CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

December 15, 2006

The Year Draws to a Close With Robust Portfolio Gains

The sharp rise since Thanksgiving in foreign currencies has given another boost to our portfolios.

The rise in foreign currencies indirectly benefits other Core investments.

As the holidays approach, our investment returns are providing an early present to us all. Let us hope that the fine action now augurs well for 2007.

In the middle of October, the dollar started to fall in relation to foreign currencies. During the week of Thanksgiving, while trading in the US was subdued, the dollar suddenly tumbled in value and the European currencies began to advance very sharply. The euro now stands just a few pennies below its all-time high; the pound sterling has reached its highest levels against the dollar since the early 1990s.

Our portfolios had already been gaining strongly during the autumn; the fall in the dollar's value pushed them higher. Several of our investments benefit, directly or indirectly, as foreign currencies appreciate, including the oil-related and commodity investments. Commodities are generally priced in dollars and as the dollar falls, commodity prices rise. Our large holdings in foreign currency money market funds rise in step with foreign currencies. Non-US stock investments enjoy the benefit of foreign currency appreciation when their values are translated into US dollars.

Although the price of crude oil remains about twenty percent below the highs from the summer, stocks of companies in oil-related businesses are trading well above their summertime levels. We have had substantial investments for three years in oil stocks. During this year, we have added investments in alternative energy companies and water-related businesses, the prospects for which seem quite attractive. International equity markets, those of the developing countries as well as of Japan and Europe, were quite strong again this year.

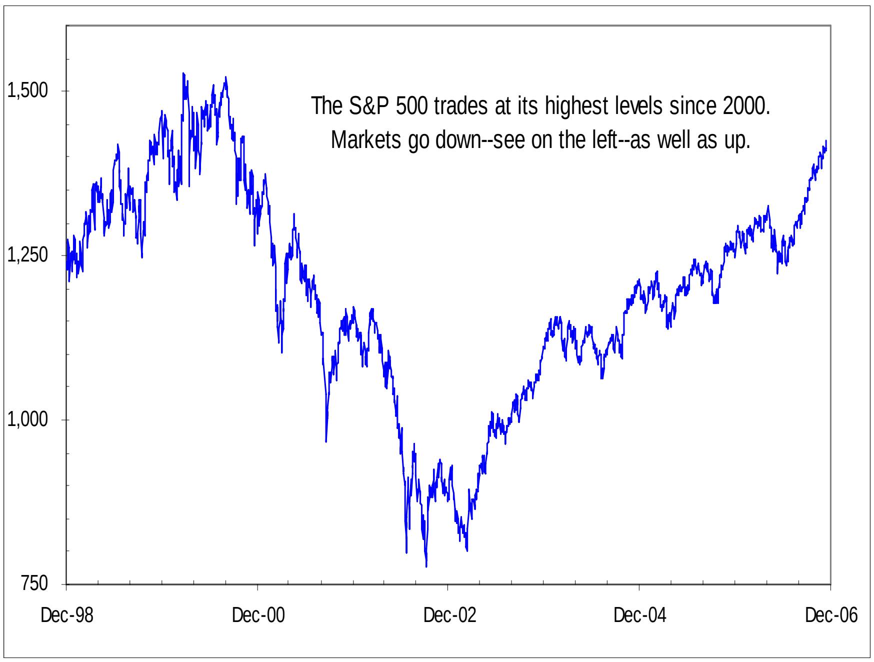
As a consequence of gains in these assets and the continuing rally in US stocks, Core's portfolios have earned very strong returns this autumn. We near the end of another year of good returns, achieved, we believe, with relatively low risk. For example, as the year ends, Core's portfolios in the aggregate hold about 29 percent of your assets in US and foreign currency money market funds. In times like now, when almost all stock markets are strong, it

By:

John N. Mayberry

may seem entirely unnecessary to invest in anything but the risky assets. Why hold money market funds that yield 5 percent per year when stock markets are rising at the rate of 5 percent per quarter? The answer is simple: Stock markets go down as well as up. Since it is impossible to know when the inevitable bear markets will begin, it is sound practice to make investments in assets--like money market funds--that continue to earn money when stocks fall. And money market investments provide a source of investment funds to take advantage of opportunities that arise when stock markets fall. The good outcome is to earn returns in line with the stock markets when they are strong--as we have this year--while keeping a meaningful portion of our capital safe from the investment risks that stocks present.

A personal note of thanks



The opportunity to manage your investments is a great gift from you to me. The investment process is endlessly absorbing and stimulating. It holds enormous interest for me. When one invests well there is a real sense of accomplishment. It is a privilege to be able to work with you and I am very grateful to you for it.

May we all enjoy this season of holidays and may 2007 present a more peaceful aspect to the world than has 2006.

CORE Comments

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CORE Comments

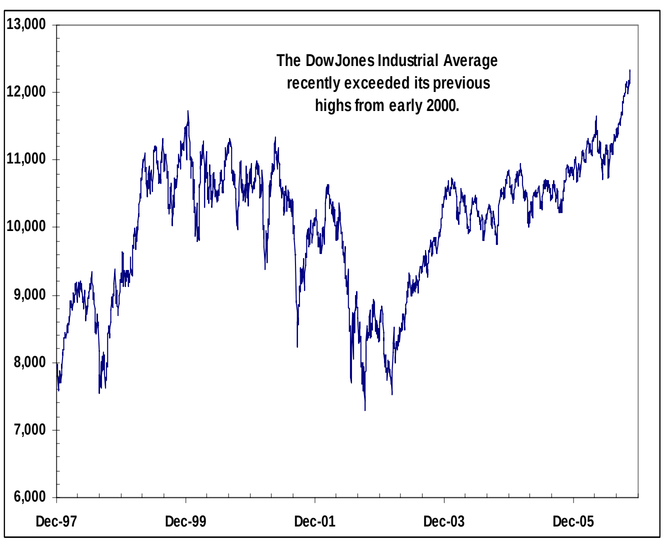
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

November 20, 2006

A Late Year Stock Rally

The Dow and other US stock market indices have set a series of new highs. The recovery from the 2000 to 2002 bear market is welcome and has helped the stock portion of your portfolios. If one takes inflation into account, the US stock market stands well below the records set in 2000.

In the last few months, stock markets around the world have rallied quietly but productively. The Dow Jones Industrial Average and the Russell 2000 (the main index for US small company stocks) have reached all-time highs. Core's investments have thrived and we are on the way to another year of solid returns. Investors are confident and liquidity is ample around the globe. Worrisome factors from the spring and summer--fear of damage from hurricanes, the Israeli-Hezbollah war, Iran's nuclear program, to name a few--no longer arouse anxiety. (The hurricane season was gentle; the cease fire in Lebanon holds; attention to the Iranian threat has waned.) The run up to the US elections and their outcome were benign to the markets. Even the faltering residential real estate market may be aiding securities investments: Last week saw another report of a deep decline in construction of new homes; housing starts in October were a whopping 27% below those in October 2005. It is plausible to think that, as investment in new home construction falls, more capital will find its way into stock markets.



Recent investments. In August, we made initial investments in two exchange-traded funds, one for alternative energy investments, the other for investments in water-related industries. More recently, we added an investment in the exchange-traded fund that invests in "emerging markets", i.e., the stock markets of developing countries, an investment we have previously held. The alternative energy and water-related investments have, in fact, earned some money for us in the brief period of our investment. We are happy about that, but we view these as long-term investments, on the notion that the development of alternative energy sources and water resources is inevitable, necessary, and likely to be quite profitable.

Investment risk. As you may remember, I have been writing all year about the high prices of risky assets. Our recent investments, in the aggregate, amount to only about 10 percent of your portfolios. Even after these new investments, money market funds (dollar-denominated and foreign) still comprise 25 to 40 percent of most portfolios. It is amply

By:

John N. Mayberry

clear that my concerns about investment risk have not yet been realized. After a sharp but brief bout of selling in May and June, calm and confidence have returned. You may recall that during the late spring and early summer, I sold our investments in emerging equity markets, considering those to be our riskiest portfolio positions. Earlier this month, I took a small step back into this investment asset, by buying a position in the emerging markets fund.

The trading in stocks of oil-related companies is interesting. Crude oil itself has fallen by more than 20 percent since August. The fund holding all the oil-related stocks in the S&P 500, a long time investment of ours, traded last week less than 2% below its high from the summer.

This tells us that companies in the oil business will make plenty of money with crude oil priced at $50 per barrel.

A proper assessment of risk is the most difficult aspect of investing. Risk is not a constant. Consideration of the stock markets of the developing countries--the emerging markets--may illustrate this: for the last five decades, the currency and securities of the United States, the dollar and our bonds and stocks, have been deemed the world's least risky. Far to the other end of the spectrum have been the currencies and securities of the third world, to employ the old term. More recently, with the fall of the Soviet Union and the global spread of trade and investment capital, the developing countries have adopted many practices of the economies and markets of United States, Western Europe and Japan. As globalization of capital markets has progressed, the currencies and securities of emerging markets have become less risky. Because of the happy combination of increasing stability and appealing growth prospects in developing countries, emerging markets have attracted investment capital from around the world. Investors in emerging markets have been well rewarded and the investments have come to be a useful part of a well-conceived investment portfolio.

The interplay of liquidity and hedging instruments may account for the willingness of investors to pay up for risky assets.

Some assets classes--notably emerging markets--that had been quite risky decades ago have become less risky as globalization has spread and economies and markets have matured.

Indeed, it may be argued that while emerging markets have become safer, American investments have become riskier. As the debt of the United States to the rest of the world grows and as our geopolitical position weakens, it is sensible to regard US investments as riskier than before. Over the last several years, Core has held greater proportions of foreign investments and we have cut our US bond and stock investments. These interconnected processes are not yet complete: the relative attractiveness of foreign investments will grow.

High prices for risky assets; a possible explanation. Two other factors contribute, I believe, to ever higher prices for risky assets: Liquidity--the money to invest and spend--has grown worldwide, a result of central bank activity and of the proliferation of credit derivative products. Increasingly complex derivatives produce ever greater amounts of investment capital. With these same derivatives come tools to offset the risk of holding a given investment. Sophisticated investment funds can invest large amounts of capital in certain investments, confident that they can pass the risk of those investments on to other institutions. Hence, such a fund can invest greater amounts and pay higher prices for risky assets without increasing portfolio risk for their portfolios.

This is a complex subject that deserves more than one paragraph of comment. Core does not employ such derivatives to hedge the risk in our portfolios. When we consider portfolio risk to be high, we sell the risky positions and hold money market funds. Even with our large cash positions, we have earned a healthy return this year, while keeping risk low.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

October 3, 2006

Investing Slowly

Short-term moves in markets are often driven by hedge funds and similar pools of fast-moving capital. We are long-term investors. We move slowly and cautiously, avoiding undue risk and seeking to identify the long trends in which we can earn money.

After a sharp but brief bout of selling in May and June, the markets recovered their poise in the summer and began to rise. From an inauspicious opening, the stock market staged a stately, if undramatic summer rally. Behind the rally lay events that did not happen: no awful hurricanes damaged oil production or refining facilities; the cease fire in Lebanon was not broken; Iran did not push the West too hard in its bomb development. These non events permitted oil prices to fall. Crude oil prices fell from $78 a barrel in late summer to $58 this week. As oil and gasoline prices fell, traders concluded that inflation risk was lower, and that consumers would keep spending, despite signs that the housing market had begun its fall. The tone of the stock market turned positive and stock prices pushed higher.

The bond market rendered a different interpretation of these developments. Long-term bond prices rose sharply and yields fell. Ten-year treasury bond yields fell to a level 0.5% below the yield on Fed funds and treasury bills, an uncommon development that usually predicts recession or a sharp decline in economic growth. Apparently, fixed-income investors interpreted the fall in oil prices to be a prediction that slowing economic growth would lessen demand for oil. Bond traders took the fall in home sales and in housing prices as the long-expected end of manic housing price appreciation. The bond market appears to conclude that as the housing market cools, consumers will spend less and the economy will slow. If the bond market is correct, the stock market is probably wrong: If the economy slows, corporate profits--the basic driver of stock prices--can hardly be expected to flourish.

Where does risk lurk and how do we price it? The apparent contradiction between the views of stock investors and bond investors raises the persistent investment question: Do the markets properly reflect the real risks that investors face? My answer: Sometimes. But not now.

Oil prices have fallen by more than one fifth in a few weeks. What does this mean? Have the major oil exporters--Saudi Arabia, Iran, Venezuela, Nigeria, Russia and others--suddenly become paragons of political stability and friends to the West, ready to assure United States, Japan, Europe and China of steady and growing supplies of crude oil? Have the problems in extracting, transporting, and refining oil been solved, so that we can now be confident that oil supplies will grow as fast as the demand for oil? To pose these ques-

By:

John N. Mayberry

tions is to answer them. The world is not safe and its geopolitical frictions (to use a mild term) present real risks to the oil markets. Limitations in capacity to produce oil will remain for some time, until new sources of oil are developed and new refining facilities are built. While limited capacity persists, the risk of periodic interruption to oil supplies remains. It still seems to me that we can expect further problems in the oil market and higher prices once again. (In August and September, as oil and other commodity prices fell, our oil- and commodity-related investments, which have been so productive for a few years, pulled back in price. In our portfolios overall, gains in our other investments offset these declines.)

The trading in commodities and oil since August seems to suggest that the days of high oil and commodity prices are over. Maybe. But it is more likely that prices will move back up again. We remain holders of these positions.

My view is that the housing market in the United States presents serious risk to the economy and to investors--to say nothing of those who have borrowed money to make speculative investments in residential real estate. I stick to my warnings of global financial imbalances--characterized by huge indebtedness in the United States and huge surpluses in China, Japan, and other Asian mercantilist economies--although nothing untoward has yet come to pass.

In May and June, the markets seemed to recognize that these are serious problems; the prices of risky assets fell. Then calm was restored and prices began to rise again. The risks did not go away; the market's focus was merely diverted from the risks by more immediately engaging stories about investment opportunity. The dollar stopped its decline, oil prices fell, and stock prices rose.

Experience teaches us that the markets often appear to present less risk than actually exists. (There is an old saw to the effect that if traders knew that the world would end at 3:00 this afternoon, they would hold off selling until 2:55.) One way in which risk is disguised is by the actions of very short-term traders, including hedge funds. Speculators are willing to take risky positions because they believe they will be able to exit positions quickly and at favorable prices. Markets are increasingly driven by hedge funds, alert for short-term opportunities. As opportunities emerge, huge sums are invested, causing price movements that are swifter and more exaggerated in amplitude that than the opportunities may really warrant.

Short-term price swings are not an impediment to long-term and conservative strategies. We can take advantage of "irrational" price moves to advance our slower and more cautious approach.

The investment capital for which Core has responsibility--yours--should not be moved at such a pace. Most hedge fund investors can take far greater risks than a typical Core client. For most of Core's clients, it is best to make low-risk investments with good prospects for long-term gains. We can and should avoid chasing short-term but high-risk opportunities. We can be confident that with patience and discipline we will achieve our investment goals.

Although short-term movements in markets may be contrary to our investment positions from time to time, the markets do accommodate long-term investors like ourselves. If we are roughly accurate in our basic analysis of where the world is headed; if we can identify the types of investments that will benefit from the forthcoming developments; if we restrict investments in expensive and risky securities, then we will achieve good results. We will make money as the years roll by and we will avoid serious loss in the periodic and inevitable bear markets.

New investments. In August, I wrote of our proposed investments in alternative energy and in industries involved in all aspects of the water business. We have completed our initial investments in these, via two Exchange-Traded Funds. The world needs more non-oil sources of energy and more readily available clean water. I believe we will benefit from our new investments in the coming years.

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CORE Comments

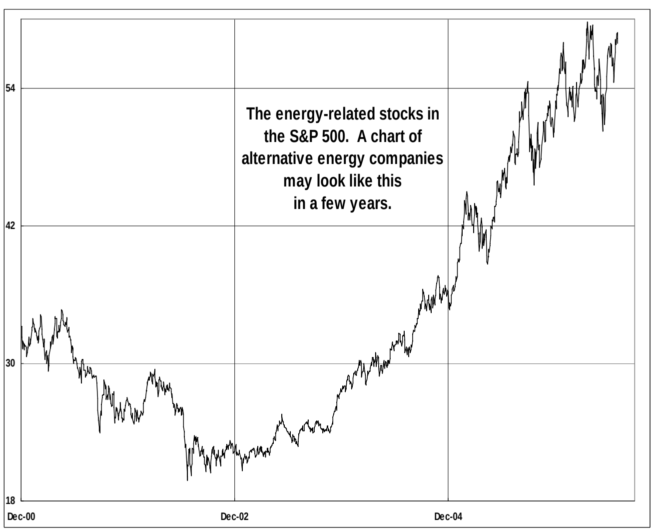
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

August 6, 2006

Opportunities . . . from Problems

Investment opportunities lie on the other side of the problems that trouble us. Investments in alternative energy are likely to be quite profitable precisely because of the problems--political and environmental--created by our dependence on oil

My constant worry is about risk lurking in the portfolios Core manages. Core's primary duty to clients is to preserve the value of your capital. With the many threats, potential and real, to the investments we hold, I am alert to the things that can go wrong. Discussion of these risks forms the customary subject of these investment letters. The litany of woes I have addressed in my letters to you the last year include Iran's nuclear programs and the problems associated with our dependence on foreign oil, the restrictive monetary policies of the major central banks, high prices of risky assets, the risk of terrorism in an anti-American world, and America's unsustainably large indebtedness to the rest of the world.



The energy-related stocks in the S&P 500. A chart of alternative energy companies may look like this in a few years.

Happily, many of these problems create low-risk investment opportunities. This less gloomy aspect of our work is the fun part. In this letter, we first offer a brief review of some of these investments that have earned very attractive returns in the last few years. Then, let us give consideration to those opportunities that offer themselves to us now.

Then: Risk of deflation, opportunities in inflation. From the latter part of 2002 and for several years, the markets and the Federal Reserve Board were very concerned with the risk of deflation. During the depression in the '30s in the United States and for much of the last fifteen years in Japan, deflation--falling prices--caused real economic hardship and it proved quite difficult to overcome. The Fed's policy of very low interest rates was maintained for so long in the early part of this decade chiefly to overcome the risk of deflation. Of course, the remedy was policies that would promote inflation. In 2003 and 2004, we took note of some investment opportunities offered to us by these inflationary policies and made a series of investments that paid off quite handsomely. (We retain some of these investments today.) We recognized that "real assets", like commodities, oil stocks, and utilities, would thrive in the inflationary period that lay before us. Since we made these investments, we have earned more than 50% from them.

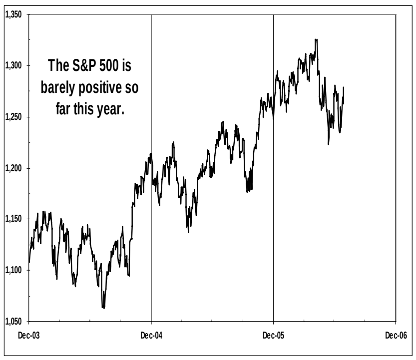
By:

John N. Mayberry

Now: Risks in oil dependency and global warming, opportunities . . . The problems created by our voracious appetite for oil scarcely need elaboration. We continue to hold our oil-related investments. Demand for oil remains high and growing while supplies are limited and vulnerable to disruption by hurricanes, war, and politics. But, the solutions to oil dependency are known and achievable. We have begun to invest in companies engaged in alternative energy development and production. Universities, companies and countries around the globe are developing technologies to meet the world's energy requirements from sources that do not cause carbon emissions and do not put us in the thrall of foreign oil-producing countries whose interests are hostile to ours. The future of alternative energy industries is virtually certain to be robust and profitable.

We have earned returns that exceed those in the US stock and bond market, because of opportunistic investments several years ago. With our large cash positions now, we can withstand difficult markets and invest for the future.

In addition to alternative energy investments, two other areas offer very promising futures and good investment opportunities: water and biotechnology. The ever-growing demand for clean and accessible water affords investment opportunities in water-related industries, including filtration, environmental controls, industrial uses, water utilities, and electronics.



Biotechnology, as an investment term, refers generally to companies engaged <u>exclusively</u> in drug development. It does not include the big pharmaceutical companies like Merck and Pfizer, which have enormous drug development programs, but are in every other phase of the drug business. As promising drugs emerge from biotech companies, the development companies typically enter into marketing agreements with the big pharmaceuticals, or the biotech companies are purchased outright by the big companies. Research into the genetic code of humans offers extraordinary promise for drug development; technological advances accelerate the process.

Each year, Core Asset Management Company files with the SEC a Form ADV with information about our company. If you would like a copy of Part II of Form ADV, please contact us and we will send one to you.

The rewards for investment in alternative energy, water, and biotech may not be realized in a short time. Our oil-related stocks, utilities, and commodity investments bore fruit quickly, but these investments may not reward us so quickly. To employ a common metaphor, I suggest that we view the investments we make this year as the orchardist views the planting of seedlings. We are making small investments now, and can expect to harvest the fruits of these investments for many years in the future.

A brief review of markets and returns. Despite worsening global political conditions, horribly exacerbated by the fighting in Lebanon, stock markets have recovered their poise after turbulence in May and June. We hold large positions in US and non-dollar money market funds because of our sense that investment risk is high. Despite these cash holdings, our returns are far higher than the broad US stock and bond markets this year. Our large cash positions enable us to begin to plant our investment seedlings. We will tend them carefully.

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July 12, 2006

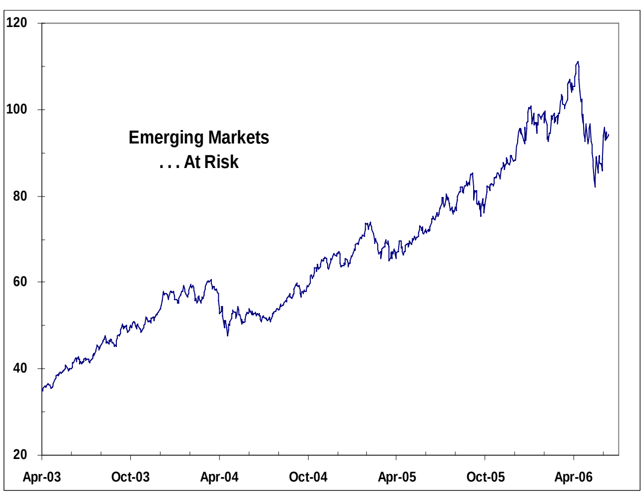
Modest Investment Gains in a Down Market

In the second quarter, stocks and bonds fell in price around the world. Our accounts, in the aggregate, earned a positive return.

Our investment activity over the last three months has had the effect of reducing portfolio risk.

The just-concluded second quarter of this year may have marked the end of the three-year bull market in stocks and other assets, and the beginning of a new cycle in financial markets. This new period, we believe, will be characterized by greater volatility and increased risk. In the last three months, Core has taken significant steps to reduce risk in the portfolios we manage. This letter will outline our investment actions and give our assessment of the investment picture. First, a brief review of major investment markets in the second quarter.

Stock markets around the world fell during the second quarter. In general, secondary markets--like the Nasdaq and stock markets in developing countries--fell by the most. Bond prices fell and interest rates rose around the world. The US dollar declined against major foreign currencies. Commodities, as a class, rose a little in price, although the aggregate results mask very big moves up and down in individual commodities. Given the losses in stocks and bonds, we are pleased to report that our accounts overall rose by a small amount during the very difficult quarter.



We have sold almost all bond investments and all emerging market equities, i.e., all stocks in companies in developing countries. We have invested proceeds of these sales in US dollar and in foreign currency money market funds. We have made these changes because the world's major central banks are all pursuing restrictive monetary policies, which policies pose serious obstacles to many investment assets.

The extended period of extremely low interest rates and very loose monetary policy by the central banks of Japan, Europe, and the United States began in 2001, first to mitigate the effects of the bear market in stocks that began in 2000, then to forestall significant economic disruption from the September 11th attacks, and finally (in the United States) to prevent deflation (falling prices) from occurring. The effect of very cheap money, offered by the central banks in amounts far greater than

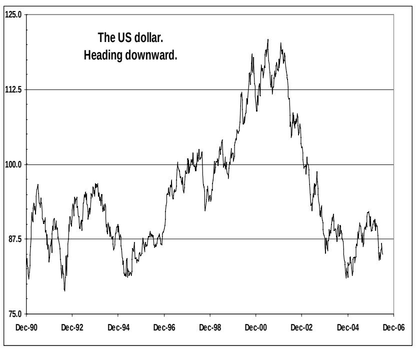
By:

John N. Mayberry

needed for economic activity, was to encourage investment in risky assets. As markets around the world were flooded with liquidity, one asset class after another rose to quite astounding levels, levels that bore scant relation to the inherent risk in these asset classes. Residential real estate and commercial real estate (via REITs) have reached levels in relation to interest rates never before imagined. Similarly the stocks and bonds of developing countries--emerging market debt and equity--have increased enormously in price. Surely the effects of free flows of capital around the world and more sophisticated markets in developing countries has provided a sound basis for <u>some</u> of the increase, but by no means all of it.

When central bank policies were loose and interest rates were low, risky investments thrived. Now the tables have turned. Core has sold its riskier investments.

For two years, the Federal Reserve Board has been increasing short-term interest rates in the US by baby steps. From such a low starting point--Fed funds stood at 1% until June 2004--rates remained abnormally low until this year. Now, at 5.25%, short-term rates are reasonably high and destined, I believe, to go higher still. The European Central Bank has also been raising rates for about a year and will raise rates further. A few months ago, Japan's central bank announced the end of its policy of Quantitative Easing, during which short-term interest rates have been 0% and the central bank has pumped enormous amounts of cash into the system. Since the announcement, Japan's money supply has fallen sharply, as the central bank has withdrawn funds otherwise available for investment. A number of very astute investors consider Japan's money supply decrease to be the primary cause of the world-wide sell off from mid May through mid June.



What next? In my judgment, press reports and commentary to the effect that the Fed is nearly finished raising rates represent wishful thinking. Inflation is back and the Fed will keep raising rates--until there is a financial crisis or until there is a real economic slowdown. It seems likely that Japan and Europe will continue their restrictive monetary policies. In this environment, risky and overpriced investment assets may suffer, hence our sales of these. Our portfolios hold high-quality investments with relatively low risk and with good prospects for investment gains. Our investments in US dollar money funds and foreign currency money funds are now substantial; they have at least three good characteristics: Their risk is very low, the income earned is relatively high and set to go higher, and they provide a source of funds to make other investments as opportunities arise. If the restrictive monetary policies of which we write do result in a bear market in some assets, we will have cash available to invest when the dust settles.

In the last three months of market turbulence, I have written several investment letters, which, read together, give a more rounded view than any of the single letters. These, and our other letters, may be found on Core's website at www.coreasset.com/publications/newspage

Commodities, Oil and the Dollar. Although there have been some large swings in prices of individual commodities including oil, these still appear to be good investments for us, with relatively low risk. I expect that oil prices will remain high until there is a meaningful slow down in the economies of China and the United States. The sharp sell-off in the dollar in April is probably just one more step in its long-term decline. Our foreign currency money market investments will benefit as the dollar falls in value.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

June 6, 2006

Reducing Risk in Turbulent Markets

A volatile period has given investors the jitters. We have been selling some investments. We hold large positions in US dollar and foreign currency money market funds, awaiting low-risk opportunities.

The character of investment markets has changed in the last two months. Core has been adjusting portfolios and selling riskier positions. An explanation of our actions and analysis of the present environment follows: In April, I wrote that the central banks of the United States, Europe, and Japan were, for the first time in years, all pursuing tighter monetary policies. The currency and bond markets began to respond to this by the middle of April: the dollar fell sharply against major foreign currencies and US treasury bond prices declined as yields rose above 5%. By the middle of May, commodities and equity markets world-wide began to fall. After two or three years of abnormally low volatility, large daily swings in prices have become the norm.

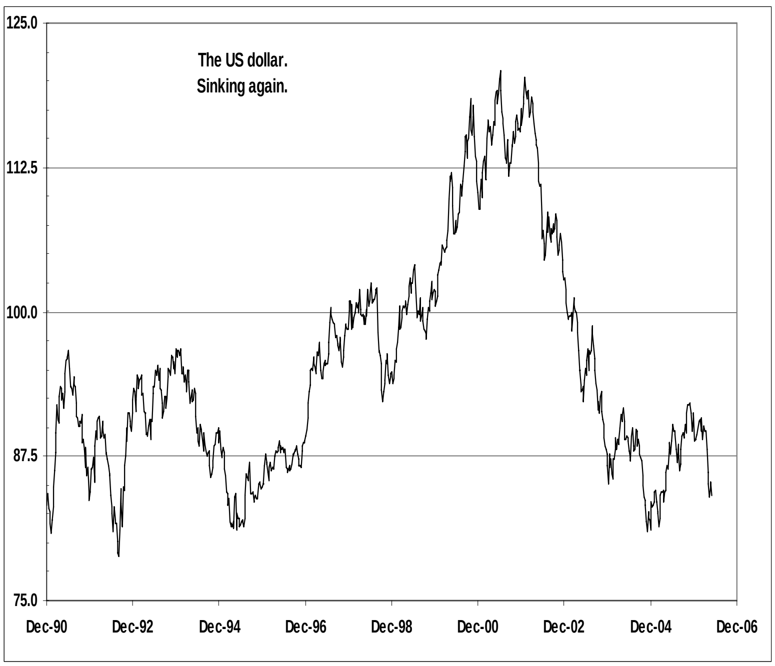
As this unfolded, we sold almost all bonds, domestic and foreign, in client portfolios and invested the proceeds in money market funds, both US dollar money funds and foreign currency funds. Our expectation was--and is--that bond prices will fall and that foreign currencies will gain in value against the dollar. We wrote in April that risky assets continued to flourish, despite the restrictive policies of the Fed and other central banks. Beginning in mid-May, the bloom came off equities, particularly the most risky ones: those of the developing countries, called “emerging markets” in the parlance of investment markets. After three years when risky investments performed extremely well, markets suddenly came to appreciate anew that risk implies the possibility of investment loss. All stock markets have fallen in recent weeks. The US market has fallen least; Japan and the European markets by a bit more; most emerging markets have fallen quite sharply. To a lesser degree, commodity prices also have fallen since mid May.

By:

John N. Mayberry

Emerging Markets. In response to this new volatility and sudden declines in emerging markets--and because of the likelihood of further declines--we have sold a portion of our foreign stock positions, generally selling emerging market positions. The chart on the first page shows the remarkable rise in emerging markets in the last three years, during which the movement has been almost straight up. There have been periods of equally dramatic declines over the last few decades. The greater maturity of many stock markets in developing countries and the world-wide flow of investment capital that is a feature of globalization make a huge decline in emerging markets unlikely. However, in a situation like the present--when investment markets have turned cautious and prices are quite high--the prudent approach is to reduce risky positions and raise cash.

Commodity markets and oil-related stocks continue to offer good returns with relatively low risk. We maintain these investments.



Commodities. Prices of physical commodities have also fallen since mid May, but the decline has been minor and, in my judgment, temporary. The rise in prices of many commodities since 2004 has been significant, but it appears likely that commodity prices will be higher next year. In the past century, bull markets in commodities have generally lasted for fifteen years or more. We are probably in early stages of a long period of rising commodity prices. Since 2004, we have had meaningful investments in a commodity fund and in oil-related stock investments. These have been productive. At present, I have no inclination to reduce the positions.

The US dollar. The dollar resumed its decline in April and today set a new one-year low against the euro. It seems likely that it will fall further in the months ahead. Because of this, we have invested a good portion of the proceeds of our sales in a foreign currency money fund.

Investment risk. When markets become turbulent and selling appears, our approach is to reduce our risky positions. Long-term bonds are quite risky, as are the stock markets of developing countries. The dollar itself is an overpriced and somewhat risky asset. We have reduced investments in these assets. The assets that have relatively low risk and rather good prospects include commodities and oil-related stocks, as well as foreign currency money market funds. We have maintained or added to these positions. From time to time, a number of markets fall simultaneously and sharply. We have witnessed a moderate version of this in recent weeks. At such times, overall portfolio values are bound to suffer. However, large cash positions mitigate loss and safeguard capital that we will invest when the waves of selling subside and attractive opportunities are on offer.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

May 15, 2006

The Turning Point…
...Markets Become Rational.

Core has been selling bonds, foreign and domestic, in recent weeks, as global interest rates rise. We have increased investments in currencies other than the dollar, to take advantage of the dollar's decline.

Since the middle of April, global markets have become volatile. Reassuring progress in various investments assets has suddenly been interrupted; a whiff of panic is in the air. After more than a year of quiet gains, the dollar has fallen by 7% in a few weeks. Precious and industrial metals prices, following a stately period of advance, have risen at a manic pace to record highs for some metals, 25-year highs for others. Yields on bonds in America, Europe and Japan are rising; bond prices are falling. Crude oil prices exceeded post-Katrina highs and gasoline prices moved above $3 per gallon, stimulating panicked and irrational policy suggestions by elected officials. Until last week, tock markets around the world remained undisturbed by the ructions in currency, commodity and bond markets, then stocks cracked as well.

Over this period of weeks, Core has been making significant portfolio changes. This letter offers an analysis of the markets and an explanation of our investment actions. First the investment changes:

Yields on bonds have begun to rise around the world; bond prices are falling. Because I expect this to continue, we have sold most intermediate- and long-term bonds in your portfolios. (In the aggregate, among all our accounts, we have reduced bond holdings from about 25% to about 10%.) As discussed below, we have invested most of the proceeds in US dollar and non-dollar money market funds.

The dollar is falling against the other major currencies; I expect this to continue. Hence, we decreased our US fixed-income investments and increased non-dollar money fund holdings. We may reduce US bond positions further.

By:

John N. Mayberry

As mentioned, we have sold US and foreign bonds in recent weeks. We have purchased foreign, non-dollar money market funds with most of the proceeds. The Franklin Templeton Hard Currency fund is the non-dollar money fund in which we invest. (Note that while this is a "load" fund for retail investors, we can purchase it for our clients without a commission.) We have kept some of the proceeds of our US bond market sales in US money funds, the yields for which have become much more attractive as the Fed has raised rates.

Our recent investment changes in equities have been few, but recall that we made significant equity investments last year. With the firm conviction that foreign stocks offered better prospective returns than US stocks, we increased aggregate foreign equity investments from 6% to 27% during the course of 2005. Because of very strong foreign stock markets this year, that portion has grown further, to about 30%. We are considering decreasing equity positions.

The fall in bond prices and the dollar's renewed decline make sense. There is more to come.

Rational Markets. The recent turbulence in investment markets seems like a delayed reaction to increased inflation and the extraordinary financial imbalances around the world, of which we have written repeatedly. One might conclude that the markets are finally beginning to act rationally: The dollar is falling, as it should given America's indebtedness to the rest of the world; bond yields are rising, reflecting the inflationary price increases in oil and other commodities. Higher volatility in global stock markets seems normal in the present environment: interest rates are rising and the major central banks have restrictive monetary policies, as I wrote last month.

Although some commodities have soared in price this year, especially industrial and precious metals, we plan to keep our commodity investments. The bull market in oil and other commodities is far from its end.

The recent volatility in prices of many investments indicates that risk is high. We are taking steps to protect your capital.

Commodities. There has been more comment in the general media about commodities this year than in the last two decades, or so it seems. Higher oil prices have, of course, been well observed for two years or more, but now the press has discovered the soaring prices of industrial commodities and precious metals. (Indeed, the parabolic curves described by charts of zinc and copper prices this year are a wonder to behold.) The question for us, investors since January 2004 in physical commodities, is whether we should sell or continue to hold our investments. I believe that we can hold our commodities investments, mindful that the ride may be less placid than in '04 and '05.

Price increases in industrial commodities like copper reflect significantly increased demand from China and the real constraints on producing enough to meet demand. An obvious example about demand is the need for copper wire to electrify the buildings China is putting up everywhere . Enormous price rises in gold and silver, which are much less significant for industrial purposes, may be caused in part by rising demand for jewelry in China and India. In addition, higher gold prices reflect profound (and well-founded) skepticism about the likelihood of America's servicing its mountains of debt to the rest of the world. America's debt increases at the rate of $800 billion per year. The dollars with which this debt will be repaid will be worth less than today's dollars. It appears now that inflation and dollar depreciation will be America's "solution" to its debt problem. A loss in confidence in the dollar's future value makes gold prices rise.

Managing risk. Managing investment portfolios involves the seeking of opportunity and the mitigation of risk. With the increase in so many investment assets since the end of 2002, opportunities are far fewer and risk is much higher. Central banks are carefully, but surely, restricting liquidity and raising the cost of money. Risk management is our primary responsibility in this world with very high asset prices, with profound political and ideological tension between oil producers and the oil consumers, and with huge financial imbalances between the creditor countries (Japan and China) and the debtor, America. Our investment moves in the last month have lowered risk in your portfolios. We remain vigilant.

CORE Comments

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

April 20, 2006

Bond Yields Rise . . .
. . . But Risky Investments Climb

In the first quarter, international stocks and energy stocks were very strong. Bond prices fell.

Core's portfolios, with their broad mix of investment assets, produced gains.

More than a year ago, Alan Greenspan noted that the persistence of low interest rates for long-term US bonds presented a "conundrum" when the Fed was steadily raising short-term rates. Until recent weeks, this conundrum continued. In the latter part of 2003, 3-month treasury bills yielded 1% and 10-year treasury bonds yielded 4.5%. In the beginning of this year, 3-month bills yielded 4.5% and 10-year bonds still yielded 4.5%.

During this period, Japan's central bank was pursuing a zero-interest rate policy to put an end to Japan's stubborn deflation; the European central bank maintained an accommodative, low-interest rate policy. Indeed, it was not until June 2004 that the Federal Reserve Board began its long, slow process of raising short-term rates by baby steps. The easy-money, low interest rate policies of these central banks encouraged investors to make riskier investments, and, taking the cue, investors poured capital into risky investments. The result now is that almost all investible assets trade at high prices, at least when measured by traditional risk standards. It has been increasingly hard for Core to find undervalued investment assets with good prospects.

Central bank policies encouraged risky investments in recent years. But now, the central banks of Japan, the United States and Europe are raising rates and tightening monetary policy.

Restrictive monetary policy will hurt risky investments. Interest rates will rise and the dollar will fall.

Offsetting the central bank actions are the policies of China and OPEC countries. Their purchases of US dollar assets have kept the dollar strong and US rates low.

For how much longer will these foreign purchases continue?

Things may now be changing: last week, the yield on the ten-year treasury exceeded 5% for the first time since 2002. Last month, Japan's central bank announced the end of its policy of "Quantitative Easing". The European central bank has begun to raise short-term rates. Thus, for the first time in years, the world's three major central banks are all pursuing restrictive monetary policies. Japan has not yet begun to raise rates, but its announcement tells us that rate rises are on the way.

The investment effects of tight money policies. The eventual investment outcomes are clear; the timing of these is utterly opaque. Long-term US interest rates will rise further. The dollar will fall in value. The prices of risky investment assets will better reflect their real risks. (Should emerging-market debt be priced to yield less than Fannie Mae's mortgage-backed debt--with its implicit US government guarantee? No.)

BRIC and Petro-Dollars--or Why Timing is Impossible. When will risky assets fall in price? Will ten-year treasury bond yields continue to rise, or will yields first fall back again to 4.5%? One can have opinions about this, but the timing is unknowable. Many factors--factors that have kept US interest rates low, and that have rewarded investors in emerging market debt and other risky assets--persist today. So long as these factors outweigh the effects of rising short-term rates and other coordinated tight-money policies by the

By:

John N. Mayberry

three major Western central banks, yields will stay low and prices of risky assets will stay high.

OPEC countries and the growing Asian economies have accumulated vast foreign reserves. Their investment activities have a tremendous effect on all investment markets.

The acronym "BRIC" refers to Brazil, Russia, India and China. Until recently, the economic effect of these countries was limited to the political risks they posed from time to time to America, Europe and Japan. But now, as we know, the economies of these countries have taken center stage in the world. Their accumulation of foreign reserves through ever-expanding trade surpluses now amounts to at least $1.3 trillion. Of similar magnitude are the trade surpluses and foreign reserves of oil exporting countries. Relentlessly high oil prices and ever-expanding demand for oil have given OPEC countries (and non-OPEC oil exporters like Russia) enormous inflows of dollars. Foreign reserve accumulation by the OPEC and BRIC countries and the free flow of this capital around the world have transformed investment markets in ways not imagined a decade or two ago.

For their own reasons, OPEC countries and the Asian central banks have purchased huge sums of US treasury bonds and other US assets. This has caused US interest rates to stay low and has favored many risky assets.

When their buying choices change, markets will turn sour. We will have cash to invest when markets offers better opportunity.

"Non-economic" investors. The anomalous feature of BRIC and OPEC capital is that decisions about investing it are "non-economic". Private investors like us make investment decisions with the idea of achieving the highest total return consistent with the risk level we tolerate. By contrast, central banks--including the Western ones--invest their capital primarily to achieve desirable economic and political effects for their countries. For example, China's central bank uses much of the surplus it generates through its trade to buy US treasury bonds. This is in China's interest: it has the twin effects of (a) keeping down the value of China's currency in dollar terms and, (b) by keeping US interest rates low, thereby stimulating US consumer demand for Chinese products. This is a non-economic investment decision in that it causes China to put too much money into an overpriced asset, namely US treasury bonds. However, the political and other economic benefits to China are deemed to be greater than the investment risk it assumes in holding so much of its capital in US treasuries.

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Because non-economic investors control so many trillions of dollars, their investment decisions skew investment markets in ways that may be considered irrational. Back to our China example: if China continues its very large purchases of US treasuries, then treasury bond yields will stay low. If Japan continues its weak-yen policy, the dollar will remain strong against the yen. So long as these conditions are in place, the prices of risky investment assets will appreciate and the gap between those prices and their "real" values will widen further.

What will change the pricing of risk? When OPEC and BRIC countries change their capital allocation and reduce the rate of investment in US treasuries and other dollar-based assets, interest rates here will rise, perhaps significantly. The dollar will fall in value, particularly against major Asian currencies. Inflation in the United States will rise; the economy here will slow. Financial markets around the world will be less forgiving of investment risk and far more volatile.

Our solution. Because three-month treasury bills, the "riskless" investment, yield essentially as much as ten-year treasury bonds, one should reduce investment in bonds and keep the proceeds in money market funds, both US dollar money funds (the usual ones) and non-dollar money funds. One should reduce holdings in other risky assets that have risen well above their "real" values. Although the timing of a repricing of risk is uncertain, it does lie ahead of us. When it comes, those holding cash (in dollars and other currencies) will have attractive investment opportunities. This is Core's approach; we have begun to put this into effect.

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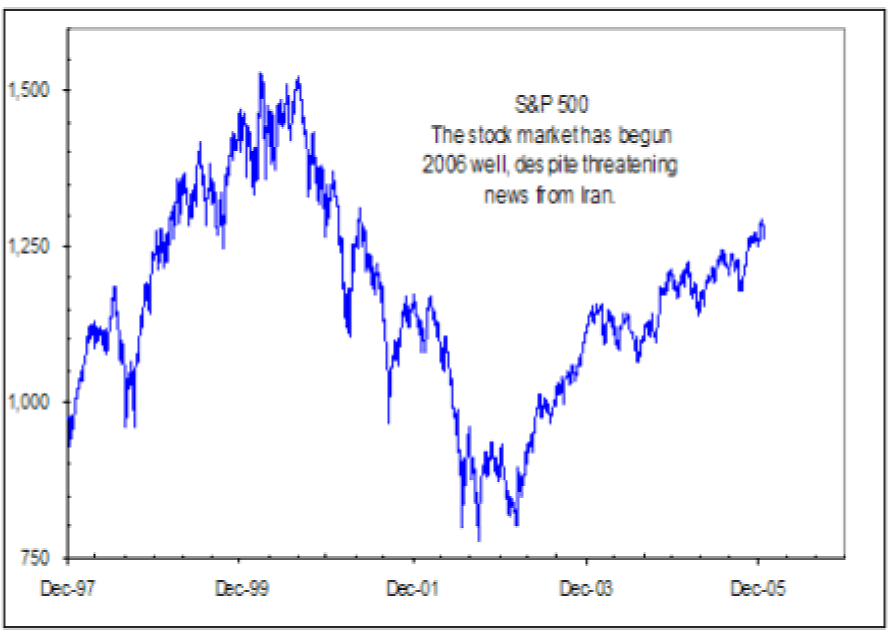
CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

January 30, 2006

Iran, Oil, the Bomb . . .
. . . Investment Risk in a Dangerous World

Dependence on foreign oil by Europe, America and Japan increases the power of oil-producing countries hostile to our interests.

Iran's recent announcement of its intention to resume development of enriched uranium and its subsequent threat to cut oil supplies if sanctioned by the international community very neatly present the world's dilemma. The refusal of America and the other rich countries to develop alternative sources of fuel to meet energy needs has made us dependent upon the oil-producing countries, many of which are hostile to Western interests. As oil demand has risen to within two percent or less of the world's capacity to produce, the power of the oil-exporting countries has increased enormously.



This power grows inexorably: global competition for sources of oil has become intense. India and China have become very large oil importers and, with their high rates of economic growth and huge populations, their future demand for oil becomes a key element in their present decisions. Iran presents India and China with a very unappealing choice: join Europe and America in the effort to prevent Iran, their near (and unreliable) neighbor, from building atomic bombs, or turn a blind eye to the nuclear risk in hopes of gaining a "secure" supply of oil in the coming years.

Unfortunately, Iran is hardly the only unfriendly oil producer: Venezuela is a destabilizing force in this hemisphere; its oil wealth affords President Chavez a very potent tool for his mischief. Saudi Arabia funds madrassas throughout Asia to inspire and cultivate a generation of anti-Western Muslims. The Central Asian oil producers are thuggish dictatorships whose future adventures may make Iran appear to be a moderating force in the world. Nigeria, a profoundly corrupt and failed country, is utterly unreliable today as a steady producer of oil; there is little reason to expect a more benign future.

by
John N. Mayberry

It is not too late for America, Japan, and Europe to take actions to prevent matters from worsening, but the political will is utterly absent. There is nothing surprising about the present situation and the future dangers: growing demand and the absence of significant new sources of oil in Europe and America have long been known. Japan has for years imported every drop of oil it consumes.

The strength of the business interests that support oil use--and dependence on foreign oil--overwhelm rational political decision making. The development of alternative energy sources, greater efficiencies in energy use, and energy conservation measures can all be accomplished much more swiftly. If there were a clear will to take these steps--akin to the will the West applied in past decades to weapons development, to containment of the Soviet Union, and to lunar landings--the (nasty) oil producers would overnight realize that their game was up. Iran's bargaining power to resist countries opposing its development of the bomb would disappear.

There are obvious and well-known solutions to this problem. Does the West have the political will to make needed changes?

Investment implications. I leave to the reader the assessment of the likelihood of real change in our way of using petroleum. How does one invest in this world as it is? In the recent few years, some decisions have been simple and clear: invest in industries that profit from our dependence on oil and that benefit from the increasing demand for oil. The related investment--in other commodities besides petroleum--has also prospered. Like the oil market, other commodities have constraints on production and growing demand; these factors raise prices. There is little reason to think this will change soon, but when and as the political climate matures, we will reduce those investments. Core has begun to make initial investments in alternative energy and these will grow.

These investments represent the approach of seeking and exploiting opportunity. Well and good. The other, equally important aspect of portfolio management is managing risk, a particularly cogent concern as we consider likely events in the course of Iran's quest for nuclear weapons.

Portfolio diversification reduces risk to a degree. Our bonds are not likely to suffer much in a crisis. But, it is impossible to eliminate all investment risk.

In the last three years, the investment world has become less concerned with risk and has sought the higher returns available in traditionally riskier investments. A clear example is the flow of investments, including those of Core's clients, into the stock markets of developing countries, formerly referred to as emerging markets. The tremendous investment in REITs over the last three or four years is another example. This flood of dollars, chasing high REIT dividends and reflecting the general infatuation with all things real estate, has pushed REIT investments to levels of valuation never before seen. There will come a time when these riskier investments become recognized more for the risk they present than for their opportunity. A global political crisis involving oil supplies or bomb development by Iran may present the occasion for a reassessment of investment risk. Unwillingness by China to continue to buy US treasury bonds with the dollars they collect from their sales to us might also cause a stir in financial markets.

Core manages risk in two ways, first by maintaining significant investments in securities that will suffer the least from a crisis. Our US treasury bonds are an example. Our foreign bond holdings are another. (These investments may even benefit from a crisis.) The second approach to managing risk is alertness to signs of stress--financial and political--and preparation for action to reduce the riskier positions in portfolios. This is the bit that keeps one up at night.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

January 10, 2006

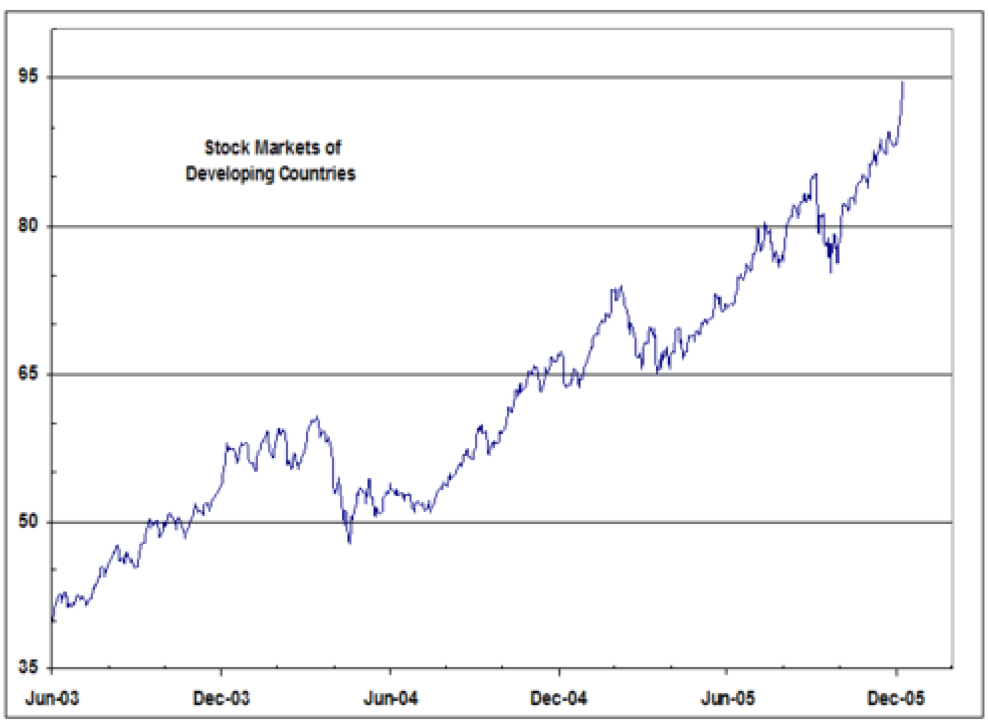
2005, A Fitful, Quiet Year . . .
. . . A Racing Start to 2006

by
John N. Mayberry

The significant feature of the financial markets in 2005 was the extent to which foreign stock markets beat the US market. Quite likely, this will continue in 2006 and beyond. During the course of 2005, we increased your investments in foreign stocks, through a variety of Exchange-Traded Funds (ETFs) and mutual funds. These foreign investments helped us earn returns higher than available in the US stock and bond markets. I expect to broaden our foreign investments in 2006 and expect we will again realize benefits from larger non-US investments.

Foreign stock markets were stronger the US stocks, especially the markets of developing countries, shown in the chart below.

The strength in foreign stock markets is, in part, a measure of the vibrancy of the developing economies in Asia. The ever-easier movement of capital around the world permits us to deploy your investment assets in these distant, rapidly growing markets. Globalization of investment capital and the "democratization" of investment opportunities--through ETFs and other types of securities--have broadened the range of available investments in ways barely imaginable two decades ago.



The new availability of low-cost foreign investments is timely: Investment opportunity in America will continue, but ours may not be the most dynamic economy nor the most attractive investment destination in the years just ahead of us. American stock and bond were essentially flat in 2005. The Dow fell by a fraction of a percent, the S&P 500 rose by less than 5% (including dividends) and broad measures of the US bond market showed gains, with interest, in the range of 2% to 3%. Foreign stock markets did better.

The aggregate return in 2005 for all the capital we manage was about 7% net of our fee. (Variation among individual accounts arises from the differing levels of risk we take for different people.) Without foreign investments and without targeted investments in energy-related equities and commodities, we would have been hard pressed to earn more than 3% to 5%.

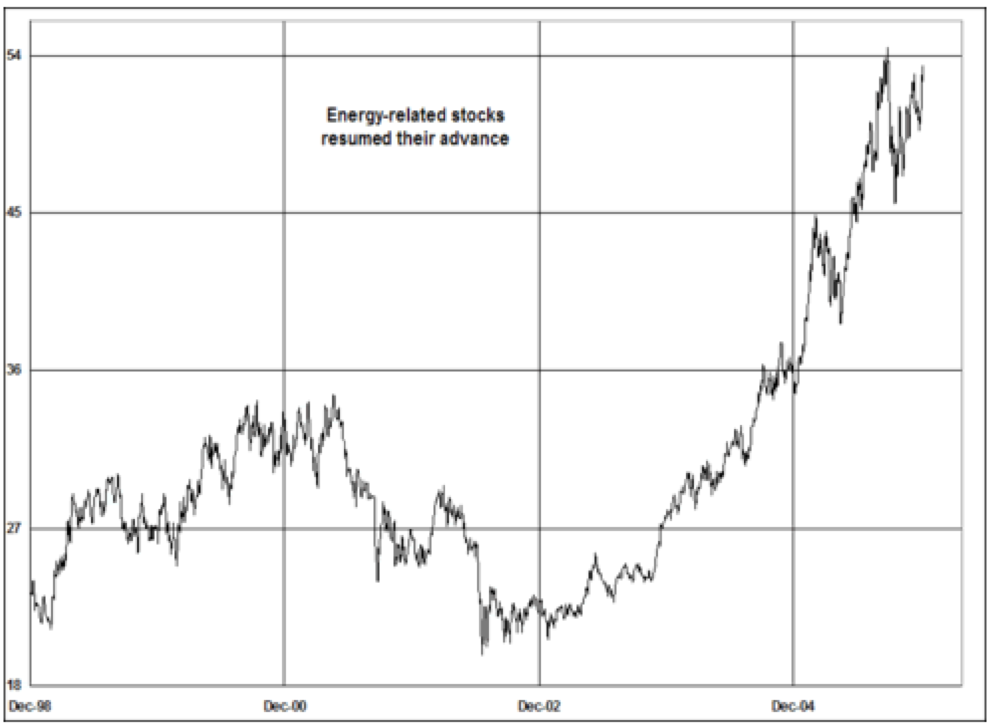
A broad measure of stock markets in "developing" countries gained 31% in 2005.

The EAFE index, measuring the stock markets of "developed" countries, rose by 11%.

US stocks gained less than 5% in 2005.

Foreign stock markets. In addition to the dynamism and rapid economic growth in many of the developing economies, China, India and others, many of these stock markets are valued more attractively than the US stock market. Through these investments, we are able to buy faster growing companies at lower prices than in the US. Valuation measures favor foreign stock investments.

As we decreased our large investments in foreign (non-dollar denominated) bonds, we used the proceeds to buy foreign stocks both in developing markets and in Japan and Germany. Japan's economy, prostrate for over a decade following the bursting of its stock market and real estate bubbles, has begun to grow. Its stock market, exceptionally weak for fifteen years, has rallied very strongly as optimism about Japan grows. Separately Germany, characterized by high unemployment and very low growth for years, shows increasing signs of vigor, rising exports and growing corporate profits. Its stock market has also come to life and shows promise for 2006.



Oil and related investments. China's nearly insatiable appetite for oil, world-wide production problems, and hurricanes all were factors driving stocks of energy companies higher again this year. The oil-related stocks in the S&P 500 gained 39% in 2005, after a (mere) 32% gain in 2004. The adjacent chart shows the extraordinary rise in these investments in recent years. The recent peak in energy stocks and oil prices followed hurricanes Katrina and Rita in September. In the autumn, oil stocks and crude oil and gasoline prices traded below those levels, giving rise to calmer inflation reports and increasing consumer confidence. Notwithstanding recently favorable news, fundamental pressures on oil prices remain unsolved. These include constraints on extraction and refining of oil and its products, growing demand from developing economies (notably, but not only, India and China), anti-Western sentiment in many countries with oil reserves, and domestic US policies that encourage oil consumption. Because of longer-term forces keeping oil prices high, we retain significant energy investments.

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Commodities. Core's largest single investment is in Pimco's Commodity fund, an investment that replicates a broad-based index of physical commodities denominated in dollars. The same global trends that drive oil prices higher move the prices of other commodities, as well. Industrialization in the developing economies in Asia, solid growth in America, and under-investment in commodity production over the last decades all push commodity prices higher.

We made this investment in January 2004 and it helped our portfolios with a 15% gain in 2004. In the year just past, commodity inflation increased further and we earned a 20% return in the fund. There is increased speculation in commodities; the headline-making news about oil prices and gold's recent ascent to 20-year highs above $540 per ounce give cautious investors like ourselves some pause. Volatility in commodity prices will remain high, but it seems likely to me that most commodity prices will be higher as 2007 begins than they are now.

You may read about a tax ruling and its effect on the Pimco Commodity fund we hold in many accounts. Pimco has informed us how it will address the issues the IRS raises and assures us that the fund will continue its investing.

The commodity fund and a tax ruling. The Pimco fund employs certain "swap" transactions to replicate the performance of the Dow Jones-AIG commodity index. The Internal Revenue Service recently announced a ruling that appears to disallow the use of these swaps by a mutual fund. The rule will go into effect on June 30, 2006. This revenue ruling and its possible affect on our commodity fund has generated adverse press attention. It appears, however, that Pimco has solved the problem:

Last week in a conference call for institutional investors in the fund in which I participated, Pimco reported that it can use a different type of security, so-called "structured notes", to achieve the same effect as its commodities swaps. These notes are widely used in the mutual fund industry and elsewhere and the IRS accepts them for mutual funds. Pimco assured us that it will be able to continue offering and managing its commodity fund after June 30, 2006. Pimco plans to make a public announcement to this effect shortly. I have confidence in Pimco and we have ample time--more than five months--to evaluate its proposed solution.

In 2005, the dollar rose against the euro and the yen and yields on long-term bonds remained stable. Neither was expected when 2005 began.

The dollar, the Fed, and the bond market. As usual--one might say invariably--the currency markets and the bond markets confounded expectations in 2005. A year ago, the Federal Reserve was in the midst of its well-advertised process of raising short-term interest rates. (Recall that after the bursting of stock market bubble, the 2001 recession, and the September 11th attacks, the Fed lowered short-term interest rates to 1%, and kept those rates very low for a long time.) In the middle of 2004, the Fed began raise these rates by 0.25% at each meeting of the Fed's Open Market Committee (FOMC), every six weeks or so. Given the near certainty, as 2005 began, that the cycle of rate increases would continue, it was widely expected that long-term rates--and, quite importantly, mortgage interest rates--would also rise.

And, at the end of 2004, the US dollar had been falling for 30 months against major foreign currencies. America's trade deficit was widening; its net debt to the rest of the world was huge and growing fast. Given the near certainty that America's trade and current deficits would continue to grow, it was widely expected that the dollar's value would decline further.

The dollar rallied in 2005 as interest rates rose in America while remaining stable in Japan and Europe.

But, as short rates rose, bond yields fell, for reasons that remain quite obscure.

As we know now, these confident expectations about bonds and the dollar were confounded by reality. The dollar rallied quite strongly against major foreign currencies; the currency markets focused on rising short-term US rates and largely ignored our external deficits. And, yields on long-term bonds fell even as short-term rates rose, a phenomenon that occasioned much analysis but no convincing explanation. (When the Fed began raising short rates, the yield on the Treasury's composite of bonds maturing in more than 10 years was 5.20%. At the end of 2004, that same yield was 4.71%. By the end of 2005, the yield had fallen further, to 4.58%.)

The US stock market gained about as much in the first week of January as it did in all of 2005.

Announcements by the Fed and China caused the dollar to fall sharply against the euro and yen.

On January 3, the Fed released minutes of its December FOMC meeting, which suggested that its process of raising rates was nearing its end. This triggered an enormous world-wide rally in stocks, a rally in bonds and further decline in their yields, and the biggest two-day drop in the dollar's value against the euro in years. Two days later, China announced that it intends to change the management of its foreign reserves, implying--probably--that it will be holding a smaller percentage of its reserves (which are approaching $1 trillion) in dollars. Taken together, the Fed's announcement and China's suggest that the dollar, having risen in value in 2005, will resume its decline. This will benefit our foreign bond and our commodity investments. I venture no prediction about yields on US bonds, but continue to focus on the Treasury's inflation-adjusted bonds, discussed in previous letters.

Core can assist with required minimum distributions from IRAs and can provide reports for income tax returns.

IRA distributions and tax reports.

IRA distributions. Owners of IRAs and other qualified plans must take distributions from these plans beginning in the year in which one turns 70 1/2 years old. The brokers that hold one's IRA--Schwab or others--report on the monthly statements the minimum amount that one is required to withdraw. Thus, one's recently-received year-end brokerage statement shows this amount, which may be transferred to another taxable investment account or to one's bank account. The distribution may be taken at any time during the year--many take regular monthly or quarterly distributions--or it may be withdrawn in a lump sum. If taken in a lump sum, it is probably sensible to take the distribution early in the year.

Reports of investment income. We can provide you or your tax preparer with clear and simple tax reports showing capital gains, interest and dividends in the form required for tax returns. We will be happy to assist in IRA distributions and to send or email tax reports. Please contact us by phone (800 451 2240 or 415 332 2000) or email (JNMayberry@coreasset.com), if you would like our help with either.

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