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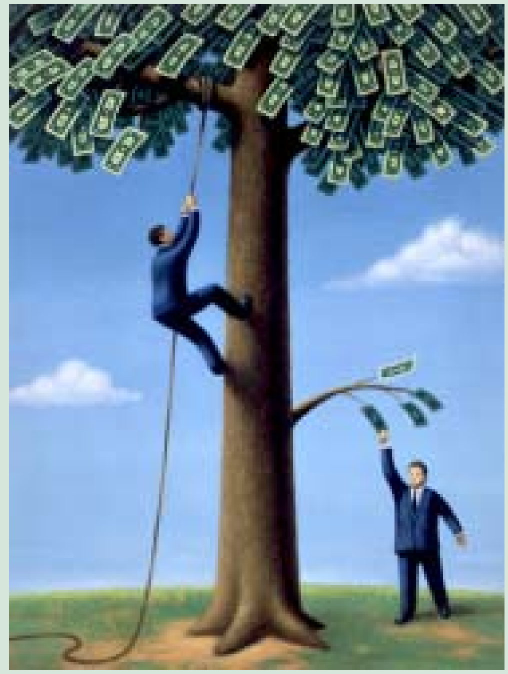

RISK PART 2

JUNE 25, 2007

In our last newsletter we examined the role of risk in your portfolio. I described how Andresen & Associates has attempted to manage the risk in your portfolio via diversification through a uniquely large spectrum of investment choices.

Specifically, we examined the past. This time let's examine the present and the future. *Our contention is that as the 2000 stock market decline has receded from memory, investors have become more and more tolerant of risk.* Investors have become complacent, and this is not a good thing. When our financial climate changes, as it appears to be doing, investors will face more risk than they expect. Normally, in such a situation, investors panic.

The graph on the opposite page is a scatterplot containing a few of our core mutual funds so you can see the relative risk of what we've normally chosen in the past. Each dot represents a mutual fund.

As before, the horizontal axis is **risk**, represented by standard deviation. This is a measure of raw volatility, not correlated risk. In other words, by this measure an investment may go up and down, but it may do so in concert with others or alone. The more an investment is located to the right, the more risk it has had in past years.

The vertical axis represents **reward**. The higher an investment is located on the graph, the greater its rewards have been in the past.

Obviously the perfect investment would be in the upper left corner of the graph. A bad investment would be positioned in the lower right.

This graph also depicts some of today's most popular picks: Real Estate, Latin America, and China. Investors have been showering these sectors with money recently. As you can see, they have done so while ignoring the innate volatility of their choices.

As they did with tech in the late 1990's, investors do this when they become more greedy than fearful. This is an indicator that the average investor is riding a bubble of enthusiasm and is now addicted to the narcotic fantasy of easy money. If you ask the average investor what will happen in these three sectors, they will reply with the well-worn mantra that "This Time Is Different".

This time may well be different. Perhaps Latin America and China have finally broken the chains of corruption and poverty. But meanwhile, their stock markets are overvalued. The railroads in 1880's United States demonstrated this illogical reality. The new technology of rail transportation revolutionized the world, but the sector's high-flying stocks routinely collapsed. Therefore, it is quite possible to advance genuine change in the world, but stock valuations will eventually seek a level of common sense. Positive economic or social change does not ensure a good market. Attractive valuations are the everlasting requirement for a financial market to retain current prices and to increase in value.

Consider what this tells us about the average investor. Here we go again. If not Latin America and China, the average investor will seek something else to chase until it blows up in his or her face. And when I talk about the "average investor", obviously I include Wall Street and the hedge funds. We're all human.

Now we have an investing environment replete with relatively complacent investors. And here comes the storm. Well, maybe. Actually we are facing a lot of unusually contradictory data at present. I will discuss this in greater detail in our upcoming Quarterly Review.

10 YEAR RISK/REWARD SCATTERPLOT

10 Year Risk/Reward Scatterplot

	10 Yr Standard Deviation	10 Yr Mean
Benchmark: S&P 500 TR	15.09	7.78
Fund/Stock:	--	--