

Boosting International for Venturesome Only

by Walter S. Frank, Chief Investment Officer

We are recommending an increase in the international stock fund allocation for Venturesome investors from 30% to 40%. Correspondingly, we are recommending a decrease in the money fund allocation from 20% to 10%. We want to emphasize that the new advice is for Venturesome investors only. There is no change in our recommended allocations for Moderate and Conservative investors.

The new advice gives an increased international flavor to the Venturesome portfolios. We are aligning our allocation advice even closer to our general views about the attractiveness of overseas markets relative to that of the domestic market.

The new Venturesome allocations are now 40% domestic stock funds, 40% international stock funds, 10% specialty funds, and 10% money funds. Another way of looking at the new advice is that we making a modest increase in our stock fund allocation for those investors who have indicated a greater tolerance toward risk.

Here are the changes we will be making to the Venturesome model portfolios. **MONEYLETTER Venturesome**—Buy \$15,000 of Metzler/Payden European Emerging Markets (MPYMX). Sell \$15,000 of Schwab Money Market. **Fidelity Venturesome**—Buy \$15,000 of Fidelity Latin America (FLATX). Sell \$15,000 of Fidelity Cash Reserves. **Vanguard Venturesome**—Buy \$13,000 of Vanguard European ETF (VGK). Sell \$13,000 of Vanguard Prime Portfolio.

Reading the pause

Readers will note that we are reversing part of the cash position we raised for Venturesome investors some two months ago. (See *MONEYLETTER* June 23, 2006.) At the time we explained that we were raising the cash position

because we had become uncertain about how rigid the Fed was going to be in its inflation campaign. At the time it was not clear how big a role the obviously softening economy was going to play in the Fed's considerations.

Since then it has become clear that the policymaking body is aware that it can overdo in its zeal to contain inflation. That is what the pause is all about. At the same time we have gotten more and more indications recently that the economy's slowing has the potential (we repeat, potential) of going further than just lowering the economy's growth rate modestly below its speed limit.

Consequently, what we have seen from Wall Street sources that we take seriously is a lowering of expectations about how high the Fed will go. Our own view, as readers know, is that the odds are high that the Fed is already done. We still do not hold that view with 100% certainty, but the odds are higher than they were two months ago that such is the case.

The risks from Fed policy are not as high as they were. That is why we believe Venturesome investors can now reasonably lower their cash reserve position.

Is This A (New) Old Market?

What are we driving at? We are asking whether the May-June global markets correction marked a turning away from the risk-be-damned market of 2003-2005 and a return to the old risk-respectful markets of the past. We believe it is too early to tell, but for the moment the tilt is on the side of caution.

We all know (only too well) that we had a powerful correction two months ago that clawed chunks of profit out of emerging market stocks (and bonds), Japanese and Indian stocks, U.S. and international small company growth stocks, etc. The correction turned the financial market on its head. What had been good was now bad, and what was bad (we should say dull and uninteresting) was now good. You can see a bit of what we are talking about by looking at our stock fund rankings. Leading the pack in the domestic list are value funds—and large-cap value funds at that. The revolution has not been as pronounced in the international list, but there we see many funds invested in old, draggy Europe among the leaders (as the market saw it until May) and many fewer Asian funds on top.

A small-cap perspective

One portfolio manager who does think that the market has changed is John LaPorte who has managed the small-cap T. Rowe Price New Horizons Fund for almost twenty

Market Trends

	Trailing 12-Mo Trend	Forward 6-Mo Estimate
Economy	Higher	Higher
Interest Rates	Higher	Flat/Higher
Dollar	Lower	Flat/Lower
Inflation	Higher	Flat/Higher
Dow	Higher	Higher
NASDAQ	Flat	Higher
Europe	Higher	Higher
Japan (Nikkei)	Higher	Higher
Hong Kong (Hang Seng)	Higher	Higher

(continued on page 2)

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years. We always find LaPorte's views interesting and insightful. We never come away without learning something.

In a recent in-house T. Rowe Price interview, LaPorte made clear that he believes something profound has occurred. As he said, "I think that what we had in May and early June was a wake-up call that riskier asset classes don't go on outperforming forever."

Just to remind you, small-cap growth stocks took a drubbing in the correction, performing much worse than the S&P 500. LaPorte cites this as evidence that investors are now demanding higher risk premiums. That is, investors now insist that riskier assets trade at lower valuations relative to less risky assets than they have in the past few years. As he pointed out, it was the riskier parts of the small-cap market that suffered the most in the correction.

Looking ahead, LaPorte thinks that the days of small-cap outperformance relative to large-caps is over. This is not a new theme for him. As LaPorte frankly states, "I am one of those market predictors who have thought that the small-cap run was long in the tooth and who would not have been surprised if the seven-year outperformance of small-caps had ended a year or two ago. I do think that this probably marks an inflection point in the relative outperformance of small-cap stocks."

Keep in mind that we are talking about the *relative* performance of small caps (with an emphasis on growth) vs. the rest of the market. When it comes to the domestic stock market as a whole, LaPorte has a more encouraging outlook.

"...as long as corporate earnings growth stays positive, as long as small-cap companies can continue to grow their earnings—probably not at a double-digit rate as they have for the past three plus years, but at a more sustainable 5% to 10% overall rate—I think there is no reason for those stock prices to suffer a major decline."

Does LaPorte travel?

Turning to overseas markets, how far does LaPorte's view on risk premiums apply? We think the answer is only partly. Our view, of course, is by necessity tentative, but the evidence over the last month is that the appetite for risk has not totally disappeared. It appears to us that when it comes to overseas markets, greed is again holding its own against fear.

We see two reasons for this. First, the opportunities for gains in emerging markets, developing Asia and recovering Japan are so great that they overwhelm concerns about risk. Put another way, investors calculate that they are being paid to take risk. The risk premiums are higher than they appear.

The other reason, somewhat allied, is that the risk is actually less than generally considered. The poster-boy example for this is emerging market debt. In the rush for safety after May 10th, emerging markets, both debt and equity, were hit badly.

During the prolonged selling, Martin Jansen, Senior Portfolio Specialist, ING Investment Management, wrote in the *ING Investment Weekly*, "A strong case can be made

that the relative risk vs. developed economies has diminished substantially in recent years. In the aggregate, major emerging economies have amassed considerable foreign exchange reserves, have prudent fiscal policies, are running current account surpluses, and have a broader economic base than was the case a decade ago."

Jansen is making the case that investors simply overestimated emerging market risk.

We lean toward the first, and less sophisticated, possibility. Never forget the hedge funds. When the first crack appeared, the hedge fund pack ran to protect profits. As the selling abated and long-term investors held firm, the new opportunities opened by the lower prices brought buyers back in, and recovery began. The potential gains were too large to be ignored.

Bifocals needed

As we see it now (always subject to change) attitudes toward risk have shifted in the American market, while the shift is only partial in overseas markets. There is some shift toward less risk abroad, as witness the relative performance of European funds. (There is also better economic performance occurring. Is this a shift that would have occurred anyhow?) Yet some of the riskier markets abroad, such as India, are recovering nicely. The lure of long-term rapid growth will not be ignored for long. \$



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The Fed Is Done (Maybe)

Stocks rallied sharply the week of the 15th, essentially on good inflation news both from the Producer and Consumer Price Indexes. You could almost hear the market saying: the Fed has won. Unfortunately, it is never as easy as that.

There were some one-time factors involved, especially with the Consumer Price Index (CPI), that are unlikely to be repeated when this month's price indexes are released next month. One that stands out is a big (almost 4%) drop in apparel prices. It is unlikely we will see another drop for this month, let alone an eye-popper.

While we do not expect the coming price numbers to reinforce the Street's new found bullishness, we do expect a continuation of weaker activity numbers that will keep the Fed from further rate increases. We are sure, though, that the inflation numbers will keep the Fed on edge. Expect to hear more growls from the Fed that will shake up the market periodically. In the end, though we do not believe that the growls will lead to action.

Overall, the U.S. market is performing well, but a slowing economy is not an optimum condition for stocks.

Fund changes

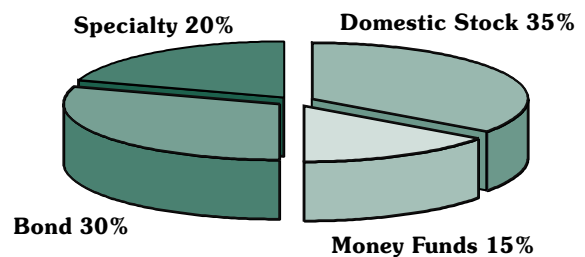
In line with the Hotline of Wednesday, August 2nd we made the following changes as of Thursday, August 3rd: **Fidelity Venturesome**—Sold 1,183 shares of Fidelity Fifty (FFTYX) @ \$22.60 and purchased 1,923 shares of Large Cap Value (FSLVX) @ \$13.90. **Fidelity Conservative**—Sold 773 shares of Independence @ \$20.00. Purchased 1,112 shares of Large Cap Value. **MONEYLETTER Venturesome**—Sold 1,664 shares of Bridgeway Small Cap Value (BRSVX) @ \$15.16. Purchased 328 shares of Morningstar Large Value (JKF) @ \$76.96. **MONEYLETTER Moderate**—Sold 1,161 shares of Bridgeway Small Cap Value. Purchased 229 shares of Morningstar Large Value. **MONEYLETTER Conservative**—Sold 859 shares of Bridgeway Small Cap Value. Purchased 169 shares of Morningstar Large Value. Sold 1,511 shares of Royce Opportunity (RYPNX) @ \$13.01. Purchased 709 shares of Fairholme Fund (FAIRX) @ \$27.72. **Vanguard Conservative**—Sold 537 shares of Vanguard Small Cap Value (VISVX) @ \$15.59. Purchased 637 shares of Vanguard Dividend Growth (VDIGX) @ \$13.14.

In line with the Hotline of Wednesday, August 9th, the following changes were made as of Thursday, August 10th: **MONEYLETTER Venturesome**—Sold 2,323 shares of Janus Orion (JORNX) @ \$8.60. Purchased 1,131 shares of Powershares Dynamic Large Cap Value (PWV) @ \$17.66. **MONEYLETTER Moderate**—Sold 2,495 shares of Orion and purchased 1,215 shares of Dynamic Large Cap Value. Sold 944 shares of Forward International Small Cap (PISRX) @ \$16.45. Purchased 855 shares of Icon Europe (ICSEX) @ \$18.16. **Vanguard Venturesome**—Sold 1,659 shares of Vanguard Capital Value (VCVLX) @ \$11.57. Purchased 1,465 shares of Dividend Growth (VDIGX) @ \$13.10.

The Hotline of Wednesday, August 16th recommended the sale of Marsico 21st Century (MXXIX) in the **MONEYLETTER Conservative** portfolio. The recommended replacement was Kinetics Paradigm (WWNPX). Details in the next issue. The Hotline of Wednesday, August 22nd also carried the new allocation recommendations that appear on page one. \$

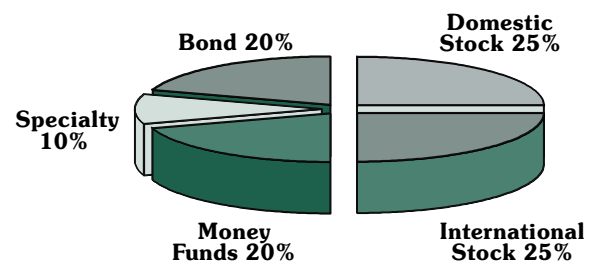
CONSERVATIVE

Seeks steady long-term growth of capital with limited short-term volatility



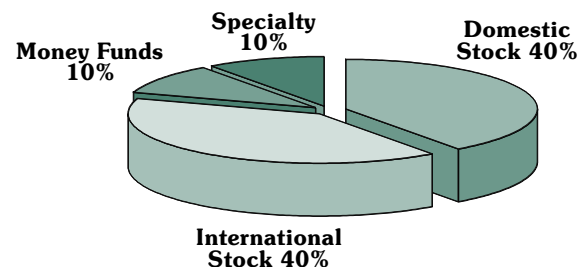
MODERATE

Seeks greater long-term growth than the Conservative Portfolio by taking prudent risks



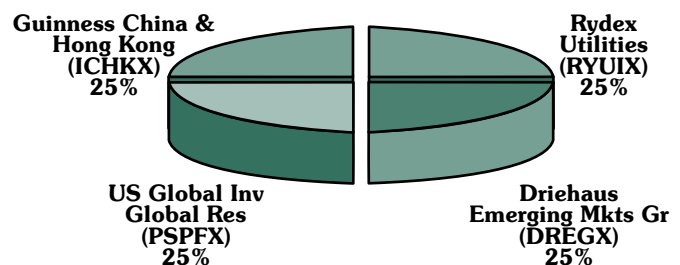
VENTURESOME

Seeks maximum long-term growth by accepting greater short-term volatility



SELECT

Seeks maximum long-term growth by assertively upgrading fund positions



Domestic Stock Funds

RANK	8/18 2006	1 Mo Ago	6 Mo Ago	Ticker Symbol	FUND NAME	Fund Type	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE	RISK		NTF/ w/f
										1 mo.	6 mo.	12 mo.	PER SHARE	Std. Dev.	Beta	
1	1	—	—	JFK	Morningstar Large Value (iS)	LCVal	B	B	B	6.6%	9.4%	18.3%	\$77.73	—	—	—
2	3	—	—	PWV	Powershares Dynamic LC Value	LCVal	B	B	B	6.8	7.3	17.1	17.98	—	—	—
3	5	111	—	GEVIX	Columbia Disciplined Value CIZ	LCVal	B	B	B	6.3	6.6	18.8	15.73	9.1	0.98	a
4	43	68	—	USCGX	USAA Capital Growth	SCGro	*	H	H	8.9	4.8	18.6	8.78	15.0	1.52	fSA
5	—	—	—	LSVRX	Loomis Sayles Value Ret	LCVal	B	B	B	6.4	6.4	18.0	20.50	7.4	0.90	A
6	6	159	—	CGMFX	CGM Focus	MC	*	B	B	3.7	6.5	21.3	38.35	22.4	1.50	sa
7	4	161	—	SAOPX	Salomon Brothers Opportunity	MCVal	B	B	B	4.7	6.9	15.4	56.22	0.9	8.54	fa
8	8	—	—	VTV	Vanguard Value ETF	LCVal	B	B	B	5.6	6.4	14.7	62.65	—	—	—
9	7	181	—	VIVAX	Vanguard Value Index	LCVal	B	B	B	5.6	6.3	14.8	24.42	8.2	1.00	fSA
10	14	—	—	ELV	DJ WI US LargeCap Value (stTr)	LCVal	B	B	B	6.4	5.9	14.1	76.43	7.4	0.86	—
11	26	—	—	NYC	NYSE Composite (iS)	LC	(B)	(B)	(B)	7.1	4.8	14.5	77.00	—	—	—
12	12	—	—	IWD	Russell 1000 Value (iS)	LCVal	B	B	B	5.3	5.5	14.2	75.74	8.0	0.99	—
13	16	—	—	IWW	Russell 3000 Value (iS)	LCVal	B	B	B	5.5	5.3	14.0	98.76	8.3	1.03	—
14	25	112	—	FAIRX	Fairholme Fund (2%r<60d)	MC	(B)	(B)	(B)	4.1	5.6	14.9	27.62	8.4	0.71	fSA
15	20	105	—	MQIFX	Mutual Qualified (2%r<7d) CIZ	MCVal	H	H	H	5.6	5.1	13.1	21.44	8.0	0.82	sa
16	10	217	—	VEIPX	Vanguard Equity-Income	LCVal	B	B	B	5.1	5.5	12.4	24.72	7.6	0.91	fSA
17	29	268	—	DGAGX	Dreyfus Appreciation	LC	(B)	(B)	(B)	5.7	6.5	9.1	42.84	7.6	0.79	FSA
18	27	—	—	FSLVX	Fidelity Large Cap Value	LCVal	(B)	(B)	(B)	5.9	4.1	14.6	14.01	—	1.00	Fa
19	2	6	—	NEEGX	Needham Growth Fund (2%r<60d)	SCGro	H	H	H	6.6	1.6	19.8	39.72	25.7	1.19	FSA
20	11	34	—	WWNPX	Kinetics Paradigm (2%r<30d)	MC	B	B	B	4.2	4.2	16.5	22.79	10.8	1.05	FSA
21	13	249	—	TWEIX	American Century Equity Income	LCVal	B	B	B	4.3	6.2	11.0	8.49	6.8	0.77	FSA
22	34	180	—	FEQIX	Fidelity Equity-Income	LCVal	H	H	H	6.1	4.4	12.7	55.91	9.8	1.08	FSA
23	23	—	—	VDIGX	Vanguard Dividend Growth	LCVal	H	H	H	6.2	4.6	11.9	13.39	7.1	0.88	fSA
24	19	178	—	VWNFX	Vanguard Windsor II (closed,\$10k)	LCVal	H	H	H	5.3	4.7	12.8	33.46	7.9	0.90	fSA
25	71	82	—	FLVCX	Fidelity Leveraged Co (\$10k,1.5%r<90d)	MC	*	H	H	5.2	2.9	17.5	28.42	18.1	1.75	Fa
26	58	8	—	JSVAX	Janus Contrarian	LC	*	H	H	6.8	2.1	17.0	16.23	13.6	1.29	SA
27	24	—	—	IVE	S&P 500 Value (iS)	LCVal	H	H	H	5.2	4.6	13.1	70.42	8.6	1.07	—
28	38	247	—	PVLDX	Allianz OCC Value D (2%r<7d)	LCVal	*	H	H	7.2	4.4	10.4	16.81	11.8	1.25	FSA
29	46	108	—	TAVFX	Third Avenue Value (\$10k,1%r<60d)	SC	H	H	H	6.6	3.8	12.7	58.71	9.3	0.82	FSA
30	18	—	—	DVY	DJ Select Dividend Index (iS)	MCVal	(B)	(B)	(B)	5.1	6.2	8.8	65.98	—	—	—
31	17	146	—	ICSLX	ICAP Select Equity	LCVal	H	H	H	5.1	3.9	13.5	39.68	9.1	0.94	fSA
32	15	148	—	HOVLX	Homestead Value (2%r<30d)	LCVal	B	B	B	3.4	4.7	13.5	35.57	9.2	0.96	A
33	33	136	—	DODGX	Dodge & Cox Stock (closed)	LCVal	H	H	H	5.4	3.8	12.4	147.10	9.5	1.02	sa
34	52	175	—	SLASX	Selected American Shares	LC	H	H	H	5.4	3.8	12.0	42.43	8.7	0.93	SA
35	145	19	—	BPTRX	Baron Partners	MCGro	H	H	H	7.0	1.8	14.5	19.90	13.3	1.15	FSA
36	32	—	—	NY	NYSE 100 (iS)	LCVal	H	H	H	5.6	4.1	10.3	69.51	—	—	—
37	114	97	—	CBMDX	Wells Fargo Adv C&B Mid Cap Value	MC	H	H	H	6.4	2.9	12.0	21.80	13.0	1.32	FSA
38	152	11	—	RYPX	Royce Low Priced Stock (closed,1%r<180d)	SC	H	H	H	5.5	0.4	19.0	16.79	15.4	1.38	fSA
39	42	127	—	MUTHX	Mutual Shares (1%) CIZ	MCVal	H	H	H	5.2	3.5	11.5	25.47	6.9	0.71	sa
40	30	243	—	OAKBX	Oakmark Equity&Income (2%r<90d)	Bal	H	H	H	3.1	5.1	10.5	26.35	6.6	0.78	FSA
41	147	152	—	FFIDX	Fidelity Fund	LC	H	H	H	6.8	2.6	11.0	33.33	8.5	0.93	FSA
42	50	141	—	BEGRX	Mutual Beacon (2%r<7d) CIZ	MCVal	H	H	H	5.8	3.4	10.4	16.56	7.6	0.76	sa
43	56	256	—	VASVX	Vanguard Selected Value (\$25k,1%r<1yr)	MCVal	H	H	H	5.9	4.0	8.3	20.08	9.9	1.08	fSA
44	63	—	—	QEF	S&P 100 (iS)	LC	H	H	H	5.9	3.9	8.5	60.30	7.2	0.90	—
45	67	50	—	FVDFX	Fidelity Value Discovery	MC	H	H	H	5.3	1.3	15.8	16.77	11.6	1.19	F
46	59	114	—	LLSCX	Longleaf Partners Smallcap (closed)	SCVal	H	H	H	4.8	2.5	13.4	28.56	11.2	1.09	fa
47	61	143	—	TRMCX	T. Rowe Price Mid Cap Value (closed)	MCVal	H	H	H	5.3	2.8	11.9	25.06	11.1	1.19	fSA
48	49	193	—	SMCDX	Wells Fargo Advantage MC Disciplined	MCVal	H	H	H	3.9	2.9	13.7	22.26	10.0	0.96	FSA
49	54	236	—	GABAX	Gabelli Asset (2%r<7d)	MC	H	H	H	4.9	3.9	9.5	44.82	10.2	1.09	FSA
50	41	—	—	DIA	Dow 30 Industrials (Diamonds)	LCVal	H	H	H	5.3	3.4	10.0	113.80	8.6	1.03	—
51	87	—	—	RYPX	Royce Value Plus (1%r<180d)	SCGro	*	H	H	4.9	-1.1	21.9	12.94	16.9	1.54	FSA
52	31	—	—	IWS	Russell MidCap Value (iS)	MCVal	H	H	H	4.0	3.1	12.7	133.80	10.0	1.18	—
53	60	214	—	TWVLX	American Century Value	LCVal	H	H	H	5.5	3.5	9.3	7.33	7.9	0.94	FSA
54	66	—	—	IWN	Russell 2000 Value (iS)	SCVal	*	H	H	4.4	2.3	13.7	72.70	13.6	1.50	—
55	36	216	—	PRFDX	T. Rowe Price Equity-Income	LCVal	H	H	H	5.1	3.6	9.6	27.62	8.9	0.98	fSA
56	95	119	—	CRMMX	CRM Mid Cap Value Inv (closed)	MC	S	S	S	6.3	2.2	11.2	28.64	10.0	1.04	FSA
57	73	186	—	FDEQX	Fidelity Disciplined Equity	LC	H	H	H	5.5	2.7	10.8	29.35	9.1	0.97	FSA
58	68	168	—	TGDVX	TCW Diversified Value N	LCVal	H	H	H	5.9	2.9	9.7	15.12	10.4	1.08	FSA
59	21	170	—	SAIFX	Salomon Brothers Investors	LCVal	H	H	H	4.4	3.2	10.6	21.62	9.9	1.06	fa
60	70	263	—	WWALX	Weitz Value Fund (\$10k)	LCVal	S	S	S	3.7	5.4	6.2	37.16	7.7	0.80	FSA
61	44	4	—	JORNX	Janus Orion	MCGro	*	S	S	4.0	0.6	17.5	8.84	13.3	1.37	FSA
62	80	213	—	RSVAX	RS Value	MC	H	H	H	4.8	3.0	9.7	26.09	12.0	1.01	FSA
63	132	79	—	FDSVX	Fidelity Discovery	LC	S	S	S	6.7	1.3	11.1	12.01	8.7	0.86	fSA
64	75	235	—	TGIFX	TCW Dividend Focused N	LCVal	H	H	H	5.8	3.2	7.7	12.31	9.7	1.03	FSA
65	124	28	—	ATASX	ABN AMRO/TAMRO Small Cap N	SC	*	S	S	6.0	0.0	14.7	18.08	15.8	1.52	FSA
66	112	130	—	FGRTX	Fidelity Growth & Income II	LC	S	S	S	5.8	1.2	11.7	10.37	8.2	0.86	Fa
67	45	104	—	UMBSX	UMB Scout Stock	LC	H	H	H	4.8	1.8	11.7	15.38	7.7	0.91	FSA
68	86	174	—	TGLNX	TCW Galileo Equities N	LC	S	S	S	4.1	2.6	10.9	16.43	10.8	1.13	FSA

Bold funds are currently held in *MONEYLETTER* model portfolios.
Advice: B=Buy, H=Hold, S=Sell, (B), (H), (S) = advice new this issue,
 * = not for this portfolio.

Std. Dev.: Standard Deviation based on trailing 3-yr. returns.

Beta: fund's correlation to the market (S&P 500 = 1.0). A fund with a beta greater than 1.0 is more volatile than the S&P 500.
NTF/wtf: NO TRANSACTION FEE/with transaction fee (F/f) for Fidelity, (S/s) for Schwab and (A/a) for TD Ameritrade.

Domestic Stock Funds (continued)

RANK	8/18 2006	1 Mo Ago	6 Mo Ago	Ticker Symbol	FUND NAME (Max. Load)	Fund Type	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE PER SHARE	RISK		NTF/wff
										1 mo.	6 mo.	12 mo.		Std. Dev.	Beta	
69	74	1	HDPMX	Hodges Fund (2%r<90d)	MC	*	(S)	(S)	3.2	-1.9	22.9	24.24	19.0	1.85	FSA	
70	47	—	HRIVX	Heartland Value (2%r<10d)	SCVal	*	S	S	3.2	1.0	15.9	49.41	16.9	1.57	FSA	
71	153	91	MERDX	Meridian Fund (2%r<60d)	MCGro	S	S	S	6.7	0.8	10.9	39.11	13.8	1.36	fa	
72	90	—	SPY	S&P 500 (SPDR)	LC	S	S	S	5.4	2.3	8.9	130.70	7.8	1.00	—	
73	140	3	FMCSX	Fidelity Mid-Cap Stock (closed,.75%r<30d)	MCGro	*	S	S	5.3	-0.5	16.2	27.94	13.8	1.29	Fsa	
74	88	—	IVV	S&P 500 (iS)	LC	S	S	S	5.4	2.3	9.0	130.90	7.8	1.00	—	
75	82	126	SSMVX	Wells Fargo Adv SC Value Cl Z (closed)	SC	S	S	S	2.9	1.2	14.9	31.96	16.3	1.44	fSA	
76	89	204	FSMKX	Fidelity Spartan 500 (\$10k)	LC	S	S	S	5.5	2.1	8.8	90.35	8.8	1.00	Fa	
77	57	257	YACKX	Yacktman Fund (2%r<30d)	LCVal	S	S	S	5.0	3.4	6.3	15.67	8.8	0.92	FsA	
78	129	106	FDSSX	Fidelity Stock Selector	LC	S	S	S	5.7	1.1	10.8	25.87	8.9	1.00	Fsa	
79	91	208	VFINX	Vanguard 500 Index	LC	S	S	S	5.5	2.1	8.7	120.30	7.8	1.00	fSA	
80	100	—	VV	Vanguard LargeCap ETF	LC	S	S	S	5.3	2.1	9.1	57.86	—	—	—	
81	111	144	FTRNX	Fidelity Trend	LC	S	S	S	5.9	1.2	10.1	59.84	8.9	1.00	Fsa	
82	168	147	SLSSX	Selected Special Shares	MC	S	S	S	6.1	1.4	9.2	13.13	12.3	1.28	SA	
83	35	5	MXIX	Marsico 21st Century (2%r<30d)	LC	(S)	(S)	(S)	2.5	-0.4	19.3	13.70	14.2	1.36	FSA	
84	122	241	WEHIX	Weitz Hickory (\$10k)	MC	*	S	S	4.0	3.9	5.9	34.56	10.5	1.10	fSA	
85	120	260	CFIMX	Clipper Fund	LCVal	S	S	S	5.6	3.2	5.3	86.94	8.8	0.83	Fsa	
86	64	212	PRDGX	T. Rowe Price Dividend Growth	LC	S	S	S	4.9	2.3	8.3	23.71	8.4	0.94	fSA	
87	76	—	DSV	DJ WI US SmallCap Value (stTr)	SCVal	*	S	S	4.2	1.1	12.4	65.14	13.5	1.53	—	
88	190	9	MNSCX	WellsFargo Adv Small Cap Growth (closed)	SCGro	S	S	S	6.4	-1.2	14.7	12.95	17.1	1.53	fS	
89	136	—	JKJ	Morningstar Small Core (iS)	SC	S	S	S	4.5	0.4	13.5	78.02	—	—	—	
90	137	232	VQNPX	Vanguard Growth & Income	LC	S	S	S	5.8	1.7	8.2	33.01	8.3	1.04	fSA	

Dow Jones
NASDAQ
S&P 500

5.4%
5.9
5.3

2.4%
-5.2
1.2

7.8%
1.3
6.8

indexes do not
include dividends

International Stock Funds

1	5	8	JAOSX	Janus Overseas (2%r<90d)	Int'l	*	H	H	11.4%	10.6%	46.8%	\$38.80	15.1	—	FSA
2	1	1	PRLAX	T. Rowe Price Latin America (2%r<90d)	LatinA	*	*	(B)	11.1	5.0	55.9	31.69	20.5	—	fSA
3	3	2	FLATX	Fidelity Latin Amer. (1.5%r<90d)	LatinA	*	*	(B)	10.9	2.8	53.3	38.77	19.8	—	Fsa
4	2	6	DREGX	Driehaus Emerging Mkts Gr (2%r<60d)	Int'l	*	B	B	8.1	5.6	48.3	33.33	17.9	—	FSA
5	26	68	ACFFX	Columbia Acorn Intl Select Z	Int'l	*	H	H	11.2	12.1	27.2	24.10	11.5	—	Sa
6	4	—	ICSEX	ICON Europe	Europe	*	B	B	9.4	10.3	33.0	18.64	13.9	—	FSA
7	25	57	USIFX	USAA International	Int'l	*	(B)	(B)	11.3	11.1	27.4	27.40	9.4	—	—
8	—	—	MPYMX	Metzler/Payden Europe Emg Mkts (2%r<30d)	Europe	*	(B)	(B)	8.6	6.9	41.5	28.82	21.4	—	FSA
9	24	—	FEZ	DJ Euro Stoxx 50 (stTr)	Europe	*	H	H	11.7	11.1	25.4	48.97	12.6	—	—
10	13	24	HAINX	Harbor International (2%r<60d)	Int'l	*	B	B	10.6	8.9	31.7	57.66	11.2	—	Fsa
11	33	—	ADRA	Asia 50 ADR (BLDRS)	Pacific	*	H	H	11.1	8.5	31.4	30.25	13.7	—	—
12	9	—	IEV	S&P 350 Europe Plus (iS)	Europe	*	B	B	10.1	11.5	25.1	95.40	10.6	—	—
13	16	—	EZU	MSCI EMU (iS)	Europe	*	H	H	11.1	10.5	25.6	92.17	12.1	—	—
14	14	—	VGK	Vanguard European ETF	Europe	*	B	B	9.9	11.1	24.2	62.10	—	—	—
15	11	73	VEURX	Vanguard European Stock Index (2%r<60d)	Europe	*	B	B	9.7	11.1	24.2	32.77	10.7	—	fSA
16	20	65	DODFX	Dodge & Cox Intl Stock	Int'l	*	H	H	9.4	10.2	26.5	40.38	11.2	—	fSA
17	47	—	ITF	S&P 150 Topix (iS)	Japan	*	H	H	11.6	6.5	32.3	123.30	15.7	—	—
18	15	59	OAKIX	Oakmark International (2%r<90d)	Int'l	*	H	H	9.5	10.4	25.1	26.40	9.2	—	FSA
19	6	12	FSEAX	Fidelity SE Asia (1.5%r<90d)	Pacific	*	H	H	9.6	7.5	32.0	24.17	17.2	—	Fsa
20	29	42	VTRIX	Vanguard International Value (2%r<60d)	Int'l	*	H	H	9.9	8.6	28.3	40.14	11.1	—	Fsa
21	36	52	VWIGX	Vanguard International Growth (2%r<60d)	Int'l	*	H	H	10.6	9.0	26.0	23.99	10.1	—	fSA
22	40	34	ARTIX	Artisan International (2%r<90d)	Int'l	*	H	H	10.8	8.6	26.4	28.73	10.6	—	FSA
23	31	25	ACINX	Columbia Acorn Intl Z (2%r<60d)	Int'l	*	H	H	9.8	8.1	29.1	38.46	11.6	—	Sa
24	34	69	SWINX	Schwab International Index (1.5%r<180d)	Int'l	*	H	H	9.6	9.9	24.4	20.38	9.6	—	S
25	22	43	FECAX	Fidelity Europe Capital App. (1%r<30d)	Europe	*	H	H	9.2	8.3	28.4	26.08	13.3	—	Fa
26	35	61	ICEUX	ICAP Euro Select Equity (2%r<30d)	Int'l	*	S	S	9.8	8.9	26.1	37.07	10.9	—	fSA
27	41	67	CMISX	Columbia Intl Stock ClZ (2%r<60d)	Int'l	*	S	S	10.7	8.8	24.7	19.11	10.0	—	fSA
28	23	—	ADRD	Develop Mkts 100 ADR (BLDRS)	Int'l	*	H	H	9.4	10.4	22.8	27.18	10.5	—	—
29	7	3	SLAFX	DWS Latin Amer Equity S (closed,2%r<30d)	LatinA	*	H	H	10.0	0.0	47.7	54.23	21.1	—	Sa
30	32	—	FEU	DJ Stoxx 50 (stTr)	Europe	*	H	H	9.7	10.6	20.7	44.98	10.6	—	—
31	21	17	SCOPX	DWS Pacific Opp Eq. S (closed,2%r<30d)	Pacific	*	H	H	9.6	7.5	28.2	18.54	14.9	—	FSA
32	8	—	ILF	S&P 40 Latin America (iS)	LatinA	*	H	H	10.5	0.7	43.6	144.10	19.2	—	—
33	51	60	SCINX	DWS International S (2%r<180d)	Int'l	*	S	S	11.3	7.9	24.2	57.14	10.5	—	FSA
34	79	—	EWJ	MSCI Japan (iS)	Japan	*	S	S	11.6	5.5	29.3	14.03	16.0	—	—
35	30	—	ADRU	Europe 100 ADR (BLDRS)	Europe	*	S	S	8.6	10.7	20.3	27.20	11.0	—	—
36	62	41	VPACX	Vanguard Pacific Stock Index (2%r<60d)	Pacific	*	H	H	10.4	7.0	26.8	12.05	13.8	—	fSA
37	18	7	FEMKX	Fidelity Emerging Mkts (1.5%r<90d)	Int'l	*	H	H	10.0	1.6	40.5	20.88	17.8	—	Fsa
38	91	20	FJPNX	Fidelity Japan (1.5%r<90d)	Japan	*	S	S	12.1	3.6	31.8	17.55	19.0	—	Fa
39	17	32	BJBIX	Julius Baer Intl Eq A (closed,2%r<90d)	Int'l	*	S	S	9.3	6.4	27.7	40.98	11.9	—	FS
40	45	21	PRIDX	T. Rowe Price Intl Disc. (2%r<90d)	Int'l	*	S	S	8.2	6.9	28.1	45.93	12.9	—	fSA
41	38	—	ADRE	Emerging Mkts 50 ADR (BLDRS)	EmerMkt	*	S	S	9.6	2.8	36.2	32.63	17.9	—	—
42	12	35	ARTKX	Artisan Intl Value (2%r<90d)	Int'l	*	H	H	6.4	8.6	26.5	25.80	10.5	—	FSA
43	67	—	VPL	Vanguard Pacific ETF	Japan	*	S	S	10.4	6.4	25.8	64.07	—	—	—
44	58	45	FOSFX	Fidelity Overseas (1%r<30d)	Int'l	*	S	S	9.4	7.3	24.6	45.51	12.1	—	Fsa
100	10	56	ICHKX	Guinness China & Hong Kong (2%r<90d)	Pacific	*	S	S	4.1	4.5	11.3	21.77	16.9	—	FSA

Bond Funds (next issue on page 6: Specialty Funds)
 8/18/2006

Ticker Symbol	FUND NAME	Fund Type	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE PER SHARE	Std. Dev.	Yield	NTF/wft
						1 mo.	6 mo.	12 mo.				
FFRHX	Fidelity Floating Rate High Inc (1%r<60d)	BnkLoan	B	*	*	0.6%	0.9%	2.2%	\$9.92	0.66	5.48%	Fa
BUFHX	Buffalo High-Yield (2%r<180d)	HighYld	*	*	*	1.5	1.8	3.6	11.00	3.44	5.72	FSA
FAGIX	Fidelity Capital & Income (1%r<90d)	HighYld	*	*	*	2.3	1.8	3.9	8.50	4.82	6.30	Fsa
SPHIX	Fidelity High Income (1%r<90d)	HighYld	*	*	*	1.6	1.0	2.8	8.80	3.91	7.01	Fsa
JAHYX	Janus High Yield (2%r<90d)	HighYld	*	*	*	1.0	2.4	3.3	9.53	3.77	7.29	FSA
NTHEX	Northeast Investors Trust	HighYld	*	*	*	1.3	4.6	7.6	7.57	3.67	7.92	fa
PHYDX	PIMCO High Yield (2%r<30d)	HighYld	*	*	*	1.7	1.3	3.0	9.61	4.05	7.03	FSA
STHYX	Strong High Yield Bond (1%r<180d)	HighYld	*	*	*	1.5	2.4	4.7	7.65	3.62	7.27	FSA
STHBX	Strong S-T High Yield	HighYld	*	*	*	1.0	2.3	3.9	8.50	1.37	5.29	FSA
PRHYX	T. Rowe Price High Yld (closed,1%r<1yr)	HighYld	*	*	*	1.3	1.7	2.4	6.84	3.73	7.66	fsa
TGHNX	TCW Galileo High Yield Bond	HighYld	*	*	*	1.4	1.6	3.3	6.81	4.58	7.59	FSA
VWEHX	Vanguard High Yield Corporate (1%r<1yr)	HighYld	*	B	*	1.5	1.6	4.0	6.07	3.57	7.20	fsa
BEGBX	American Century Intl Bond	Int'l	*	*	*	3.1	4.8	1.9	13.65	8.12	1.91	FSA
SSTGX	DWS Global Bond S (closed,2%r<30d)	Int'l	*	*	*	2.2	2.3	2.1	9.59	4.43	8.58	Sa
FNMXI	Fidelity New Markets Income (1%r<90d)	Int'l	*	*	*	4.0	1.1	8.9	14.79	7.09	5.84	Fsa
RPBIX	T. Rowe Price Int'l Bond (2%r<90d)	Int'l	*	*	*	2.7	3.9	0.8	9.56	7.80	2.91	fsa
BGNMX	American Century Ginnie Mae	IntTerm	*	*	*	1.9	0.8	1.4	10.10	2.24	4.90	FSA
CPTNX	American Century Government Bond	IntTerm	*	*	*	1.6	1.0	0.9	10.36	2.83	4.40	FSA
ACITX	American Century Inflation Adj	IntTerm	B	*	*	2.9	0.8	2.4	10.78	5.16	5.49	FSA
BBHIX	BBH Inflation Indexed Sec (1%r<30d)	IntTerm	B	*	*	2.8	0.9	-1.1	10.51	5.11	4.69	FSA
DODIX	Dodge & Cox Income	IntTerm	*	*	*	1.7	1.6	2.4	12.49	2.53	4.77	fsa
DRBDX	Dreyfus A Bonds Plus	IntTerm	*	*	*	2.1	1.3	1.8	13.37	3.72	4.93	FSA
DRGMX	Dreyfus GNMA	IntTerm	*	*	*	2.2	1.0	2.2	14.26	2.69	4.33	FSA
SCSBX	DWS Core Plus Income S (closed,2%r<15d)	IntTerm	*	*	*	2.2	1.3	1.9	12.58	3.40	4.92	Sa
FTRGX	Federated Total Return Govt	IntTerm	*	*	*	1.8	0.9	0.5	10.54	3.62	4.83	fsa
FINPX	Fidelity Inflation-Protected Bond	IntTerm	B	*	*	2.7	1.2	2.5	10.97	5.20	1.82	Fa
FTHRX	Fidelity Intermediate Bond	IntTerm	*	*	*	1.7	0.8	0.4	10.21	2.91	4.27	Fsa
FSTGX	Fidelity Intermediate Govt	IntTerm	*	*	*	1.6	0.8	0.5	9.97	2.89	3.88	Fsa
FBNDX	Fidelity Investment Grade	IntTerm	*	*	*	2.2	0.8	1.0	7.33	3.30	4.23	Fsa
IEF	Lehman 7-10 Year Treasuries (iS)	IntTerm	*	*	*	2.1	0.6	0.0	81.95	5.72	4.15	—
AGG	Lehman Aggregate Bond (iS)	IntTerm	*	*	*	1.9	1.1	1.5	99.01	—	4.48	—
TIP	Lehman TIPS Bond (iS)	IntTerm	B	*	*	2.1	0.7	2.2	101.27	—	5.50	—
MBDFX	Managers Fremont Bond	IntTerm	*	*	*	2.4	0.9	0.8	10.23	3.49	4.49	fsa
PRRDX	PIMCO Real Return (2%r<7d)	IntTerm	*	*	*	3.1	1.2	0.8	10.97	5.18	4.50	FSA
PTTDX	PIMCO Total Return (2%r<7d)	IntTerm	*	*	*	2.4	1.2	1.0	10.37	3.41	4.14	FSA
PTMDX	PIMCO Total Return Mortgage (2%r<7d)	IntTerm	*	*	*	2.4	1.9	1.8	10.54	2.59	4.08	FSA
PRGMX	T. Rowe Price GNMA	IntTerm	*	*	*	2.1	0.7	1.1	9.32	2.25	4.93	fsa
PRCIX	T. Rowe Price New Income	IntTerm	*	*	*	2.2	0.8	0.7	8.83	3.29	4.51	fsa
TGMNX	TCW Galileo Total Return Bond	IntTerm	*	*	*	1.9	1.9	2.8	9.73	2.81	4.58	FSA
USAIX	USAA Income	IntTerm	*	*	*	2.0	1.2	2.0	12.03	3.48	4.86	A
VALBX	Value Line U.S. Govt Sec	IntTerm	*	*	*	1.7	1.4	1.8	11.32	3.01	4.59	FSA
VFIIX	Vanguard GNMA	IntTerm	B	*	*	2.4	1.2	2.8	10.14	2.61	5.00	fsa
VIPSX	Vanguard Inflation Protected Sec	IntTerm	B	*	*	2.8	1.4	3.0	12.05	5.07	5.60	fsa
VFITX	Vanguard Intermediate Term U.S. Treasury	IntTerm	*	*	*	2.0	0.7	0.3	10.70	4.18	4.71	fsa
VBMFX	Vanguard Total Bond Market Index	IntTerm	*	*	*	2.2	0.9	1.1	9.90	3.53	4.77	fsa
STVSX	Wells Fargo Adv Govt Sec Inv	IntTerm	*	*	*	1.8	1.1	0.7	10.28	3.36	4.69	FSA
MNTRX	Wells Fargo Adv Total Return Bond	IntTerm	*	*	*	2.0	1.3	1.0	11.98	3.42	4.36	fSa
WTIBX	Westcore Plus Bond (2%r<90d)	IntTerm	*	*	*	2.0	2.0	2.9	10.44	3.26	5.51	FSA
KIFIX	FifthThird Bond	LngTerm	*	*	*	2.1	1.3	1.2	9.73	3.43	4.32	fa
MGFIX	Managers Bond	LngTerm	*	*	*	2.8	2.8	4.4	24.38	3.92	4.01	FSA
FSICX	Fidelity Strategic Income	Multi	B	B	*	2.3	2.8	4.7	10.49	3.93	5.35	Fa
LSBDX	Loomis Sayles Bond Instl (\$100k,2%r<60d)	Multi	B	B	*	2.9	3.3	8.3	14.04	5.33	6.13	fsA
LSBRX	Loomis Sayles Bond Retail (2%r<60d)	Multi	B	B	*	2.8	3.1	8.0	14.00	5.30	5.95	FSA
RPSIX	T. Rowe Price Spectrum Income	Multi	*	*	*	2.5	1.3	2.8	11.87	3.23	4.40	fsa
SCSTX	DWS Short-Term Bond S (closed,2%r<15d)	ShfTerm	B	*	*	0.9	2.1	3.4	9.94	1.36	4.30	Sa
FSHBX	Fidelity Short-Term Bond	ShfTerm	B	*	*	1.0	1.1	1.3	8.84	1.44	4.04	Fsa
JASBX	Janus S-T Bond	ShfTerm	B	*	*	0.4	1.6	2.3	2.87	1.23	3.39	FSA
SHY	Lehman 1-3 Year Treasuries (iS)	ShfTerm	B	*	*	0.6	1.6	2.6	79.99	1.34	3.70	—
MGIDX	Managers Int. Duration Govt	ShfTerm	*	*	*	2.3	2.0	2.8	10.47	2.42	4.20	FSA
MGSDX	Managers Short Duration Govt	ShfTerm	B	*	*	0.5	2.3	4.0	9.65	0.56	3.79	FSA
PTLCX	PIMCO Low Duration (2%r<7d)	ShfTerm	B	*	*	1.3	1.2	1.2	9.91	1.44	3.21	fa
SWBDX	Schwab S-T Bond Mkt Index	ShfTerm	B	*	*	1.1	2.1	2.3	9.89	1.93	4.16	fS
SSTBX	Strong S-T Bond	ShfTerm	B	*	*	1.0	2.2	2.8	8.50	1.44	4.43	FSA
PRWBX	T. Rowe Price S-T Bond	ShfTerm	B	*	*	1.0	1.7	2.2	4.67	3.84	1.41	fsa
VFSTX	Vanguard Short-Term Investment Grade	ShfTerm	B	*	*	1.1	1.9	2.6	10.50	1.54	4.03	fsa
VSGBX	Vanguard S-T Federal	ShfTerm	*	*	*	1.1	1.8	2.2	10.24	1.65	3.73	fsa
VFISX	Vanguard S-T Treasury	ShfTerm	B	*	*	1.0	1.5	1.9	10.27	1.56	3.80	fsa
MNSGX	WellsFargo Montgomery S Dur Govt (closed)	ShfTerm	B	*	*	0.9	2.0	2.2	9.85	1.39	3.92	fSa
BTINX	American Century Target 2010	ZeroCpn	*	*	*	1.8	1.3	1.0	88.98	5.25	4.34	FSA
BTFTX	American Century Target 2015	ZeroCpn	*	*	*	3.3	0.1	-0.4	76.00	8.69	4.36	FSA

Fees and Performance

Q I would like to follow one of your suggested portfolios of mutual funds. I have two questions:

1) Do your portfolio returns include the cost of buying and selling funds? Some funds even have a penalty to sell them often or early.

2) The funds in your portfolio are from many different companies. Instead of buying/selling from them and dealing with so many companies, are there better ways to buy/sell from one source?

— S.Y., San Jose, CA

A **MONEYLETTER** deducts any fund-imposed fees from the returns reported in our model portfolios. An example of such a fee would be an early redemption fee, say one percent on any sale if the fund is held less than 180 days. These fees vary from fund to fund and are generally designed to curtail short-term trading.

Indeed, you can conveniently trade most of the funds we recommend (many with no transaction fee) at a discount brokerage. Charles Schwab, TD Ameritrade, and Fidelity are three prominent services. Brokerage fees are not factored into **MONEYLETTER**'s reported returns. For instance, let's say you purchased a fund in your Schwab account that is not a "no transaction fee" fund. That trade would cost you a "ticket charge" at Schwab. We do not factor these fees in because:

- 1) these fees vary among brokers and are often based on the size of the trade;
- 2) you could avoid it altogether if you bought the fund directly from the fund family.

It is therefore not practical to include in our calculations. \$

HOTLINE

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Wednesday at 7:00pm (ET)

(continued from page 8)

tative criteria. Now, however, the managers feel the fund is well-positioned, stating, "We have completed the assembly of the highest-quality portfolio of international businesses that the fund has ever owned." \$

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c/o Southeastern Asset Management
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100% U.S. TREASURY FUNDS

	7-Day	30-Day	1-Year
Gabelli US Treasury MMF	5.00%	4.95%	3.99%
Vanguard Treasury MMF	4.79	4.75	3.91
Amer Century Capital Presv Fund/Inv	4.60	4.57	3.70
T. Rowe Price US Treasury MF	4.57	4.51	3.60
JPMorgan 100% US Treas MMF/Morgan	4.55	4.50	3.58
RMK Select Treas MMF/CI A	4.54	4.49	3.53
HSBC Investor US Treas MM/CI D	4.53	4.43	3.41
US Treasury MF of America/CI A	4.49	4.44	3.51
Schwab US Treasury Money Fund	4.46	4.42	3.51
Wells Fargo Adv 100% Treas MMF/CI A	4.41	4.37	3.47

GENERAL PURPOSE TAXABLE FUNDS

	7-Day	30-Day	1-Year
MFS Money Market Fund	5.24%	5.20%	4.20%
TIAA-CREF Money Market Fund	5.22	5.20	4.21
Vanguard Prime MMF/Retail	5.22	5.20	4.21
Harbor Money Market Fund	5.17	5.15	4.14
PayPal Money Market Fund	5.16	5.14	4.34
Pioneer Cash Reserves Fund/CI I	5.10	4.84	3.83
Dreyfus BASIC MMF	5.09	5.04	4.05
GE Money Market Fund	5.08	5.06	4.08
Marshall Prime MMF/Investor Class	5.08	5.05	4.09
SSgA MMF/CI A	5.08	5.05	4.10

TAX-FREE GENERAL PURPOSE FUNDS

	7-Day	30-Day	1-Year
Alpine Municipal MMF/Investor	3.43%	3.51%	3.09%
Vanguard Tax-Exempt MMF	3.40	3.46	3.01
Fidelity AMT Tax-Free Money Fund	3.22	3.30	2.84
DWS Tax-Exempt Money Fund	3.15	3.22	2.75
Fidelity Municipal MMF	3.14	3.20	2.75
T-E Portfolio/Managed Shares	3.12	3.16	2.69
Dreyfus BASIC Muni MMF	3.10	3.19	2.72
Fidelity Tax Free Money Market	3.10	3.17	2.72
Tax-Exempt MF of America/CI A	3.10	3.10	2.58
Amer Century T-F MMF/Inv Class	3.09	3.14	2.72
Marshall Tax Free MMF/Class Y	3.09	3.15	2.74
T. Rowe Price Summit Muni MMF	3.09	3.13	2.67

TAX-FREE STATE-SPECIFIC FUNDS

	7-Day	30-Day	1-Year
Vanguard PA Tax-Exempt MMF	3.38%	3.45%	2.99%
Vanguard NY Tax-Exempt MMF	3.36	3.42	2.97
Vanguard OH Tax-Exempt MMF	3.36	3.43	2.99
Vanguard NJ Tax-Exempt MMF	3.34	3.41	2.94
Vanguard CA Tax-Exempt MMF	3.32	3.38	2.93
Fidelity PA Municipal MMF	3.10	3.19	2.69
Fidelity FL Municipal MMF	3.09	3.17	2.71
Fidelity NY Municipal MMF	3.08	3.09	2.65
Fidelity AZ Municipal MMF	3.07	3.13	2.69
Fidelity CT Municipal MMF	3.07	3.13	2.66

Taxable equivalent yield = yield / (1—total effective tax bracket). Funds are ranked by 7-day yield; 7-day and 30-day yields are compound yields as of 8/15/06. Third column refers to 1-year total return. Criteria for inclusion include: top-yielding unrestricted retail funds only, with minimum initial investment <\$25,000 and assets >\$100 million.

Source: iMoney.net's Money Fund Report (800) 343-5413

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Longleaf Partners International Open Again

Back on February 6, 2004, Longleaf Partners International's board decided to close the fund to new assets. At that time, the fund's managers were having a difficult time finding investments that meet their undervalued criteria. Cash levels in the fund were rising due to both portfolio sales and cash inflows. To protect its existing shareholders, the board closed the fund until "such time when attracting new assets would again benefit shareholders."

Apparently that time has come, as the fund reopened to new investors on July 10. So what's changed? A sharp correction in May created new investing opportunities by putting high-quality stocks in the discount-price category. In addition, the fund's cash level, which had ballooned to 30% of net assets, declined to less than 5%. According to the fund, new cash will allow the fund to take advantage of future market volatility. "Much has changed in the past decade, but not the alternating cycles of fear and greed that have always characterized markets. In the second quarter, fear came back to a table previously ruled by greed. This type of environment usually creates opportunities for long-term investors, and the second quarter was no exception," the managers opine.

Picky investors

As the fund closure showed, the managers are clearly unwilling to compromise their investing parameters. In a nutshell, their goal is to find "strong, competitively entrenched businesses that are run by capable, vested, shareholder-oriented management teams, and that sell for substantially less than corporate worth." They take that "vesting" criteria a step further as far as their own firm is concerned, as not only the managers, but also the employees and affiliates of Longleaf and Southeastern Asset Management (the fund's advisor) are one of the fund's major shareholder groups.

Through a rigorous analysis, the managers assess the value of a firm's assets, its ability to generate cash flow, and come up with an intrinsic value. They buy only when the stock is selling at discount of at least 40% of that value. And the managers don't just dip their little toes into these waters. When they commit to a stock, they often plunge fully in. The entire portfolio consists of only 20 stocks. The top ten holdings account for 60% of the fund's assets. Once the managers make a purchase, they are willing to wait patiently. And with some of these undervalued or misunderstood stocks, it can take a lot of patience since the payoff can be quite some time away. Portfolio turnover is a paltry 17% annually, and stocks tend to stay in the portfolio for five years or longer.

Meanwhile, the managers pay little heed to sector or country weightings, letting the chips fall where they may.

Looking at sector weightings a bit more broadly than in the table below, the fund has 30% of assets in consumer goods, 24% in media, and 23% in financial services.

Top Five Sectors & Countries (% of Assets)

Insurance	20.1%	Japan	24.6%
Broadcasting & Cable	16.0	United States	21.4
Technology	14.2	France	10.6
Automobiles	5.7	Canada	9.2
Medical & Photo Equip.	5.7	United Kingdom	8.7

As of June 30, 2006

According to the managers, more than one-half of the portfolio consists of "perma-holdings," which they describe as "companies with superior economics that dominate their industries and delight their customers." They cite a number of firms in this category: Nestle, Dell, YUM! Brands, News Corp, Shaw Communications (Canadian cable operator), Philips Electronics, Olympus Corp. (via their medical business), BskyB (British broadcaster), Cemex (cement, Mexico), and Cheung Kong (leading property builder in Hong Kong), among others. In fact, the latter was purchased recently, with the fund's last full position of cash, along with Hutchison Whampoa, which is the world's largest owner of container ports. The managers note that these firms could not be dislodged from their leadership positions, even by "the best capitalized new competitor." They acknowledge that some face temporary problems, but remain convinced that their franchises will become more valuable over time.

Fund Performance (Total Return)

2006	+3.2% (8/10)	2002	-16.5%
2005	+12.9	2001	+10.5
2004	+10.2	2000	+25.9
2003	+41.5	1999	+24.4

Reasons for the lag

After being at the top of the foreign large-cap value pile in 2000 and 2001, the fund's performance since has more often lagged than lead its peers. A 3.2% return through August 10 puts it near the bottom of the category for the year-to-date. Management attributes this sustained lag to a number of factors. They say they have made some analytical mistakes, but by far the main reason has been the high cash balances the fund carried over the past three years as they waited for ideas that met both qualitative and quanti-

(continued on page 7)

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