

INTERIM REPORT - PORTFOLIO ALLOCATIONS

24th August de 2011

Further to our 19th August Interim Report here are our allocation suggestions and general overview. In our August 10th communications I attached a list of ETF/investments which we had been monitoring since early last year. These are "Value" selections IE. Investments which have reached price levels we view as particularly attractive against actual and projected...three to five years... forward earnings. It is important to remember that the portfolios we manage, range from high five figures to tens of millions USD. With a minimum allocation of circa \$8KUSD per investment our proposals are, by necessity different. In addition as well as attempting to understand the psychology of markets we must contend with computers which distort buying and selling prices. The volatility experienced over the past few weeks has been exacerbated by pre-programmed "Trading ahead" computer buying. Indeed the majority of "buy orders" I made over the last few weeks were at specific prices approximately 4% less than the lowest value reached. Some got to within 1% of our order price, but only for a micro second. Therefore the specific suggestions listed below are influenced by many different factors.

A year ago this week, the S&P500 was hovering at 1200-1205. I had assumed that the then anticipated message which was expected by the FED chairman Ben Bernanke; would be to announce a second round of "quantitative easing". The fundamental implications of such a move would be expected to "devalue" the US Dollar. The expected impact would help USA based exporters; increase commodity prices and create pressure on emerging market countries economies to over heat. Under normal circumstances this would help USA large cap (exporting) companies; raise costs on basic material, food and oil. I and most other economists...that follow fundamentals... believed that this would create a short term small rally and once the overall negative downside aspects of this move were understood that markets would retrace and test the next lower support level. IE. S&P500 at 1180. Instead we experienced a 16% increase.

Considering the outstanding difficulties of the Eurozone sovereign debt as well as a number of major emerging markets implementing policies to punish capital inflows, the increase was unsustainable. Therefore any correction based on fundamentals must disregard most if not all of this "stimulated" rally.

This being the case I sought opportunities which had fallen at least 10% below the 16% gain or had unique value parameters such as free cashflow combined to quality dividend payment records matched to growth potential. Once selected, I waited until valuations matched levels with sufficient upside to "risk or mid term" trend awards. The list of Value investments sent to you a few weeks ago (11th August) were presented with their percentage fall from their 52 week high and their upside gain when those highs were recovered.

SUMMARY.

I view a correction, when 10-15% is lost from my "Fair value" and



as stated above I viewed the rally from a year ago to earlier this year as an effect of the stimulus rather than underlying fundamentals.

I believe that the US shall avoid a technical recessions...unless policymakers can once again snatch defeat from the jaws of "good policies"... however I still believe that inevitable weak market data will still "roil" markets occasionally, as sentiment is particularly fragile. This brings us back to computer and their "trading ahead" programmes. The recent buys we implemented were approximately 1% higher in costs because computers bought ahead of each of our trades.

In addition and much more importantly many of the algorithms use a "penny" differential process which...without being too technical" create volume and trend distortions...add to volatility and price levels. A simple example would be that other computers that read "trends and trading volumes" have different algorithms that recognize "up or down" trends then buy into whichever movement is identified. A third set of computers serving institutional "value" buyers, then kick in and buy the lower trend when a defined pre programmed buying price is reached. This raises value which the "trading ahead" computer recognizes and the process starts again. Perhaps, one of the least beneficial uses of our modern computer age; certainly a frustrating one for the majority of investors as it can reduce profit opportunities. Our investing strategy must therefore incorporate not only the fundamentals, market psychology, current news but somehow circumvent pre programmed computers to best position portfolios going forward.

EVALUATION AND EXECUTION.

Notwithstanding the above there has been a huge failure of policy makers to deal with the crisis and that's led to a general loss of confidence. The 2008/9 financial induced recession was so big and so recent that it's remained at the front of the market's psyche. The interbank lending rates between European banks has once again reached levels where banks horde...rather than lend... money. This could lead to a grinding credit crunch in the southern euro zone as banks look to reduce dependency on both the ECB and wholesale funding, and be a

major drag on economic recovery. However even as banks deposit loans back with the ECB, it's the promise of this money that means a full-blown liquidity crisis as seen in 2008 is reasonably remote. The market remains sceptical of any near-term resolution to the debt crisis in Europe or political commonsense in the USA and I view it as extremely unlikely that the FED chairman will be allowed to announce a QE3 stimulus package. Never the less he does have a number of options which are likely to be used. Whether they are discussed in his Jackson Hole speech is debatable.

The most likely outcome will be a speech which will present a new strategy whereby the FED will sell their two year bond holdings and buy longer dated paper. This will shrink the interest rate curve between short and long T-bills. In addition I expect him to state that insufficient data exists to confirm that the USA is entering a "double dip" recession and that US banks are in a much better capital position to meet the liquidity needs should the Eurozone situation deteriorate into a "haircut" if the sovereign debt situation worsen. Indeed if little is said then many market watchers will take comfort from that fact.

The emotional side of the equation is understandable given the recent past. Last year Bernanke's Jackson Hole speech was enhanced by better sentiment index and production figures within two weeks. Combined they gave support, strength and reassurance to the markets. Although I believe that sentiment index levels and production figures...due within the next week... will be better, the current problems which weigh on the markets have little chance of any quick resolutions. However, fundamentals do not support more than a slow but still positive growth. The variables are the political ineptitude possibilities. Certainly in the USA the Republicans would rather fight next years elections with many of the outstanding issues unresolved, whereby they can present the solutions to the electorate as part of their election process. Neither can we assume that the Eurozone can find much relief beyond a bigger, more efficient short term "band aid". Therefore our strategy is to invest toward fundamentals and where possible obtain benefit from over panicked selling of markets.

The S&P500 index reflects how markets have changed. Since the beginning of 2007 major companies have expanded their operations globally. Today the index is more reflective of global markets rather than predominately the USA. I expect the US to grow anemically in the second half but the world will grow between 3.5-4%. The S&P500 would be expected to reach circa 1300+ on those performances. This would be a gain from today's values of 12%. Short term sentiment/panic volatility could easily undermine the rise or erode its staying power, but fundamentals would support this level. In the mid to longer term; IE 3-5 years, public support for political change will address a certain level of the outstanding fiscal/debt issues. I view this as extremely positive for markets two to ten years forward.

Short term consensus is another matter. The expectations that Ben Bernanke could compose a speech which would meet all the requirements of a disparate and many faceted needs, would be superhuman. The FED has sufficient independency to create a "stealth" QE3 programme without increasing the monetary base. The ECB in conjunction with the IMF and the wealthier EU countries can increase their rescue fund to meet short term needs. However, no matter how much financial systems are reinforced or indeed even beneficially and completely overhauled; until job creation programmes are seen to be in place and working the current angst levels will still prevail. Therefore before we view the opportunities that our suggested investments can be expected to accrue, we must first try to assess the downside risks.No matter how I crunch the numbers the worst value I can reach...using fundamentals... on the S&P500 would be 9% below Monday 22nd August's closing value. Around 1020 (this incluyes further panic cause by disinflationary scenarios and a continued lack of transparency in real bank debt exposure. NOTE: this has improved somewhat as the Basle III requirements have stipulated the ratios. Unfortunately the too big to fail banks are still reluctant to publically publish the size of their "bad asset" levels. However I view this more as a competitive reluctance issue rather than an insurmountable financial obstacle. Banks are already reducing staffing levels to cut expenses and are looking to sell assets to raise capital to meet the Basle III requirements. The downside is that even although US banks and even European banks are all in a much better financial position than 2008 and face a much less perilous series of challenges; devoid of new initiatives credit/lending is once again hard to find. If credit is restricted then the general economical situation has little chance of funding a recovery. In any event few people are concerned as to whether new stimulus programmes to assist banks are instigated. For sentiment improvement to rise significantly job creation and house prices must rebound. The latter will need at least another year although some programmes could be instigated (see below) to assist. As stated above it therefore seems unlikely that the US politicians would hand their opponents a positive outcome before next year's election. All of the above does little to suggest that any positive "take" from Friday's speech of Ben Bernanke would have much traction unless other positive news can be found.

With the current emotional state of investors these outstanding issues could easily trigger another round of selling, especially if the FED chairman's speech disappoints, or its content doesn't pass pragmatic analysis. However, metaphorically we are viewing a body that has allowed itself to become run down, overweight and with poor hygiene, susceptible to catching flu and other viruses. The doctors have stated that he needs to change his habits or these recurring events will continue. His neighbors may avoid him as he is sick, but his doctor has not called the hospital to arrange a cancer screen. Therefore our evaluation acknowledges that panic could send markets below my assessed bottom, but notwithstanding either a natural or politically induced disaster, do I believe that fundamentals would allow it to remain there long, even in an emotionally charged /panic investment environment.

EXECUTION.

The computer driven "trading ahead" causes considerable problems in allocating buys. It therefore requires a "twin prong" approach. If we use **BPT**, BP Prudhoe Bay Royalty Trust as an example. It pays a high dividend of 9.6% and as such when sold or bought as it has a relatively low daily volume of 125,000 shares traded each day "trading ahead" computers can serious affect price levels. It often fell to near \$100USD between the 11th and 14th August but whenever I put and offer to buy 2000 shares the price would rise between 5-6%. This is because of the relatively low volume traded. In comparison **E** Eni and **MRO** Marathon Oil Corporation each have daily trades of circa

1.8million. Their dividends are 6.2% and 2.4% respectively but their upside possibilities considerably more than BPT. Upside expectations of **E** and **MRO** over 18months I would suggest to be twice to three times that offered by **BPT**. This would be especially true if oil prices were to fall because of lower demand and remain so for two or three quarters. To return to execution possibilities the two tiered approach requires that selections are made on two levels. The first is to compete with other buyers and computers at appropriate advantageous moments and the second method is to establish a buying order list at specific discounted price levels. The former as discussed can be variable as to best buying price success however as the investments on our buy list are generally already 20-30% below their recent highs even a few percent difference still offers considerable upside and ensures that if markets rebound they participate in the gain.

The alternative is to fix a price for each investment. The downside is that values may not fall to the buying price. I had established twelve additional buy opportunities approximately 6-7% below today's prices; none dropped low enough to trigger the buy; although we were within 1.5% of many. An additional variable is the different value of portfolios. A portfolio of \$100,000USD has less flexibility than one of \$5 million USD however a correlation as to general opportunities exists. Therefore before describing our execution process let us review the current market one final time.

Corporations are generally well diversified with considerable amounts of cash on hand. Their outlook when negative tends to identify political and other fiscally induced risk/problems impacting their marketplaces. Never the less, most companies have been regularly out performing their projections. In addition I believe that the next round of industrial performance statistics will be positive. This should support markets, however until we see a considerable change in overall sentiment then consumers will be reserved and companies reluctant to spend; unless they see a particularly attractively priced acquisition to cheaply purchase a growth opportunity.

There are many positive fiscal programmes that could and indeed should be implemented both in the US and Eurozone which would positively change overall sentiment. I believe in the short term the former won't and the latter can't. I believe it is unlikely that Ben Bernanke will be able to change sentiment. Indeed I believe that his speech; for many market watchers will likely disappoint. This presage a further volatile period as trading volumes will be relatively low, which brings us back to mid and long term opportunities at discounted values as markets are trading on political inaction and consumer sentiment rather than pragmatic fundamentals. We made the following purchases to most of the Portfolios as they reached our buy levels against our eighteen months estimate percentage increase ratios. We are a little less bullish than overall analyst predictions for one year growth. Never the less our ratios offer the risk reward matrices to provide our upside targets. The analyst one year targets are shown as a value.

TKR	INVESTMENT	BUY PRICE	PRICE From High %	18 mth estimate	%	Analysts Estimate
BRK B	Berkshire Hathaway	69.98	-20.45%	\$78.30	12%	\$82.40
VIS	Vanguard Industrials ETF	55.69	-24.42%	\$63.94	16%	\$68.60
MRO	Marathon Oil	25.83	-51.61%	\$34.10	32%	\$38.12
CTB	Cooper Tyre and Rubber	11.23	-54.56%	\$16.50	46%	\$20.25
HAO	Guggenheim China Small	23.08	-34.73%	\$27.60	18%	\$30.20
	Companies ETF					
E	ENI	35.89	-36.14%	\$46.80	31%	\$56.85
KWT	Market Vectors Solar Energy	7.88	-46.36%	\$11.20	42%	\$12.70

The above investments offer a number of benefits. Apart from being generally oversold they spread across various sectors and geographic locations.

SMALLER PORTFOLIO (under \$125K)

At the most appropriate moment in the coming weeks and months we would sell 40% of the above holding to \$4-5K USD levels. This would allow cash holdings to be increased for future (Minimum entry \$8K) purchases. If volatility continues then we would place order buys between 6-8% below recent lows. With a two to three year outlook, upside possibilities are considerable.

MEDIUM PORTFOLIO (under \$500K) and LARGE PORTFOLIO

The larger available portfolio size enables a more aggressive "Low buy order price" strategy as a greater number of possibilities can be targeted, without the need to cash part of the initial holdings, unless a specific strategy can be enhanced. Equally wider diversification will enable a part of the portfolio to target investments against their dividend yields and M&A likelihood.

CONCLUSION.

Fear is driving the market. For the "cooler heads" the coming few weeks...even months... is a particularly positive moment. When markets are awaiting a speech from a FED chairman to provide some direction or reassurance or are more worried about a political misstep or mistake; then the fundamentals have broken down. This is not considered a positive indicator for short term market valuations. However, whether markets rise or fall over the coming weeks will be solely on confidence factors. Somewhere within that process specialists will assess the movement against fundamentals and from that point pragmatically educate the world as to the trends' sustainability. Either way we should be able to benefit.

Regards

Alan Lamb