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After a relatively flat 1st quarter, the stock market – as reflected by the S&P 500 index – had a strong 2Q. April's strength continued into May with the index setting a new all-time high by month's end. In June, the stock market showed some volatility and ended lower for the month. Overall, the S&P 500 index was up a strong 6.3% (including dividends) for the quarter and about 7% for the year.

Despite these solid returns, pessimism grew as the 3rd quarter began. The fixed income market was spooked by higher interest rates in some US Government debt and by the unusual difficulty some private equity firms had in arranging financing for a couple of deals. Housing concerns continued especially in the sub-prime lending area while growth in corporate earnings was the slowest in years, and the dollar continued to be weak versus the Euro and British Pound.

Given all these problems, some observers are predicting volatile times ahead. If this occurs, we must remain focused on the long-term and ignore the daily ups and downs along the way.

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This letter continues the segment discussing factors used to invest your money.

When is the right time to buy a stock? For investors using my approach, the best time to buy is when the stock is selling at a sufficient discount to what I believe it is worth. Executing this strategy, though, is more of an art than a science.

In theory, when a stock is selling for a reasonable price, you simply buy some and wait for it to go up. In practice, once you start buying (usually following a stock price decline), sometimes the stock will continue to decline while other times it will start going up. For example, when a stock becomes unpopular, sometimes it becomes even *more* unpopular than you expect. In November of 2004, with Pfizer selling for the lowest price in years, I began accumulating shares. I kept buying during 2005. Finally, in December 2005, with the stock down almost 18% from my original purchase price, I made one additional purchase. During the following two weeks, the stock rose almost 20% after the company announced a significant increase in its dividend and a court ruled favorably in a key patent lawsuit. By contrast, sometimes when a stock drops, other investors recognize the same value that you see and quickly undo the stock's price decline. This happened in June 2005, when I purchased shares of UPS. Before I was able to buy more, the stock quickly rose in value.

In summary, the key to buying stocks is to wait until they are on sale and then buy in chunks. While the actual timing of purchases can be a bit dicey, success comes from buying good companies for less than they are worth and waiting patiently for their value to be properly recognized by the stock market.

Thank you for your confidence.

Brad

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