ValueWorks
quality assets. compelling valuations.

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A Return to Returns

With little fanfare, the markets this year are providing fair to modest returns. Year-to-date the indexes are up 8.5% for the S&P, 10.8% for the Dow, and 2.9% for the Nasdaq. For the quarter, the returns of those indexes were more uniform at 5.6%, 5.3% and 4.1%. The disparity in the quarter was more between large-cap and small-cap than anything else. Smaller companies performed much less well. Specifically, the Russell 2000 small cap index rose 0.4%.

The ValueWorks Capital Appreciation group is up 10.6% so far this year with a return for the quarter of 3.6%.* Overall, I believe we are on sound footing to earn solid returns over the next several years.

The market and economy are clearly both in periods of transition. Economically, we have moved into the mid-stage of a classic economic recovery. Earlier low interest rates brought the economy out of recession. This year rates were raised to the level required to keep the economy from overheating. The very predictable and expected impact of a slowing in the most cyclical/interest rate sensitive areas of the economy has occurred. Home construction starts have slowed, residential real estate is clearly cooling, and auto sales continue to moderate. We have also begun to see the first important declines in commodity prices. As a result, the economy appears to be expanding at something close to a 2.5% annual rate – not too fast and not too slow.

ValueWorks' Top 10 holdings:**

1. Wachovia Corp
2. Pfizer Inc
3. Bausch & Lomb
4. Sun Micro
5. Boeing Company
6. Walt Disney
7. Cypress Semi
8. General Motors
9. Rowan Companies
10. Schering-Plough

—as of 9/30/06—

**see notes on p4 for additional information

The question now is whether this slowing becomes a contraction, or if increased economic activity in other areas offsets the weakness in housing and autos, etc. Over the past six-eight weeks, the equity markets seem to be reflecting an anticipation of continued growth spurred on by the positive implications of lower oil/energy prices. I could see this as the beginning of a longer trend, not just of lower energy prices but lower commodity prices overall. Such a development would offer the twin benefit of higher purchasing power for consumers and lower inflationary pressures for policy makers. While a downward trend in energy and commodity prices would have a negative impact on profit margins for companies operating in those fields, it would have a positive impact on the profit margins of all the companies that use those commodities. That could well extend the market advance that began in late July (just as energy prices peaked).

Over time, I unequivocally expect declines in commodity prices given the high levels of profitability associated with current levels. The question is of course whether this decline happens sooner rather than later, and what happens to overall price levels until then.

*All ValueWorks' figures are Gross of Fees. For additional information on returns, including net performance, see page 4.

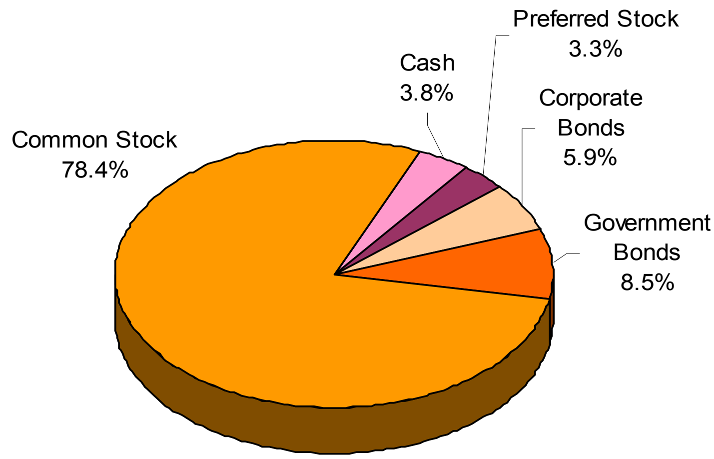
My view of the situation is relatively positive; near-term high commodity prices would most likely be driven by tight supply and demand. As supply is increasing given the aggressive pace of capital investment, end markets will remain tight only to the extent that demand continues to grow. And increasing demand for energy and basic commodities is pretty axiomatically tied to economic growth. So long as that remains true, I would expect to see the economic cycle stretch-out, driven in the near-term by increased capital investment in commodity areas.

Conversely, the recent weakness we have seen in energy/commodity prices may represent an economy that is no longer growing faster than its ability to expand commodity outputs. If so, the recent pull-back in energy/commodity prices may well be the beginning of a long-term decline. That would have benefits for financial companies and consumer product companies, and of course consumers generally. The market action since mid-July is quite consistent with this interpretation, given that those sectors have provided market leadership as energy prices have declined. If this continues to play out, the positive implications for the economy and the financial markets could be prove quite significant and long-lived. This would make sense to me given the time that has passed since the last period of market enthusiasm.

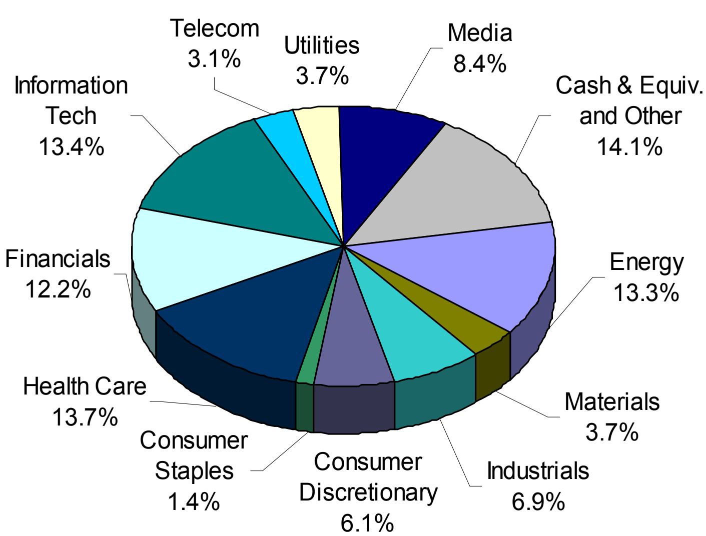
In positioning portfolios, we will nevertheless continue to hedge our bets. Prudence dictates that our goal is not to be the most right in any given period, but rather to avoid significant downside in the inevitable instance of being out-of sync with a particular market trend.

—Charles Lemonides, CFA

Asset Class Diversification-- Balanced Composite*



Sector Diversification-- Capital Appreciation Composite*



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Pie chart information updated through 6/30/2006.

ValueWorks
critical thinking. independent research.

Defining our Philosophy:
At ValueWorks we define value investing as buying the best-quality assets at the best possible prices. We like to think of ourselves as bargain hunters: it is our goal to pay only $0.50 to $0.75 for $1.00 worth of assets. We evaluate the component parts of a company, assigning each of its assets a dollar value that, when added together, comprises the underlying value of the company; if this is higher than the company's stock price, we consider it an investment opportunity.

Defining our Process:
1) Identification. We monitor the financial markets to identify securities that match our investment criteria—focusing on opportunities that appear misunderstood by the general market.

2) Appraisal. First we identify the assets; then we appraise them. This allows us to determine the company's *underlying value*. We then decide whether the assets are of high quality and therefore likely to appreciate over time.

3) Assessment. Here we assess any claims against a company's assets; we then compare the market price of the claims to the company's *underlying value*. If a particular security trades at a discount, we identify factors that could eliminate the valuation gap and increase its price. We then make a decision on the purchase of the security.

4) Re-Evaluation. We continuously monitor our positions to determine if our original investment thesis still applies, taking necessary action to optimize our portfolio.

5) Exit. We exit a position when a security either reaches full valuation or changes in its outlook invalidate part of our original thesis.

Our objective is uncomplicated, but achieving it requires a high level of research, expertise, discipline and independent judgment. By applying this framework consistently we remove emotion from the investment decision making process, enabling us to capitalize on inefficiencies built into the market.

About our Portfolio Structure:
We believe risk can be better contained through educated security selection than through overdiversification. Consequently, our position sizes range between 3 – 5 % of the overall portfolio value. Fully invested portfolios tend to hold 25 – 35 individual investments.

We enter investments that we view as 25 – 50% undervalued and sell them when we see them as fairly priced. Our anticipated holding period tends to be one to two years which results in only modest portfolio turnover.

Because our decisions are based on research and sound fundamentals we view depressed price action on our securities as buying opportunities rather than sell signals.

We use senior debt and preferred instruments—offerings that can be easily misunderstood by traditional equity or fixed income investors—to gain equity type returns on safer vehicles.

About our Client Services:
ValueWorks provides independent investment management on an individual account basis. Our clients receive the benefits of owning securities directly, coupled with the advantages of having a dedicated portfolio manager.

Working directly with your financial consultant, we evaluate your investment profile and build a plan designed to meet your specific goals.

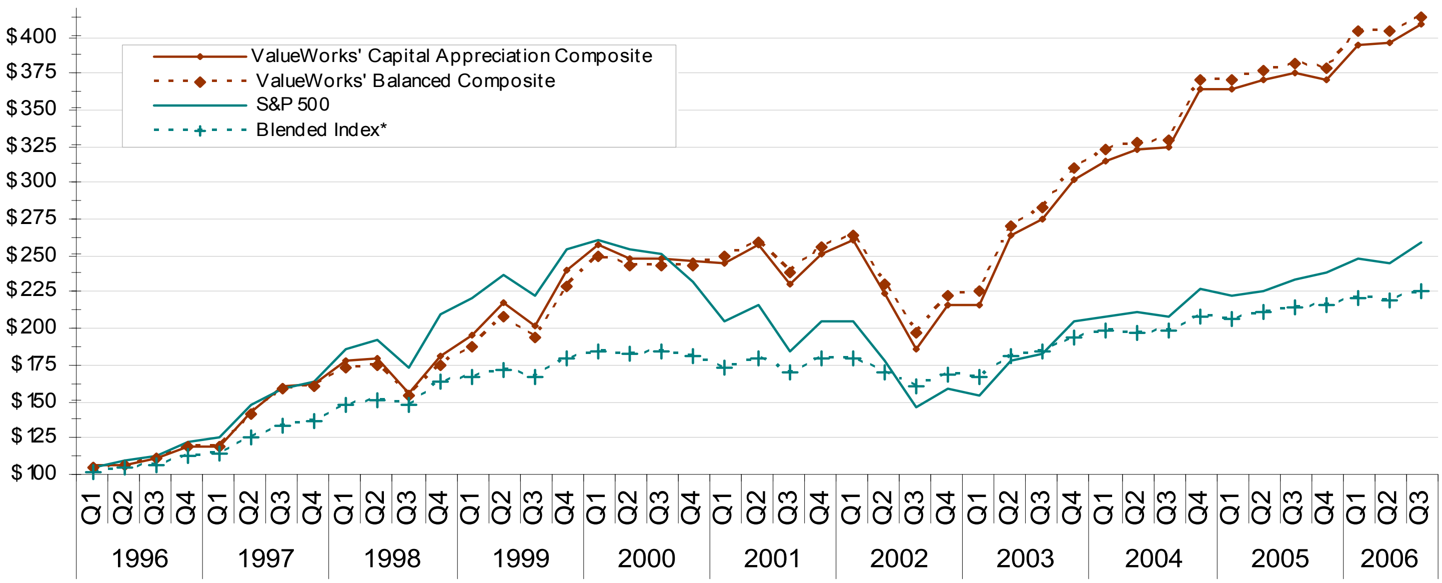
As a high-end investment alternative, you receive:
- Individual review of your portfolio requirements
- A separately tailored portfolio created and maintained to your investment objectives and risk tolerance
- Access to the Portfolio Manager on an ongoing basis with timely and responsive communication
- Flexibility to meet your changing tax requirements and investment needs Comprehensive quarterly performance reports.

Working within the framework of our value investment discipline, we build portfolios that cover a wide spectrum of risk-tolerance, from aggressive to much more conservative and income oriented.

ValueWorks Performance Review

3rd Quarter: June 30th—September 30th, 2006

Historical Growth of $100 (gross of fees)



Trailing Performance Data

	ValueWorks' Capital Appreciation Composite			ValueWorks' Balanced Composite		
	Gross of fees	Net of Fees	S&P 500	Gross of fees	Net of Fees	Blended index*
10 year	13.91	12.16	8.60	14.04	12.16	7.74
7 year	10.66	9.10	2.22	11.43	9.65	4.35
5 year	12.13	10.58	6.99	11.67	9.95	5.79
3 year	14.10	12.57	12.31	13.41	11.81	7.02
1 year	9.18	7.72	10.78	8.23	6.62	5.22
2006 YTD	10.56	9.48	8.52	9.09	7.87	3.83

*The "Blended Index" is a calculation comprised of 50% S&P 500 and 50% Merrill Lynch Domestic Master Bond Index.

The above benchmark indices are unmanaged indices. The benchmark performance numbers reflect the reinvestment of dividends and interest but do not reflect the deduction of any fees or expenses. ValueWorks' value investing style is not limited to the securities in any of the above indices and utilizes specific investment techniques which are not utilized in the above indices and which may or may not increase volatility. Returns include all dividends, interest, accrued interest and other cash flows received as they may result from the implementation of a particular investment strategy. Trade date accounting has been used. Results for the full period are time weighted. Accounts are included in composite at the start of the first full period under management. From 1996—Q1 1998 exiting accounts are included through the period in which they left. Starting in Q2 1998 exiting accounts are included through the last full period under management. Results were generated at other firms prior to 9/30/01. Information on other composites is available on request.

As of 9/30/2006 the Capital Appreciation Composite consisted of 437 accounts and $141,492,953 in assets; while the Balanced Composite consisted of 111 accounts and $68,584,847 in assets. Together this represents 99.46% of total accounts and 87.82% of total assets.

Past performance is not a guarantee of future results.