

SOUND ADVICE

Volume XX, Number 7

Subscription Rate: \$195 per year

July 20, 2007



Forget about the Goldilocks Market. We are now in the Santa Claus Market, where leveraged buyouts make every day Christmas. Groups snap up companies with the expectation that with a bit of financial engineering, some ruthless downsizing, and bye and bye a market happy to buy back as an IPO what it sold in a leveraged buyout, they will make a fortune.

So one day when I turned on my monitor and saw that Fastenal had bolted almost 10% higher, I wondered what was happening? My knee-jerk answer was maybe a Santa Claus wants FAST? That turned out to be wrong. In fact, Fastenal once again flummoxed bears by coming in with higher results than analysts expected and the shares took off.

But the steady drum beat of private investment groups using OPM (Other People's Money) has become the emblem for the bull market in 2006 and 2007. I'm not complaining. If someone insists on paying whatever it takes to own something, then by all means we should sell it to him—isn't that the punch line for Benjamin Graham's Ying-Yang Mr. Market fable?

However, when a market becomes intoxicated by leveraged buyouts, there is not only the likely risk that rational pricing ceases to guide buyers and sellers, but also the inevitable final episode when it all collapses.

I know how smart these modern masters of the universe are touted to be, but the very fact that the smartest among them are running to sell their successful businesses to the public in IPOs should tell you everything you need to know about how the story ends.

—Gray Emerson Cardiff

Mid-Year Tally

Last month's buy signal was opportune as stock prices boomed since then. See the updates section for details about our performance over the previous month. Since July starts the second half of the year, it's time to take a look at how the *Sound Advice* portfolio has performed. Overall, the news is fine: our portfolio is up 12.6% versus the Standard & Poor's 500's 9.7%, the Dow Industrial's 11.5% and the Nasdaq's 12.1%. We can attribute some of that success to maintaining our commitment to energy and natural resource stocks, but for those who think that successful investing is being all-in in a single sector, the other part of this success is an eclectic portfolio of ideas that all started with low historical valuations.

So far this year, we have sold seven positions, of which six were for gains and one, **Friedman Billings Ramsey** was at a loss. There were three others, which we continue to hold, that were down 10% or more. **Coeur d'Alene**, which has lost 15.8% so far this year, has been weak along with other precious metals stocks as gold and silver retreated from peaks hit earlier in 2007. CDE also had the specific problem of a court decision that shut down a major new mine. See the updates for better news there. **Boston Scientific** is down 15.4%, though it has extricated itself from some of the quicksand of negative news that pulled it down earlier this year. Finally, **HRPT Properties Trust**, the only property REIT we hold now, is off 10.9%. At this level, we think this REIT offers an exceptional value.

On the plus side of the ledger, returns were excellent. Looking at the 17 best performers, those with returns of 20% or more, you'd expect to find the hottest of hot sectors: energy and natural resources. You won't be disappointed: **EnCana**, the Canadian natural gas company, is up 40% this year, **Transocean**, the ultra-deepwater driller, has moved 34.7% higher, **Anglo-American**, the South African holding company with exposure to coal, diamonds, gold, platinum, iron and other commodities with a promising toehold in China is up 32.4%, **Icon Energy Fund**, overweighted toward energy service companies, is up 29.4%, and **Royal Dutch**, the multinational integrated energy giant, has added 20.9%. There are a couple of natural-resource related companies that continue

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to boom such as **Agrium**, the Canadian fertilizer manufacturer, up 45.4% thanks to near insatiable demand for its nitrogen-based products, which use natural gas as their feedstock. Finally, **CSX**, the transcontinental railroad, is up 40.8%. Railroads, the ideal carriers for bulk goods like coal, corn and wheat, are working at capacity.

However, there are ten others not related to natural resources that are prospering. Three of these winners came to us as spinoffs or tracking stocks from what now must rate as one of our best recommendations, **Liberty Media**, which John Malone used as a holding company to accumulate positions in companies Liberty actively managed and in other companies held passively for investment purposes such as huge hunks of News Corp and Time Warner. Malone has been described as the "Jascha Heifetz of restructuring, playing complex pieces on his various corporate instruments..." **Liberty Global**, which combines a play on the weak dollar through its far-flung ownership of cable transmission assets in Europe, Asia, South America and the rising popularity of cable entertainment, Internet and data transmission in these markets, is our best performer, up 52.7% to date. Second is **Discovery Holdings**, which captured some of Malone's interests in cable network content through its Discovery Channel stable of companies, and is up 48.9%. Then there is **Liberty Capital**, a tracking stock that gauges the market value of the parent company's holdings in Time Warner and Starz Entertainment. LCAPA is up 27.7% so far this year.

So natural resources and media stocks have rewarded us. The other seven significant winners include **Schering-Plough**, which validated our faith in its prospects even when it was on the floor in 2003, is up 37.7% so far. **Honeywell**, the aerospace, defense and controls blue chip and part of the Dow 30, is up 34%. **Fastenal**, a distributor and seller of nuts, bolts, tools and materials for manufacturers, builders, and repair

services, has added 32.9% since its recommendation just three months ago. **Tetra Tech**, in the business of rehabilitating water and other environmental cleanup projects, had been relatively quiet ever since a great spurt shortly after we recommended it, now has come to life, adding 29.5% in 2007. **Sony**, the Japanese media and electronics manufacturer, is up 23.4%, while **Molson Coors**, the beer brewer perennially considered the stepsister to the much larger Anheuser Busch, not only has outperformed Busch since we recommended it but continues that pace this year, adding 22.3% versus BUD's nearly flat 3.2%. Finally, **Sprint Nextel**, the biggest pure domestic wireless investment, that we deem undervalued because of how poorly the merger with Nextel has progressed, is up 20.8% since its February introduction.

As you know, we are opportunistic buyers, and go wherever we gauge the market has underpriced a company or a sector. The best word for our style is "eclectic." However, if there is any trend in what we are putting into the portfolio lately, companies with exposure to technology and telecommunications are popping up more frequently. The irony is that eight years ago, we would not have touched any of them. So the wheel turns.

We are also interested in finding more companies like **Tetra Tech** and **Insituform** that will benefit from infrastructure spending. We also believe that precious metals stocks by the end of this year will have more than recovered from their ho-hum performance so far in 2007, since we expect the dollar to continue to stumble as the subprime story gets worse. We also believe that inflation, which Pollyannas continue to view as benign because it is "non-core," that is because since the economists in Washington exclude energy and food from the "core" inflation figures, they therefore do not really matter, will also rise if only because wage demands are responsive to the real-world cost of living. And in the real world, food and energy loom large. **SA**

Gray Cardiff's Sound Advice is published monthly by S.A. Newsletters, LLC. Editor-in-Chief: Gray Emerson Cardiff. Managing Editor: Steve Horwitz. Executive Editor: Linda Cardiff. Office Manager: Angela Castellano. Subscription rate: \$195 per year. Send subscription requests to: Sound Advice, 939 Hartz Way, Suite 210, Danville, CA 94526. Phone: (925) 838-6710. Fax: (925) 838-0522. Information presented in Sound Advice may be used provided the newsletter—its name and address—is mentioned as the source. The information contained herein has been carefully compiled from sources believed to be reliable, but accuracy cannot be guaranteed. ©2007 S.A. Newsletters, LLC.

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Compassion on a Budget

The graying of America, the inexorable aging of baby boomers, is the demographic trend easiest to detect and profit from. Healthcare, medical devices, businesses that cater to the interests and welfare of the elderly, and senior housing are investments we have profited from in the past whenever the market put them on sale. Every aging American will rely on one or more of these businesses. However, the needs essential for an aging population inevitably lead to end-of-life issues, which brings us to **Odyssey Healthcare (ODSY—Nasdaq)**, the second largest and the purest investment choice among companies that provide hospice care. End-of-life care is still in its infancy, and offers the potential for significant profit, especially because ODYSY shares, we think, are currently on sale.

HOSPICE CARE

Hospice care in the United States did not formally exist before 1974 when the first hospice opened in New Haven, Connecticut, and did not gain wide exposure until Congress in 1983 established hospice care as a Medicare benefit. Though hospices are popularly thought to be where you go when nothing more can be done, they provide essential services, especially relief from pain, and both physical and spiritual care for those for whom no curative procedure remains or who decide that the physical and emotional costs of postponing death are too much. Today there are approximately 3000 hospice programs in the United States, which deliver care primarily to clients in their own homes.

The incentives for government to extend benefits to hospice care are both humane and financial. Surveys support what most of us instinctively understand: we do not wish in our final days to be treated as objects in a hospital bed. We prefer to end our lives not in an institution but among family. Financially, when a patient no longer can benefit from the curative procedures hospitals are best able to provide, it is far less costly to spend those last days either at home or in a setting that doesn't demand expensive high-tech tools, and staffs of medical specialists and nurses.

Originally, hospices cared primarily for cancer patients, but today serve those with a wide range of terminal conditions, though cancer still affects the single largest portion of hospice clients (32% of clients at Odyssey). The other major conditions are end-stage

heart disease (18%), dementia (18%) and debility (15%). About 60% of clients are cared for in their own homes; the balance resides in various care situations ranging from assisted living to hospitals.

Under Medicare coverage, there are four levels of care: Routine Care, which takes place in the client's home or other residence, which in 2006 accounted for 97% of Odyssey's service days and is reimbursed at between \$116 and \$185 a day; Continuous Care, which is billed on an hourly basis and can cost for a full day between \$676 and \$1081. Continuous Care addresses episodes of acute pain or other severe medical issues and is also delivered in the client's home or other residence. Continuous Care accounted for 1.2% of last year's total days of care delivered. General Inpatient Care provides care equivalent to Continuous Care but is delivered in a hospital or other inpatient facility. It is billed at between \$520 and \$807 per day, and accounted for 1.6% of Odyssey's 2006 care delivery days. Respite Inpatient Care is provided in a hospital or other inpatient facility, anticipates routine care, and is intended to relieve for a period up to five days volunteer caregivers—almost always family members—from their demanding responsibilities. It is billed between \$123 and \$180 per day, and accounted for 0.2% of Odyssey's delivered days of care.

ODYSSEY

Odyssey, with a market cap of \$417 million and revenues last year of \$410 million, started in 1996, and went public in 2001. Growth lately has been both organic and by acquisition, but in its earliest years ODYSY got its biggest boost from acquiring existing hospice programs, something we will return to in discussing how the shares have fared. Last year, Odyssey initiated five new hospice programs, and expanded existing programs by 4.5% (vs. 4.1% in 2005). Management expects this year to start three or four new programs. Historically, however, Odyssey built itself through linking established hospice programs (60 acquired since the company began in 1996). Last year, however, it acquired just one program in Georgia, and in 2007 so far has added only a single small operation in Valdosta, GA.

Demographics drive and channel Odyssey's growth. In 2000, it is estimated 35 million Americans were 65 and older (12.4% of the total U.S. population). By 2020,

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with the tide of Baby Boomers cresting, it is projected that there will be 54.6 million in that age group (16.3%). Geographically certain regions contain greater concentrations of older residents, and Odyssey has more than half of its programs in the nine states that account for nearly half of the U.S. population aged 65 or older.

Odyssey, which is domiciled in Texas, has its greatest concentration, 22 programs and three inpatient facilities, in that state. Texas, though it ranks 47th in terms of the percentage of population that is 65 or older, stands fourth (behind California, Florida and New York) in terms of absolute numbers of 65 and older residents (2.07 million). Odyssey, though the concentration of potential clients per state is important, relies on a strategy that emphasizes metropolitan areas with large populations. Each of its programs and facilities is located in either a large city or on its outskirts. Odyssey also is developing satellite offices, extensions of its primary locations that allow it to offer its services to clients in greater metropolitan areas.

Odyssey went public in 2001, rose modestly until 2003 when its shares took off, more than doubling to \$39 between February and November. Fueling that rise was a fast acquisition of other hospice services and the construction of four hospices as well. Investors anticipated Odyssey could continue to expand revenues and profits indefinitely. Bullish investors were wrong, and also failed to factor in the costs involved in both melding new programs into the existing business and building and staffing those expansions. In 2003, the number of hospices increased from 50 to 65, a 30% jump; admissions advanced by 21%; days of care by 35%; cash flow from operations spurted by 47%, and revenues rose by 39%. But the next year, when the pace of growth slowed to only a 12% expansion of hospice programs, a 15% growth in admissions and a 25% increase in days of care, revenues and income from operations respectively increased by “only” 26% and 8%, while earnings per share, which had rocketed in 2003 by 43% in 2004 barely budged, up a modest 10%. Without a turbo-charged expansion program, the shares began to fall, bottoming at \$7.19 in October of that year. The shares reached \$20 at the start of 2006, then retreated again on poor numbers and have muddled around \$11-13. Without a high-speed growth story to whet investors appetite, the market now considers Odyssey stuck between a rock and a hard place: a fixed rate of reimbursement for services and the not

entirely predictable costs of caring for terminally ill clients.

CHALLENGES

The hospice care business presents relatively low financial barriers to new competitors. According to the latest figures, between 2004 and 2005 the number of hospice care providers grew by 8.9% to 2850, of which 54% were not-for-profit. However, the regulatory, billing, and logistical responsibilities inherent in the business do present serious obstacles to survival of new entrants into the business. Odyssey, as a large, seasoned hospice care provider, has the requisite skill set to meet these responsibilities. Though Odyssey has an advantage of size versus most competitors, there are other large providers, Vitas Healthcare and VistaCare, and similar services are also offered in-house by nursing homes, hospitals, and home healthcare companies. Odyssey is larger than Vista (market cap of \$417 million vs. Vista at \$167.3) but is overshadowed by Vitas, a subsidiary of Chemed (market cap of \$1.7 billion), which also, strangely, owns Roto-Rooter. As a subsidiary, Vitas had 70% more in revenues last year than did Odyssey.

Because hospice providers receive nearly all of their revenue from Medicare and Medicaid, they are in effect agents for government programs which set reimbursement levels. Hospice providers have absolutely no ability to adjust their billing to reflect what individual clients require. Aside from the company’s mission to provide care, controlling expenses is the most crucial part of how Odyssey operates. Each client is monitored by a team of medical and social professionals including a supervising physician, a registered nurse, a home health aide, and a chaplain. On an as-needed basis, physical therapists, dieticians and other specialists can become involved in the process. Hence, wages are the single greatest cost component. Last year, two-thirds of Odyssey’s direct hospice care costs, which accounted for nearly 60% of total expenses, were consumed by employees’ salaries, benefits and payroll taxes. Furthermore, as a percentage of costs, these wage-related expenses relative to 2005’s ratio rose 10%. Over the last couple of years, Odyssey has been able to push other costs, such as drugs, lower, but the major burden is wages.

Despite the inevitable role hospice care will play in an aging population, it remains a relatively obscure sector. ...Use of hospice care is growing not just because the elder population is growing but also because more families are becoming aware of the Medicare benefit.

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Medicare adjusts its rates annually, but only toward the end of the fiscal year, which leaves providers in the awkward position of not knowing how much of their request for reimbursement will be paid. Medicare puts a cap on what it will pay annually for hospice care: a dollar amount cap that currently sits at \$20,585, (estimated to be \$21,244 for FY2007). Hospice providers including Odyssey persistently have difficulty with the absolute dollar cap. To add insult to injury, last year Odyssey had to refund to Medicare \$15.4 million not because of exceeding the Medicare cap but because Medicare itself had miscalculated the reimbursement rate.

Odyssey and other providers are lobbying Congress to address the conflict between its promotion of hospice care with the Catch-22 nature of reimbursements. On the one hand, Congress has encouraged broader use of hospice care for all end-of-life conditions, and has done away with any time limit to how long the hospice benefit remains available. Provided the client is diagnosed by two physicians to have a terminal stage condition that is expected to result in death within six months, that person can be admitted to a hospice program, and that client can receive multiple extensions of coverage as long as two physicians recertify a terminal status.

But Congress has not addressed the problem that whereas the typical original hospice care clients were cancer patients, whose medical deterioration was both easy to project and relatively rapid in its course, today clients with much less predictable conditions form the majority. Such patients, even with Routine Care, can exhaust the Medicare annual limit, and should they need repeated expensive treatment not just for the condition that qualified them as hospice clients but also for any of the other non-terminal illnesses they might also have, hospice bills can grow to inpatient hospital levels. This leaves hospices with unattractive alternatives: take only clients with either clearly defined prognoses, discontinue service to clients if they exhaust their budgeted coverage or absorb those costs and risk bankrupting their care programs.

Under these conditions, Odyssey seeks to control its mix of clients, which means that those admitted to its programs should not be overweighted with cases that require extraordinarily expensive care or have a high probability of recertification after recertification. This is not to say that such clients are not admitted. Rather no hospice program can accept every potential client without running the risk of bankruptcy. Were Congress to address the problems created by the gulf between costs and duration of coverage and depth of care and

how they are funded, hospice care providers would be relieved of a terrible moral burden. They also would boom.

Such relief anytime soon from Congress seems unlikely. The primary concern among those skeptical about the hospice sector is that the federal government, strapped for funds, will freeze the reimbursement schedule or even try to cut payments. We'll address this below.

A final problem for Odyssey was resolved last year when the company made a \$13 million settlement with the Department of Justice over billing irregularities that were flagged in 2002. Such shenanigans concern us, but the ODSY's board of directors cleaned house, getting rid of the CEO and others who might have countenanced such activities. Though the company did not admit guilt in its settlement agreement, it did agree to comply with a tough set of rules for through 2011.

Odyssey's fallen stock price reflects both its slowed growth and revenues. However, though the Medicare cap problem is part of the explanation, there are other, more positive reasons for slowing profits. For example, getting inpatient facilities built, staffed and running siphons away cash, as does expanding its marketing arm and instituting a unified computer system to track patients and costs across its many programs. Such costs, we bet, are a springboard for subsequent profitability.

UPSIDE

Odyssey might be out of favor with most investors, but is running its business well. The balance sheet is entirely free of debt, and the management team brought in after the Department of Justice fined the company for billing irregularities has been eliminating costs and improving operations.

We view hospice care providers as a subset of the nursing home care business, though admittedly the services provided are significantly different, and as Odyssey evolves more inpatient care is being provided. Despite the inevitable role hospice care will play in an aging population, it remains a relatively obscure sector. Standard & Poor's survey of the Healthcare Industry, for instance, neglects to discuss hospice care. Use of hospice care is growing not just because the elder population is growing but also because more families are becoming aware of the Medicare benefit. Odyssey itself is accelerating that pattern by putting more money into employees tasked to cultivate referrals from natural feeder sources such as hospitals, assisted living and nursing homes.

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Hospices remain a very fragmented business, offering opportunities for consolidation, which has slowed at Odyssey but can be picked up again should the right assets become available. Furthermore, not just a rising population of potential customers but that rising percentage of families now aware of a Medicare-funded benefit are going to put pressure on hospices to accommodate more customers.

As for arguments that Medicare, facing a rising tide of aging Americans, will squeeze hospice care providers and other healthcare companies in an attempt to save money, we wonder if the exact opposite won't turn out to be the case. First, if Medicare discourages hospice care by reducing reimbursements, hospice care will shrink, which would result in greater pressure on nursing homes and hospitals. Hospice care is not only compassionate but also relatively economical compared to nursing and hospital care. Second, the very boomers who will put pressure on all forms of medical and social care for the elderly will make it extremely difficult for politicians to economize at their expense. Remember, the demographic slice which is more punctual about voting are those between 65 and 74, followed by those 75 and over.

WHO IS BUYING?

Odyssey has been buying back its shares over the last couple of years, committing \$27 million in total, and the prices paid remain above where shares are

trading today. If individual and most institutional investors have abandoned ODSY, there are some significant exceptions. Most recently Wellington Management, a prominent institutional money manager, notified the SEC that it controls 10.3% of ODSY's common, Shapiro Capital Management, an Atlanta money manager with an absolute value-oriented approach, has increased its position to 4.9 million shares or 14.4% of shares outstanding. Finally, management is motivated to get the share price back to a respectable level, since the exercise price for most options senior management owns are well above current levels.

VALUATIONS

Odyssey shares are trading close to their historical average annual low valuations. Price to Sales is at 1.02, well under the average annual low of 1.25. Price to Book Value, which has averaged 2.6 at its average annual low, currently stands at 2.3. Price to Cash Flow is at 14.2 versus a average historical low of 13. Only Price to Earnings, which has an average historical low of 15.7, stands noticeably above that benchmark at 22.1. For the rest, the historical average lows are roughly half of the highs. This is not to say that we expect Odyssey to double quickly, but we do think its role in hospice care has a bright future, that revenues and earnings are primed to rise, and that concerns about Medicare funding strangling the industry are overblown. We recommend buying ODSY up to \$14. **SA**

PORTFOLIO UPDATES

Since the June letter closed on the 15th, the market has been rocketing up and down, but lately it's been up and up big. Over that period, the Dow has added 2%, the S&P 1.3% and the Nasdaq 3.1%. The *Sound Advice* portfolio tacked on 2.5%.

Three double-digit winners were **Liberty Global** up 13.2%, **Coeur d'Alene** up 13% and **Fastenal** up 12.2%. See the mid-year tally that starts on the front page for background on **Liberty**. **Coeur** got knocked down this year after a federal court forced it to shutter operations at its Kensington mine in Alaska until the company could come up with an environmentally acceptable method of disposing of mine waste. The bounce back this month reflects optimism that a solution is emerging. Also, precious metals as a group are firming up. **American Century Global Gold Fund**

added 7%. Even the **Prudent Bear Fund**, which you'd expect to be a loser during a bull rush for the general market, added 1.2% thanks to its positions in junior gold and mining companies, which it holds as a hedge against a weak dollar—which did weaken some more last month. As for **Fastenal**, which had a torrid start three months ago when we recommended it just before it announced better than expected results, did the same for the latest quarter, and was rewarded with a 9.9% jump that day on the news, and 12.2% for the month. As stock markets sizzled in mid-month, so too did much of the U.S. Hot weather supported natural gas prices and helped natural gas producers like **EnCana**, which lately haven't gotten much good news. We're pleased with ECA's sharp bounce back from the mid-\$40s hit in March, but for the last couple of weeks natural gas

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prices have gone into reverse and taken ECA along with them. Investors are waiting for what had been a cool summer to heat up and for what has been a slow start to the hurricane season to pick up. We're not weathermen, and even if we were, we'd probably get the forecast wrong. We just think that EnCana is well positioned to take advantage of continued high energy prices, and that natural gas is more likely to be more expensive in the future. Even with the warmer days, ECA is down 2.4% since the June letter.

It is becoming progressively harder and riskier for energy companies to find new reserves, and it makes good sense to go "drilling" on Wall Street to increase the amount of oil controlled by each share. This can take two forms: first, shrinking the number of shares outstanding has exactly the same impact on shares as finding a new elephant field except you don't have any dry holes or

rapacious governments ready to rip you off should you find this holy grail of energy exploration, and you don't run the risk of sinking tens of millions into a dry hole. Another solution is to acquire other companies. Expect this to pick up.

If supply is getting harder to increase, the stiff prices for oil—now firmly in the low \$70s—have done absolutely nothing to tamp down demand. Two weeks ago, the International Energy Agency issued its Medium-Term Oil Market Report, which asserts that easy accessibility of oil has peaked and is declining steadily. Short of a collapsing global economy, we should expect demand to remain high. Even if we were to erase all geo-political risk, the price of oil will remain well above where energy companies today are modeling their capital expenditure budgets. Though at *Sound Advice* we are distinctly uncomfortable when our recommendations soar, as has energy, in this case we are looking to add more exposure to energy stocks and funds. **Transocean**, the ultra-deepwater driller, added another 5.8% and is most leveraged to expectations for energy prices. Just as we are at the mercy of the energy companies as long as we consume energy, so too are the energy companies at the mercy of those who provide them with what they cannot survive without, which starts with the tools to find and lift oil and natural gas, which explains why BP just signed a \$900 million contract with Transocean to build and deploy an ultradeep drillship. That BP, as other energy companies

over the last couple of years have done, feels it necessary to commission its own drilling ship at a price that would have been stunning before energy prices crashed through the OPEC-imposed \$28 collar is another argument that the energy majors believe high-cost oil and natural gas are here to stay. Can we foresee the day drilling companies will have overplayed their hand and find themselves saddled with too many rigs? Yes,

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but that day is far enough down the road not to be an obstacle to higher prices for such drilling and exploration assets and for shares in companies like Transocean. **Royal Dutch** along with the other big multinationals is also doing nicely, adding 6.5%, and 21% this year. **Icon Energy Fund**, rich in energy service positions had stalled recently, but after the IEA report ICENX jumped and is up 3.7. Then there is **Agrium**, the fertilizer manufacturer, which because it uses natural gas as the primary feedstock for its nitrogen fertilizers we had always treated as a kissing cousin to energy. Now that ethanol has become part of the energy supply, it is all the more yoked to energy. On the final trading day of June, agricultural commodities were in turmoil as planting figures were announced. The big news, which we wrote about over the last few months and should come as no surprise, is that corn planting is up nearly 19%, driven by high corn prices, which in turn are driven by demand for food and for energy (ethanol). Growing corn demands high levels of fertilizer, which means that not only is agricultural production going great guns but the need for what Agrium produces grows along with those stalks. Since the last letter, AGU is up another 8%.

The **New York Times** dropped 6.2% as investor interest in newspaper takeovers, recently focusing on Dow Jones, the owner of the *Wall Street Journal*, cooled. We believe pessimism about the future of newspapers, though well founded on changing technologies, overlooks a handful of special cases, the most significant

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Income With Growth	Symbol	Exchange/ Phone	Price/ N.A.V.*	Yield**	Buy Limit	ACTION
HRPT Properties	HRP	NYSE	\$10.80	7.78%	\$11.50	BUY
Diversified Growth						
Agrium	AGU	NYSE/TSE	\$45.74	0.24%	\$47.00	BUY
American International	AIG	NYSE	\$69.55	0.72%	\$75.00	BUY
Boston Scientific	BSX	NYSE	\$15.41	0.00%	\$18.50	BUY
Coca-Cola Enterprises	CCE	NYSE	\$24.35	0.99%	\$26.00	BUY
ConAgra	CAG	NYSE	\$27.20	2.65%	\$29.00	BUY
CSX Corporation	CSX	NYSE	\$48.23	0.83%	\$51.00	BUY
Disney	DIS	NYSE	\$34.37	0.90%	\$37.00	BUY
Dodge & Cox Intl.Fund	DODFX	800-621-3979	\$50.78	1.12%	N/A	BUY
Excelsior Value & Restructuring	UMBIX	800-446-1012	\$61.99	0.77%	N/A	BUY
Fastenal	FAST	NASDAQ	\$47.32	0.89%	\$50.00	BUY
Fidelity Japan Fund	FJPNX	800-544-8888	\$18.49	0.00%	N/A	BUY
Gabelli Global Telecom	GABTX	800-422-3554	\$26.63	0.53%	N/A	BUY
Getty Images	GYI	GYI	\$49.05	0.00%	\$56.00	BUY
Honeywell	HON	NYSE	\$60.14	1.51%	\$64.00	BUY
Insituform Technologies	INSU	NASDAQ	\$22.09	10.84%	\$25.00	BUY
Johnson & Johnson	JNJ	NYSE	\$63.43	2.36%	\$69.00	BUY
Liberty Capital	LCAPA	NASDAQ	\$125.13	0.00%	\$130.00	BUY
Mattel	MAT	NYSE	\$26.53	2.45%	\$32.00	BUY
Microsoft	MSFT	NASDAQ	\$29.82	1.34%	\$34.00	BUY
Molson Coors Brewing	TAP	NYSE	\$92.86	0.88%	\$100.00	BUY
Newell Rubbermaid	NWL	NYSE	\$29.61	2.84%	\$32.00	BUY
New York Times Co.	NYT	NYSE	\$24.27	2.88%	\$27.00	BUY
Odyssey Healthcare	ODSY	NASDAQ	\$12.36	0.00%	\$14.00	BUY
Perrigo	PRGO	NASDAQ	\$20.55	0.88%	\$23.00	BUY
Sara Lee	SLE	NYSE	\$17.29	2.31%	\$20.00	BUY
Schering-Plough	SGP	NYSE	\$32.48	0.68%	\$37.00	BUY
Sony	SNE	NYSE	\$52.75	0.41%	\$59.00	BUY
Sprint Nextel	S	NYSE	\$21.70	0.46%	\$24.00	BUY
Superior Industries	SUP	NYSE	\$22.54	2.84%	\$24.00	BUY
Tetra Tech	TTEK	NASDAQ	\$23.43	0.00%	\$26.00	BUY
Third Avenue Value Fund	TAVFX	800-443-1021	\$66.08	5.05%	N/A	BUY
United Parcel	UPS	NYSE	\$75.15	2.02%	\$82.00	BUY
Wal-Mart Stores	WMT	NYSE	\$49.15	1.36%	\$52.00	BUY
WisdomTree Dividend Top 100 Fd	DTN	NYSE	\$62.64	3.16%	N/A	BUY
Xerox	XRX	NYSE	\$19.90	0.00%	\$21.00	BUY
Energy/Natural Resources						
American Cent. Gold Fund	BGEIX	800-826-8323	\$19.86	0.25%	N/A	BUY
Anglo American PLC	AAUK	NASDAQ	\$32.32	1.81%	\$36.00	BUY
Coeur d'Alene	CDE	NYSE	\$4.17	0.00%	\$4.00	BUY
EnCana	ECA	NYSE/TSE	\$64.11	0.94%	\$75.00	BUY
Icon Energy Fund	ICENX	800-764-0442	\$41.09	8.18%	N/A	BUY
Plum Creek Timber	PCL	NYSE	\$43.30	3.70%	\$46.00	BUY
Royal Dutch Petroleum	RDS.A	NYSE	\$84.22	2.91%	\$87.00	BUY
Transocean	RIG	NYSE	\$108.94	0.00%	\$112.00	BUY
Aggressive Growth						
Comcast	CMCSA	NASDAQ	\$27.97	0.00%	\$30.00	BUY
Discovery Holdings	DISCA	Nasdaq	\$23.95	0.00%	\$27.00	BUY
Electronic Data Systems	EDS	NYSE	\$27.87	0.72%	\$30.00	BUY
Liberty Global	LBTYA	NASDAQ	\$44.50	0.00%	\$50.00	BUY
Maxim Integrated	MXIM	NASDAQ	\$34.96	1.89%	\$38.00	BUY
Mitsubishi UFJ Financial	MTU	NYSE	\$11.23	0.85%	\$16.00	BUY
The Prudent Bear Fund	BEARX	800-711-1848	\$5.74	1.74%	N/A	BUY
Symantec	SYMC	NASDAQ	\$19.80	0.51%	\$22.00	BUY
Time Warner	TWX	NYSE	\$20.86	1.05%	\$24.00	BUY
Western Digital	WDC	NYSE	\$21.28	0.00%	\$25.00	BUY

*Prices as of the market close on Friday, July 13, 2007

**Yield represents all distributions during current calendar year divided by share price.

BUY, HOLD, SELL OR LIMIT IN BOLD SIGNALS CHANGE IN ACTION OR LIMIT

Sound Advice Market Indicators for July

of which is the NYT because of its rich content and its iconic reputation. Furthermore, the Times is making solid progress in developing an Internet presence. We can afford to be patient with the Old Gray Lady.

Boston Scientific slid 6.1% on absolutely no solid news. The stock is in Wall Street limbo until investors decide the market for drug-coated stents has recovered from a series of published studies that, we believe, overhyped their negative aspects. Also, new competition is entering the market, and though BSX owns the right to produce what is the most promising of the newest stents, it also must pay a hefty royalty for that privilege. Finally, the remaining problems inherited from the acquisition of Guidant have to be resolved. Boston Scientific is sitting on valuable assets. It just has to make them work.

American International Group is under a cloud as the subprime mess worries Wall Street. AIG, is far too strong (market cap of \$180 billion) for its exposure to be devastating. We are talking about a flea on an elephant. Nonetheless, the market punished the shares, dropping the price 4.2%. Most stocks are bought to be sold, but when an AIG or a **Johnson & Johnson** goes on sale, it should be bought and built upon.

As the dollar has slipped, companies' foreign investments have prospered. **Dodge & Cox International Stock Fund** is up another 4.4%, **Fidelity Japan Fund** 3.5%, though **Sony**, which has been on a run this year, dropped 3.3% as competition heated up in the game console market. **Mitsubishi UFJ**, Japan's largest banking company, was down 3.7% on disappointment that the Bank of Japan continues to postpone an increase in interest rates. Putting some direction in the Japanese yield curve would be helpful to bankers.

If MSFT hasn't begun to fulfill our expectations—it's been only a month—our other forays into technology are starting to pay off. **Maxim Integrated**, the semiconductor manufacturer, rose 6.4%, **Western Digital**, the hard drive maker, added 7.7%, while **Electronic Data Systems**, the information and technology management company, tacked on another 2.7%. Though **Xerox** today is not much thought of as a technology company, it is being thought better of as a force in the copier and printing industries, and added 5.5% amid expectations that earnings, to be announced on July 25, will be strong. **SA**

The Sound Advice Market Indicators

The Diffusion Index of Lagging Indicators gives "Sell" signals when all of its individual lagging economic indicators rise above their respective levels of six months earlier. This reveals a strengthening economy and inflationary pressures ahead.

The Diffusion Index of Leading Indicators gives "Buy" signals when its individual leading economic indicators drop below their respective levels of six months earlier. This reveals a softening economy and a ripe atmosphere for a lasting decline in interest rates.

We have modified the selection of the individual leading indicators that make up our Diffusion Index of Leading Indicators. Two of the indicators we were previously using, the average weekly claims for unemployment and the manufacturers' new orders for consumer goods, were continually being revised each month, sometimes so extensively that buy signals would change due to the revisions. The new leading indicators we are using now are (1) average weekly hours for manufacturing, (2) manufacturers' new orders for non-defense capital goods, and (3) interest rate spread between 10-year Treasury bonds and the federal funds rate. The latest signal came from the Diffusion Index of Leading Indicators, a 100% reading in December

Buy Signals		Sell Signals	
Date	S&P 500	Date	S&P 500
Sep-69	94.51	Feb-69	101.50
Nov-74	71.74	May-73	107.20
Jan-81	132.97	Aug-77	97.75
Sep-85	184.06	Dec-83	164.36
Mar-89	280.00	Oct-87	280.16
Oct-92	415.10	Sep-89	347.33
Feb-97	798.38	Jan-95	464.72
Feb-03	841.15	Sep-99	1,383.60
Dec-05	1,248.29	Jul-05	1,234.18

2005. Prior to our modifications, the 100% reading came in June 2007.

If we had followed the signals from our modified Diffusion Indexes over the years, we would have done very well indeed. The results are shown above. Between each "Buy" signal and each "Sell" signal, the S&P 500 rose substantially without exception. The average gain was 34 percent, not counting dividends. On an annualized basis the gain was 17.7 percent per year. Confining stock investing to these times would have produced substantially more profits than a single buy-and-hold strategy.

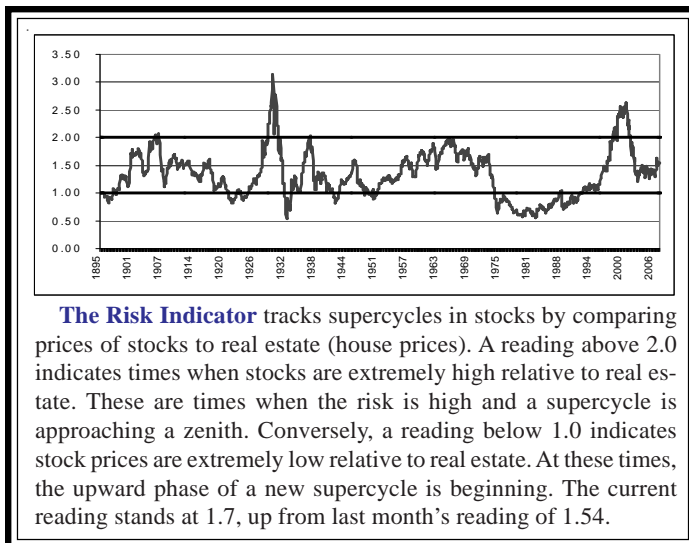
During the intervening periods between "Sell" signals and "Buy" signals, the market was all over the place — sometimes crashing, sometimes meandering, and occasionally

Sound Advice Market Indicators for July

advancing. On average, the S&P 500 increased 6.8 percent during these times. On an annualized basis, not counting dividends, the gain was a paltry 0.6 percent per year, a return that could have easily been beaten many times over with safe investments such as Treasuries, short-term bonds, or other low-risk investment.

Why does the market crash sometimes after “Sell” signals and sometimes not? We believe the answer lies in the shear level of the market at the time “Sell” signals occur. If the market is high, it is logical to expect stronger corrections than when it is not. How high is high? We can detect how high the market is with the Risk Indicator. If the Risk Indicator is close to or above 2.0, we know the market is high relative to real estate, and likely contains a high degree of risk. This was indeed the case in September 1999 when the Diffusion Index of Lagging Indicators flashed a “Sell” signal and the Risk Indicator was (substantially) above 2.0. The peak came in six months, marking the end of the bull market as well as the peak of Supercycle Five. The market subsequently crashed. The S&P 500 dropped 39 percent until the next “Buy” Signal was given by the Diffusion Index of Leading Indicators in February 2003 (which was the exact month that bear market low point was reached). During that decline, most stocks suffered greater losses. The NASDAQ dropped nearly 80 percent.

Conversely, the market does not suffer lasting declines after “Sell” signals when the market is low, and not filled with risk. For example, the “Buy Signal” in November 1974 was one month from the bottom of that bear market, and it was at a time when the Risk Indicator was below 1.0. Consequently, this “Buy” signal market also marked the beginning of Supercycle Five. As the upward phase of Supercycle Five ensued, the market did not experience lasting downturns after “Sell” signals. Instead, the bull run was merely interrupted with short declines, sideways movements, and sometimes even advances. Even the three-day decline in October of 1987, which became known as



the “Crash of 87”, was followed by a stampede of buyers snapping up bargains. I remember seeing individual investors lined up to invest outside discount brokerage offices because the phones were log-jammed with buyers.

However, as previously noted, when Supercycle Five reached its peak and the Risk Indicator climbed above 2.0, the decline was severe after the September 1999 “Sell” signal due to the excessive heights to which prices had previously been propelled.

We recommend remaining fully invested in the *Sound Advice* model portfolio at all times. We use the *Sound Advice* Market Indicators to influence our approach and nature of our recommendations. When “sell” signals are in force, our recommendations are defensive in nature. We will be looking for special situations and are likely to recommend taking profits more readily. Conversely, during “buy” signals, our recommendations will be more aggressive. We believe that these proprietary indicators have been important factors in our ability to consistently outperform the market averages. The chart below shows how *Sound Advice* recommendations have performed versus the S&P 500.

Since 1-1-2000

Sound Advice versus the S&P 500

An Investment of \$25,000 becomes:

Start Date	S&P 500		Sound Advice*		
	Annual Return		Annual Return	Advantage Over S&P	
From 1/1/2000	\$29,910	2.4%	\$59,822	12.3%	\$29,913
From 1/1/2003	\$47,929	15.4%	\$56,941	20.2%	\$9,013
From 1/1/2006	\$31,997	17.5%	\$33,885	22.8%	\$1,887

* These returns assume an equal amount is invested in all *Sound Advice* Model portfolio positions at the time of the initial recommendation.

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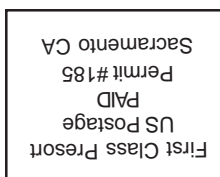
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