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ValueWorks

quality assets. compelling valuations.

Volume 8,2 **Q2 2010**

After a massive advance from March of 2009, the equity markets backed off in the second quarter. The S&P 500 pulled back -11.4% in the quarter, and is now nearly 57% above its trough 15 months ago. The numbers for the Dow & Nasdaq respectively are declines of -9.2% and -11.6% for the quarter and advances of almost 50% and 70% from their low points in 2009.

The framework through which I put this in context is the following: first, the economy is in better shape today than it was a month ago, three months ago, six months ago, or eighteen months ago. There has been a clear and inarguable increase in economic output, despite the fact that the pace of improvement has been uneven. Second, there remains plenty of room for more improvement. Third, it appears more-likely-than-not that the policies that have allowed for recovery (specifically stimulative monetary and fiscal policy) will remain in place to drive further growth.

Still, market advances are never steady. The advance from March 2009 has already been interrupted by a several sharp declines – the latest being the deepest. Such declines are inevitably occasioned by real world challenges and real risks. Surely, poor economic policy could derail this recovery. We note that the stagflation of the late 1970's occurred as the governments of all the major economies adapted fiscally restrictive austerity programs. The discussions from Europe and, to a lesser degree, in the US, are starting to sound a bit too familiar, and represent a warning sign. (The global malaise of the '70's was eventually broken when – with Ronald Reagan President and Paul Volcker at the Fed -- the US combined high interest rates with massive fiscal stimulus.)

That said, the slow pace of the recovery and very low employment levels at very least argue that the Fed's policy of very low interest rates will be in place for an extended period. Further, while there is talk of cutting back government deficits and government spending, we do not see those plans having an impact on the ground in the economy within the next twelve months, by which time conditions could be quite different.

In short, I consider the biggest risk to the nascent recovery to be that monetary and

Top 10 holdings*:

1. Calpine Corporation
2. Micron Technology
3. Corning Inc
4. 3M Company
5. Boeing Company
6. Cisco Systems Inc
7. WellsFargo PFD Series L
8. Williams Companies
9. Hewlett-Packard Co
10. Zimmer Holdings

—as of 6/30/10—

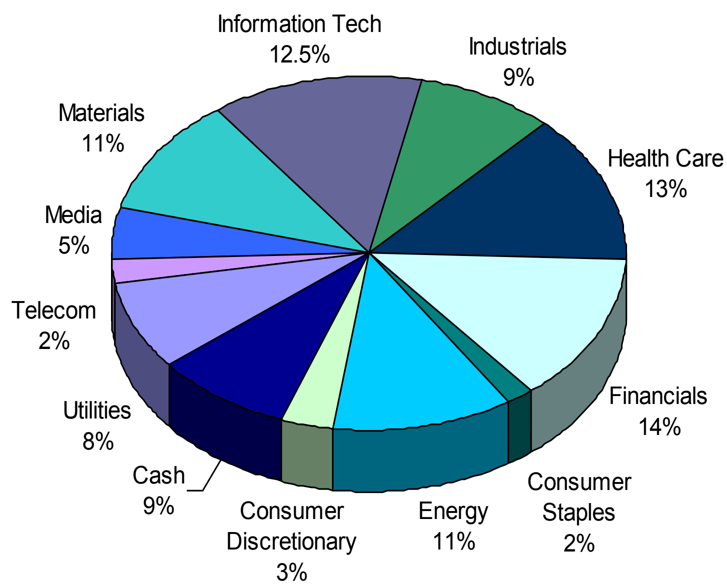
*see notes on p4 for additional Information fiscal stimulus are withdrawn too early. Clearly there is an active debate about the effectiveness and appropriateness of those policies – especially fiscal stimulus/deficit spending. But a valid criticism of those policies requires providing an alternative explanation for why the economy transitioned from meltdown to its current state of growth (however stop-start and herky-jerky that growth might be). I believe in the effectiveness of stimulative tools because they provide the only logically consistent explanation I can find for the economy's going from dramatic contraction to sluggish growth.

Beyond our expectation of economic improvement, the confidence in our investment posture is grounded in the compelling prices we are paying to control valuable business franchises. After a decade of stagnant markets, company valuations have become increasingly discounted from one market trough to the next. Consistent with this perspective, the opportunity and expected returns have simply expanded as the process has worn on. In this latest market swoon we added exposure to both Corning Inc. and Live Nation Entertainment, having recently pealed back some exposure that had run its course.

If history is a guide, those who are well-committed at the end of this period of stagnation will be those investors positioned to earn the hearty returns offered in the next economic cycle.

— Charles Lemonides, CFA

Sector Diversification--
Capital Appreciation Composite



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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:

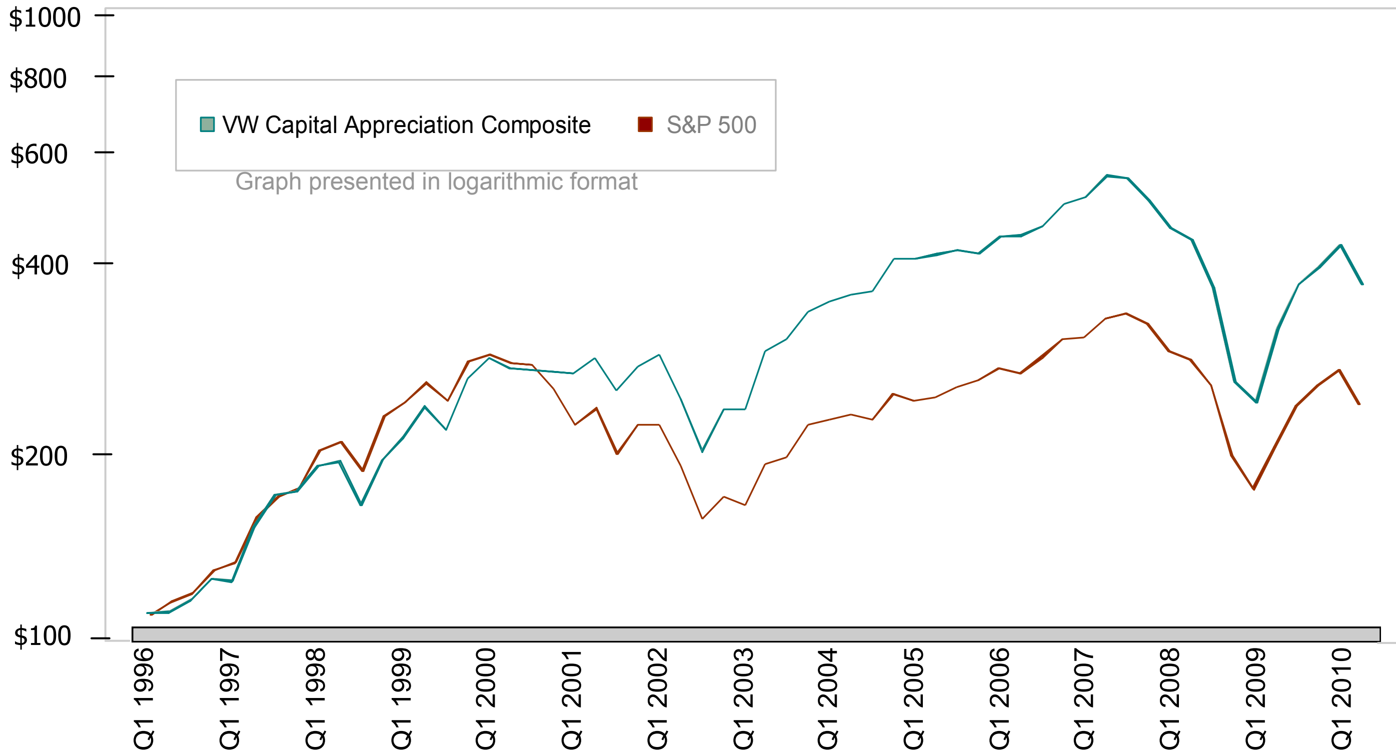
- Individual review of your portfolio requirements
- A separately tailored portfolio created and maintained to your investment objectives and risk tolerance
- Access to the Portfolio Manager on an ongoing basis with timely and responsive communication
- Flexibility to meet your changing tax requirements 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

2nd Quarter: March 31st, 2010 -- June 30th, 2010

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*
YTD	-5.74	-6.40	-6.67	-4.49	-5.19	-0.53
1 year	16.29	14.72	15.86	17.22	15.52	13.04
5 year	-2.10	-3.43	-0.55	0.40	-1.10	3.01
7 year	3.38	1.96	2.64	5.19	3.62	4.26
10 year	2.96	1.53	-1.46	4.59	2.95	3.02

*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 avail-

As of 6/30/2010 the Capital Appreciation Composite consisted of 231 accounts and $70,208,946 in assets; while the Balanced Composite consisted of 76 accounts and $33,313,375 in assets. Together this represents 99.03% of total accounts and 72.80% of total assets.

Past performance is not a guarantee of future results.

CAPITAL APPRECIATION COMPOSITE

	Total Firm	Composite Assets		Annual Performance Results			
Year End	Assets (in Millions)	USD (in Millions)	Number of Accounts	Composite: Gross	Composite: Net	S&P 500	Composite Dispersion
2009	152	78	241	48.83%	46.92%	28.06%	7.86%
2008	112	58	311	-47.02%	-47.74%	-36.96%	8.58%
2007	295	178	515	1.50%	0.15%	5.49%	5.93%
2006	267	159	411	19.08%	17.44%	15.79%	4.22%
2005	209	119	340	1.81%	0.31%	4.91%	3.73%
2004	165	78	158	20.03%	18.42%	10.88%	4.20%
2003	121	49	93	40.27%	38.25%	28.69%	4.71%
2002	75	33	58	-14.06%	-15.23%	-22.10%	3.53%
2001	85	36	51	2.05%	0.64%	-11.88%	8.31%
2000	80	35	69	2.28%	0.68%	-9.11%	6.64%
1999	81	36	79	32.56%	30.46%	21.04%	15.60%
1998	66	26	78	11.60%	9.68%	28.58%	6.03%
1997	39	9	30	35.65%	32.96%	33.36%	3.84%
1996	26	6	20	19.77%	17.13%	22.96%	4.06%

BALANCED COMPOSITE

	Total Firm	Composite Assets		Annual Performance Results			
Year End	Assets (in Millions)	USD (in Millions)	Number of Accounts	Composite: Gross	Composite: Net	Blended Index	Composite Dispersion
2009	152	38	79	45.64	43.53	16.78%	5.15%
2008	112	33	91	-40.29%	-41.20%	-18.18%	4.82%
2007	295	76	128	4.06%	2.51%	6.45%	3.78%
2006	267	74	113	17.37%	15.61%	9.98%	3.26%
2005	209	65	120	2.29%	0.73%	3.80%	3.29%
2004	165	65	104	19.71%	18.04%	7.70%	4.01%
2003	121	52	84	39.07%	36.86%	16.16%	5.68%
2002	75	33	63	-13.69%	-15.24%	-6.15%	3.52%
2001	85	37	62	4.87%	3.10%	-1.29%	7.36%
2000	80	34	72	6.28%	4.35%	1.02%	5.50%
1999	81	36	73	31.32%	28.89%	9.95%	11.30%
1998	66	37	93	9.13%	7.15%	19.33%	7.63%
1997	39	24	54	34.81%	32.51%	21.18%	4.33%
1996	26	15	29	18.66%	16.54%	12.96%	3.60%

DISCLOSURES

Past performance is not indicative of future results.

Balanced Composite *contains all accounts with a balanced mandate. For comparison purposes the composite is measured against a 50/50 blend of S&P 500 and Merrill Lynch Master Bond Indices. The blended benchmark is calculated on a quarterly basis.*

ValueWorks has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®).

ValueWorks is a separate registered investment adviser. Prior to September 30th, 2001, ValueWorks was a subdivision of M&R Capital. The firm maintains a complete list and description of composites, which is available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results.

The U.S. Dollar is the currency used to express performance. Gross returns are shown as supplemental information and are stated gross of all fees and transaction costs; net returns are reduced by all fees and transaction costs incurred. Wrap accounts pay a fee based on a percentage of assets under management. Other than brokerage commissions this fee includes investment management, portfolio monitoring, consulting services, and in some cases, custodial services. Wrap accounts make up 100% of the composite for all periods shown. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year beginning December 31, 2001. From January 1, 1996 to December 31, 2001 dispersion reflected an equal weighted dispersion. Additional information regarding the policies for calculating and reporting returns is available upon request.

The investment fee schedule for the composite is as follows: Low and high rate for wrap sponsors: 1.25% and 2.75%, respectively. Fee schedules from individual wrap sponsors are available upon request. Actual investment advisory fees incurred by clients may vary.

The Balanced Composite was created December 31, 1995. Performance presented prior to October 1, 2001 occurred while the Portfolio Manager was affiliated with two prior firms and he was the only individual responsible for selecting the securities to buy and sell. ValueWorks' is in compliance with the GIPS standards for the period October 1, 2001 through December 31, 2007. In addition, a performance examination was conducted on the Balanced Composite beginning October 1, 2001.