

# SOUND ADVICE

Volume XX, Number 3

Subscription Rate: \$195 per year

March 16, 2007

## Do You Need A Million Dollar Budget To Beat Wall Street?

When the market goes over the cliff, or even stumbles which it did in late February, many stop and wonder how we could have been so foolish as to risk our financial health in a market that can be so painful? One day, we're hitting new highs. The next, we're trying to determine where the bottom might be. Accept the obvious truth: markets fluctuate, and part of making money over the long haul inevitably involves losing it too.

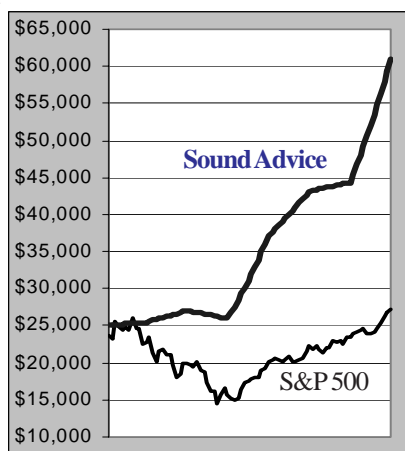
The quality of advice that emerged during the late February swoon was all over the board, and some of it just plain overboard. Congenital bears announced that finally the apocalypse was upon us. At the other end of the spectrum, knee-jerk bulls proclaimed that this was just a healthy pause to slow the market down, a springboard to even higher prices. Those poor people on CNBC, whose job descriptions must include "be bullish 24/7," looked miserable, cheering any upswing, and grudgingly acknowledging each retreat. At one point on Thursday, when the Dow opened down 200 points after Wednesday's mild bounce that followed Tuesday's 416 point drubbing, they muttered about Doug Kass

from Seabreeze Partners Management, a notable short-side player, who announced on the Monday before Shanghai collapsed and global stock markets went south that his short position was now 100%. The gist of the CNBC evaluation of Kass' exquisitely timed commitment was that Kass gets to be right three or four days a year.

Frankly, I don't understand why they badmouth the bears, since if the CNBC crew truly believed in the market, they would accept that it runs both ways. In fact, if they truly understood investing, they would appreciate that down markets, whether the down lasts a week or a year, are when shrewd investors make money by taking advantage of others' pessimism. Perhaps the CNBC mindset merely reflects the dangerous truth that most can deal only with a rising market, and miss entirely the usefulness of a decline.

Nonetheless, CNBC is the dominant source of TV financial information. Derided as "Bubblevision" thanks to its unrelenting bullishness during the bubble, if nothing else it's a true barometer for investors' mood. In addition to the core programming CNBC during the trading day,

### Performance History: Sound Advice versus the S&P 500



Since 1-1-2000

#### An Investment of \$25,000 becomes:

Start Date	S&P 500		Sound Advice*		
	Investment	Annual Return	Final Value	Annual Return	Advantage Over S&P
From 1/1/2006	\$28,762	12.6%	<b>\$33,752</b>	<b>28.9%</b>	<b>\$4990</b>
From 1/1/2003	\$43,082	13.9%	<b>\$56,867</b>	<b>21.7%</b>	<b>\$13,785</b>
From 1/1/2000	\$26,885	1.0%	<b>\$61,741</b>	<b>13.4%</b>	<b>\$34,856</b>

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

# Need A Million Dollar Budget to Beat Wall Street?

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there are satellite shows such as Fast Money and On the Money. The best known must be Mad Money, 60 minutes of Jim Cramer manically opining on the prospects for individual stocks.

## *JIM CRAMER*

Bull markets always have had media stock touts, but Cramer, I believe, is something new. Certainly back in late 1999 and early 2000 he set himself and his followers up for disaster by declaring that tech stocks were the only way to make money, even though if you looked at his portfolio as revealed in SEC filings, you discovered he had plenty of exposure to less sexy, and sometimes downright dowdy companies that were hardly momentum darlings. It's not that he exhorted investors to do one thing, and did the opposite. Rather, he recognized that what the public wanted was bullishness on what was hot, while personally he appreciated some balance in his portfolio. Maybe he learned something from the aftermath of that mistimed bullishness, since today one feature of the Mad Money format is "Am I diversified?" during which callers lay out their portfolios for Cramer to decide whether they are balanced.

Lately, Cramer has been dueling with Henry Blodget, another media creation from the bubble years, whose errors of judgment far outstrip anything Cramer did. Blodget is barred for life from the financial industry because of his role as an Internet analyst at Merrill Lynch in recommending highly stocks of companies he privately considered "crap" in order to curry favor and financial rewards for Merrill's investment banking arm. He has carved out a new career as a financial journalist, most notably covering the Martha Stewart trial for *Slate.com*, and more recently writing a financial advice column for the same site that culminated in a book, *The Wall Street Self-Defense Manual*. Blodget, no fool, appreciates the irony of his new role as a defender of the small investor, though the rest of us might find his new persona as sincere as Paris Hilton trying to play Miss Manners.

Blodget tossed down the first challenge in his column at the end of January, branding Cramer's Mad Money advice "terrible," though Blodget did recognize that in addition to the Mad Money manic Cramer "there is, of course, another James J. Cramer—the one who graduated from Harvard Law School, writes an often sober and astute column in New York magazine, and might actually have put up decent numbers at a hedge fund in the 1990s ... That Cramer is a smart man."

Within days, Cramer shot back, calling Blodget "a disgrace to the business and a creep" during an

appearance on the Don Imus radio show, and took CNBC to task for giving Blodget airtime to plug his book. Blodget came back quickly on Slate in a less confrontational tone by responding to readers' arguments in favor of Cramer.

The one that caught my attention rebutted Cramer's insistence that "you have to do your homework" before putting your money into his recommendations. Blodget belittles the prospects a puny private investor can achieve, because the little guy lacks the tools professionals wield. "Remember, your competition—all other traders—are primarily full-time professionals who do nothing but research and trade all day long. Unless you have a multimillion-dollar research budget, a platoon of brilliant analysts, relationships with salespeople at all major brokerage firms, relationships with senior managers at every company, a Rolodex full of industry contacts, and a decade or two of trading experience, you will be at a serious disadvantage no matter how much research you do. Remember, too, that the vast majority of professionals, even those who possess all of the above advantages, lose the speculation game (because it is really hard to win)." Blodget, belittling even well-connected analysts and fund managers, recommends a diversified portfolio of index funds for retail investors. Perhaps this is true for investors with neither the time to identify funds (to say nothing of individual stocks) with potential for long-term superior performance, nor the temperament to tolerate market fluctuations. But it underestimates what well prepared retail investors like you and I can do.

I was floored by Blodget's smug arrogance that what analysts do is beyond the skills of anyone without an armada of contacts, number crunchers and a multimillion dollar research budget. Obviously, as publisher of *Sound Advice*, I am biased in favor of what an individual investor can accomplish without the access the disgraced Blodget, who had all these tools but instead betrayed his clients, considers essential. We do not do anything that any reasonably intelligent investor can do by using tools that are available to all of us.

The metrics we use are pretty simple: the standard price ratios are dominant, and we put them in the context not of the current market but of the individual stock's historical ranges. We tend to be optimistic about management's ability eventually to realize the value we discern, though at times that gap between value and price was created by poor management decisions, especially acquisitions. It took new management to get **Time Warner** moving in the right direction after it merged with AOL. We have a couple of more current instances that are still not resolved such as **Boston**

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The SEC last week launched Operation Spamlot, an attempt to reduce those touty-tacky emails promising incredible returns. Rather than try to stop at their sources the tide of unsolicited come-ons, the SEC has suspended trading in shares of the touted companies. All trade on the Pink Sheets, a relatively unpoliced badland where caveat emptor reigns.

You might ask yourself, what are the schnooks who buy this stuff thinking? The answer comes from that initial twitch originating somewhere deep in the brain's most primitive place: I could get rich on this! Do the math: \$5000 invested in what looks like a lock that will return 1000% in a year. I confess that when I read these emails, there's a nanosecond during which that reptilian part of my brain kicks in.

Preparing the cover story that talks about Jim Cramer's Mad Money show, I watched a few installments. Cramer dramatically warns his audience not to buy his recommendations immediately, since not only would they be buying in the thinly traded aftermarket but also because even in the following days the "Cramer Effect" can distort prices. So it was amazing to see that in the 60 seconds immediately after Cramer recommended a stock, it rocketed higher by 10% and then fell back to even, then charged higher again. The fascinating part of that trading pattern is not just that Cramer's audience violated his advice but that other audience members were primed to short that stock as soon as the Cramer Effect hit. The ones who made the quick kill were the shorts.

Greed makes us miss the obvious.  
--Gray Emerson Cardiff

## Maxim at Minimum

A funny thing happened to tech companies on the way to the future. Well, maybe it wasn't very funny for shareholders who drank the Kool-Aid that Wall Street was distributing and paid silly prices based on silly valuations back in the late 1990s. For those who were two-fistedly grabbing tech stocks and either dumped them during the darkest times when they were down by 75% or more or held on waiting to at least "get back to even" before bailing, it's no consolation that over the last four years those shares have recouped some of their losses. Really, if you are still holding names like Cisco, Intel, Sun, Microsoft, Amazon, Yahoo!, or EMC, you are underwater anywhere from 85% (Sun) to 56% (Oracle) from their 2000 highs. For those of us who were too dumb to understand the allure of New Era stocks, today's prices and valuations are more attractive, and seven years after the party peaked, we're ready to pick and choose among the discarded.

**Maxim Integrated Products (MXIM—Nasdaq)** enjoyed the semiconductor industry's steep rise that took wing in the early 1990s. MXIM soared above better known names like Intel and Advanced Micro Devices. At one point in 2000, MXIM wore a triple-digit P/E ratio. The shares bottomed in the fall of 2002, and though they have increased by roughly 50% since then, their rebound fizzled out in June 2004, and trails the overall tech sector despite Maxim being one of the most respected and profitable semiconductor makers.

The problem is pretty simple. The supply of semiconductors currently exceeds demand, and prices are soft. For most industries, a cyclical downturn is natural, and offers an excellent opportunity to buy. It should be no different here, even though the technology sectors and their fans are still having trouble with the concept of a business cycle, since until 2000, they blithely assumed their sectors were immune to the financial gravity that is the business cycle.

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# Sound Advice on Maxim Integrated Products

## WHAT MAXIM DOES

Investing is hard enough when you are looking at companies whose products we recognize and use. For example, if you are considering investing in [Sara Lee](#), there are few mysteries about food products. And we've all seen the "Intel Inside" logo on computers, but most have no clue as to what that Intel microprocessor does. Semiconductors are solid state objects whose electrical conductivity can be controlled over a wide range, and are the building blocks from which complex circuits and processors are built.

Maxim is in the analog and mixed-signal end of the business. More semiconductor manufacturers march to a digital beat, that is, because computers and so many other electronic devices are based on digital technology that can process only simple discrete signals. The older analog technology that transmits data in a format that tracks the continuous physical world (e.g. a vinyl recording played on a turntable is analog; a Compact Disc is digital) is mistakenly considered as obsolete as those pure analog media such as a 33 RPM vinyl record.

To the contrary, though electronic devices do converse in digital language, we, their users, live in an analog world, from which all signals must be translated for these devices as digital inputs and trans-

lated out again for us non-digital people as analog outputs. As *Standard & Poor's* notes in its last survey of the semiconductor industry "It is a curious irony that, as more information is digitized, more and more analog chips are required to assist the digital chips that process, transmit, and store information so handily in the digital language of zeroes and ones. Analog or "linear" semiconductors are used to handle continuous signals found in the real world, such as sound, light, heat, and pressure. In a common example, a mobile phone has a digital signal processor (DSP) at its heart, but it relies on a cluster of analog chips around the DSP chip to convert the voice signals to digital format for manipulation by the DSP, and then translate them back again to analog format for listening. Analog chips also are needed to manage power usage, which is particularly important for portable electronics, where battery life is a key product feature."

In fact, analog circuits are showing faster growth (11.9%) in revenues than are digital chips, though flash memory chips are showing the fastest growth of all (13.7%). However, most flash memory chips, which are primarily used to store data in cameras, audio and video playback devices, have become commodities that compete primarily on the basis of price. Indeed,

the commoditization of technology products is technology's curse, since no one can maintain fat margins for long. Competitors develop a me-too version, or the manufacturer of the original product introduces the next-generation version, and makes the previous version somewhat obsolete. To a significant degree Maxim is insulated from some of this commoditization, because many of its products are highly engineered for products with long lives.

Maxim, like many semiconductor makers, was founded by engineers and industry veterans, and its engineer-centric culture is its biggest asset, since the training to design analog semiconductors involves a longer apprenticeship than for digital circuits. *Morningstar* notes that because "major U.S. research universities haven't trained sufficient numbers of analog engineers for two decades [has] only made these workers more valuable." Hence, retaining engineers is essential in Maxim's world, and the company enjoys a reputation for keeping its most productive workers. Maxim estimates it lost about 1% of its engineering staff last year, a modest number in the tech world.

## MAXIM'S ADVANTAGES

Maxim's mix of clients provides diversification. Sales are distributed

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## Sound Advice on Maxim Integrated Products

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roughly evenly into four sectors: computing (pcs, servers, peripherals, storage and financial terminals), high-end consumer goods (cell phones, digital cameras, digital tvs), industrial (including automotive), and communications.

Not surprisingly, Maxim is seeing its biggest growth in the hottest consumer areas. Hence, sales to laptop makers as well as high-end consumer product manufacturers led revenues last year, and offer the brightest future expansion for sales.

The flipside for these expanding high volume markets is that margins are somewhat slimmer than for circuits sold to industrial and automotive customers. This explains why Maxim is reporting somewhat lower overall margins for the past few quarters. Also, these volume customers linked to consumer demand are less able to predict how many units their products will consume, since their needs depend on fickle consumers. This creates inventory problems for Maxim: stockpile too many, and you might end up writing off some as excess inventory; stock too few and you delay deliveries.

The trick for Maxim will be to cut costs for these high volume products, and also learn how to cope with their volatile demand fluctuations. Management believes it can do this, and thus bring profit margins for these high volume customers more in line with those derived from sales to industrial equipment and automotive clients.

In the industrial and automotive sectors, sales tend to be more stable because the products into

which Maxim's circuitry goes have much longer product cycles and demand patterns.

Sales are also diversified geographically: about three quarters of revenues come from clients outside the United States. Asia accounts for more than half of all sales, and Chinese companies, at around 23%, constitute the largest market after our own. Hence, Maxim is a prime beneficiary of any further weakness for the dollar.

### **SEMICONDUCTOR CYCLE**

Analysts, who were so convinced that the semiconductor industry was insulated from the business cycle,

**If we look at where Maxim shares stood at their bottom in 2002, today's price ratios suggest we are at or close to another bottom. At the end of September 2002, Maxim hit \$22, and traded at a P/E of 28, a P/S of 6.5, a P/CF of 21, and a P/Bk of 3.8. Each of these ratios currently stands below that low-water mark except for price to book, which is around 4 today versus 3.7 in the fall of 2002. In short, we think MXIM, though hardly cheap in comparison to non-tech cyclicals, in the context of its specific history, is attractive.**

have become acutely aware of just how vulnerable all tech products are to fluctuations in demand. In the wake of the 2000 collapse and subsequent feeble demand for semiconductors, MXIM's sales per share dropped 32% in 2002 while earnings were down 22%. In 2006 earnings dropped 13% as demand again troughed during the second

half of the year, which has left Wall Street skeptically waiting for evidence of increasing orders.

This is nothing more than the downside of the semiconductor business cycle, and no one should be surprised at disappointing numbers. During last month's conference call, Alan Hale, the interim CFO, reported that Maxim's 12-month order backlog had declined from the previous quarter by 2.9% to \$402 million. Gross bookings had slipped by 1% to \$500 million. Furthermore, revenues for the next quarter are expected to be weak, perhaps down as much as 6%. After hearing Hale, analysts were quick to ratchet down their price targets and directional recommendations for share prices. However, anytime there is even a hint that sales might be perking up—such as last month when Apple introduced its iPhone concept not only did Apple jump but so did the shares of any company that might be a supplier to Apple. Maxim was up 2.4%—buyers jolt the share prices for the entire semiconductor sector. When there is no follow through, prices settle back again. At some point, there will be follow through. That is when you want to have accumulated your position, not afterward.

We're content to be a buyer during this fallow season not only because we're confident that the chip cycle will swing upward at some point and that Maxim products will prosper, but also because Maxim has a beautiful balance sheet buttressed by generous cash flow that gives it immense flexibility to im-

# Sound Advice on Maxim Integrated Products

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prove its business and benefit shareholders while we wait.

## **WHERE TO USE FREE CASH FLOW**

Even in slow times, Maxim is a cash cow, throwing off hundreds of millions in free cash flow (operating cash flow less capital expenditures and other costs of running the business). Since the fourth quarter of 2002, Maxim has paid a dividend, which began with a token annual payment of 8 cents (0.02% yield) to today's 62.4 cents (1.9%), which puts it among the few companies in the tech sector that pay a meaningful dividend. Last year, free cash flow ran at \$481 million, down from the previous year's outstanding \$566.6 million, and is expected to reach \$580 million this year.

In the most recent conference call, when the new CEO, Tunc Doluca, was asked how the company might use its cash hoard, the first alternative he mentioned was an increase in the dividend. Second, he said he wanted the company to resume its share buybacks. Third, he said Maxim is always interested in "very opportunistic" deals, conceding, however, that in the company's history they have been very few, since "we don't want to take a lot of risk in that area."

## **MAXIM UNDER A CLOUD**

Maxim currently is not buying back shares until it has restated its earnings because of how the company priced options, a problem currently affecting some 140 U.S. cor-

porations. After reviewing how Maxim awarded options, auditors concluded that the company would restate its numbers from 2000 through March 2006, since adjustments due to option dating will produce "material" differences. Maxim has not filed either a recent 10Q nor the 2006 10K. Management presiding over the second-quarter conference call relied on provisional numbers, and could not provide clarity on earnings.

This has put a cloud over Maxim and obscures previously reported results. Not surprisingly, it also has depressed MXIM's share price, since the market punishes companies in trouble as if the worst possible outcome is unavoidable.

We don't dismiss the significance of corporate officials lining their own pockets at the expense of shareholders, but we also don't expect the issue to cripple Maxim or its shares once the company has fessed up. In a press release accompanying the options report, Maxim noted that in connection with the investigation its previous CEO and Chairman of the Board, Jack Gifford, who had continued as a "strategic advisor" after retiring at the end of last year, had resigned that role, and also that Carl Jasper, the CFO, had departed as well.

Gifford's abrupt resignation implies he played a part in whatever options problems are now upsetting Maxim, though it would be wrong to see Gifford as some glad-hander who contributed little but took much. In fact, Gifford was a pioneer in the industry, a founder of Maxim, and lived Maxim's best qualities: a focus on analog circuits,

a commitment to research, and an ability to develop new products and churn them out cost-effectively.

## **VALUATIONS**

Valuations are attractive. Maxim has been a publicly traded company only since 1989, and for much of the 1990s traded at unsustainable multiples of the standard ratios such as price to cash flow, price to sales, price to book value, and price to earnings. Certainly these numbers skew the average historical lows for such valuations, especially because of Maxim's relatively brief history. If we look at where Maxim shares stood at their bottom in 2002, today's price ratios suggest we see, to be at or close to another bottom. In September 2002, Maxim hit \$22, and traded at a P/E of 28, a P/S of 6.5, a P/CF of 21, and a P/BK of 3.7. Each of these ratios currently stands under that low-water mark except for price to book, which is around 4 today versus 3.7 in the fall of 2002. In short, we think MXIM, though hardly cheap in comparison to non-tech cyclicals, in the context of its specific history, is attractive.

Over the last few months, we've been recommending fallen angels from the tech bubble, and expect there will be more. Our reasoning is consistent with the arguments we made for REITs, for natural resource stocks, and for other companies and sectors down on their luck. Do we know when the demand cycle for analog chips will turn higher? No. Do we know it will? Yes. Maxim is cheap today, and worth buying up to \$36. **SA**

## PORTFOLIO UPDATES

On February 27<sup>th</sup> the market fell apart, and though there's been enough rebound that pundits are now tut-tutting what transpired as just a normal correction, what we saw was a wake-up call that complacency and cheap credit (they are related, you know) might be drying up.

We cannot stress enough how Japan's ultra-low interest rates have provided much of the easy money for so much of the global equity binge. If you want evidence, all you need do is look at what suffered the most once Shanghai started the retreat: high-yield stuff, currency-related investments, REITs (another high-yield proposition), and anything that speculators used leverage to magnify their profits got hammered more than the rest of the market. The drop in natural resource shares and even precious metals—which traditionally serve as a safe harbor during financial storms—suggest how borrowing financed much of equities' buoyancy. **These concerns prompt us to sell two positions: Friedman, Billings, Ramsey, and Telecom New Zealand.**

Even after the U.S. equity markets regained their composure, since the last letter, the Dow is down 2.4%, the S&P 2.5%, and the Nasdaq 2.9%. The *Sound Advice* portfolio dropped 1.2%, or on a total return basis, 0.9%. **Sprint Nextel**, last month's recommendation, had an excellent start, adding 8.3%. Management announced results for the last quarter: higher revenues and better-than-expected earnings were good news, while a loss of 306,000 postpaid subscribers was bad news. None of this comes as a surprise, and leaves intact the thesis we presented in the February issue: the melding of Nextel and Sprint remains a rocky work-in-progress that will prove profitable.

Perhaps expectations of such encouraging results explains why S had advanced over the last few weeks, but obviously it came as a surprise to most of Wall Street, which

greeted it with a 4.6% jump on the day. Don't presume that it's up, up, and away for Sprint. Our scenario acknowledges the company has problems that likely will push the stock down at certain points.

Given the market's downward tilt, the **Prudent Bear Fund** performed as expected, adding 4.3% as its bias toward short positions and long Treasuries pushed its NAV higher.

**Getty Images** exploded in mid-February when rumors began to circulate that it was in advanced negotiations to acquire Jupitermedia, a smaller competitor specializing in rights free images, a relatively low-margin business but a thorn in Getty's side because Jupiter has cut prices. Then later in the week, Getty announced it had agreed to buy WireImage for \$200 million. WireImage, one of the biggest distributors of celebrity images, fits nicely with Getty's other lines. After celebrating the potential deals, the market started to reconsider, and shaved off most of the runup, and when the parties announced

negotiations to acquire Jupiter had ended, GYI dropped some more, finishing the month down 2.5%.

**Friedman Billings Ramsey** has been painful as its mortgage-REIT

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portfolio has gotten slammed repeatedly by an extremely poor environment for such debt. We are selling FBR despite believing it's been overly punished for exposure to the mortgage market. We also are selling **Telecom New Zealand**, because we are concerned about what could happen to all Kiwi positions should interest rates trend lower there, or rates rise elsewhere, thus diminishing the Kiwi dollar's attractiveness. A good part of our 46% run since introducing NZT last August comes from the jump in the exchange rate, and now is as good a time as any to take our profits.

More positively, the offspring from Liberty Media keep on giving: a spinoff, **Discovery Holdings**, jumped 7.4% after announcing a fine quarter for its various entertainment assets. **Liberty Global**, another spinoff exposed to European and Asian media, added 2.9% and **Liberty Capital**, a tracking stock for Liberty Media's passive and some actively managed businesses, contributed a 1.2% increase. Behind the Liberty

## Sound Advice: Portfolio Updates for March 2007

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family's run is the holding company's announcement that it is exchanging shares in CBS for a TV station in Green Bay, Wisconsin and \$170 million in cash. Liberty is also on the verge of acquiring from Time Warner the Atlanta Braves. This comes on the heels of a much bigger deal between Liberty and News Corp. that swaps Liberty's substantial News Corp. holding for a controlling interest in the satellite TV provider, DirecTV, cash, and control of three regional cable sports networks. Liberty is liquidating its passive interests in major corporations for real assets, and seems to be positioning itself to become an operator not a spectator. Several other stocks surged such as **Molson Coors** (+5.8%) **Agrium** (+10.3) but it's probably more useful to look at values, we believe, the market drop has created. **Perrigo**, the generic OTC and prescription drug maker, made two acquisitions since the last letter, and both of them are expected to add immediately to profits. Last month, it announced a \$56 million purchase of dermatological products from Glades Pharmaceuticals, and last week added the purchase for \$12 million of a privately held manufacturer of store-branded anti-lice and nit products. Both acquisitions are excellent fits for Perrigo. The first deepens its prescription salve business, and the second adds a significant product line missing from Perrigo products. They bought both at a good price. The market in its wisdom chopped PRGO down, and since the last letter it is off 3%. We think this is an invitation to build your position.

**Boston Scientific** is another opportunity. Unlike PRGO, news has been negative and has dropped it 9%. BSX and other stent makers earlier in February got some relief from previous negative news about the risks drug-coated stents present to a

small segment of patients, but almost as soon as that report appeared, a piece in the *New York Times* noted that bypass surgery, another way to deal with blocked blood vessels, is again receiving consideration in some cases that more recently had been treated with stents. The problem, of course, is that bypass surgery involves cracking the chest and is very, very serious surgery. We think that stents have a bright future, though we are quite prepared to accept that in that future other procedures have a role.

We also believe that Boston Scientific will make its pricy acquisition of Guidant pay off. But in the mean time, the costs involved in that deal and the continuing negativity surrounding BSX stents and Guidant defibrillators has put BSX in the hot seat, which got hotter last week when Moody's implied Boston's bond rating is headed toward junk status, not good news but also not unexpected given the pressures Boston faces. Additionally, law suits stemming from Guidant products sold before BSX acquired it, are numerous and worrisome for investors. None of this was hidden from us when we recommended Boston Scientific. Our thesis remains unchanged: Boston Scientific plus Guidant can now be bought for less than the market cap of Boston Scientific before it acquired Guidant. Certainly this fire-sale price takes into account the problems listed above, but, we think, far overstates their damage. At some point, we will look back to BSX at under \$16 and wonder how the market missed such a bargain.

We're also interested in natural resource stocks, which dropped not only because speculative money retreated but also because markets worried that the Shanghai implosion signaled a slowing in the Chinese economic juggernaut, a conclusion

we believe to be false. Indeed, just as we are closing the March issue, news (<http://www.nytimes.com/2007/03/10/business/10yuan.html?ref=business>) is circulating that China is about to launch a national investment bank similar to a very successful program run by the Singapore government to diversify national holdings away from passive currency and bond positions to the ownership of "strategic assets" — mines, oil fields, whole companies — around the world, especially in developing countries in Africa and Latin America." This isn't entirely new, and will institutionalize initiatives we've described earlier in which Chinese corporations have acquired interests in Canadian, South American, and African energy and metal still underground. Don't expect China to thrust \$1 trillion into the market tomorrow, but watch companies closely that both have rich assets in these regions and are already doing business with China. For just a random example, think **Anglo American**. Despite the downdraft that hit natural resource shares, AAUK eked out a 0.4% rise. **Plum Creek Timber** lost 4.8%, **Royal Dutch** 2.2%, **EnCana** 1.5%, while **Transocean** kept its head above water adding 0.4%, and **Icon Energy Fund** added a respectable 1.4% for the month.

We also think the dollar has not finished dropping, so keep precious metals in your portfolio. **Couerd'Alene** added 0.9%, while **American Century Global Gold Fund** gave back 5.2%.

Coincident with Japan raising its short-term rates to 0.5%, the Yen strengthened against the U.S. dollar, which automatically had a positive impact on Japanese share prices when translated back into dollars. **Fidelity Japan Fund** added 4.6%, **Sony** 5.6%, and **Mitsubishi UFJ** 3%. **SA**

# Sound Advice Portfolio for March 2007

Income With Growth	Symbol	Exchange/ Phone	Price/ N.A.V.*	Yield**	Buy Limit	ACTION
HRPT Properties	HRP	NYSE	\$12.73	6.60%	\$14.00	BUY
Senior Housing Properties	SNH	NYSE	\$23.23	5.85%	\$27.00	BUY
<b>Diversified Growth</b>						
Agrium	AGU	NYSE/TSE	\$39.37	0.28%	<b>\$42.00</b>	BUY
American International	AIG	NYSE	\$69.07	0.72%	\$75.00	BUY
Boston Scientific	BSX	NYSE	\$15.77	0.00%	\$20.00	BUY
Coca-Cola Enterprises	CCE	NYSE	\$20.25	1.19%	\$24.00	BUY
ConAgra	CAG	NYSE	\$25.14	2.86%	\$29.00	BUY
CSX Corporation	CSX	NYSE	\$37.85	1.06%	\$40.00	BUY
Disney	DIS	NYSE	\$34.37	0.90%	\$37.00	BUY
Dodge & Cox Intl.Fund	DODFX	800-621-3979	\$44.62	1.28%	N/A	BUY
Excelsior Value & Restructuring	UMBIX	800-446-1012	\$63.22	0.76%	N/A	BUY
Fidelity Japan Fund	FJPNX	800-544-8888	\$17.70	0.00%	N/A	BUY
Gabelli Global Telecom	GABTX	800-422-3554	\$22.84	0.61%	N/A	BUY
Getty Images	GYI	GYI	\$49.74	0.00%	\$56.00	BUY
Honeywell	HON	NYSE	\$47.23	1.92%	\$50.00	BUY
Johnson & Johnson	JNJ	NYSE	\$62.14	2.41%	\$69.00	BUY
Liberty Capital	LCAPA	NASDAQ	\$108.25	0.00%	\$110.00	BUY
Mattel	MAT	NYSE	\$27.70	2.35%	\$29.00	BUY
McDonald's	MCD	NYSE	\$44.15	0.52%	\$47.00	BUY
Molson Coors Brewing	TAP	NYSE	\$86.35	0.95%	<b>\$92.00</b>	BUY
Newell Rubbermaid	NWL	NYSE	\$30.59	2.75%	<b>\$32.00</b>	BUY
New York Times Co.	NYT	NYSE	\$24.00	2.92%	\$27.00	BUY
Perrigo	PRGO	NASDAQ	\$16.55	1.09%	\$20.00	BUY
Safeway	SWY	NYSE	\$34.27	0.68%	\$38.00	BUY
Sara Lee	SLE	NYSE	\$16.70	2.40%	\$18.00	BUY
Schering-Plough	SGP	NYSE	\$23.85	0.92%	\$28.00	BUY
Sony	SNE	NYSE	\$52.49	0.41%	\$55.00	BUY
Sprint Nextel	S	NYSE	\$19.47	0.51%	\$21.00	BUY
Superior Industries	SUP	NYSE	\$22.06	2.90%	\$24.00	BUY
<b>Telecom New Zealand</b>	<b>NZT</b>	<b>NYSE</b>	<b>\$26.22</b>	<b>8.52%</b>	<b>N/A</b>	<b>SELL</b>
Tetra Tech	TTEK	NASDAQ	\$17.06	0.00%	\$20.00	BUY
Third Avenue Value Fund	TAVFX	800-443-1021	\$60.32	5.54%	N/A	BUY
United Parcel	UPS	NYSE	\$70.63	2.15%	\$82.00	BUY
Wal-Mart Stores	WMT	NYSE	\$47.42	1.41%	\$52.00	BUY
WisdomTree Dividend Top 100 Fd	DTN	NYSE	\$59.10	3.16%	N/A	BUY
Xerox	XRX	NYSE	\$17.05	0.00%	\$18.00	BUY
<b>Energy/Natural Resources</b>						
American Cent. Gold Fund	BGEIX	800-826-8323	\$18.44	0.27%	N/A	BUY
Anglo American PLC	AAUK	NASDAQ	\$23.90	1.81%	\$29.00	BUY
Coeur d'Alene	CDE	NYSE	\$4.29	0.00%	\$5.50	BUY
EnCana	ECA	NYSE/TSE	\$47.89	1.25%	\$52.00	BUY
Icon Energy Fund	ICENX	800-764-0442	\$31.52	10.66%	N/A	BUY
Plum Creek Timber	PCL	NYSE	\$38.62	4.14%	\$41.00	BUY
Royal Dutch Petroleum	RDS.A	NYSE	\$65.12	3.76%	\$74.00	BUY
Transocean	RIG	NYSE	\$77.57	0.00%	\$82.00	BUY
<b>Aggressive Growth</b>						
<b>Comcast***</b>	<b>CMCSA</b>	<b>NASDAQ</b>	<b>\$26.12***</b>	0.00%	<b>\$30.00***</b>	BUY
Crescent Real Estate	CEI	NYSE	\$20.27	7.40%	\$22.50	BUY
Discovery Holdings	DISCA	Nasdaq	\$17.24	0.00%	<b>\$18.35</b>	BUY
Electronic Data Systems	EDS	NYSE	\$27.60	0.72%	\$30.00	BUY
<b>Friedman, Billings, Ramsey</b>	<b>FBR</b>	<b>NYSE</b>	<b>\$5.92</b>	<b>3.38%</b>	<b>N/A</b>	<b>SELL</b>
Liberty Global	LBTYA	NASDAQ	\$30.40	0.00%	\$32.00	BUY
<b>Maxim Integrated</b>	<b>MXIM</b>	<b>NASDAQ</b>	<b>\$33.02</b>	<b>1.89%</b>	<b>\$36.00</b>	<b>BUY</b>
Mitsubishi UFJ Financial	MTU	NYSE	\$11.93	0.80%	\$16.00	BUY
The Prudent Bear Fund	BEARX	800-711-1848	\$5.87	1.70%	N/A	BUY
Symantec	SYMC	NASDAQ	\$16.84	0.59%	<b>\$22.00</b>	BUY
Time Warner	TWX	NYSE	\$19.87	1.11%	\$22.00	BUY
Western Digital	WDC	NYSE	\$18.18	0.00%	\$20.00	BUY

\*Prices as of the market close on Friday, March 9, 2007

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

\*\*\*Comcast split 3:2 on 2/22/07

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

(...continued from inside front cover...)

**Scientific**'s purchase of Guidant, or **Symantec**'s acquisition of Veritas, or, last month's recommendation, **Sprint** after it bought Nextel. Blending two companies is always a challenge, especially when the acquirer overpays, or has a poorly conceived business model for the new entity. The value is still there, and either current management or someone else will unlock it.

Just look at our performance numbers on the front page to see what's possible. We're not so vain to believe that we're unique at doing what Blodget claims only the best-heeled professionals can aspire to accomplish. There are other newsletters and there are other

individual investors who have market-beating results. There are mutual funds that run rings regularly around their benchmark indexes and around funds that mirror those indexes. Blodget is just plain wrong.

If you were rocked by last month's turbulence, welcome to reality. If you responded to those tough days by buying selectively, congratulations on what ultimately will be a profitable decision. Meanwhile, keep looking for opportunities, and keep reading *Sound Advice*. If you see a red alert on this issue advising that your subscription needs renewal, please choose from the generous options on the facing page.

## The Sound Advice Market Indicators:

**The Diffusion Index of Leading Indicators** gives "buy" signals when all five of its 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. **Currently, 40% of its leading indicators are above their levels of six months earlier.**

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While 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 and we 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.

**The latest signal came from the Diffusion Index of Lagging Indicators, a 100% reading in October, which constitutes a "sell" signal.**

**The Risk Indicator**, which tracks the Supercycle, the overarching investment climate as expressed by the relative prices of real estate and equities, remains firmly in favor of equities being overpriced versus real estate. The current reading stands at 2.7.

### History of the Signals

- \* 2003 In March, just before the surge in the market, the indicators gave a buy signal. The S&P 500 advanced more than 40%.
- \* 2000 In May, close to the peak of the market, the indicators signaled the end of the bull market. The market subsequently dropped 40%.
- \* 1995 In March, the indicators gave a sell signal. Then in July, they gave a buy signal. The S&P rose 153% until the next sell signal in May 2000.
- \* 1988 In January, the indicators signaled the subsequent bull market that took stock prices up 95% until the next signal.
- \* 1987 Six weeks before the 1987 Crash, the indicators gave a sell signal.
- \* 1981 A buy signal occurred close to the beginning of the next bull market that carried stock prices up 145%.
- \* 1980 A sell signal warned of that year's bear market.
- \* 1974 With the Dow Jones trading below 700, the indicators issued a buy signal, announcing a 6-year bull market.
- \* 1973 They signaled a "sell" just prior to the bear market that cut stock prices in half by October 1974.
- \* 1970 The indicators signaled the beginning of the new bull market.
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