullish approach, but we are wired to buy when others sell. Lately you are being inundated with opinions and news that reinforce the pessimistic story line. If there is one truth about successful investing, it is this: if you are in this for long-term, significant profits, you should never be in synch with received opinion. The consensus, though it might be right at the moment, eventually turns out to be wrong. Or as Ben Graham put it, the market in the short-run is a voting machine that registers popularity. In the long run, it is a weighing machine that registers value. SA

**GAMCO Global Telecommunications Fund**

The **GAMCO Global Telecommunications Fund (GABTX)**, which is managed by a trio of seasoned

<b>GAMCO Global Telecommunications Fund Top 10 Positions</b>	
<b>Rogers Communications</b>	<b>5.14%</b>
<b>America Movil SAB (ADR)</b>	<b>4.83%</b>
<b>DIRECTV, Cl. A†</b>	<b>4.50%</b>
<b>Telefonica SA (ADR)</b>	<b>4.36%</b>
<b>Deutsche Telekom (ADR)</b>	<b>3.44%</b>
<b>Verizon</b>	<b>3.36%</b>
<b>United States Cellular</b>	<b>3.24%</b>
<b>Vimpel-Communications (ADR)</b>	<b>2.98%</b>
<b>Telephone &amp; Data Systems</b>	<b>2.93%</b>
<b>TeliaSonera AB</b>	<b>2.59%</b>
	<b>36.72%</b>

investors led by Mario Gabelli, like most of our funds shows scant changes over time. Its 4% turnover rate,

## Portfolio Updates

Since the last letter was priced on June 4th equities have zigged back and zagged forth. The back part occurred up until the last week before we priced the July portfolio. The forth part occupied that final week. Overall, the Dow added 2.7% (but was down 2.5% at the low), the S&P 1.2% (-4% at the low), the Nasdaq lost 1% (-5.7% at the low) and the pan-market Wilshire 5000 added 0.9% (-4.2% at the low), which suggests that investors when they did start buying gravitated toward the largest companies, the sorts that populate the S&P 500 and dominate the Dow. Over the same period, the *Sound Advice* portfolio added 1.5%.

The June issue highlighted five stocks we think are promising going forward. As a group, they added 0.8%, mostly because **Tetra Tech**, the month's worst performer, which we discuss on page 2, got walloped (-7.9%) on scant hard news but bountiful concerns over where revenue will come from when government and commercial clients are postponing infrastructure expenditures. As for the other four, Leucadia was flat, **Maxim Integrated**, the chip maker bucked the weak Nasdaq and added 4.2%, **Transocean**, as value investors began to nibble, added 3.3% and **Johnson & Johnson**, the epitome of a mega-cap, defensive stock, led this quintet adding 4.4%. JNJ as we go to press continues to have problems with its over-the-counter products manufactured in a plant in Puerto Rico. We do not believe this is a significant problem, though it's taking longer to resolve than we had expected.

Several trends that had been pushing stock prices lower either have run their course or are in remission. For instance, the collapsing Euro, one consequence of the sovereign debt crisis in Europe, reversed direction shortly before U.S. share prices firmed. The S&P 500 both on the downside and the up has closely tracked the Euro's changing price. Concerns that China's economy would slow are muted, and anxiety that the artificial exchange rates for Chinese currencies also is lower after Beijing said it would adjust them modestly. The market does continue its preoccupation with whether we are heading back into recession. As earnings season begins on July 12th when Alcoa leads off, we'll have a better handle on reality. We suspect that sales and earnings will be

up nicely compared to the same quarter in 2009. The wildcard will be what companies say about the next quarter and the foreseeable future. Glum outlooks will hurt the overall market and regenerate that very nice cloud of pessimism that grew over the past three months of declining share prices. It's not that we're hoping for bad news, it's just that our best opportunities come in depressed markets.

There's been a sharp run up in fertilizer companies for the last few days, and **Agrium** has been among the hottest, adding 12.7% after being down 4.5% just a week ago. AGU did expand recently its South American chain of retail stores that sell fertilizers and other agricultural products, but that is a minor current. The major tide seems to be anticipation of greater consumer demand, which presumes an improving global economy.

**Boston Scientific** was close behind AGU, adding 12.5% on no major news, though it did begin clinical trials on a promising device that monitors defibrillator activity and alerts physicians whenever a patient is in trouble. Pessimism about BSX is thick, but all that it needs is a quarter or two of better-than-expected results and it would do very nicely. Other healthcare positions were mixed: as noted Johnson & Johnson did well, though UnitedHealth Group, the HMO, slid 1.2% and Hambrecht & Quist LifeSciences Fund fell 2.2%. Stryker, the orthopedic device and hospital equipment company, added 0.8%.

One of the few companies to report quarterly results was **CarMax**, which came in with excellent numbers for the previous quarter that slingshot the shares up by 9% on the day. Profits per sale, turnover rate and comps with the same quarter last year all brought buyers into the shares. There appears to be a shortage of first-rate used cars, the sort of vehicle KMX buys and sells. The best news came from sales in the wholesale division, through which CarMax generally sells its less than prime vehicles. There was also a marked improvement in profits from financing. We said "seemed" not because the 9% gain wasn't real, but because KMX at the same time was selected to replace XTO Energy in the S&P 500, which obligates index funds built around that index to



This table is updated with live prices, charts & buy limits on our website:

<http://www.soundadvice-newsletter.com>

Income With Growth	Symbol	Exchange/ Phone	Price/ N.A.V.*	Yield**	Buy Limit	ACTION
CommonWealth REIT***	CWH	NYSE	\$24.87	8.04%	<b>\$28.00</b>	BUY
Telecom New Zealand	NZT	NYSE	\$6.84	10.38%	\$7.25	BUY
<b>Diversified Growth</b>						
Agrium	AGU	NYSE/TSE	\$58.17	0.19%	\$65.00	BUY
CarMax	KMX	NYSE	\$19.35	0.00%	\$26.00	BUY
CGM Realty Fund	CGMRX	800-343-5678	\$21.64	2.86%	N/A	BUY
Dodge & Cox Intl.Fund	DODFX	800-621-3979	\$30.12	1.45%	N/A	BUY
Dodge & Cox Stock Fund	DODGX	800-621-3979	\$91.84	1.19%	N/A	BUY
Fastenal	FAST	NASDAQ	\$52.07	1.34%	<b>\$60.00</b>	BUY
Gabelli Global Telecom Fund	GABTX	800-422-3554	\$18.27	1.81%	N/A	BUY
Honeywell	HON	NYSE	\$41.27	2.94%	\$49.00	BUY
International Speedway Corp.	ISTA	NASDAQ	\$25.81	0.62%	\$31.00	BUY
Johnson & Johnson	JNJ	NYSE	\$60.54	3.24%	\$68.00	BUY
Leucadia National Corp.	LUK	NYSE	\$20.41	0.00%	\$27.00	BUY
Mattel	MAT	NASDAQ	\$22.57	3.32%	\$26.50	BUY
Microsoft	MSFT	NASDAQ	\$24.27	2.14%	\$33.00	BUY
Molson Coors Brewing	TAP	NYSE	\$44.16	2.17%	\$52.00	BUY
Stryker Corp.	SYK	NYSE	\$52.38	1.15%	\$60.00	BUY
Superior Industries	SUP	NYSE	\$13.30	4.81%	\$18.00	BUY
Tetra Tech	TTEK	NASDAQ	\$19.53	0.00%	\$26.00	BUY
Third Avenue Value Fund	TAVFX	800-443-1021	\$43.61	2.61%	N/A	BUY
United Parcel	UPS	NYSE	\$60.06	3.00%	\$70.00	BUY
UnitedHealth Group	UNH	NYSE	\$29.27	1.78%	\$38.00	BUY
Wal-Mart Stores	WMT	NYSE	\$49.43	2.45%	\$60.00	BUY
Xerox	XRX	NYSE	\$8.22	2.09%	\$11.00	BUY
<b>Energy/Natural Resources</b>						
Anglo-American PLC	AAUKY.PK	PINK SHEETS	\$18.37	0.00%	\$22.00	BUY
Fidelity Select Nat. Gas Fund	FSNGX	800-544-8888	\$28.05	0.22%	N/A	BUY
Plum Creek Timber	PCL	NYSE	\$35.62	4.72%	\$40.00	BUY
PowerShares Water Resources ETF	PHO	NYSE	\$15.64	0.51%	\$19.00	BUY
USAA Precious Metals & Minerals	USAGX	800-862-6909	\$37.10	0.03%	N/A	BUY
<b>Aggressive Growth</b>						
AOL Inc.	AOL	NYSE	\$20.28	0.00%	\$28.00	BUY
Boston Scientific	BSX	NYSE	\$6.46	0.00%	\$8.50	BUY
Comcast	CMCSA	NASDAQ	\$18.07	1.80%	\$21.00	BUY
Davis Financial Fund	DFIBX	800-279-0279	\$22.46	8.21%	N/A	BUY
Ford Motor Convertible Pfd	F.PRS	NYSE	\$41.50	7.28%	\$50.00	BUY
H&Q Life Sciences Fund	HQL	NYSE	\$9.05	7.07%	<b>\$9.91</b>	BUY
Liberty Global	LBTYA	NASDAQ	\$27.74	0.00%	\$32.00	BUY
Maxim Integrated	MXIM	NASDAQ	\$17.83	4.49%	\$21.00	BUY
Symantec	SYMC	NASDAQ	\$14.55	0.00%	\$20.00	BUY
Third Avenue Focused Credit Fd****	TFCVX	800-443-1021	\$10.64	3.96%	N/A	BUY
Time Warner	TWX	NYSE	\$30.19	2.78%	\$34.00	BUY
Transocean	RIG	NYSE	\$51.83	0.00%	\$65.00	BUY
UltraShort 20+ Treasury ProShares	TBT	NYSE	\$36.99	0.00%	N/A	BUY

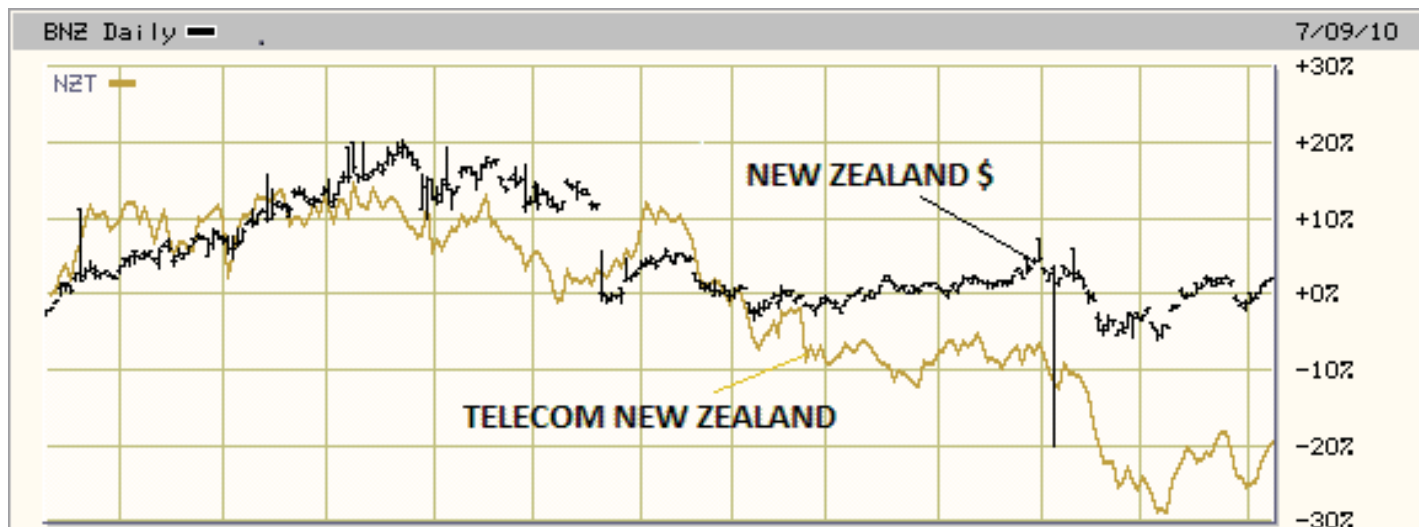
\* Prices as of Friday, July 9, 2010

\*\* Yield represents all income during previous 12 months divided by current share price. Note that all fund distributions fluctuate annually.

\*\*\* Name and Ticker changed from HRP (HRP--NYSE)

\*\*\*\* Covers distributions from Aug 31, 2009 - June 30, 2010

BUY, HOLD, SELL OR LIMIT IN BOLD INDICATES A CHANGE IN ACTION OR LIMIT



buy it. Either way, it was a good week for KMX. But it was a bad month. The shares even with that one-day jump fell 7.6% along with most retailers as the market worries that consumer confidence is weakening again and without an improvement in the employment picture that even the employed will hoard cash and avoid using their credit cards. We're optimistic about CarMax's future. Not only is it the largest used-car dealer, but KMX is not even scratching the surface of what it can become, since CarMax accounts for a mere 2% of used-car transactions.

**Ford** last week announced it was reducing its debt by \$4.055 billion, which is good for the balance sheet and is another step toward the company's full recovery. Most attention was paid to the \$3.8 billion portion in payment to the UAW's medical care fund, but it's the other \$255 million that is worth our notice, since it covers the \$4.05 Ford had deferred on our Convertible Preferred Shares plus 21 cents in interest on that amount and 81 cents for the current quarterly dividend that will be payable along with the \$4.26 on July 15th. The record date was June 30th. Going forward Ford will pay its dividend regularly.

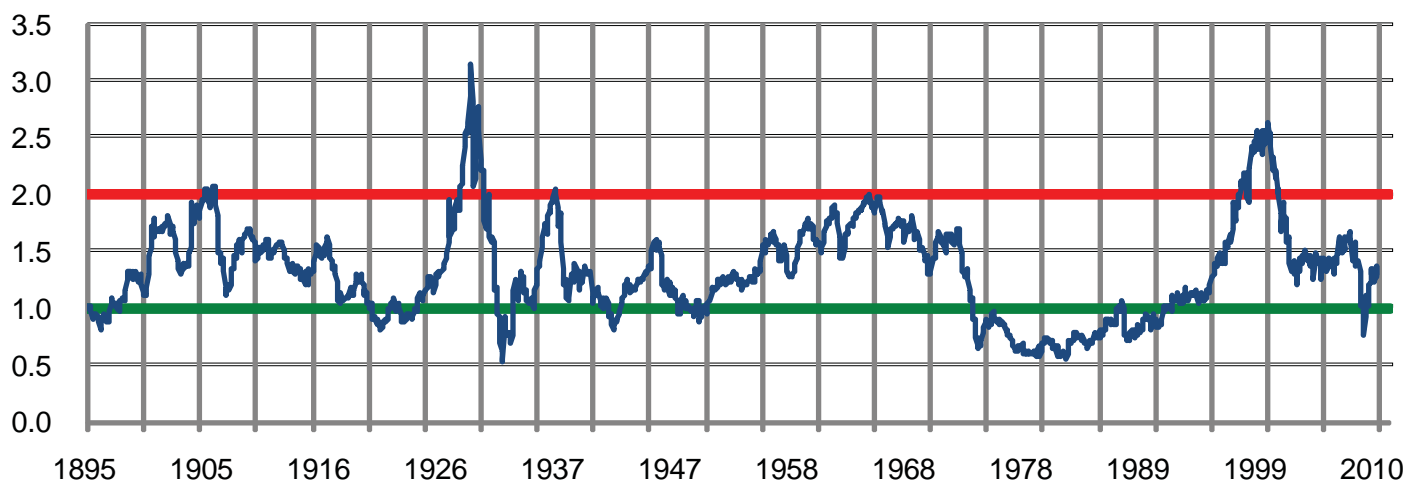
If you've been searching fruitlessly for price quotes on **HRPT Properties Trust (HRP—NYSE)**, the story is that as of July 1st it has changed its corporate name and symbol to **CommonWealth REIT (CWH—NYSE)**. In addition, the company has done a reverse split, which means that for every four shares of HRP that you own, you now own a single share of CWH. The dividend also has been increased. The previous quarterly distribution had been 12 cents a share. On that basis, the reverse split would have resulted in a 48 cent per share distribution. The new distribution will be 50 cents a share, a 4.16% increase. In the wake of the announcement the new shares were

extremely volatile: down as much as 6% one day, up the same the next. Since the last letter, CWH settled down 3%. **CGM Realty Fund**, which we discuss on pages 4-5 added 2.5%.

Another income-oriented position, **Telecom New Zealand**, has snapped back, adding 9.8% in part thanks to figures showing continued expansion in the local economy that helped move the value of the NZ dollar higher against the U.S. dollar. The chart above tracks the share price against the NZ dollar. With the yield currently just under 10%, the question is where the telecom company will set its distributions going forward. Reasonably the amount will be lower, and if that is the case we expect the share price would move a bit higher.

Consumer staples did OK. **Mattel**, the toy company, added 8.2%, outpacing Hasbro, the other major publicly traded toy company, which had been approached by a private equity firm looking to buy it. That deal seems to have gone away, though both toy makers are running well ahead of the overall market even in a sluggish economy.

Technology stocks, as the Nasdaq's relative underperformance suggests, have staggered downward during the decline. In the market's 2009 recovery, it was the Nasdaq, which always attracts extreme views of the future, that led, reflecting optimism that demand would surge. As skepticism about a recovery rose this spring, tech stocks dropped. With the exception of **Maxim** and **Symantec** (+4.5%), our tech positions are down this month. **Xerox** lost 7.4% and **Microsoft** 5.9%. If there is to be a recovery, both of these will outperform the overall market. Meanwhile, beer seems to be keeping investors' spirits up. **Molson Coors** added 6.1%. **SA**



The Risk Indicator measures the overall risk in the stock market by plotting the ratio of stock prices to home prices. See *The Science of Making Money in Turbulent Stock Markets* for a full explanation of the Risk Indicator and the Diffusion Indexes. Median home prices have been flat for the last ten months, so the risk indicator is primarily a reflection of stock prices. The latest reading is 1.18. This reading reveals that stocks are still below their average relative to house prices, and present a better value. The February 2009 reading of 0.77 marked the low for this cycle as well as the beginning of Supercycle 6.

## The SoundAdvice Diffusion Indexes

The Diffusion Index of Leading Indicators gives “Aggressive” signals when all four of its individual leading economic indicators drop below their respective levels

of six months earlier, providing a zero percent reading. This reveals a soft economy and a ripe atmosphere for a lasting decline in interest rates.

### Track Record of the Diffusion Indexes

If we had followed the signals from our Diffusion Indexes over the years, we would have done very well indeed. The results are shown below. After each “Aggressive” signal, the S&P 500 produces an annual return of 19 percent. During “Caution” signals, the market was all over the place — sometimes crashing, sometimes meandering, and occasionally advancing. On average, the S&P 500 increased at an annual rate of only 1.62 percent.

Aggressive	S&P	Caution	S&P
Sep-74	68.12	Apr-76	101.90
Nov-79	100.00	Oct-83	167.65
Dec-84	164.48	Jun-85	188.89
Jul-86	240.18	Aug-87	329.36
Mar-88	265.74	Jun-88	270.68
Mar-89	280.00	May-89	313.93
Oct-89	347.40	Mar-93	449.74
Feb-97	798.38	Dec-98	1,141.00
Oct-00	1,429.40	Dec-00	1,320.28
Jun-03	974.50	May-05	1,191.50
Jul-06	1,276.66	Mar-08	1,325.43
Apr-09	865.33		

As far back as February and March 2009 we were projecting that our Diffusion Index of leading indicators would hit zero in March, and mark an important buying opportunity. We made that projection by assuming that the leading indicators would not improve in the current economic environment. In fact that signal arrived in March, very close to the bottom, officially giving us an “Aggressive” signal.

An “Aggressive” signal coming at a time when the Risk Indicator is close to 1.0 reveals that Supercycle 5 has come to an end, and that Supercycle 6 is born. See *The Science of Making Money in Turbulent Markets* (which you received with your subscription) for a history of Supercycles. You will also receive an updated copy when you renew your subscription.

The Diffusion Index of Lagging Indicators gives “Caution” signals when all three of its individual lagging economic indicators rise above their respective levels of six months earlier, providing a 100 percent reading. This reveals a strengthening economy and inflationary pressures ahead. Our next signal will come from this Index. This Diffusion Index currently stands at 0 percent, which means that all of the individual lagging indicators are below their levels of six months earlier.



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