ValueWorks
quality assets. compelling valuations.

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Volume 8,2 **Q3 2010**

Markets ended the quarter with a powerful rally, making up much of the decline from March and generating modest gains for the year. Specifically, the S&P 500, the Dow Industrials, and the Nasdaq Composite each rose by 11.3%, 11.1% and 12.5%, respectively. That translated to a year-to-date gain for those averages of 3.9%, 5.6%, and 5.1%. As shown in the tables on page 4, our portfolios very much participated in the third quarters' sharp advance; our Capital Appreciation accounts were up 11.3% for the quarter and 4.9% YTD (gross of fees).

One striking feature of the past six months has been the tight range of returns. Day-to-day, week-to-week and month-to-month, it made unusually little difference if you were invested in large companies versus small companies, or growth stocks versus value stocks, etc. Stocks are very much moving as a group, with a distinctly narrow difference between one group of investments and another. In moments of market enthusiasm, stocks have risen as a uniform group. When markets have retreated, shares have declined as a group.

During this back-and-forth window, the effects of easy monetary policy have continued to seep into the real economy. While economic conditions remain challenged, it is clear that the overall economy is growing. It is also clear that some companies are performing better than others. I therefore expect this back-and-forth period to give way to period of positive overall market action and bigger upside moves in some share prices than others.

Top 10 holdings*:

1 Mesabi Trust
2 Corning Inc.
3 Calpine Corp.
4 Rowan Companies Inc.
5 Boeing Company
6 3M Company
7 Cisco Systems Inc.
8 Williams Companies
9 Micron Technology Inc
10 Dow Chemical Company

—as of 9/30/10—

*see notes on p4 for additional Information

The combination of an improving economy and a similarity of returns is extending a trend that has emerged over the past decade. Specifically, more and more of the biggest discounts between share-prices and business-values are being offered in the highest quality, fastest growing companies. This trend is increasingly reflected in our holdings.

Our conviction that monetary policy works has been quite consistent over the years. I've tried to be clear that I see the financial crisis largely in terms of a credit and liquidity cycle. The implosion happened because credit conditions were tightened to reign in the excess of the 2004-2007 period. The tightening was appropriate, but it went too far. It was not reversed in time to allow for a modest correction and soft landing. Instead, the takeover of the GSE's (Freddie & Fannie) and incoherent leadership in September of 2008 set off an all-out panic.

The story of the past two years has been of restoring confidence and liquidity in order to bringing economic activity back to where it was before the panic was unleashed. The heart of that long process is extraordinarily easy monetary policy. We see the economic events of the last quarter as quite consistent with that process continuing to gradually play itself out. The economy is not yet healthy – the damage caused by the panic takes time to heal – but we are continuing to move in the right direction. And we are moving in that direction because monetary policy is working.

But after a sharp run from March 2009 to March 2010, equity markets have see-sawed back and forth. This six month pause makes plenty of sense to me given the feverish pace of the advance. Markets do not go in one direction, and it is virtually inevitable that somewhere along a near doubling of equity prices there would be a pull-back. We view the move down from March as simply that. Interestingly, while the moves from March to now have been quite sharp, they have also been quite broad and indiscriminate. This is consistent with investor emphasis on broad themes and concerns rather than individual corporate developments.

One unusual consequence is that investment returns have really tended towards the average. As noted above, this can be seen in the similar performance of the major averages. Another indication is the performance of the Russell 1000 value index, the Russell 1000 growth index, and the Russell 1000 index whose returns for the last quarter were all in the range of 4.36% to 4.49%. It is also reflected in the tight range of performance between better performing and poorer performing managers. And it is also represented in the high correlation between the daily return of individual shares and the market average (which has been cited in the Wall Street Journal recently as over 0.7 compared to a more typical level of under 0.5).

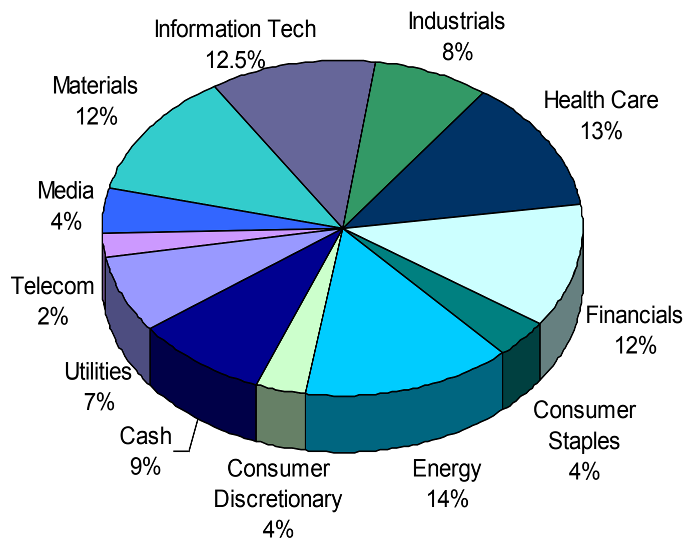
However, corporate developments have not been uniform. Some company's operations are performing better than others. But that outperformance is not being reflected in share prices. This has extended a trend that has emerged over the past decade – specifically, that better quality companies have become increasingly attractively priced. This has now gone so far that we are often finding the biggest disconnect between share prices and business values to be in the highest quality companies whose businesses are performing the best.

It is the stark opposite of what was offered investors ten years ago. We are not sorting through problem companies to uncover hidden gems – we are finding them in plain sight in some of the highest quality businesses. That is an atypical conclusion for a value oriented manager.

This conclusion is very much being reflected in our portfolios. It is a fair characterization for Boeing – who will be delivering its Dreamliner to customers in a matter of months. It is a fair characterization of Corning Inc, Chesapeake Energy, Cisco Systems, and Hewlett Packard. It also fits Eli Lilly and Zimmer Holdings, as well as Pfizer and Boston Scientific. As a result, our portfolios have continued to migrate into higher quality and better valued investments. We consider this to be an exposure that will serve us well over the years ahead.

— 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:

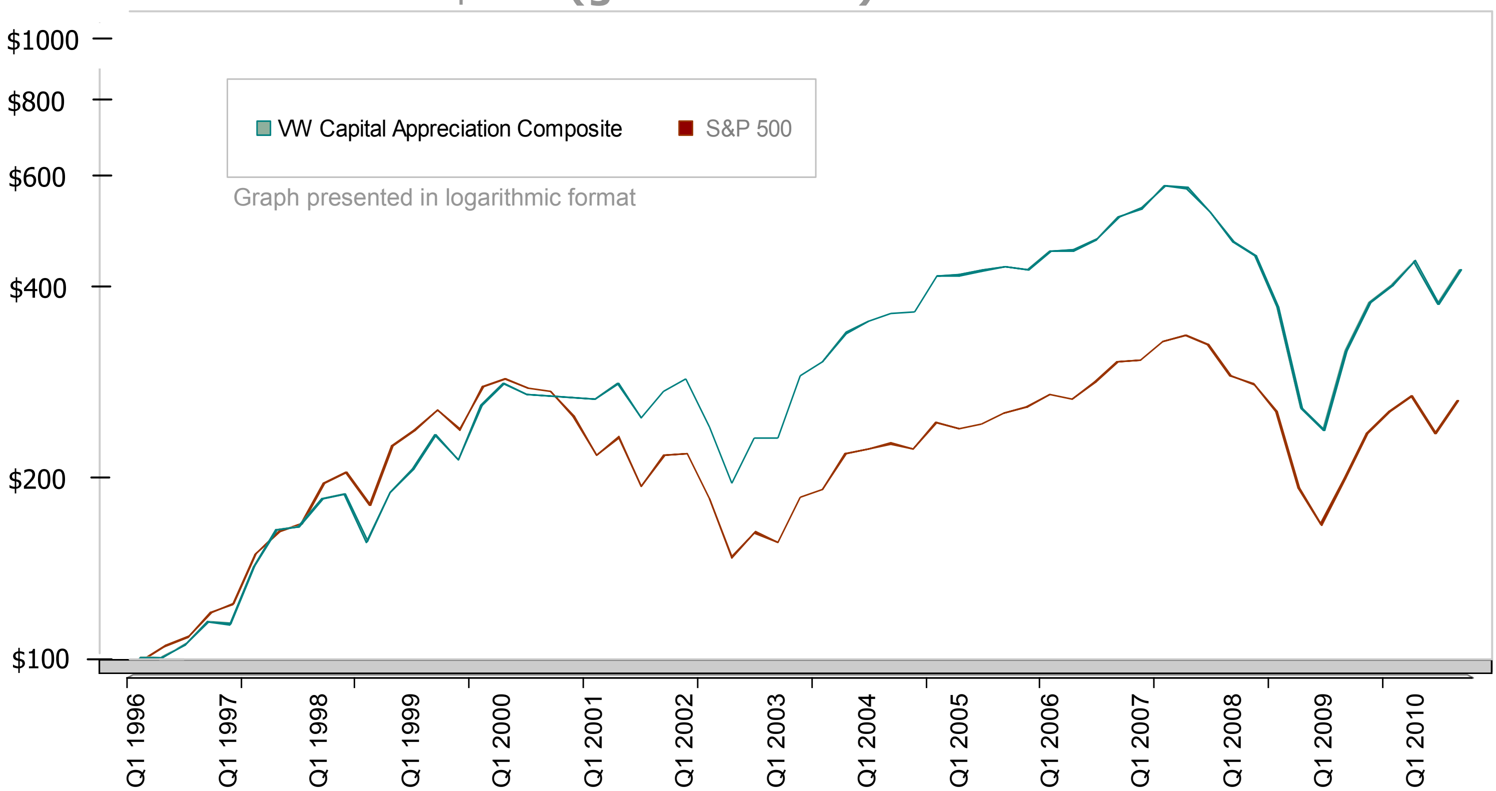
- Individual review of your portfolio requirements
- A separately tailored portfolio created and maintained to your investment objectives and risk tolerance
- Access to the Portfolio Manager on an ongoing basis with timely and responsive communication
- Flexibility to meet your changing tax requirements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

3rd Quarter: June 30th, 2010 -- September 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	4.91	3.84	3.88	5.61	4.46	6.35
1 year	11.16	9.66	11.55	11.50	9.89	10.29
5 year	-0.26	-1.61	0.87	2.16	0.65	4.09
7 year	4.30	2.87	2.52	5.99	4.42	4.36
10 year	4.11	2.66	-0.30	5.64	4.00	3.61
LIFE*	9.29	7.62	6.23	10.25	8.45	6.78

* Life is 14.75 years

*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 9/30/2010 the Capital Appreciation Composite consisted of 227 accounts and $76,029,618 in assets; while the Balanced Composite consisted of 75 accounts and $36,227,135 in assets. Together this represents 99.02% of total accounts and 71.93% of total assets.

Past performance is not a guarantee of future results. This material is approved for client use.

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.