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# Money Matter\$



A Quarterly Newsletter from Sommers Financial Management

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## What You Should Know About Mutual Funds by Harry Maurer

Mutual funds offer the investor a way to participate in the growth of the global economy, by spreading risk across a wide range of investment vehicles, often stocks or bonds. Does this mean that all mutual funds are good? NO! Their "goodness" depends on the return that you receive from them. This return is based on the fund performance less the cost of owning the funds. The cost of owning the funds, in general, consists of loads and fees charged by the fund company.

**Loads:** When your broker purchases a mutual fund for you, the fund often has a load associated with it, which is deducted from the value of your account. Suppose on January 1st you were to give your broker \$100,000 and that your broker purchases for you a fund whose load is 5.75%. That means you have paid your broker \$5,750 simply for purchasing the fund for your account.

Even worse, there may be high annual fees associated with the maintenance of your fund. Let's look at the graph below, to see how a typical mutual fund (in this case, the Morgan

Stanley S&P 500 Index Fund) compares to the Spyderys, an Exchange-Traded Fund (ETF) tracking the S&P 500 Index. The former has a 5.75% load and an annual expense ratio of 0.88%. The latter has no load and a paltry 0.11% expense ratio.

Suppose on January 1st you deposit \$100,000 into your brokerage account and that the S&P 500 Index grows at 10%. If your broker buys for you \$100,000 of the Morgan Stanley fund, then at the end of the first year, your Morgan Stanley assets are worth \$102,846. If your investment had instead been the Spyder ETF, you would have, after the first year, \$109,890.

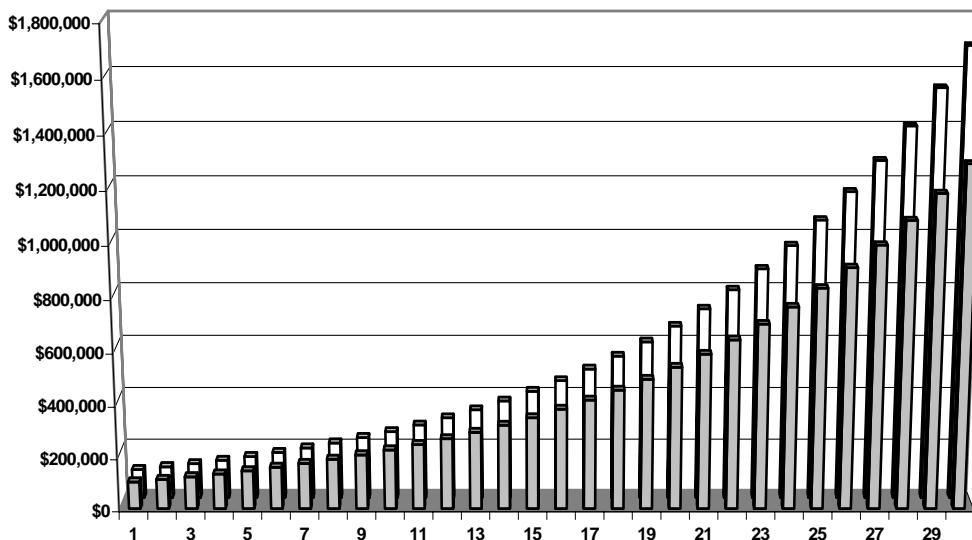
Why the difference? Because the loaded fund started the year with \$5,750 less, and the annual return had 0.88% chopped off instead of a mere 0.11%. Loads and high expense ratios explain why 90% of mutual funds perform worse than the market averages.

The difference becomes even greater, each year. At the end of the 30<sup>th</sup> year, the Morgan  
*(Continued on page 2)*

*Be sure to make your 2005 IRA contributions by April 15th, 2006!*

### Annual Returns

- Dow Jones Industrial 30 Average : 5.8 %
- Standard & Poor's 500 Index: 9.7 %
- Nasdaq Composite Index: 13.7 %
- Russell 2000 Small Company Index: 17.4 %
- Sommers Financial Management's "MODEL 25" PORTFOLIO (see next page for an update): 25.7 %



## Mutual Funds — *continued from page 1*

Stanley fund is worth \$1,292,445 and the Index ETF is worth \$1,693,344. **Where did the extra \$400,000 go? Into a vacation home, *but not yours*.**

What can you, as a savvy investor, do to optimize your returns? Simply this: **Make sure your advisor never puts funds with loads or high expense ratios into your portfolio.** Often, the value of funds managed by the company your advisor is with are worth questioning. Compare the excellent performance of Exchange-Traded Funds and No-Load Index Funds to the performance of any proprietary mutual fund—and ask yourself why your advisor ever had *you* invested in “*their*” favorite funds.

### Sommers Financial Management’s “MODEL 25” PORTFOLIO Update

The Model Portfolio continues to grow at a pace nearly three times the S&P 500’s return with a simple buy-and-hold strategy with the 25 most attractive equities.

This quarter, the portfolio basically doubled the 4.4% return of the S&P 500 Index, continuing to outperform.

**Outgoing** stocks from the portfolio during the first quarter of 2006 include:

- **American Eagle**—up 17% since last quarter
- **China National Drilling**—up 18% this quarter
- **Colgate**—up 6% in the first quarter of 2006
- **Dow Chemical**—down 3.6% this quarter
- **Doral Financial**—up 2% in the quarter
- **Ipsco**—a nice run-up of 29% this quarter!
- **Maxim**—flat in the quarter, and out of the portfolio
- **Nokia**—up 12% in the first quarter of ‘06
- **SEI Investments**—a rise of 15% this quarter
- **Tessera Technologies**—up 27% since December

**Incoming** stocks to the portfolio this quarter include:

- **Actions Semiconductors**—This Chinese semiconductor manufacturer produces itsy bitsy chips for consumer gadgets like iPods and other MP3 players.
- **CompuCredit**—Credit card and consumer loan provider, trading at a P/E of 10 and 1.7 times cash.
- **Syneron Medical**—Israeli medical equipment maker specializing in cosmetic skin care to treat acne and cellulite, and to help in the removal of unwanted hair.
- **J2 Global**—I figured out how they make so much money and are growing so fast—Sommers Financial is now a paying customer—and JCOM is back again.
- **K-Swiss**—This shoe maker is in the top 25, again.
- **Patterson Energy**—An oil and natural gas driller.
- **Toll Brothers**—Luxury homebuilder back in the top 25 with a P/E of 7 and return on equity of 32%.
- **US Bank**—This one just missed last quarter, and is now #8 with a P/E of 12 and paying a dividend of 4.3%.
- **Viropharma**—Biotech specializing in antibiotics for

#### Returns for our Model Portfolio versus the S&P 500 Index

	<u>Model Portfolio</u>	<u>S&amp;P 500</u>
Three Months	<b>10.0 %</b>	3.7 %
One Year	<b>25.7 %</b>	9.7 %
Three Year Annual Avg.	<b>N/A</b>	17.6 %
Annual ROR Since Inception	<b>36.5 %</b>	12.0 %

specific problems, in a patent battle with generics and the FDA. It’s been a bumpy ride (up 780%, then down 50%), and looks to only have upside from here.

- **Washington Mutual**—This old friend has come back into the portfolio after righting the ship by closing mortgage centers and trimming unnecessary staff.

<u>Company Name</u>	<u>Symbol</u>	<u>SFM Rank</u>	<u>% Gain since purchased</u>
Actions Semiconductor	ACTS	1	33.4 %
Bank of America	BAC	19	3.3 %
Burlington Resources	BR	7	11.1 %
CompuCredit	CCRT	21	(1.5 %)
Syneron Medical	ELOS	14	(0.9%)
First Marblehead	FMD	5	85.7 %
Harley Davidson	HDI	15	25.0 %
Intel	INTC	18	(20.8 %)
Innovative Solutions	ISSC	16	(27.5 %)
J2 Global	JCOM	23	0.0 %
Johnson & Johnson	JNJ	20	(3.3 %)
K-Swiss	KSWS	24	0.0 %
Linear Technology	LLTC	11	(7.2 %)
Microsoft	MSFT	22	0.9 %
NetEase.com	NTES	6	14.1 %
NVR, Inc.	NVR	4	81.2 %
Southern Peru Copper	PCU	2	51.6 %
Patterson Energy	PTEN	13	11.9 %
Q Logic	QLGC	9	24.8 %
Shanda Interactive	SNDA	17	(35.7 %)
Toll Brothers	TOL	10	(8.2 %)
Taiwan Semiconductor	TSM	12	40.1 %
US Bank	USB	8	(0.3%)
Viropharma	VPHM	3	(32.9 %)
Washington Mutual	WM	25	0.0 %