

Student Investment Fund

2005-2006

Annual Report



<http://org.business.utah.edu/investmentfund/>

2005 – 2006 Student Managers

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Investment Fund Advisor: Dr. Elizabeth Tashjian



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HISTORY

In October 1998, David Eccles School of Business finance students joined the D.A. Davidson & Co. Student Investment Fund program, which allows students to invest \$50,000 in a working stock portfolio. The purpose of this program is to bolster student learning outside the classroom in a real-world setting. The original \$50,000 remains intact year to year, supported by D.A. Davidson. Any returns above five percent are split in half and shared by the firm and the Student Investment Fund. D.A. Davidson guarantees students against any losses below the original \$50,000 mark, which will be replenished year to year if necessary. Since October 1998, D.A. Davidson has given over \$16,000 directly to the student portfolio based on performance and Bill Child, CEO of R.C. Willey Home Furnishings, has donated another \$5,000 to the fund. In 2004, we began a new fund, the School Fund, which is funded by donations to the Student Investment Fund. In March 2004, U students received an additional \$50,000 from Hal Milner in a program similar to D.A. Davidson's. Last year, Mr. Milner donated over \$3,000 to the School fund based on his portfolio's performance.

Beginning in October 1998, students formed a Student Investment Fund Club and met regularly to develop an investment strategy, research and invest in specific stocks, listen to investment professionals, and to track their investments. The original club that first year was comprised of 12 students and their advisor, Liz Tashjian.

That first year, the students eventually selected a strategy of investing in volatile stocks in the technology and finance sectors. Between January and April 1999, the portfolio realized returns of more than 40 percent. In April, the students voted to sell a third of their equity positions to reduce the fund's risk over the summer. By the end of the summer, the portfolio's annualized return was 35 percent.

In the fall of 1999, the Student Investment Fund developed from a club into a restricted-enrollment class. This class is limited to 18 students, and students wishing to take it must apply for acceptance. The class extends across the full academic year. The class meets once a week to track the Fund and to research potential investments. Each year, students are required to publish an annual report listing the Fund's activities. In 2003, the class was designated as an honors class. The Fund is subject to an annual audit by fellow students in the accounting society Beta Alpha Psi.

In September 1999, D.A. Davidson calculated earnings from the first year of the Fund, and students earned more than a 35% return. The 2000-2001 class learned some painful lessons about diversification and selling strategies. The group had significant holdings in Global Crossing and Exodus Communications, both telecom companies that ended up in bankruptcy. The 2001-2002 class managed to outperform both the S&P and Nasdaq indexes, losing a mere 22% during the year the class managed the portfolio. The next year's class had a better outcome, earning 30% on a relatively balanced portfolio from August, 2002 to August, 2003. Since the spring of 2004, the fund has adopted a strategy of investing in a portfolio of small cap stocks. The 2004-2005 class earned returns of

about 20%. Over the time they managed the fund, the S&P gained less than 10% and the NASDAQ index was up about 16%.

STRATEGY

Davidson and Milner Portfolios

The prior managers had adopted a strategy of investing in small cap stocks in the Davidson and Milner portfolios. They believed that small caps held the greatest potential for the following reasons.

1. Small cap stocks' aggregate performance over the last 80 years has yielded 17% annualized returns compared to the overall market return of 11%.
2. Small caps have the highest volatility and as each class's management tenure lasts only 12 months, small cap stocks present a better opportunity for us to see the results of our actions.
3. Small cap companies are typically more focused in scope and are more easily understood.

The prior managers invested in small cap stocks they concluded were undervalued. Initially, we adopted a similar strategy. Beginning in late January, our strategy began to diverge and we began to make investments in large cap stocks. Our first large cap investment was in Occidental Petroleum, an independent oil and gas company. Oil prices were very high and continued to be robust and we wanted to increase our exposure to energy prices. Subsequently, we invested in Wal-Mart, which is expanding into rapidly growing countries such as India, and in Intel and Applied Micro Devices. We believed that there would be increased demand for chips and we were unsure whether Intel or AMD would be the stronger performer. Over this interval, we continued to invest in small cap stocks, as well.

In the early part of the year, we held fairly strictly to a policy of selling stocks when the stock price rose to our pre-determined target or following price declines from which we believed it was unlikely the stocks would recover quickly. After selling Shuffle on February 8 and watching the price recover, we did not sell any additional stocks.

We made an effort to keep our cash holdings to a minimum to maximize our chances of gains.

On September 1, 2005, shortly after we inherited the portfolios, the Davidson portfolio's value was reset to \$50,000. Mr. Milner generously chose not to reset his portfolio and left the prior year's gains under our management. Consequently, the value of the Milner portfolio was about 1.2 times the value of the Davidson portfolio. The previous managers had bought equal amounts of stock in the two portfolios. To maintain similar return performance on the two portfolios, we voted to allocate future investments 45% to the Davidson portfolio and 55% to the Milner portfolio.

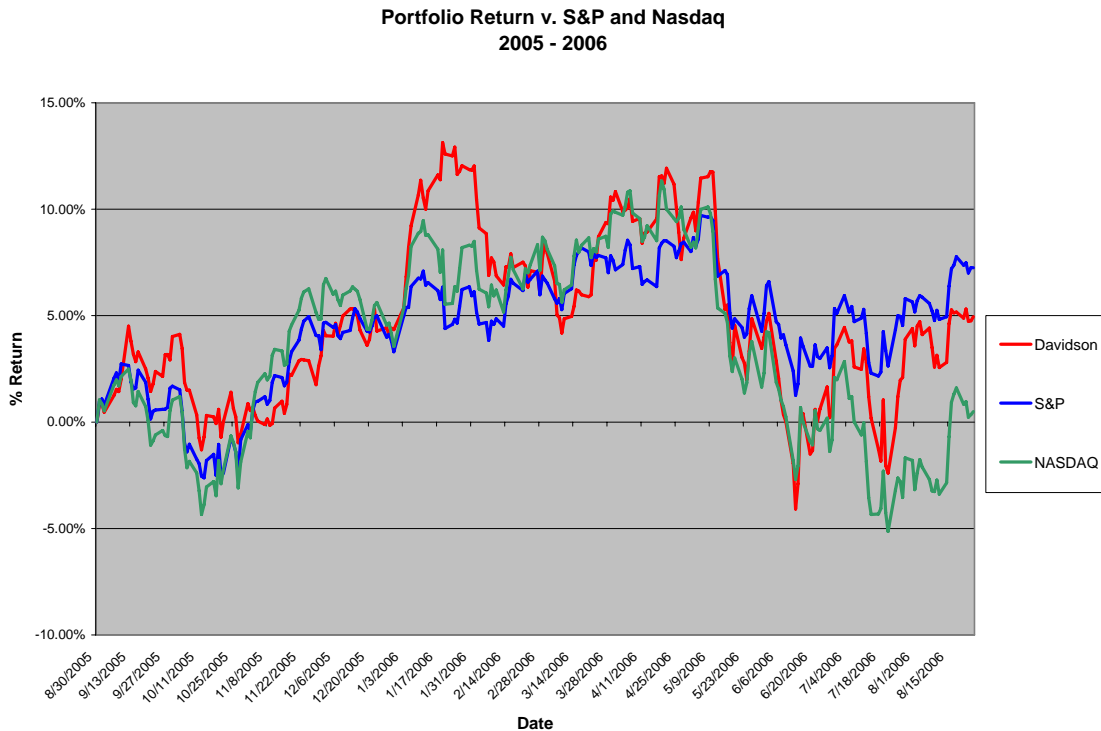
School Portfolio

The investment objective for the school portfolio is growth, with a three-to-five year investment horizon.

DAVIDSON AND MILNER PORTFOLIO PERFORMANCE

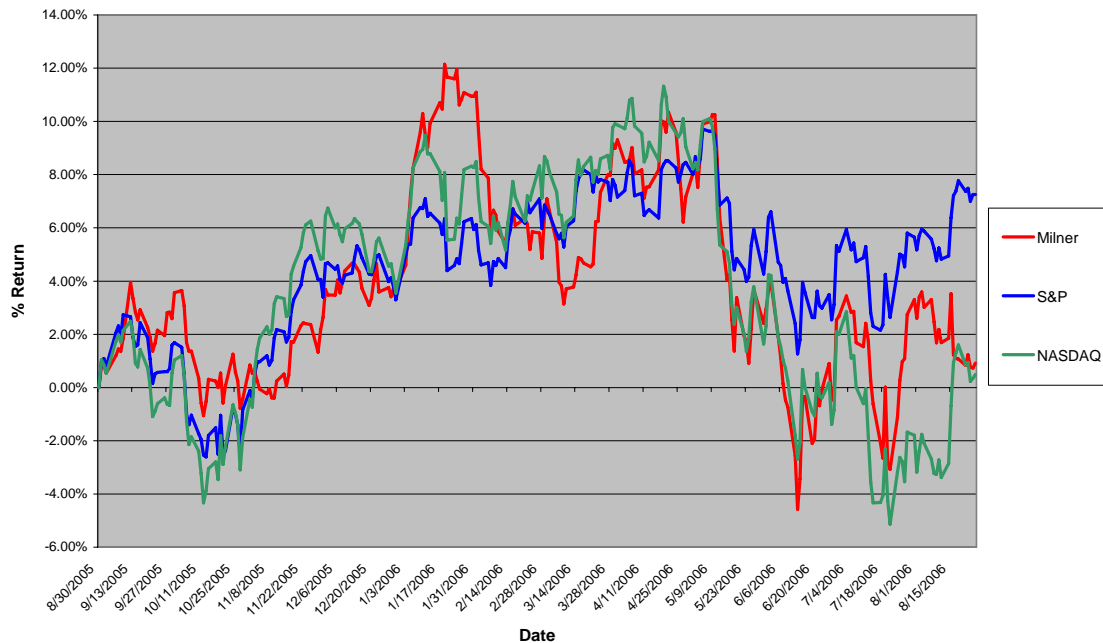
Overall performance

From the date we assumed control of the funds, the Davidson portfolio gained 4.95% (valued on August 25) as compared to the S&P 500, which yielded 7.25% and the NASDAQ index, which returned 0.49%.



Over our tenure, the Milner portfolio gained 0.92% (valued on August 25) as compared to the S&P 500, which yielded 7.25% and the NASDAQ index, which returned 0.49%. Although we now make comparable investments in both the Davidson and Milner portfolios, some of the stocks we inherited were not held in similar proportions in the two portfolios. In addition, the Milner portfolio is 15% invested in cash, while the Davidson portfolio is only invested 8% in cash.

**Portfolio Return v. S&P and Nasdaq
2005 - 2006**



Individual stock performance

Davidson & Milner portfolios						
Ticker	Date inherited or acquired	Initial price	Date sold or valued	Final price	Dividends	Gross return
Inherited stocks						
AIR	30-Aug-05	17.35	24-Aug-06	20.96	0.000	20.8%
CAB	30-Aug-05	19.98	2-Nov-05	16.333	0.000	-18.3%
SKYW	30-Aug-05	23.19	23-Nov-05	30.05	0.030	29.7%
GTK	30-Aug-05	28.87	24-Aug-06	34.86	0.340	21.9%
IWO	30-Aug-05	66.94	24-Aug-06	69.63	0.255	4.4%
ICLR	30-Aug-05	40.00	24-Aug-06	69.85	0.000	74.6%
TINY	30-Aug-05	11.35	24-Aug-06	9.60	0.000	-15.4%
MTH	30-Aug-05	75.27	31-Aug-05	77.00	0.000	2.3%
Acquired stocks						
SNIC	29-Sep-05	21.03	9-Nov-05	15.5315	0.000	-26.1%
DIET	2-Nov-05	4.39	26-Jan-06	7.3436	0.000	67.3%
PDC	2-Nov-05	17.65	24-Aug-06	13.75	0.000	-22.1%
STX	3-Nov-05	15.61	25-Jan-06	25.80	0.000	65.3%
ARO	28-Nov-05	24.23	12-Jan-06	29.97	0.000	23.7%
FORD	11-Jan-06	11.03	26-Apr-06	10.20	0.000	-7.5%
FORD	30-Nov-05	17.59	26-Apr-06	10.20	0.000	-42.0%
USNA	26-Jan-06	39.60	24-Aug-06	43.89	0.000	10.8%
SHFL	30-Jan-06	25.93	8-Feb-06	22.7975	0.000	-12.1%
OXY*	30-Jan-06	47.15	24-Aug-06	52.81	0.180	12.4%
CERN	10-Feb-06	42.10	24-Aug-06	44.61	0.000	6.0%

INTC	15-Feb-06	21.33	24-Aug-06	18.56	0.200	-12.0%
WMT	15-Feb-06	46.36	24-Aug-06	43.70	0.504	-4.7%
CRYP	16-Feb-06	25.04	24-Aug-06	25.11	0.190	1.0%
AMD	17-Feb-06	40.39	24-Aug-06	24.76	0.000	-38.7%
NXG	26-Apr-06	4.01	24-Aug-06	3.55	0.000	-11.5%

* split adjusted

Transaction summary

Davidson and Milner Portfolios					
Ticker	Number of Shares	Inherited Price	Purchase Price	Sales Price	Current Price (Aug 25)
Stocks we sold					
SKYW	200	23.19	N/A	30.05	23.27
CAB	200	19.98	N/A	16.333	19.17
MTH	100	75.27	N/A	77.00	39.98
SNIC	300	N/A	21.03	15.5315	14.545
STX	400	N/A	15.61	25.80	20.56
ARO	80	N/A	24.23	29.97	23.91
FORD	350	N/A	17.59	10.20	4.98
FORD	500	N/A	11.03	10.20	4.98
DIET	1000	N/A	4.39	7.3436	3.56
SHFL	500	N/A	25.93	22.7975	27.74
Stocks we hold					
AIR	400	17.35	N/A	N/A	20.62
GTK	400	28.87	N/A	N/A	34.88
IWO	250	66.94	N/A	N/A	69.93
ICLR	150	40.00	N/A	N/A	69.73
TINY	150	11.35	N/A	N/A	9.49
PDC	400	N/A	17.65	N/A	14.05
USNA	150	N/A	39.6	N/A	43.97
OXY	120*	N/A	47.15	N/A	53.41
CERN	100	N/A	42.1	N/A	42.10
INTC	200	N/A	21.33	N/A	18.90
WMT	100	N/A	46.36	N/A	43.88
CRYP	250	N/A	25.04	N/A	24.37
AMD	100	N/A	40.39	N/A	24.56
NXG	2500	N/A	4.01	N/A	3.64

* split-adjusted

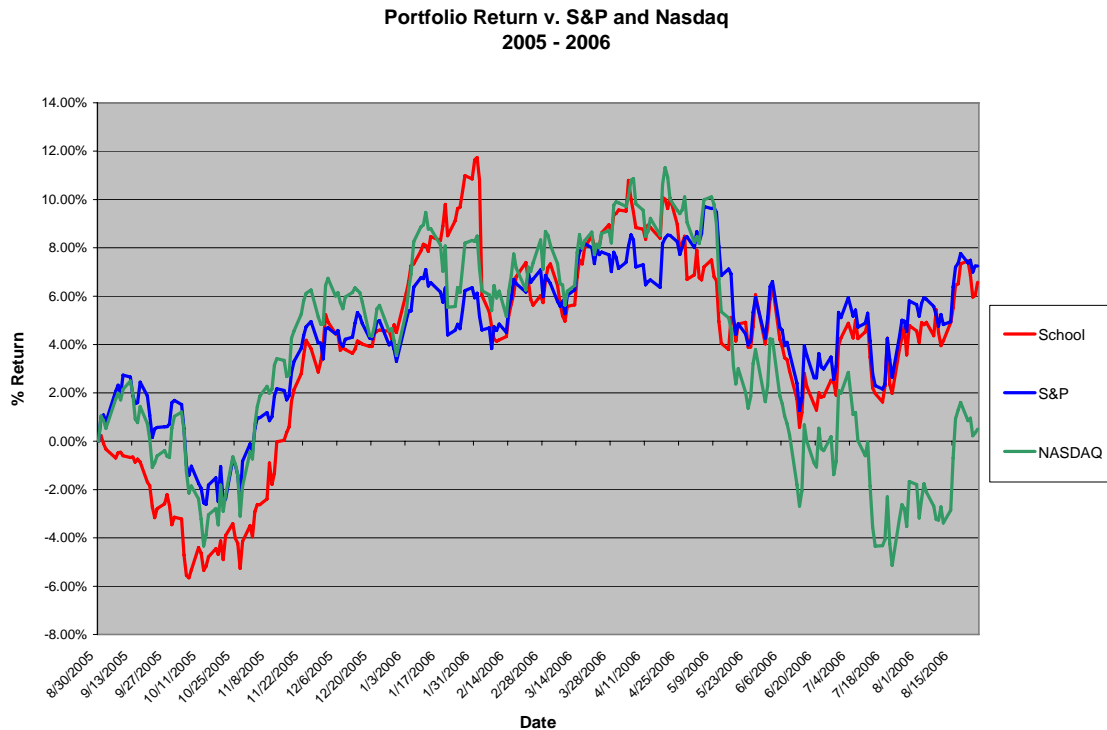
In general, our decisions to sell in the Davidson and Milner portfolios were good: most of the stocks we sold are currently trading at prices below our sales price. With the exception of Harris & Harris (TINY), the inherited stocks we retained have performed well. In the first part of the year, we purchased and then sold some of our best performing investments, including stock in E-Diet, Seagate Technology, and Aeropostale. Most of our underperformance comes from the stocks we purchased beginning in mid-February after abandoning our small stock focus. Including initial

transaction costs, we have unrealized losses of \$2,665.21 on three large firms, Intel, WalMart, and Advanced Micro Devices.

SCHOOL PORTFOLIO PERFORMANCE

Overall performance

From the date we assumed control of the funds, the School portfolio gained 6.58% (valued on August 25) as compared to the S&P 500, which yielded 7.25% and the NASDAQ index, which returned 0.49%.



Individual stock performance

School portfolio						
Ticker	Date inherited or acquired	Initial price	Date sold or valued	Final price	Dividends	Gross return
Inherited stocks						
MSFT	30-Aug-05	27.18	24-Aug-06	25.74	0.350	-4.0%
AMC	30-Aug-05	15.60	24-Aug-06	16.90	1.900	20.5%
Acquired stocks						
FOSL	19-Oct-05	16.00	24-Aug-06	17.23	0.000	7.7%
SNIC	19-Oct-05	18.50	9-Nov-05	15.53	0.000	-16.0%
STX	3-Nov-05	15.54	24-Aug-06	20.41	0.240	32.9%
MTX	28-Nov-05	55.91	24-Aug-06	50.88	0.100	-8.8%
DE	30-Nov-05	69.27	24-Aug-06	73.27	1.170	7.5%

Transaction summary

School Portfolio					
Ticker	Number of Shares	Inherited Price	Purchase Price	Sales Price	Current Price (Aug 25)
Stocks we sold					
SNIC	100	N/A	18.50	15.53	14.545
Stocks we hold					
MSFT	200	27.18	N/A	N/A	25.85
AMC	300	15.60	N/A	N/A	16.87
FOSL	200	N/A	16.00	N/A	17.58
STX	100	N/A	15.54	N/A	20.56
MTX	50	N/A	55.91	N/A	50.83
DE	35	N/A	69.27	N/A	73.89
COP	62	N/A	62.73	N/A	66.30

The school fund, which is focused on long term growth, outperformed the other two funds this year. Over the academic year, the S&P outperformed the NASDAQ index, so it is not surprising that this fund did better than the two funds more focused on small cap stocks. We would have been better off selling Seagate in this portfolio at the same time as we sold Seagate in the other two portfolios.

PRESENTATIONS TO PROFESSIONALS

In January 2001, the University of Utah Student Investment Fund made its first presentation to members of Utah’s business and investment community. Dick Pratt, Chairman of Richard T. Pratt Associates, hosts what has become a biannual event. The presentations give the Student Fund Managers the opportunity to prepare and deliver stock market recommendations to a highly respected professional audience and to receive feedback on their work.

Cabot Oil and Gas

On February 7, 2006, a team comprised of student managers for the Fund presented an equity analysis of Cabot Oil and Gas (COG:NYSE) to local business leaders and other distinguished guests. COG is an independent explorer and producer of natural gas and crude oil and also sells brokered natural gas. Those professionals in attendance included Brad Baldwin of Commerce CRG, Dave Broadbent of Ivory Homes, David Carlebach and Jean Perschon of Goldman Sachs, Paul Dougan of Equity Oil Company, Art Lipson of Western Investments, Brent Maxfield, formerly with KPMG, Jill Mortensen, Rex Thornton, and Greg Thornton of D.A. Davidson, Rich Potashner of Merrill Lynch, Dick Pratt and Ramona Stromness of Richard T. Pratt Associates, John Scowcroft and Amy Sunderland of Wasatch Advisors, Seth Shaner of Finch Capital, and Devin Thorpe and

Don Rands of Thorpe Capital, John Lunt of Lunt Capital, and Ruth Novak, formerly with Hercules.



The student managers recommended a buy at \$48.50 per share. The team felt that Cabot Oil and Gas was undervalued with respect to competition on three premises. First, the market had not fully accounted for the flexibility in the capital structure of COG. Second, the market had not fully valued management's ability to add value to shareholder's through investment. Finally, Cabot's positioning in the Eastern United States and Canada created economic barriers and new opportunities that were not fully priced into the stock.



Moreover, the team believed that Cabot was a strong company in a strong industry. The energy sector had led the market in 2005 due to increasing oil and gas prices. Still, the team believed, imbalances in supply and demand and a residual optimism that prices would retract left gas prices below equilibrium levels.

Strong companies in the industry would benefit from the ensuing price correction. The team targeted Cabot as a strong company based on four characteristics: solid financial records, a clean balance sheet, a healthy reserve replacement ratio, and a history of shareholder-friendly cash allocation. The management team at Cabot Oil and Gas has shown that the company has these characteristics and is capable of maintaining them.

Our investment decision was based on a one-year holding period with an exit price target of \$65.30 per share. This conclusion was supported by the price to cash flow and price to earnings multipliers that showed COG was undervalued against close competitors. Furthermore, the discounted cash flow analysis lead to a similar conclusion. COG closed at \$54.87 on August 25, 2006, more 13% higher than when the buy recommendation was proposed.



The presentation provided an excellent opportunity for all student managers of the Fund to recognize mistakes made during the analysis. Discussion was very constructive and the informal time following the presentation provided the student managers with a unique occasion to meet with the professionals.

E-Trade Financial Corp.

On March 21, 2006, the 2005-2006 University of Utah Student Managed Portfolio presented a full stock analysis of E*Trade Financial Corp. to a number of top local business professionals. Professional participants included Nick Bapis, David Broadbent, Paul Dougan, Fred Fairclough, John Lunt, Brent Maxfield, Rich Potashner, Dick Pratt, Tom Rugh, Greg Schow, Jon Shear, Karen Shepherd, Rex Thornton, Greg Thornton, Devin Thorpe, and Bill Wirthlin.

The students concluded that E*Trade was overvalued and recommended that investors should short sell E*Trade. An alternative strategy they advocated was to purchase the July 2006 \$25 put contract for \$1.30. In order for the investor to make a profit, E*Trade stock price would need to fall \$2.64, or 10% to \$23.69, by July 2006. Their analysis was based on the following observations as of March 16.

- E*Trade is changing its business model and becoming more of an online banking institution as opposed to an online brokerage. The primary source of its revenue has switched from brokerage commissions to net interest income.
- Although the number of online investors and trading volumes are expected to grow in the near future, due to the competitive pricing structure in the industry, the trend of decreasing average commission revenue per trade will continue.
- E*Trade Financial Corporation is currently overvalued. Based upon the assumptions and facts outlined in the discounted cash flow analysis and multiples comparison, we determine a fair value for E*Trade to be \$20.60 per share. At the close of trading on March 16, 2006, E*Trade was priced at \$26.33, which would represent an inflated value of 21%.

On July 21, the last trading day for the July options, E*Trade closed at \$21.95. Ignoring transaction costs, a short position would have earned a 17% return, and a put would have earned a return of 135%.



In addition to a 30 minute presentation, the group wrote up a full-length stock analysis of the company. After the student presentation, Nick Bapis and Dick Pratt provided some commentary on the analysis followed by a general question and answer session. In general, the professional audience counseled the students to be wary of the strategy of shorting a market leader in a rapidly growing industry.

R.I.S.E CONFERENCE

From March 30 to April 1, 2006, eleven students from the Student Investment Fund attended the Redefining Investment Strategy Education (R.I.S.E.) Conference. The R.I.S.E. Conference took place at the University of Dayton in Dayton, Ohio. This was the sixth year the global investment forum met, bringing leading students, faculty, and Wall Street experts together in an interactive learning environment, to discuss a range of pertinent issues facing tomorrow's leaders in finance.



R.I.S.E. VI included keynote presentations by a group of internationally renowned industry leaders, including Richard Bernstein (Merrill Lynch), Dr. Bob Froehlich (Deutsche Asset Management), Elaine Garzarelli (Garzarelli Research, Inc.), Jim Rogers (author of Adventure Capitalist), and many others.

There were 15 specialized breakout sessions focusing on a range of investment and academic program development related issues and security analysis. Other offerings included portfolio management workshops and five different career strategies forums. The R.I.S.E. conference was a great learning opportunity, contributing to the Fund's future performance.



INVESTMENT CONFERENCE

On Friday, April 14, we hosted a conference for students participating in investment funds at Westminster, Weber State, Utah State, and BYU. Students from each school made a brief presentation on their fund's organization and on their school's investment philosophy. Three U of U alumni who work in finance spoke at the conference. Karey Barker described her experience in asset management, Jono Gardner spoke about working in investment banking in New York, and Gary Beynon described a variety of real estate-linked investments. We provided lunch to all of the participants. The speakers were excellent and the conference allowed us to interact with students from around the state.



Karey Barker is a member of the Board of Directors of Wasatch Advisors, Inc. and is a Portfolio Manager for Wasatch Small Cap Ultra Growth portfolios. Ms. Barker joined Wasatch Advisors in 1989. She graduated magna cum laude from the University of Utah with a Bachelor of Science in Finance. She also studied French and International Economics

at the Universite d'Angers in France and later obtained a Bachelor of Arts, with honors, in French from the University of Utah. She earned the right to use the Chartered Financial Analyst designation and is a member of the Salt Lake City Society of Financial Analysts.

Gary Beynon is the Chairman and CEO of OMNI Brokerage, Inc. a broker dealer specializing in direct participation private investment offerings. OMNI is a leading resource of tenant in common (TIC) properties for investors looking to complete a 1031 exchange. Prior to founding OMNI, Mr. Beynon spent 20 years sponsoring private real estate investments to affluent investors. Mr. Beynon has been selected to speak as a TIC industry expert at events and conferences and has been featured in local, regional and national publications. Mr. Beynon received a Bachelor of Arts degree and a Masters in Business Administration from the University of Utah.





Jonathan S. Gardner is a Partner at Gardner Development Company. Mr. Gardner joined Gardner Development in March of 2005. He is responsible for managing all land acquisition, development, construction and financing. Since joining 12 months ago, he has increased the pipeline to over \$300,000,000 of project value. Prior to joining Gardner Development, he spent nearly four years at CIBC World Markets' Private Finance Group. At CIBC he focused on the placement of senior and subordinated private debt for middle market companies. Prior to this, he focused on placing private equity and venture capital. Mr. Gardner graduated from the University of Utah's David Eccles School of Business in 2001 with

his BS in Finance.

SPEAKERS and FUND EVENTS

Brian Ledbetter and Jessica Rose

August 30, 2005

Fund Alumni

Topic: History and Advice

Ryan Snow

September 20, 2005

Portfolio Manager, Wasatch Advisors

Topic: Evaluating Stocks

Investment Fund Reception

September 13, 2005

Honoring Hal Milner and D.A. Davidson & Co



Dana Sowby

October 4, 2005

Associate Director, U of U Career Services

Topic: Finding a Job

Rex Thornton and Greg Thornton

October 25, 2005

D.A. Davidson & Co.

Topic: Understanding the Market

Presentation to Professionals

February 7, 2006

Topic: Cabot Oil & Gas

Hal Milner

February 21, 2006

Topic: Business Ethics and Life Lessons



Presentation to Professionals

March 21, 2006

Topic: E*Trade

KCPW Broadcast

March 27, 2006

Investment Fund managers Steve Smith and Curtis McEntire, advisor Liz Tashjian, and supporter Dick Pratt

Topic: Educational benefits of the Student Investment Fund

Rich Potashner

March 28, 2006

Merrill Lynch

Topic: Fixed Income Investing

Fred Dixon and M. E. Rhoades

April 4, 2006

D.A. Davidson & Co.

Topic: Market Trends and Stock Selection

Utah Student Investment Fund Conference

April 14, 2006

Speakers: Karey Barker of Wasatch Advisors, Gary Beynon of OMNI Brokerage, and Jono Gardner of Gardner Development Company

Participating Schools: University of Utah, Brigham Young University, Utah State University, Weber State University, Westminster College



ACKNOWLEDGEMENTS

We would like to thank the speakers who spent time sharing their advice and insights with the class. The professionals who attended our presentations provided extremely useful feedback and inspired us to work harder. Thanks to Dick Pratt for sponsoring our presentations. Hal Milner generously gave each of us a copy of Tom Friedman's book, *The World is Flat*. We are especially indebted to D. A. Davidson & Co. and to Hal Milner for making the funds available for us to invest.

We would also like to thank those who provided financial contributions to support the 2005-2006 Student Investment Fund.

- David Eccles School of Business
- D. A. Davidson & Co.
- Hal Milner
- Baltimore International Trading Company
- ASUU