



### July 2007

In this newsletter, I will articulate each investment that I hold for my clients. Since clients come on at different times, some will hold investments that others do not. Also, clients have different risk tolerances and investment needs.

First, I would like to discuss two areas that I believe will be profitable for clients. It falls within my focus of looking for undervalued companies and rapidly growing areas.

The first focus is activist situations. These are stocks of companies in which people like Carl Icahn get involved. The activists come in and make changes such as: cutting executive pay, forcing the sale of a division, increasing dividends, or decreasing the use of corporate jets. We will invest in these companies and hope for a sharp rise in a short time frame.

The second focus is on established companies doing business in emerging markets. The great demographer, Harry Dent, has pointed out that peak working years coincide with rises in GDP and the stock market. This explains the strong stock market that has risen along with the Baby Boom. Unfortunately, many of these Baby Boomers are retiring. Even as many have to work into their seventies to support themselves, it won't mitigate the losses from the other retiring Boomers.

Wharton professor Jeremy Siegel points out that developing markets' demographics will be juxtaposed to America's aging work force (along with Europe and Japan). Seigel believes that China and India will begin to buy our stocks and divisions of companies as their economies grow and ours matures. As our work force ages, China's and India's will be in the prime years of production. I agree that they will buy our assets but I do not believe that it will dampen the affects of a slowing economy.

The challenge is that it is difficult to invest directly into these economies. The best way to invest is in companies headquartered in developed countries with an established history of doing business in emerging markets. A great example is English firms that were in Hong Kong prior to the Chinese taking possession. The British have been doing business in China and Hong Kong for hundreds of years. As China grows, we will invest in firms that have been there for a long time and are that are run by Westerners. Examples are Jardine Matheson, Swire Pacific, and Standard Chartered. All of these companies get their lion's share of revenues from Hong Kong and China and have good accounting. Furthermore, they have been in business for many years and have an established track record of being friendly to shareholders.

## Investments

The first investment is **Toyota Industries**. TYIDF.PK owns 5% of the outstanding stock of Toyota Motors. It makes forklifts and auto parts. At one point in time, the company was worth more broken up than what the stock was trading. I plan on holding this investment for a long time. Toyota has a strong presence on every continent and does well in emerging markets.

**Mercury General** pays a 3.8% dividend and is rapidly spreading across the U.S. It has some of the strictest underwriting of all insurers. Insurers are good defensive stocks. People must pay their auto insurance or cannot drive. This is a long term hold.

**American Safety Insurance** is a vastly undervalued hazardous materials and construction insurer. We may sell this when the market realizes its worth because management has been issuing too many shares. Additional shares dilute our stake in the company.

**Apache Oil** is another undervalued company. Oil has already risen since we bought this stock. If and when this stock's price responds to the rise in oil, we will take profits.

**Pogo Oil** is another oil explorer. The hedge fund Third Point took an activist position and forced on two board members. Already, PPP has announced that it is selling an oil field. Hopefully, the stock price will respond.

Supermarket chain **Tesco** was originally purchased when I found out that Berkshire Hathaway had bought shares. I was hoping that the market would realize this and force the stock upwards. It did. However, I have decided that it is a long term hold. TSCDY.PK is coming into America and has a strong presence in developing markets. Furthermore, it has a nice dividend yield.

**IDT** is an undervalued company. It has about \$8 in cash per share and trades at about \$10 a share. Though its telephone calling card division is losing money, if the company were broken up, it would be worth substantially more than \$10 a share. It also began paying a 4.8% dividend yield.

Stereo speaker manufacturer **Audiovox**, like IDT, has a hoard of cash on its balance sheets. At \$14 per share, half of the company's worth is cash in the bank.

**State Auto** is a Midwest insurer with a high return on equity and good underwriting. It is a long term hold and has room to grow.

Home furnisher **Pier One** has been a dog but turned around when activists began buying shares. An activist investor forced on the proxy ballot a "pay for performance" measure for a shareholder vote. We might sell when the stock reaches \$10.

**Finish Line** shoes was thought of as a long term hold until recently. It had no debt and was building stores rapidly. Unfortunately, FINL decided to buy retailer

Gennesco. We will sell when the market digests the bad news and (if) the stock rises.

**CIT Group** issues corporate loans, leases, and student loans. The stock was doing fine until investors began to fear that CIT might be part of a leveraged buy out. Management may offer a price lower than what investors expect. We will continue to hold this company.

**KBW Insurance Trust** is an exchange traded fund holding twenty-five of the largest insurers in the country. This is what is called a placeholder. Rather than sit in cash, I would rather the money be invested in a broad range of stocks. A larger proportion of assets is invested in KIE.

#### **New Investments**

We sold our shares in **Helen of Troy**. HELE makes Old Spice, Brut, and women's hair curlers. Basically, I decided that I did not want to be in a company whose biggest customers, Wal-Mart and Target, could cancel at any time. Some clients broke even and some made close to a 50% profit. It depended on when the client opened his/her account.

We took the proceeds and bought **4 Kids Entertainment**. KDE produces a four hour block of cartoons for Fox on Saturday mornings. KDE makes trading cards for children based upon the cartoons. The company has no debt, trades at \$15, and has almost \$9 a share worth of cash. We will hope that they will have an-

other success and the stock will respond.

**Jardine Matheson** is a holding company with extensive ties to the Asian markets. It trades at \$24.45 and is denominated in dollars. Founded in the 1830s by two fellows trading opium to China for tea to Britain, Jardine is probably the best way to invest in a blue chip company doing business in the Orient. Jardine and its subsidiaries are involved in the following: the five-star hotel Mandarin Oriental, auto dealerships in China, office buildings in Hong Kong, supermarkets in Malaysia, auto manufacturing partnerships with the likes of Honda and Toyota, restaurants, finance, and construction. We hope to hold this company for a long time and participate in China's growth.

#### **Third Avenue Value**

TAVFX is a mutual fund that has done quite well for clients. As of this newsletter, the most profitable client in this fund has made 60% since April 2004. The profits vary depending on when clients opened accounts. This is our go-to fund for clients.

#### **Fidelity Money Market**

The good old money market is paying close to 5%. Any money not invested is earning this. There are no minimums to be in the money market. I noticed that Ameritrade pays their clients almost nothing for small amounts. Other discounters do this too. This tactic is how discount brokers make their profits—on the money market, not the trades.

## Experience for Holmes Osborne, CFA

Holmes Osborne began his career as a financial consultant for Merrill Lynch Private Client Group in Naples, Florida. At Merrill Lynch Mr. Osborne assisted clients in asset management and estate planning. After Naples, Mr. Osborne managed trust portfolios for Merrill Lynch Trust Company (a division of Merrill Lynch's mutual fund division) in Boca Raton, Florida. The trust department managed over \$1 billion in clients' assets. Upon leaving Florida, Mr. Osborne worked in management for Farmers Insurance Group in Los Angeles, California.

Mr. Osborne has a degree in finance from the Martin J. Whitman School of Management at Syracuse University. He is a member of the CFA Society and holder of the Chartered Financial Analyst designation. Mr. Osborne is also a member of the Los Angeles Venture Capital Association, Malibu Rotary, and on the board of the LA National Association of Business Economists.

## *Fidelity Investments*

<http://www.fidelityinvestments.com>

Clients' assets are held in custody at Fidelity Investments. At Fidelity, clients may have online access and will receive monthly statements.

All clients' information is kept in the strictest confidence. Mr. Osborne can be reached at 310-452-0910.

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