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I N V E S T O R  
**Advisory**  
S E R V I C E

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## HOW TO USE THE INVESTOR ADVISORY SERVICE

*IAS subscribers, especially new ones, often ask how to interpret and use the information that IAS provides, where the numbers in IAS come from and what they mean. The following is a summary of IAS' components, plus guides that explain the Stock Selection Guide (SSG) and the Ranking Spreadsheets. These guides may be used as a reference when reviewing past and future issues of the IAS. We hope you find them a valuable addition to your investment research. Finally, a few "Frequently Asked Questions" are answered here.*

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The **Investor Advisory Service (IAS)** is designed for investors who want to follow the investing methodologies of BetterInvesting (formerly known as the National Association of Investors Corp., NAIC) – with much of the analysis work done for them. IAS publishes a monthly report that is mailed to subscribers on the fourth Friday of each month. An annual subscription includes twelve monthly issues, with each report containing three detailed stock recommendations. The subscribers-only website is updated with the most current issue on the date of publication, as well. (Be sure that your e-mail address is on file with us so that we can notify you when the issue becomes available.)

The goal for each stock recommended is a doubling in price in five years. Not all stocks recommended will achieve that goal. Experience shows that some will do much better and some will do worse. The results have consistently been better than the Dow Jones Industrial Average and other market averages. There is no assurance that the future will be as favorable.

A portfolio of ten to twelve stocks selected from our recommendations has a better chance of doing well than just a few selections. Of course, since no one is perfect, price declines will occur in some of the selected stocks. Adequate diversification is always prudent.

IAS is an unmanaged letter advisory service. In other words, subscribers must choose on their own what and when to buy and sell. We try to help the decision-making process with the assistance of the SSG and the Ranking Spreadsheets. Both of these will be explored in detail later in this commentary.

We do not advocate a "trading strategy." We have found that holding carefully selected stocks over the long-term produces the best results. No stock follows a time schedule, though, and there are always ups and downs in stock prices. If the fundamental assumptions made at the time of recommendation deteriorate, a sale may be

recommended and follow-up on that stock may be discontinued. Remember, a torpedo can come out of the dark at any time.

If you buy ten stocks, chances are two will do much better than expected, two will be disappointments and the other six will follow the expected course. When a mistake has been made, it is best to acknowledge the error and sell the stock. Waiting to get even usually is a self-defeating strategy. If you would not buy a stock that is down 25% in price, knowing that the decline is well-justified, then why continue to hold it in hopes of recovering your investment?

## STOCKS RECOMMENDED

The three stocks recommended each month are selected and analyzed using the BetterInvesting Stock Selection Guide (SSG). All of the stocks (approximately 80 of them) that are followed by *IAS* can be found on the three ranking spreadsheets provided in the Service. The stocks are sorted by symbol, by total return and by current price to earnings ratio (P/E).

The write-up that accompanies each SSG gives the reader a good perspective on what the company does as a business and how well it is managed. This offers some insights into the elements of judgment used in preparing the SSG.

The Investor Advisory Service is designed to help its subscribers learn more about investing. At the conclusion of each write-up, investor contact information is provided including the address, telephone number and Web site address of the company so you are able to contact them for annual and quarterly reports or to do your own research on the Internet.

The investment time horizon of our recommendations is five years (or more). If a

stock meets our target of at least doubling in market price in five years, the compound annual rate of return is 14.9% plus dividend income. It takes time for value to work out, hence the expectation to hold on for the longer term. We suggest patience to allow value to develop as outlined in our recommendation.

We tend to be contrarian at times. We try not to get caught up in what may be the latest investment fad. Frequently, we will recommend stocks not on the Wall Street institutional investor's dance card, but which are likely to work out profitably over a five-year time frame.

## OTHER FEATURES

The economy has an effect on corporate profits and hence stock prices. Each month's **Investment Comments** are necessarily general in nature, but the column does review market and economic conditions with an eye on what has been happening recently and what the outlook may be for the future.

Portfolio management is not carried out in a vacuum. Interest rates and the general economy are important factors affecting stock prices. Each month, the **Key Market Indicators** section presents charts of short-term and long-term interest rates as well as the level of the Standard and Poor's 500 Index.

In the interest of keeping subscribers informed about stocks followed by *IAS*, **News of Companies** is intended to report pertinent information that reflects how the companies are doing and which may affect the stocks' performance. The most obvious newsworthy item is the quarterly earnings report for each company in *IAS*. Percent changes in sales, pre-tax profits and earnings per share are important figures to the

investor. If the number of shares outstanding has changed to the extent it affects the reported EPS, we will comment on it. If EPS are significantly affected by changes in tax rates, we will mention it.

If major news about a company that IAS follows becomes known in the month between issues, we will send a brief update by e-mail to all subscribers to make you aware of this news in a timely manner.

The **Recent Earnings Report** gives the latest quarterly earnings per share and the percent changes tabulation for companies that have reported this information since the previous issue of IAS. This is an effort to keep you informed about the fundamental progress of the companies.

## WE WELCOME YOUR COMMENTS

If you occasionally would like a short answer to a question, please e-mail us at [IAS@iclub.com](mailto:IAS@iclub.com). Your subscription does not include active portfolio management, but we will try to help you understand the process of investing if we can. We often include commonly asked questions in the **Subscriber Feedback** section of monthly issues.

Feedback in the form of bouquets or criticism is also appreciated. The latter keeps us on our toes; the former makes it all worthwhile. We are always looking for ideas and ways to serve the majority of our subscribers.

If you want the service of an investment counselor, Seger-Elvekrog Inc., the financial advisory firm that writes IAS, can manage your portfolio for you using the same principles it uses in IAS. For more information, contact the firm directly at 1-800-449-6970 or visit <http://www.seger-elvekrog.com/>.

Please note that our publication schedule is fixed, so it is possible that market prices will change between the time we go to press and when your copy arrives in your mailbox.

We heartily subscribe to the ethics of the Association for Investment Management and Research (AIMR), which puts our clients' interests ahead of our own.

### **Investor Advisory Service**

Investment advice and education since 1974, helping you become a successful lifetime investor.

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Information presented herein has been obtained from sources believed to be reliable, but the accuracy and completeness of summaries, conclusions and opinions based on this information are not guaranteed. It should never be assumed that recommendations will be profitable or will equal the performance of securities listed here or recommended in the past. IAS relies on the investing methodologies and trademarked forms of BetterInvesting, a national non-profit organization dedicated to investor education. For more information on BetterInvesting, please see [www.betterinvesting.org](http://www.betterinvesting.org).

## YOUR INVESTMENT KEY – THE SSG

We find that success in investing in stocks depends on the right combination of two essential factors:

1. Investing in good businesses that show a consistent growth of sales and earnings
2. Buying stocks only at reasonable prices.

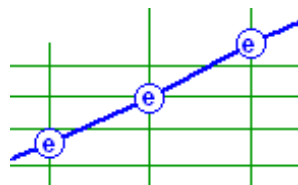
This kind of logical investing is the key to the long-term results of the classically successful investors like Warren Buffett, John Templeton or Peter Lynch. This is our experience, as well, and has enabled us to achieve results for our managed accounts significantly exceeding the stock market averages for many years.

The Stock Selection Guide (SSG) is a straightforward way to evaluate a company's standing on each of these factors. The front of the SSG presents in graphical form a picture of whether or not a company's sales and profits have been growing over the past ten years, as well as how consistent that growth has been.

As you well know from every mutual fund ad, past performance is no guarantee of future results. Still, unless something has changed, the best predictor of what to expect in the future is what has happened so far.

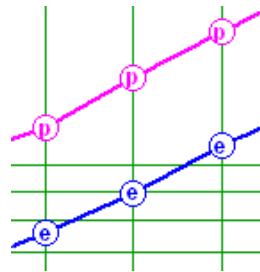
### **Section 1: Visual Analysis of Sales, Earnings, Price**

Earnings-per-share is the all-important factor that ultimately determines what a share of any stock is worth. This is graphed on the SSG by the line labeled "E" on the

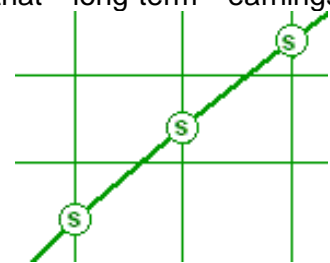


front of the graph.

The line labeled "P" for pre-tax profits should normally be pretty much in line with the earnings per share. If there is a significant difference, it is a red flag indicating that the difference should be investigated. For example, earnings per share could be growing faster than pre-tax profits because shares are being bought back.



The third line labeled "S" for company sales is just as important as the other two. The importance is that long-term earnings growth always depends on sales growth. In the short-term, earnings can be boosted by cutting expenses (such as when there is a merger), but expenses can't be cut forever. If sales are not growing at the same rate as earnings, then again, this is a matter to be investigated.



On the bottom of the first page, the SSG calculates the historical rate of sales and earnings growth to be used as a starting point for future expectations.

(1) Historical Sales Growth	_____ 23.4 %
(3) Historical Earnings Per Share Growth	_____ 22.5 %

### **Section 2: Evaluating Management**

Section 2, on the top of the back page of the SSG, shows the pre-tax profit margin (earnings before income taxes as a percent

**2 EVALUATING MANAGEMENT**

	1993	1994	2001	2002	LAST 5 YEAR AVG.	TREND	
						UP	DOWN
A % P/E or P/B Ratio (Net Earnings Total = Sales)	16.3	17.7	18.0	18.0	18.3		EVEN
B % Earnings Yield (E = Book Value)	16.8	18.9	15.7	17.2	16.6	UP	

of sales) and also net income as a percent of equity investment. It is worthwhile to see if year-to-year results are erratic or stable, and whether the trends are improving or deteriorating.

**Section 3: Price-Earnings History**

All the factors so far have been focused on the first essential issue: Does this seem to be a growing business? Starting with Section 3 on the back of the SSG, we look at the history of the price of the stock as a way of getting a reading on whether the present price is likely to be reasonable.

**3 PRICE-EARNINGS HISTORY as an indicator of the future**

This shows how stock price has risen or fallen with earnings and dividends. It is a building block for determining earnings into future stock prices.

Year	PRESENT PRICE <b>41.950</b>		HIGH THIS YEAR <b>42.190</b>		LOW THIS YEAR <b>25.700</b>		Dividend Per Share	G % Payout	H % High Yield
	A PRICE	B	C Earnings Per Share	D Price HIGH A=C	E Earnings Ratio LOW B=C	F			
	HIGH	LOW							
1 1999	26.1	9.0	0.52	50.2	17.3	0.000	0.0	0.0	
2 2000	40.7	11.7	0.69	<del>39.0</del>	17.0	0.000	0.0	0.0	
3 2001	59.0	23.9	0.89	<del>66.3</del>	26.9	0.000	0.0	0.0	
4 2002	53.9	24.3	1.10	49.0	22.1	0.000	0.0	0.0	
5 2003	42.2	25.7	1.33	31.7	19.3	0.000	0.0	0.0	
6 TOTAL		94.6		130.9	102.6		0.0		
7 AVERAGE		18.9		43.6	20.5		0.0		
8 AVERAGE PRICE EARNINGS RATIO	32.0			31.8					

The most significant item here is the current price earnings ratio (P/E). The P/E is calculated both on the basis of the last historical four quarters and based on an estimate of the earnings to be achieved in the next four quarters. If the present P/E is higher than the P/E has been historically for the last five years, it is a sign that investors may be overpaying for the stock and it is unlikely that this is a good time to buy this stock.

**Section 4: Evaluating Risk & Reward**

Section 4 on the back of the SSG presents a calculation of the comparison of an estimate of what the stock price might reasonably be expected to reach to if earnings growth is as projected and the high

price/earnings ratio that has existed over the last five years is again achieved. The possible high price is compared with a possible low price based on the company's historical low P/E, or what the stock has moved down to in recent times to determine the Up-Side Down-Side Ratio.

UP-SIDE DOWN-SIDE RATIO (Potential Gain vs. Risk of Loss)

$$\frac{\text{High Price (41)} \quad \mathbf{125.6} \quad \text{Minus Present Price } \mathbf{41.950}}{\text{Present Price } \quad \mathbf{41.950} \quad \text{Minus Low Price } \quad \mathbf{24.3}} = \frac{83.6}{17.7} = \mathbf{4.7} \text{ To } 1$$

The possible share price gain should be at least three times the risk of share price decline (that is, the stock should have an upside/down-side ratio of 3 to 1 or better) in order to give the investor a margin of security.

**Section 5: 5-Year Potential**

The remainder of the SSG refers to calculating the potential return on the stock. The most important expression of the potential return is the "% Compounded Annual Rate of Return" found on the lower right hand corner of the page.

	<b>Tot. Ret.</b>
<b>Average Yield</b>	<b>0.0%</b>
<b>Annual Appreciation</b>	<b>25.1%</b>
<b>% Compd Ann Rate of Ret</b>	<b>25.1%</b>

**Conclusions**

The Stock Selection Guide may seem a bit overwhelming at first glance because of the sheer quantity of numbers and the labels, many of which will be not very familiar. However, a careful study of the SSG will show that the elements are straightforward and will result in the investor having a much more in-depth grasp of a potential investment. It is important to recognize that investing in stocks is not a simple offhand kind of process. Careful consideration of the SSG will help an individual conclude whether to study investments on his own or whether to have a professional money manager, such as Seger-Elvekrog Inc., take care of his or her stock investing

## HOW TO USE THE IAS RANKING SPREADSHEETS

Q U A L S y m	Company Name	June 15, 2005	Price	Div	% Yld	Est. EPS	Tot. Ret.	% Gr.	Curr P/E	RV	Buy Up to	B U Y	Over- valued At	US/ DS Ratio	P/E as % Growth	Date Rec.	
A	B	C	D	E	F	G	H	I	J	K	L	M	N	O	P	Q	R

Every month, IAS publishes three spreadsheets to help investors compare the current status of recommended stocks. The three reports are:

- **Symbol Sort**
- **Total Return Sort**
- **P/E Ratio Sort**

The data contained in each spreadsheet is the same; the only difference is the order in which the companies appear.

**A** The first column is **Quality**. Each company is assigned a quality ranking from 1 to 5, with 1 being the most favorable. These rankings are determined as a combination of factors including the stocks' S&P rating and the Financial Strength and Earnings Predictability figures assigned by Value Line plus our own judgment.

**B C** The company **Symbol** and **Name** are self-explanatory.

**D** The date on which the data was prepared is provided near the Price column.

**E** **Price** reflects the closing price of the stock on the date the report was prepared.

**F** **Dividend** is the current annualized dividend rate.

**G** Dividing the dividend rate by the price provides the **% Yield**.

**H** **Est. EPS** is our earnings per share estimate for approximately twelve months into the future. For example, a report generated late in the year will use an earnings forecast for the following year.

**I** The **Total Return** column is the potential return if the stock is bought at the indicated price, achieves the growth that is projected and sells at its high P/E ratio in five years. The total return figure includes dividends over the next five years. Above average total returns are what we aim for as investors, so this may be the most important column. Keep in mind that aiming for the highest returns usually means taking on more risk.

**J** One of the driving factors behind expected stock price appreciation is earnings growth. We outline the rationale for our earnings growth projections ("**% Gr.**" on the spreadsheets) in the full write-up that accompanies each stock recommendation.

**K** Another factor that drives stock prices is valuation or P/E Ratio. We calculate the **Current P/E** by dividing the most recent stock price by the earnings per share estimate (**Est. EPS**) approximately twelve months into the future.

**L** Relative Value or "**RV**" is the current P/E compared to our judgment of the average P/E in the past. A relative value less than 100 suggests that the stock is trading at a lower P/E than in the past. This means the stock is cheaper than its historical average and can present a profit opportunity if it returns to its typical higher P/E ratio.

**M** The **Buy Up to** price for a stock is a price at which the relative value is 100% or less and the upside/downside ratio is at least 3 to 1. At or below the Buy Price, the stock has favorable risk-reward characteristics.

**N** If the current price is less than the buy price, a “B” appears in the **BUY** column.

**Note:** *The presence of a “B” in the buy column does not automatically mean that the stock is a buy.* It is important to read our most recent comments about a given stock in the “News of Companies” commentary of IAS. In the News section, we will discuss our recent assessment of the company and may provide some guidance as to whether or not we still consider the stock a buy, or whether we might recommend that profits (if any) be taken. There are circumstances when the buy signal can be misleading. Under these circumstances, our recommendations in the News section should be given more weight than the mathematical calculations that drive the buy up to and overvalued at prices on the spreadsheets. The reader should consider the spreadsheet as a screening tool which requires more in-depth analysis in order to form a judgment.

**O** The **Overvalued At** price is a price at which the US/DS ratio is 1 to 1, meaning that the potential gain is no greater than the risk, or when the current P/E ratio has reach the high for that given stock.

**P** In order to be considered a buy, a stock must have an upside/downside ratio, “**US/DS Ratio**,” of at least 3 to 1. This means that the potential gain over the next five years is at least three times our estimated risk of loss. This provides a margin of security for shareholders.

**Q** The column “**P/E as % Growth**” (or PEG ratio) compares the P/E to the expected earnings growth. A PEG ratio of 100% or less is considered extremely favorable. Keep in mind that more consistent, higher quality companies tend to trade at higher PEG ratios and less consistent companies may trade at lower PEG ratios. One should be wary of stocks sporting very low PEG ratios since it may suggest problems ahead. High PEG ratios suggest an investor is “paying up” for growth.

**R** The last column is “**Date Rec.**,” the month and year of the IAS issue when the stock was mostly recently recommended for purchase. This may not be the date that the stock was recommended for the first time in IAS – stocks may be recommended for purchase in subsequent issues as circumstances warrant.

## FREQUENTLY ASKED QUESTIONS ABOUT *IAS*

### **Q. How do you determine the Quality rating of companies?**

A. We base our Quality ratings on Standard & Poor's ratings as published in their S&P Stock Guides for a company. We convert S&P's letter ratings to numerical values, where one is the highest and five is the worst. However, we do not always accept the S&P rating and sometimes use our own judgment to alter it for *IAS*. Unlike Value Line, which is a forced ranking, the *IAS* Quality ratings are a definitive value determined using judgment. In the monthly *IAS* spreadsheet company sorts, the QUAL column stands for "quality."

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### **Q. Why are the buy and sell prices of stocks on the company sort pages different from the prices when the company was originally recommended?**

A. We reevaluate each stock on a monthly basis, and determine new "Buy Up to" and "Overvalued at" prices based on those analyses. In addition, the spreadsheets calculate a five-year potential high price slightly differently than the SSG, using analysts' estimated earnings for the next twelve months and then adding 4 years of the indicated growth rate. The objective is to reach a more accurate EPS figure on which to base the projected high price.

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### **Q. Do print and online subscribers receive different information?**

A. No. The online version of *IAS* contains exactly the same content as the printed version. Print subscribers may also read the online version on the publication date so that all subscribers can have access to each issue at the same time.

All subscribers receive occasional e-mailed alerts and updates in between monthly issues as they are generated by *IAS*.

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### **Q. How have *IAS*' recommendations performed over time?**

A. Hulbert's Financial Digest, which is generally accepted as the canonical source of information on investing newsletters, has tracked *IAS* since January 1, 1996. As tracked by the Hulbert Financial Digest, *IAS* turned in a fifth consecutive year of market-beating performance for 2004, besting the Wilshire 5000's 12.6% return with our a 14.1% performance. An investor following the newsletter's picks for the five years ending since January 31, 2005 could have earned a return of 79.8% on his or her investment (a 12.4% annual return), compared to a loss of 5.5% of the Wilshire 5000 Index (a -1.1% annual return) during the same period.

The *IAS*'s longer-term performance has also been exemplary. In the nine years ending January 31, 2005, the *IAS* gained 14.1% a year, compared to 9.1% for the Wilshire 5000.

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### **Q. How do you use analyst earnings estimates in making your recommendations?**

A. Using the Stock Selection Guide, we apply our own judgment to determine a long-term earnings per share growth rate. However, we do incorporate the EPS estimates of analysts in our own research, particularly in the spreadsheet sorts in each issue, to determine the potential high price of a stock in five years.

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**Q. What is the Stock Selection Guide?**

A. The Stock Selection Guide (SSG) is a tool developed by BetterInvesting for analyzing growth stocks. *IAS*' investment approach is grounded in BetterInvesting's methodology, and every Buy recommendation made by *IAS* is based on conclusions reached with the aid of the SSG. For more information on BetterInvesting and the SSG, visit <http://www.betterinvesting.org/>.

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**Q. When a "B" appears in the Buy column on the company sort pages, should I automatically buy that stock? Likewise, if the stock is above the "Overvalued At" price, does that mean selling is recommended?**

A. The spreadsheet does **not** contain recommendations to buy and sell. The recommendations to buy are contained in the three monthly recommendations. The infrequently rendered sell recommendations are published in the News of the Companies section. The spreadsheet sort pages are designed as mathematical renditions of the SSG for purposes of screening and bring to attention undervalued, fairly valued, and overvalued stocks. Just because a "B" is listed it does not mean "buy," however. It merely means the math suggests an investigation. Your further research will determine the final judgment. If a stock is above its "Overvalued At" price, it means the stock is overpriced and further investigation, along with use of your best judgment, should be made.

Comments in the News of Companies section will give further insight into our thinking.

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**Q. Some of the judgment values used in your analyses (such as projected E/S growth rates and P/E ratios) seem to be much higher than BetterInvesting's guidelines. Why?**

A. The SSG and other BetterInvesting tools are very valuable for those who seek to learn about investing so as to be able to provide for their future financial security. There are various levels of understanding of these tools among BetterInvesting members.

The authors of *IAS* are all *very experienced professional security analysts who have earned the designation of Chartered Financial Analysts, or CFA*. We utilize this experience in conjunction with BetterInvesting principles to produce *IAS*. We do not restrict ourselves to methods and techniques that are suitable for those who seek to learn and are still in the learning process. We attempt to provide the best advice of which we are capable. In this process, from time to time, we may stray from what BetterInvesting might seek to teach the less experienced investor.

This is not meant to denigrate BetterInvesting methods, as everyone must start the learning process somewhere. The record of those who learn and use BetterInvesting tools is excellent. Many seek to go beyond the methods taught by BetterInvesting. That is one of the techniques used by the authors of *IAS*.

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