



First  
 Class  
 Stamp

Address Label

The investment manager must put his client first in everything he does—Warren Buffett

“LOOK AT STOCKS AS BUSINESSES; LOOK FOR BUSINESSES YOU UNDERSTAND, RUN BY PEOPLE YOU TRUST AND ARE COMFORTABLE WITH, AND LEAVE THEM ALONE FOR A LONG TIME.”

“A great investment opportunity occurs when a marvelous business encounters a onetime huge - but solvable - problem.”

“There are lots of things I wish I’d done in hindsight. But I don’t think much of hindsight generally in terms of investment decisions. You only get paid for what you do.”

“Investing is the greatest business in the world because you never have to swing. You stand at the plate; the pitcher throws you Google at 700! Starbucks at 25! And nobody calls a strike on you. There’s no penalty except opportunity. All day, you wait for the pitch you like; then, when the fielders are asleep, you step up and hit it.”

—Excerpts from “Thoughts of Chairman [Warren] Buffett”- compiled by Simon Reynolds

**Stock Spotlight – ViroPharma (VPHM)**

ViroPharma engages in the development and commercialization of products that address serious infectious diseases, with a focus on products used by physician specialists or in hospital settings. Its principal product includes Vancocin for treatment of antibiotic-associated pseudomembranous colitis caused by Clostridium difficile and enterocolitis caused by Staphylococcus aureus, including methicillin-resistant strains.

The company also develops Maribavir, which is in Phase III clinical development stage for the treatment of cytomegalovirus disease; HCV-796 for the treatment of hepatitis C virus infection; and Intranasal pleconaril for the treatment of the common cold and asthma, which are both in the Phase II clinical development stage.

ViroPharma’s Notable Statistics	
Market Capitalization	\$ 620 Mil.
5 Yr. Annual Growth Projection	15 %
SFM’s Price / Earnings Ratio	9.0
SFM’s Calculated ‘Payback Ratio’	43 %
Net Profit Margin	59 %
Cash Per Share	\$ 7.90
Debt Per Share	\$ 3.57
Price Per Share (12/28/07)	\$ 8.38

January 1, 2008

# Money Matter\$



A Quarterly Newsletter from Sommers Financial Management

Ph. (503) 397-1545 [www.sommersfinancial.com](http://www.sommersfinancial.com) Volume 6, Issue 1

**Exchange-Traded, Closed-End, and Mutual Funds—Oh My!**  
 By Adam Sommers

This article will be the first in a series dissecting the more renowned mutual fund, and the more obscure closed-end and exchange-traded funds (ETFs). For background on the fund industry, as of April 2007, investor assets held in mutual funds totaled over \$11 trillion, while assets in ETFs amounted to a mere \$467 billion, though the latter figure has been doubling each year while the former remains relatively stagnant. Each type of investment vehicle has its own benefits, and **each could be the best choice for your portfolio—depending on your situation.**

Before I point out the differences, let me assure you that investors are well served by having money invested in funds of all types (but of course not all funds), because **they offer two important benefits: diversification and professional management.**

While closed-end and most mutual funds offer “active” professional management, index ETFs and index mutual funds offer “passive” management, meaning the administrators manage the fund to mimic an index, such as the S&P 500 or the Dow Jones Industrial Index.

For the active management in mutual and closed-end funds, investors must pay an annual fee, usually ranging from 0.5% to 2.5%. With passive management in an ETF or index mutual fund, annual expenses usually run between 0.1% and 0.5%, depending on the management company and the competition they face tracking the same index (more competition drives prices down—capitalism at its finest).

In addition to the annual expenses of the funds, there may be a transaction fee to invest. Mutual funds have share classes that usually indicate the fee (Load) to be levied on your investment either upon entry or exit. These fees range up to 8.5% of your investment, though a fund may be “No-Load” and “No Transaction Fee” (NTF). **While No-Load, NTF funds may sound ideal, these funds typically include a higher annual expense ratio** to compensate your broker (TD Ameritrade) for offering you the shares. However, those same extra fees can be included in a loaded or no-load fund as well—so tread carefully.

ETFs and closed-end funds trade just like a stock on the exchange, so when buying or selling shares you incur the same

commission you would on a stock purchase or sale. (TD Ameritrade currently charges between \$9.99-\$16.99)

When it comes to fees and expenses, No-load, no-transaction fee index mutual funds seem the best choice. So why choose any other, you ask? **Occasionally, the “active management” provided in certain funds is worth the extra cost. Additionally, ETFs and closed end funds offer other tangible advantages that I’ll highlight in the April newsletter.**

However, while I may recommend active management in some cases, I never recommend loaded funds to investors, as paying a fee up front is merely a way to compensate a sales representative—which is unnecessary in this day and age.

Also, due to most active mutual fund managers being “closet-indexers”, I don’t see much benefit from the added cost of actively managed mutual funds compared to index funds. That leaves index mutual and exchange-traded funds, as well as closed-end funds as my fund vehicles of choice for my clients.

**Coming up in future newsletters:**

- **The “triple-secret” benefits of ETFs and closed-end funds that the mutual fund industry doesn’t want you to know.**
- **What type of funds should be in your portfolio, and why I believe that to be so.**

### 2007 Returns

- **Dow Jones Industrial 30 Average :** 6.4 %
- **Standard & Poor’s 500 Index:** 3.5 %
- **NASDAQ Composite Index:** 9.8 %
- **Russell 2000 Small Company Index:** -2.7 %
- **SFM’s MODEL 25 PORTFOLIO:** 10.6 %

(see inside the newsletter for a detailed update of the Model Portfolio)

## Sommers Financial Management's AGGRESSIVE Stock Portfolio

Company Name	Risk Grade	P/E Ratio	Growth Rate	Expected Return
Alum. Corp of China	D	11.7	14%	25%
Actions Semiconductor	B	6.7	25%	63%
American Eagle Outfitters	D	10.0	14%	14%
Asta Funding	F	5.8	8%	9%
Biovail	D	9.5	5%	16%
Cherokee	C	12.6	8%	7%
Coach	C	12.6	19%	11%
Syneron Medical	C	9.8	16%	16%
Enesco International	D	7.8	26%	21%
Freeport McMoRan	F	8.0	26%	15%
First Marblehead	F	2.5	26%	53%
Graco, Inc.	B-	13.6	15%	8%
Grant Prideco	D	11.9	19%	12%
Harley Davidson	B-	10.3	11%	10%
J2 Global	C	13.1	19%	13%
Lam Research	C	9.7	18%	17%
New Frontier Media	D	10.2	15%	12%
NetEase	C	15.8	20%	11%
NutriSystems	F	7.7	21%	22%
Southern Copper	D	9.6	13%	12%
Palomar Medical Tech.	F	13.2	18%	15%
Qualcomm	A-	19.1	21%	10%
<b>Taiwan Semiconductor</b>	A+	13.4	22%	12%
Viropharma	D	9.1	15%	43%
World Acceptance	D	7.4	15%	10%

*The Aggressive Stock Portfolio* is made up of the 25 best prospects for total return over the next 3-5 years. This list includes more small companies—and more companies that do not pay dividends—than our other two portfolios.

We have displayed four pieces of data that seem especially appropriate for an aggressive portfolio. As you can see, the risk grades for some of the holdings are below average, due to the aggressive nature of the stocks. However, the average P/E ratio is only 10.5 due to our value-based investment philosophy. You will not see companies without profits in any of our portfolios, as we purchase businesses for our clients as owners, not traders.

The growth rate of companies in this aggressive portfolio measures an average of 17%, calculated as the consensus average of all analysts who cover the company for the estimated growth in earnings (profit) over the next five years. The “Expected Return” (avg. 19%) is SFM’s “payback yield”, which is the single most important metric we use when analyzing a business to purchase.

## Sommers Financial Management's Conservative INCOME Stock Portfolio

Company Name	Risk Grade	P/E Ratio	Div. Yield	Ret. on Equity
AstraZeneca	B	10.3	3.9%	10.8%
Boeing	A	14.4	1.6%	39.3%
BP, Plc	A+	9.5	2.5%	65.6%
Anheiser Busch	A	15.8	2.6%	61.9%
Cherokee	C	13.3	8.7%	85.3%
Colgate-Palmolive	A	19.1	1.9%	100.6%
Campbell's	A	14.3	2.4%	55.0%
Chevron-Texaco	A-	9.1	2.5%	24.6%
General Electric	A	13.0	3.0%	26.0%
Home Depot	B	9.9	3.4%	19.4%
Hershey	A	15.3	3.1%	59.5%
Johnson & Johnson	A+	15.1	2.5%	26.1%
Coca Cola	A	21.2	2.2%	30.1%
Altria	A+	14.4	4.0%	48.1%
Merck	A	20.2	2.5%	27.3%
3M	B+	13.6	2.3%	35.2%
Microsoft	A	17.6	1.2%	27.4%
Paychex	B+	20.6	3.3%	27.4%
Pepsi	A	20.4	1.9%	32.6%
Pfizer	A-	10.7	5.0%	20.2%
Phillipine Long Distance	B	14.1	4.1%	39.2%
<b>Taiwan Semiconductor</b>	A+	13.4	3.7%	17.8%
US Bancorp	C	9.3	5.1%	19.6%
US Tobacco	A	13.7	4.3%	71.7%
Verizon	A	14.6	3.9%	15.4%

*The Conservative Income Stock Portfolio* is made up of the 25 least volatile, highest yielding, reasonably valued companies on our screen.

The holdings in this portfolio received the highest grades for investment risk, as there is traditionally less risk of loss when investing in stocks of large, established, low-priced, dividend paying companies.

The average dividend yield of stocks in this portfolio is 3.5%, twice the S&P 500 Index's 1.7%. The average return on equity over the past three years for companies in this portfolio is over 37%, indicating consistent, high-quality earnings for the shareholders—which they pay out in the form of dividends. The average SFM calculated P/E ratio is a mere 14.

This portfolio consists of companies that are good long-term holdings in an equity allocation (one piece of the pie) for clients nearing or at the retirement stage of their life.

## Sommers Financial Management's ORIGINAL “Model 25” Stock Portfolio

Company Name	Value Grade	Cash Flow	Risk Grade	Market Cap
Actions Semiconductor	A+	A+	B+	Micro
American Eagle Outfitters	A	B	D	Mid
Cherokee	C	A+	C	Micro
Coach	B	A	C	Mid
Syneron Medical	A-	A+	C	Micro
Freeport McMoRan	A	A	F	Large
Federated Investors	C	A	C	Small
First Marblehead	A+	A	F	Small
Graco, Inc.	B-	A	B-	Small
Home Depot	A-	D	B	Mega
Harely Davidson	B+	C	B-	Mid
J2 Global	B	A	C	Micro
Johnson & Johnson	C	B	A+	Mega
Lam Research	A	B+	C	Mid
McGraw-Hill Publishing	B-	B	B	Mid
Altria Group	D	C	A+	Mega
New Frontier Media	A	B	D	Micro
NetEase	C	A+	C	Small
Southern Copper	C	A	D	Large
Pfizer	C	B-	A-	Mega
Qualcomm	D	A-	A-	Large
<b>Taiwan Semiconductor</b>	B	B+	A+	Large
Texas Instruments	C	B-	B+	Large
US Tobacco	D	A	A	Mid
Viropharma	A+	A	D	Micro

### New this quarter:

- Palomar Medical Tech
- Hershey
- Paychex
- Philippine Long Dist.
- McGraw-Hill Publish.

### No longer of interest:

- Zenith Insurance
- Chesapeake Energy
- NVR
- Bank of America
- Citigroup
- Maxim Intregrated
- Wachovia
- Patterson Energy
- Aspreva Pharma

## Commentary and Ramblings

By Adam Sommers

Oh my—with all the news headlines these days you'd think that guns, bottled water, and the fear of God would be the only salvation in this market. I take it with a grain of salt. The news media has a business to run, and the methods they employ are dramatic headlines and shocking stories while providing a view into the narrowest of slices of the world in which we live.

For example, if you watch the 10 o'clock news on Fox in Portland, they really don't show you what's happening with MOST folks around the city—but “if it bleeds it leads.”

When it comes to the stock market and the economy, we read headlines that spout that foreclosures are up 200% in 2007. Yawn...it's still less than 1% of homeowners—not such a big deal to most of us—unless of course we were unfortunate enough to buy speculatively with poor loan terms, something that should not occur if you include your advisor (me) in the process.

Is a recession on the horizon? No one really knows, but unemployment is at historical lows, and the global economy is chugging right along. Even if it weren't would I change my investment strategy? I think not. Market timers do not make the Forbes 400 list, and for good reason.

While we can usually gauge a good investment for the long term, it is nearly impossible to predict investment results in the short term. So my job is to assist clients in constructing an all-weather investment portfolio, and educate them in the art of avoiding reactionary moves and emotional mistakes. While this strategy often requires a strong stomach, it has proven throughout history to be the best, most consistent way to accumulate and retain wealth.

So if you find yourself wanting to jump into the next hot sector, or cower in your house with a stash of bullion, take a step back and look at your goals. Is it to avoid losing money at all costs? To grow your nest egg over the next 20 years and retire in Fiji? To live off of income provided by your investments?

Each of us have unique goals that determine our investment strategy—a strategy that doesn't include reacting to what the media feeds us. So sit back, relax, and enjoy the ride in 2008.

### Returns of SFM Portfolios versus the S&P 500 Index

	S&P 500 Index	Sommers Financial Management's		
		Model	Aggressive	Conservative
Three Month Return	-3.8 %	-4.1 %	-6.5 %	-1.1 %
Twelve Month Return	3.5 %	10.6 %	<i>available next quarter</i>	
Three Year Average Annual	7.1 %	10.2 %	NA	NA
Four Year Average Annual	8.0 %	19.4 %	NA	NA
Annual ROR Since Inception	11.3 %	27.0 %	NA	NA