



“Have it your way,” Burger King’s slogan designed to move Whoppers, when you stop to think about how the average shareholder has fared compared to insiders is itself a little whopper that is an exaggeration. “Have it our way,” is closer to the truth, at least when it comes to how the company is being taken private. Last month, among a number of larger merger stories it was announced that a private equity firm will pay \$3.3 billion (plus debt) or \$24 a share to take BK private. You might have thought, “Gee that’s a sweet deal for the shareholders.” Only in part. The real deal accrued to Goldman Sachs, Bain Consulting and TPG Capital. Sure \$24 represents a 46% premium above where shares traded before the offer, but when Burger King came public in its 2006 IPO, the price was \$17 a share, essentially where it stood before the surprise bid from another private equity group. A secondary offering in 2007 was priced at \$22, not much below what shareholders now are getting. Burger King had been something of a Wall Street urchin, moving from corporate parent to corporate parent like Pillsbury in 1967 and Diageo in 1989. Then in 2002, as Diageo sought to focus on its spirits businesses by dumping Burger King, a troika of private equity funds, TPG, Bain and Goldman, bought the struggling burger franchiser for \$1.5 billion (about 13% of that was an equity investment, the rest was borrowed). This is who made the real bucks. Even before the IPO, thanks to successive special dividends, the original buyers had received back all of their original equity investment. They were now playing with free money. The IPO and the secondary offering generated \$887 million for them, some of which paid off debt, some of which went into their pockets. Of the original partners, the three private equity funds retained some of their shares, about 32%, for which they are now going to receive \$1 billion. I wonder how the new private equity owners are planning to milk their new cow?

-Gray Emerson Cardiff

AWOL Investors

Last week’s *USA Today* was brave enough to put this headline on its front page: “Could Investors Fleeing Stocks Become a Lost Generation?” We say “brave,” because most editors remember how many of their predecessors used similar cover stories trumpeting either “the death of equities” or a “permanent bull market” just before stock prices robustly reversed those global pronouncements. Who can forget the *Economist*’s March 1, 1999 cover “A World Awash in Oil” and its prediction of \$5-a-barrel oil? The *USA Today* story, which harks back to how retail investors after the Great Crash of 1929 swore off stocks, describes chastened investor after chastened investor who has pulled out of the stock market. The reasons are many: distrust of market manipulation, distrust of regulators, anxiety over the bleak current economy, and, most of all, that they’ve lost money over the last decade, especially if they piled on at the peaks in 2000 and 2007 and/or bailed out at the bottoms in 2003 and 2009. Perhaps *USA Today* will be right. Maybe retail investing is dead for a generation, or perhaps the story is similar to the *Business Week*’s August 1979 “Death of Equities” cover story, which, to say the least, was premature. Though the full-throated bull market in stocks would not occur until 1982, stock prices did not fall appreciably below where they were when that cover hit the newsstands.

But that was then, and now is now, and maybe it really is different this time. Maybe *USA Today* is on to something. As we note in this month’s recommendation on page 3, when we were composing the piece during mid to late August, the market was dropping, pessimism was rampant. As we close this issue (September 3rd), the market has rallied strongly, dispelling at least for the moment some of that pessimism. However, even when the market has been in rally mode starting in March 2009, individual investors have missed out, it appears, on the rally.

We’ve used cash flow into mutual funds as a window into the retail investor’s mood and over the last couple of years,



it's been decidedly wary. Even during 2009's robust rally, net cash flows favored bond funds in every single month regardless of how well stocks were faring, and whenever equities faltered, that flow out of stocks and into bonds turned into a tsunami. The Investment Institute of America, the mutual fund industry's research arm, estimates that as stocks tanked during the first 25 days of last month, investors pulled \$11.1 billion out of stock funds and poured \$28.6 billion into bond funds. We expect, when we have figures for the last week of August, which saw a rising stock market and a falling bond market, that the disparity between stock and bond fund flows won't reflect that reversal.

It's not just the little guy who is exiting the market. Last month, Stanley Druckenmiller, head of Duequense Capital Management and a George Soros disciple, sent his limited partners a farewell letter confessing that after 30 years of managing money he's fallen short of his "own internal long-term standard". Yet here we are at *Sound Advice*, still believing that economy is on the mend, still imagining we can outperform the market, perhaps not at the level of Druckenmiller's "internal long-term standard," but well enough to keep our wealth growing. But it's a lonely position to hold.

Most newsletters are pessimistic now. The Hulbert Stock Newsletter Sentiment Index tracks sentiment, and as of late August, just as stock prices were about to reverse, had declined precipitously. The average market timer was so certain of a decline that they recommended shorting the market. Contrast how they felt in early August after the market had rallied. At that moment, just as stocks were about to complete a nice rally and then falter, the same universe of market timers had an average 48% long recommendation. It was even worse among newsletters that try to time the tech-centric Nasdaq. As Hulbert notes: "Their average exposure now stands at minus 50%, which means that they're now allocating half their equity portfolios to an aggressive bet that the market will continue declining." But not everyone is dour.

Indeed, we were heartened when the *Hulbert Investment Digest*, the only unbiased arbiter of newsletter performance, last month devoted its cover story to nine newsletters Hulbert has placed—at least for now—onto his "Honor Roll." We (yes, *Sound*

Advice is one of the nine) earned that distinction "by acquitting [our]selves in both up and down markets—and therefore are not predisposed to seeing the glass either as always half full or as perennially half empty. In other words, [we] are neither bullish nor bearish stopped clocks." Statistically we nine outperformed in both up and down markets over the past dozen years. Hulbert notes that our durable results did not produce the absolute highest returns (though *Sound Advice* over the last decade stands second among the still-published letters Hulbert follows), but, to use Hulbert's baseball metaphor, we all had a high on-base percentage, and if we didn't hit as many home runs as some, we didn't strike out as much as most.

What is remarkable about these nine is that even with most market observers lukewarm or worse about where the market is heading, every last one of us is bullish. Many of us are fully or close to fully invested, and even the most cautious, the *Cabot Market Letter*, though 42% in cash, wants its subscribers to start to wade deeper into stocks.

But what about the *USA Today* premonition that we could be heading back to the 1930s when the common man swore off stocks? Well, maybe we should look back not at the folktales but to the numbers during the Great Depression. If we do, we find that the environment for investors was not depressing at all. In fact, stock prices during most of the 1930s rose from their devastated low set on July 8, 1932 to a peak five years later on March 3, 1937. The Dow Jones, for instance, almost quadrupled over those years even without the little guy's participation. Prices would then drop as markets shivered in the shadow of approaching war. The Dow finally bottomed in April 1942, more than double where it had been at its low a decade earlier, and then began a strong rally through the end of hostilities in 1946.

Sound Advice anticipates a rising stock market and an improving economy. We acknowledge that runs counter to what not only most retail investors expect but also what many talking heads and money managers say. We're OK with marching to a different drummer. **SA**

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Tech is Cyclical and Right Now That's Good

It is an extraordinarily difficult time to commit funds to the stock market. Sure, there are stagnant stocks that are relatively high dividend payers, like last month's recommendation, **Pfizer**, that pay you a solid dividend as you wait for the market to turn upward. But the idea of investing in cyclical sectors when consensus expectations point toward more contraction is—if you move with the herd—patently foolish, which brings us to this month's recommendation **Seligman Premium Growth Fund (STK—NYSE)**, a recently launched (but very well seasoned) closed-end fund (CEF) that focuses on the shares of technology companies.

Why Technology?

Why buy a technology fund now? Good question because the tech-centric Nasdaq is lagging a weak market since both peaked in late April. Not only during the 1990s' bull market's final phase but over the last decade in every significant move, both to the upside and the downside, the Nasdaq has led the way. Since the April high, the Dow is off 6.8%, S&P 500 9.3% and the pan-market Wilshire 5000 9.6%, while the Nasdaq has dropped 11.7%. The notion that tech stocks were immune to the business cycle, a very popular opinion as the tech bubble in late 1999 and early 2000 boiled its way toward implosion, has mutated into the view that tech stocks are extremely sensitive to the business cycle. Our perspective on the economy remains positive, though tested by recent events: we expect to see the U.S. economy resume its recovery. If we are right, having some diversified exposure to technology makes sense.

Selecting A Fund

The simplest choice would be an ETF like the SPDRS XLK or QQQQ, an ETF that tracks the 100 largest non-financial stocks in the Nasdaq. However, we believe that a handful of fund managers whose discipline and track record demonstrate they can outperform their benchmarks are the best choice. The best of that group, we think, is Paul Wick, the lead manager for the Seligman Premium Growth Fund. He has worked for Seligman for 23 years, managed its Communications and Technology Fund, an open-ended mutual fund, for the last 20 and has lived through all phases of the sector: the total market collapse of 1987, the recessions of 1990, 2001 and our current bout, the craziness of the tech bubble, the viciousness of the tech collapse

and the two rallies of 2003-2007 and 2009. Wick has seen it all. His longevity is the exception among fund managers in ultra-volatile techland, where careers can get terminated with any market twitch.

But STK began trading only at the end of last November, hardly enough time to gauge it. However, Seligman's Technology and Communications Fund is the model for the CEF we are recommending and is the natural surrogate for how STK would have performed in earlier years. The mutual fund is among *Morningstar's* top-performing tech funds. Indeed, the five with superior records over the past few years either did not exist or were just getting started when the 2000 tech collapse hit. If you stand back and survey the chart on page 4 that covers decade, you see that even with that the hit Seligman took in 2000, it handily outperformed both the QQQQ and the largest tech ETF (XLK), which did not exist during the tumultuous 2000-2002 collapse. Furthermore, Wick performed this well despite having to manage a much larger asset base: most of these funds are minnows (assets under \$40 million), while the Seligman fund is a \$3.4 billion whale.

Wick's style respects fundamentals and is long on patience. Most of the fund's largest positions have been at its core for years and in some cases for more than a decade. In a sector whose volatility is matched by managers' rapid trading, Wick's buy and hold approach is out of step—which might explain why he has outperformed the pack.

The Closed-End Seligman Fund

Closed-end funds are commonly considered disappearing dinosaurs, which first mutual funds and now Exchanged Traded funds are supplanting. So why did Seligman roll out a dinosaur? We suspect Wick appreciates the advantages the closed-end structure gives him.

In his CEF Wick has considerably more latitude in how he manages his assets. Aside from closed-end funds being traded on exchanges throughout the day rather than being transacted between the fund itself and its shareholders after the daily market close, the most obvious difference between a mutual fund and a closed-end fund is that the manager is never forced during market declines to liquidate assets to meet redemptions from anxious shareholders. Mutual

Seligman vs. Standard Tech ETFs: 2000-2010



funds in normal times usually hold a cash buffer to meet day-to-day redemptions, since it is the fund that handles all buys and sells, but during any significant downturn in investor sentiment, a manager must raise extra cash to meet heavier redemptions regardless of his views of his portfolio's potential. Effectively shareholder concerns manage the manager. CEF shares are bought and sold between shareholders, which lets the manager focus on his portfolio. There are no redemption pressures for the closed-end fund manager. For a shrewd investor, the best time to be able to buy is when others are desperate to get out. For the mutual fund manager, forced sales are hellish. For a closed-end fund manager, they can be buying opportunities.

Also, this closed-end fund's relatively smaller size (\$259 million market cap versus \$3.4 billion for the open-ended fund) could let Wick include more shares of small cap companies, something he operationally cannot consider in the much larger mutual fund. Indeed, some of Wick's success in that mutual fund comes from his use of mid-cap stocks, which tend to have more potential for appreciation. That's even more true for small-caps.

Regular Distributions from a Tech Fund?

There is another important difference. The Premium Technology Growth Fund is structured to pay shareholders a quarterly distribution under its level distribution program, which currently yields 10.3% based on its 46.3 cent quarterly distribution. Most tech funds do not make distributions except to share short and long term capital gains. For instance, the

last time Seligman's open-ended mutual fund made a distribution was in 2001.

How does the fund expect to make these payouts when tech stocks pay no or modest dividends? The new fund generates revenue by selling options on the Nasdaq 100, which covers the largest, most liquid non-financial companies traded on the Nasdaq. According to the prospectus, the fund can sell calls worth between 25% and 90% of the value of the fund's common stocks. Income from these option sales are intended to cover most of the distribution.

Under most market conditions the writing of call options provides returns that are slightly better than the overall market. But during an explosive bull market the strategy lags a runaway market. Should the value of the mega-cap Nasdaq 100 index outperform the mid and small cap focused STK portfolio, the call option strategy would result in losses for the fund, since when the call owner exercises his option, the Premium Technology Fund would have to sell more of its shares to satisfy the options contract. In a way this sounds like the predicament that the mutual fund manager faces, forced selling. However, forced selling in a rising market is preferable to forced selling in a falling market.

Should options sales and interest on cash not be sufficient to pay out the dividend, the fund will make up the difference through a return of capital. The fund at the end of each year will distribute long-term capital gains in a single payment.

STK Top 10 Positions

	Sector	% of Portfolio	Market Cap	Relative Valuations
Synopsis	Software	7.0%	\$3.4 billion	Below Average
BMC Software	Software	6.0%	\$6.4 billion	Below Average
Apple	Computers	5.7%	\$213 billion	Average
Microsoft	Software	5.6%	\$204 billion	Below Average
Check Point Software	Software	5.3%	\$7.3 billion	Above Average
Amdocs	IT Services	4.4%	\$5.3 billion	Below Average
Parametric Technology	Software	4.0%	\$2 billion	Below Average
Symantec	Software	3.9%	\$10.8 billion	Below Average
Google	Internet	3.9%	\$143 billion	Above Average
Cisco	Communications	3.6%	\$117 billion	Average
		49.4%		

On the Roller Coaster

Tech stocks have been on a vicious ride over the last 15 years. Ten years after the 2000 collapse, few cherish the 1998-1999 bubble's euphoria. Wick's investing approach has him outperforming in normal and down years and modestly lagging during explosive up markets. With the Nasdaq down 60% from where it stood in early 2000, performance by tech-centric funds has been in shambles. Since the Premium Growth Fund has been in business for less than a year, we'll use the Seligman Information and Technology Fund's history to examine what Wick has done over that period and how his approach has fared. Seligman markets A,B and C shares, and we will use the A share version (SCMIX) since it comes closest in expenses to the closed-end fund STK.

As 2000 was getting underway after the most explosive year for tech stocks, Wick acknowledged all the positives underpinning the U.S. economy (low unemployment, low interest rates, low inflation, soaring consumer confidence, technology-driven increasing productivity) but clearly was uneasy with the speculative turn stock prices and technology prices in particular had taken: "While ... highly enthusiastic about technology, we believe that investment behavior in this area has become increasingly speculative and, as we seek opportunities in this exciting sector, we will remain committed to finding solid investment value and to considering company fundamentals." He was especially leery of the gains Internet service and infrastructure shares had racked up and had a mere 2.6% of his portfolio in such companies and had been trimming his higher valuation stocks. Where was Wick overweighted? Shares in software companies

represented 24.3% of the portfolio at the end of 1999. Wick has been consistent in favoring software firms, since they usually provide reliable revenue streams.

If Wick was wary about tech in general, he hardly was tech-phobic. As the market was approaching the end of its run, Wick's cash position was 2.9%, which suggests two things: he was pretty much fully invested and thus did not anticipate a flood of redemptions. In terms of relative performance, 2000 would turn out to be one of two years till now that Wick underperformed his peers, falling 4% further than did tech funds tracked by Lipper. That group dropped 33%.

In 2001, however, as the Lipper cohort dropped another 38% and the S&P 500 tumbled 12%, Wick was able to eke out a 4% gain thanks to common sense: "respecting valuations and fundamentals kept him away not only from the most speculative stocks, but also from the most expensive." Instead, he became "more defensive -- purchasing lower-priced stocks, and emphasizing dependable businesses with recurring and predictable revenues (=software, which that year accounted for 41% of the portfolio). He also overweighted midcap stocks, which in 2001 outperformed larger-cap stocks.

But being cautious has a price. In 2003 when the market began a multi-year rally, his fund lagged the Lipper cohort 42% versus 56%, his other shortfall year. Indeed, in 2002 as the bear market ground onward and chewed up tech stocks, Wick introduced a novel theme for a tech fund: healthcare shares, which at first glance might seem a reach, since his portfolios never had ventured beyond commonly accepted technology and communications shares. Wick's rationale was (and remains) that many of the same dynamics he

understood so well in traditional technology and communications sectors also animate life sciences companies: both rely on intellectual property, have high margins and offer significant barriers against competition. Provided they are not start-ups or are on what can be either the cutting or the bleeding edge of technology, healthcare stocks are far less volatile than most tech stocks. Even better, their shares in 2002 had been depressed during the bear market while their sales and earnings had risen. Characteristically Wick did nothing abruptly. His holdings at mid-year 2002 amounted to 2.3% of his portfolio, but by the end of 2002 that had jumped to 12.7%, its high water mark.

During 2002, a truly ugly year, Wick “outperformed” (-36.8%) both his benchmark index (-40.3%) and his peer group of tech managers (-42.9%). He observed: “Our investment process leads us to pursue companies that we believe have superior franchises and business models, are generating cash flow, are trading at reasonable valuations, and are guided by experienced management teams. We don’t change our process to be more representative of an index, and we don’t buy stocks simply because they are popular with our peers.” At the end of that year, 42% of the portfolio was in software companies’ shares. However, cash had jumped to 9.7% after the fund trimmed some of its positions in November when the market rallied. November, as it turned out, was the first real stirring before the much larger rally to come in March 2003.

Over the next four years, as the market moved higher, the Seligman fund outperformed its peers, and in 2008 when things fell apart, the Seligman fund dropped 36.5% while the Lipper group fell 43.8%. During the 2009 rally, Wick narrowly outpointed the Lipper group again (59% vs. 58%). This year—and now we can switch to the closed end fund’s performance—STK is even with the open-ended Seligman fund and trails the Lipper index for technology funds slightly.

What is Wick doing now? As of July STK healthcare positions amount to 5.7% of the portfolio and feature two device makers (St. Jude and **Boston Scientific**), Abbott Laboratories, which does both drugs and devices, Gilead, a biotech company and Life Technologies, a scientific tool company. But it’s the

tech component that will make or break results.

We’ve put up a chart for STK’s current (July 31st) portfolio. The ten largest positions in a portfolio of 52 holdings account for half of the entire fund and habitually emphasize software (6 positions) and services (1), which meet Wick’s criterion for recurring income. Only one trades at valuations higher than its peers. Also, note the market caps: Six of the core positions are mid to small cap companies, which Wick

If...the U.S. economy is in the process of struggling out of the deepest recession of our generation, it’s reasonable to expect tech to flourish. Wick’s experienced, disciplined approach to equities’ wildest sector appeals to us, and we appreciate the opportunity to take advantage of that skill set at a lower annual cost than were we to use the open-ended mutual funds Seligman offers

believes have more potential for growth and price appreciation than larger cap behemoths like Apple, Microsoft, Google and Cisco. Over the past few years, the underperformance by mega-cap tech stocks, can be seen on page 2 in the underperformance of the QQQQ versus the Seligman fund. Our experience with superb fund managers is that their holdings in less prominent names underpins

their performance. Certainly that has been the case with Wick at Seligman.

Costs

As a closed-end fund, shares of STK are purchased on an exchange at a minimal transaction cost. The expense ratio runs currently at 1.26% of its net asset value, a smaller expense ratio than for any of STK’s mutual fund siblings, which makes it more efficient to own. STK at the moment trades at a minuscule discount (-0.7%) to its net asset value. However, most of the time it has traded at a small premium, which results from the unusual level distribution policy that returns income to shareholders quarterly and when necessary returns capital to fulfill that obligation.

Summary

If you agree with our premise (and indicators) that the U.S. economy is in the process of struggling out of the deepest recession of our generation, it’s reasonable to expect tech to flourish. Wick’s experienced, disciplined approach to equities’ wildest sector appeals to us, and we appreciate the opportunity to take advantage of that skill set at a lower annual cost than were we to use the open-ended mutual funds Seligman offers. Finally, since STK trades at modest levels (the average number of shares traded year to date has been 62,000), we encourage you to use limit orders set at a price close to the last trade rather than market orders when buying or selling. We recommend buying STK up to \$20. **SA**

Portfolio Updates

When Wall Street types get honest, they're likely to tell you that the market's reason for existing is to make as many people as possible feel like fools, which is another way of saying that when the herd moves in one direction, you can expect the market itself to move in the other, something we explore in our cover essay. As we entered the last week before Labor Day, anyone who paid attention to the financial media was confident that the market was sure to fall during that last week's holiday-induced thin trading. In other words, prices would continue to absorb the punishment suffered over the previous few weeks. So, of course, the market rallied strongly into the holiday weekend. Still, since we priced the August issue, share prices have dropped between 1.3% (S&P) to 2.4% (Nasdaq). *Sound Advice* registered a 0.8% decline.

The August recommendation, **Pfizer**, increased 1.4%, double the rise for the Dow Jones U.S. Pharmaceuticals ETF (IHE). In fact, Pfizer had to overcome collateral damage from word that Lilly's experimental drug to treat Alzheimer's Disease failed (in fact, it seems to have worsened the condition at least in the far-advanced cases it was used to treat). Since Pfizer is working with Elan, an Irish drug developer, on a similar treatment for Alzheimer's, Lilly's failure shook PFE's share price, but the shares came back.

Events in a related stock don't have to be negative. We've had two clear examples so far this month. **Agrium**, the fertilizer maker, benefited from BHP Billiton's hostile approach to Potash Corp. of Saskatchewan, which has rebuffed a \$38.6 billion offer as inadequate. Agrium, which does mine some potash in Canada but is much more of a nitrogen-based fertilizer maker, jumped 9.4% since the last letter. **Symantec** got two boosts and added 7.2%. First, Intel announced it had entered a merger agreement to acquire McAfee, against which SYMC competes in the computer security market. Then a bidding war broke out between Dell and Hewlett Packard over 3Par, which markets software for large-scale data management. Symantec, through its Veritas division, also participates in large-scale data management, and its share price benefitted from the

Dell-HP confrontation. It's not that we are angling for Symantec to be an acquisition target. Rather the spike in interest in security and large-scale data management that these two deals represent reflects well on what Symantec does and goes a long way in reassuring us about SYMC's eventual recovery.

But most shares responded to investors' fears of impending economic doom. Consider **Tetra Tech**, which continues to rack up new contracts and announced a deal to acquire a Canadian engineering firm that specializes in environmental projects. All of this should improve investor views of TTEK's future, but the shares fell 7.9%. Let's see if the proposed infrastructure program rolled out over the Labor Day holiday—if it can get congressional support—can give engineering and environmental firms like TTEK a boost. Regardless, the long-term prospects for a company whose core is environmental remediation, especially for water resources, are extraordinarily bright. With a pristine balance sheet and expansion into international markets, Tetra Tech right now is a bargain.

The **PowerShares Water Resources Fund** numbers TTEK among its largest positions, and it fell 3.4%. As we've noted before, PHO aspires to own assets that exclusively focus on water-related businesses, but for the present must include companies with significant but rarely dominant exposure to water. Because of that tempering of its focus, PHO moves as much with industrial stocks as it does with water. Concerns about a weak economy translate into weakness in industrial shares. So we saw **Honeywell** fall 1.5% and **Fastenal** 2.7%.

However, auto-related shares fared better: **Ford Preferred** eked out a 0.8%, **CarMax** added 4.3% and **Superior Industries**, which sells wheels and other parts to vehicle manufacturers, leaped 9.8%. **International Speedway**, which owns tracks that host NASCAR events announced belt-tightening measures such as reducing ticket prices to keep the stands packed. Because ISCA's clients are primarily blue-collar, younger males—the very demographic hit hardest by the recession—its shares have suffered along with consumer confidence and employment numbers. Since the last letter, ISCA is down 7.7%.

This table has 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	\$26.17	7.64%	\$28.00	BUY
Telecom New Zealand	NZT	NYSE	\$7.49	9.48%	\$8.00	BUY
Diversified Growth						
Agrium	AGU	NYSE/TSE	\$72.54	0.30%	\$80.00	BUY
CarMax	KMX	NYSE	\$21.70	0.00%	\$26.00	BUY
CGM Realty Fund	CGMRX	800-343-5678	\$23.96	2.58%	N/A	BUY
Dodge & Cox Intl.Fund	DODFX	800-621-3979	\$31.77	1.37%	N/A	BUY
Dodge & Cox Stock Fund	DODGX	800-621-3979	\$93.75	1.17%	N/A	BUY
Fastenal	FAST	NASDAQ	\$49.36	1.70%	\$60.00	BUY
Gabelli Global Telecom Fund	GABTX	800-422-3554	\$19.27	1.87%	N/A	BUY
Honeywell	HON	NYSE	\$42.82	2.83%	\$49.00	BUY
International Speedway Corp.	ISCA	NASDAQ	\$24.10	0.66%	\$31.00	BUY
Johnson & Johnson	JNJ	NYSE	\$58.93	3.67%	\$68.00	BUY
Leucadia National Corp.	LUK	NYSE	\$23.10	0.00%	\$27.00	BUY
Mattel	MAT	NASDAQ	\$21.94	3.42%	\$26.50	BUY
Microsoft	MSFT	NASDAQ	\$24.29	2.14%	\$33.00	BUY
Molson Coors Brewing	TAP	NYSE	\$44.59	2.15%	\$52.00	BUY
Pfizer	PFE	NYSE	\$16.46	4.37%	\$19.00	BUY
Stryker Corp.	SYK	NYSE	\$46.09	1.30%	\$55.00	BUY
Superior Industries	SUP	NYSE	\$15.91	4.02%	\$18.00	BUY
Tetra Tech	TTEK	NASDAQ	\$19.11	0.00%	\$26.00	BUY
Third Avenue Value Fund	TAVFX	800-443-1021	\$45.20	2.52%	N/A	BUY
United Parcel	UPS	NYSE	\$67.64	0.25%	\$75.00	BUY
UnitedHealth Group	UNH	NYSE	\$33.91	1.47%	\$38.00	BUY
Wal-Mart Stores	WMT	NYSE	\$52.04	2.33%	\$60.00	BUY
Xerox	XRX	NYSE	\$9.09	1.89%	\$11.00	BUY
Energy/Natural Resources						
Anglo-American PLC	AAUKY.PK	PINK SHEETS	\$19.40	0.00%	\$24.00	BUY
Fidelity Select Nat. Gas Fund	FSNGX	800-544-8888	\$28.05	0.20%	N/A	BUY
Plum Creek Timber	PCL	NYSE	\$35.56	4.72%	\$40.00	BUY
PowerShares Water Resources ETF	PHO	NYSE	\$15.68	0.65%	\$19.00	BUY
USAA Precious Metals & Minerals	USAGX	800-862-6909	\$40.89	0.02%	N/A	BUY
Aggressive Growth						
AOL Inc.	AOL	NYSE	\$23.05	0.00%	\$28.00	BUY
Boston Scientific	BSX	NYSE	\$5.35	0.00%	\$8.50	BUY
Comcast	CMCSA	NASDAQ	\$18.21	1.79%	\$21.00	BUY
Davis Financial Fund	DFIBX	800-279-0279	\$22.46	0.00%	N/A	BUY
Ford Motor Convertible Pfd	F.PRS	NYSE	\$47.60	7.28%	\$50.00	BUY
H&Q Life Sciences Fund	HQL	NYSE	\$9.29	6.89%	\$11.02	BUY
Liberty Global	LBTYA	NASDAQ	\$29.00	0.00%	\$32.00	BUY
Maxim Integrated	MXIM	NASDAQ	\$16.91	4.97%	\$21.00	BUY
Seligman Premium Growth Fund	STK	NYSE	\$17.99	10.29%	\$20.00	BUY
Symantec	SYMC	NASDAQ	\$13.98	0.00%	\$20.00	BUY
Third Avenue Focused Credit Fd****	TFCVX	800-443-1021	\$10.98	3.84%	N/A	BUY
Time Warner	TWX	NYSE	\$31.72	2.65%	\$34.00	BUY
Transocean	RIG	NYSE	\$54.33	0.00%	\$75.00	BUY
UltraShort 20+ Treasury ProShares	TBT	NYSE	\$32.72	0.00%	N/A	BUY

* Prices as of Friday, September 3, 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 HRPT (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

Interestingly, while the shares are weak insiders uniformly have been adding to their holdings at prices below their current level, apparently buying in the open market rather than exercising options and retaining shares.

Tech stocks did not avoid the hit to cyclicals: **Microsoft** lost 4.9%, **Maxim** 3.6% and **Xerox** 5.2%.

Miners such as **Anglo-American**, which shed 4.8%, were battered. **Fidelity Select Natural Gas Fund**, amid concerns that in a slowing economy demand for energy would fall, dropped 2.3%. **Transocean**, which continues to dance to the tune of the Gulf of Mexico BP disaster, dropped 4.9%. Here we have not just concerns about energy prices but also whether and when the drilling moratorium will be lifted and especially whether BP can shift blame for what happened in the Gulf to RIG, Halliburton and other contractors. We continue to believe that not only will BP (and perhaps Anadarko and Mitsui, BP's non-operating partners in the well) based on the facts end up with almost all of the financial liabilities but that the contract RIG has with BP severely limits Transocean's exposure. Nonetheless, there is a reason we moved RIG to our Aggressive subportfolio. One exception was **Leucadia**, which, because it has significant exposure to mining and energy companies in its portfolio, often acts like a natural resource stock, added 6.9%. LUK's largest mining investment is Fortescue Mining, an Australian iron ore producer, which is being held hostage to discussions by the Australian government to impose new taxes on mining companies. The other exceptions among mining stocks were precious metals miners. It's difficult to make a case right now for gold as a hedge against inflation that remains invisible, so either the market is seeing around a very distant corner where inflation lurks or panicky investors want something perceived as sounder than the dollar. Mining companies themselves are also actively participating by snapping up rivals. First we had Kinross take Redback and now we have Goldcorp going after Andean. In any case, gold is inching toward a new high, and took the **USAA Precious Metals & Minerals Fund** up another 7.5%. Deep anxiety over the U.S. economy ruled the bond sector, which even after falling while stocks soared during their late month rally, had another big month. The **ProShares UltraShort 20+ Treasury ETF** fell 8.6%.

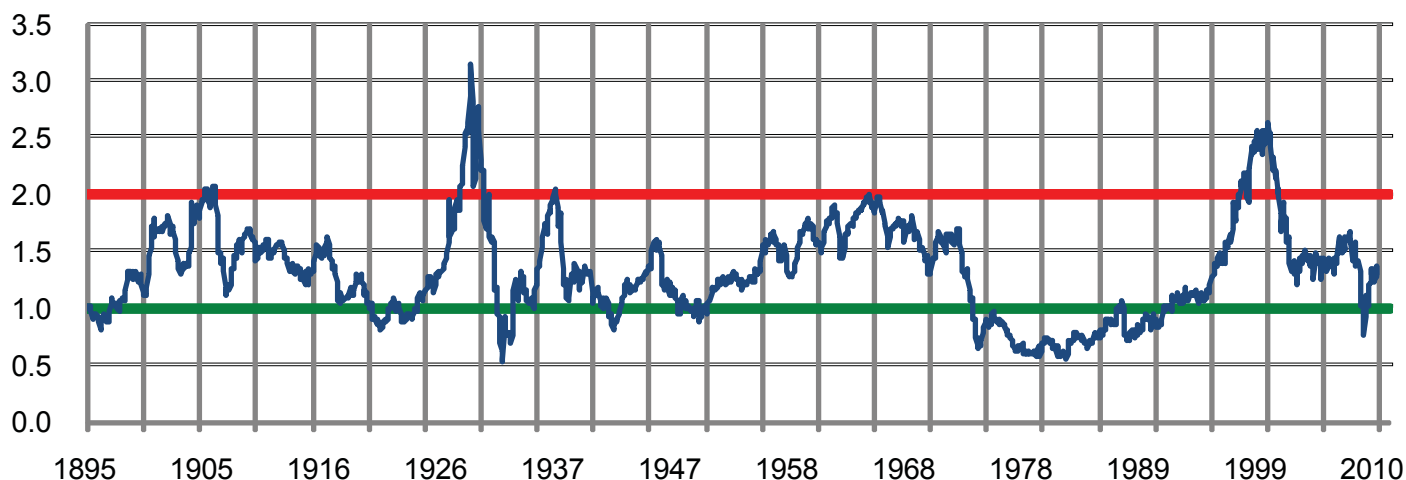
Among our diversified investments not mentioned above, the best performer was the **CGM Real Estate Fund**, which added 2% (our other REIT investment, **Commonwealth REIT**, added 0.8%), while the **Dodge & Cox International Fund** dropped 2%.

Telecom New Zealand, which got battered earlier this year as the dollar rose, has regained most of that decline and held steady this month. As we write, New Zealand is gauging damage from a major earthquake. There is no suggestion that NZT's assets have sustained extraordinary damage.

Healthcare was mixed. **Stryker**, after agreeing to buy one of its suppliers for \$150 million, is in negotiations to buy **Boston Scientific's** pain management division for about \$1.5 billion, though the deal could fall through. Boston could use the cash to reduce debt, while SYK would expand its stable of businesses. Apparently the market has something against SYK, since the shares dropped 3.9% since the last letter. Perhaps some believe Stryker is reaching too far out of its own comfort zone by getting into pain management, but Stryker's history hardly demonstrates foolishness. We think SYK is particularly attractive after getting spanked. As for Boston Scientific, which shed 7.8%, we also think it's worth investors' attention, but unlike Stryker, it has significant problems that have decimated the shares. Recent weakness has less to do with those problems than with downgrades received by Medtronic, a competitor.

Johnson & Johnson is having further product problems. This time its DePuy division that competes against **Stryker** in orthopaedic devices has to recall two hip-joint devices, which represents the 11th recall since last September. This hardly fits JNJ's reputation. Shares dropped 1.7%, perhaps buoyed by Berkshire Hathaway's SEC filing that it had doubled its ownership of JNJ to 43.1 million shares. Last year, after the company had sold off hunks of JNJ to buy preferred shares in Goldman and GE and to assist in its acquisition of Burlington Northern, its JNJ position had dwindled to 23.9 million shares. JNJ currently yields 3.7%, more than 1% above the 10-Year Treasury Note. We suspect that a few years from now when we look back at the past year, those who were buying Treasuries will wonder why they were not buying JNJ—and not just for income.

UnitedHealth, the HMO, gained 1.4% on no particular news. **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 1.28. 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

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 20.2 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		

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.

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 current reading is 25 percent, which does not change our market perspective. That will change only with a signal from the Lagging Indicators.

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 33 percent.



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