The Prudent Investor

December 6, 2007

Performance Overview

For the month of November the Model Stock Portfolio lost -10.9% versus a loss of 4.2% for the S&P 500 index (including dividends). This represents a loss of –6.7% over the S&P 500 index for the month. Table 1 shows the Model Stock Portfolio monthly and annual returns since January 2003. Year-to-date the model is down –25.0% versus the S&P 500 index's total return of 6.4%.

Table 1: Model Stock Portfolio Returns[1]

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	TPI Total Return	S&P 500 Return
2003	0.5%	1.2%	4.1%	9.5%	9.8%	6.9%	3.5%	(0.9%)	2.7%	19.2%	8.8%	8.8%	102.3%	28.7%
2004	1.4%	9.7%	3.1%	(7.6%)	1.6%	6.3%	1.7%	1.8%	5.3%	(2.2%)	11.5%	5.6%	43.7%	10.9%
2005	4.1%	2.1%	(6.3%)	(2.3%)	7.1%	6.6%	3.6%	(4.7%)	(3.0%)	(3.2%)	5.3%	2.8%	11.3%	4.9%
2006	6.6%	(3.5%)	3.4%	0.1%	(2.8%)	2.2%	(2.8%)	3.3%	1.4%	9.1%	3.0%	2.7%	24.2%	15.8%
2007	3.3%	(1.0%)	0.1%	7.7%	6.9%	(2.1%)	(18.2%)	(11.0%)	0.4%	(0.2%)	(10.9%)		(25.0%)	6.4%

Market Valuation Update

Using our modified Fed Model to gauge the fair market value of the stock market, we estimate that the market is currently undervalued relative to bonds by 35.1%. This suggests a relatively strong buy signal for stocks. See our website at www.PruInvestor.com for more information on the Fed Model.

Model Stock Portfolio

The Prudent Investor's Model Stock Portfolio for the current month is presented in Table 2. On January 1, 2005 the model was reset to equal to $50,000.

In Table 2 the column entitled "Target Ownership" represents the ideal percentage investment of each asset in the model portfolio. The Actual Ownership column (far right) represents the model's actual ownership from month to month of each stock. The two are not always identical because we take into consideration trading costs when reallocating the portfolio each month. In general, we do not adjust the allocation until the size of adjustment for any given security exceeds 2% of the total portfolio size. The Target Ownership also differs from the Actual Ownership column because we cannot buy fractional shares of a security to meet the Target Ownership percentages.

Starting a Portfolio: If you are just getting started, we recommend that you purchase all the securities in Table 2, using the Target Ownership column to calculate the number of shares needed for each security. If you do not have at least $50,000 available for investment purposes, you may wish to follow one of the Asset Allocation Models presented below and purchase mutual funds instead of individual stocks.

If you have less than $50,000 to invest but would still like to follow our Model Stock Portfolio, consider the following alternative strategy: Purchase the top 10 ranked stocks shown in Table 2 (with approximately 10% of your total invested in each stock) and hold each stock until it falls off of Table 2. Then replace the stock you sell with the highest ranked new stock in the table. This strategy will be more volatile than purchasing all the stocks in Table 2, but investment returns should be similar over time.

[1] Monthly returns for the Model Stock Portfolio for years 2003-2004 represent actual (unleveraged) returns, after all trading costs.

Table 2: Model Stock Portfolio

Rank	Stock	Current Price on 11/30/07	Target Ownership 11/30/07	Required Adjustment	Shares Owned on 11/30/07	Actual $ Ownership 11/30/07	Actual % Ownership 11/30/07
1	AMSF	15.26	4.9%		155	$2,365	4.6%
2	AOB	11.7	4.9%		165	$1,931	3.7%
3	AYR	26.42	7.1%		85	$2,246	4.3%
4	CSE	16.76	8.1%		230	$3,855	7.4%
5	CVO	20.56	3.0%	(65)	75	$1,542	3.0%
6	DAL	19.76	4.8%		125	$2,470	4.8%
7	FCX	98.93	6.1%		25	$2,473	4.8%
8	HLX	40.59	8.1%		90	$3,653	7.0%
9	HWK	16	3.9%		160	$2,560	4.9%
10	IOSP	17.56	6.2%		125	$2,195	4.2%
11	KALU	71.14	5.1%		35	$2,490	4.8%
12	NGPC	14.67	7.0%		220	$3,227	6.2%
13	NTRZ.OB	0.85	8.1%		1,400	$1,190	2.3%
14	PCAP	10.72	6.3%		200	$2,144	4.1%
15	PRS	6.39	0.0%	(400)	0	$0	0.0%
16	PSEC	14.02	6.0%		200	$2,804	5.4%
17	ROSE	18.3	5.8%		180	$3,294	6.4%
18	SUAI	6.00	0.0%	(400)	0	$0	0.0%
19	SUMT	4.82	4.6%		470	$2,265	4.4%
20	ZZCASH	1.00	0.0%	6,293	9,151	$9,151	17.6%
			100%			***$51,855***	***100%***

The adjustments to our Model Stock Portfolio this month are shown in Table 2. If you do not have low trading costs (i.e., brokerage commissions), you may wish to forego any incremental adjustments for stocks already in the portfolio. Most of them are made in keeping with our 2% rule where we will buy or sell shares once the "Target Ownership" is greater or less than 2% of the "Actual Ownership."

If you would like to follow our monthly Model Stock Portfolio, but do not wish to manage your funds yourself, please contact us. We can put you in touch with a registered investment advisor who can manage your investments for you. They will be able to take into consideration your specific tax situation when making buy/sell decisions that are recommended in this newsletter.

Asset Allocation Model

Table 3 below shows *The Prudent Investor*'s recommended asset allocation for three model portfolios.[2] These portfolios represent a solid diversified investment strategy for an investor. Suggested mutual funds are listed in the table for you to purchase. However, you may wish to substitute any or all of these funds with other funds of your preference in the same asset class. Most mutual funds within the same asset class (e.g., "Large Cap" class) have very similar returns over longer periods of time.

Note: If you follow the Model Stock Portfolio published in this newsletter each month, you may wish to use one of the Asset Allocation Models below to determine your equity/fixed-income ratio for your overall investment portfolio. Then, instead of purchasing the suggested equity mutual funds given in Table 3, you can merely purchase all the stocks in the Model Stock Portfolio shown in Table 2. This

[2] *You may wish to adjust the asset allocation of your portfolio on a quarterly basis rather than monthly. In most cases this will have only a small impact on total returns. This newsletter does not take into consideration the potential tax implications of more frequent rebalancing. For retirement accounts, tax consequences from more frequent trading are not a concern.*

substitution is not a one-to-one match with respect to diversification, but it should be sufficient to give you at least a moderately diversified stock portfolio with attractive upside potential.

Conservative Portfolio:

- **Best For:** This asset allocation is appropriate for investors who are looking to participate in the stock market but who are risk adverse. Investors nearing retirement age may wish to consider this allocation, as well as those saving for college or for a house purchase within five years.
- **Fair Value Allocation:** When the stock market is considered to be at "fair value," the Conservative Portfolio will have a 60%/40% equity/fixed-income split.
- **Current Allocation:** Based on current market conditions, the suggested equity/fixed-income allocation is 78/22.

Moderate Portfolio:

- **Best For:** Appropriate for investors who are willing to take more risk in the stock market in order to seek a higher long-term total return. Investors who are further from retirement will find this portfolio suitable to their needs. It also is recommended for investors who have under $100,000 to invest in stocks and bonds.
- **Fair Value Allocation:** When the stock market is considered to be at "fair value," the Moderate Portfolio will have a 75%/25% equity/fixed-income split.
- **Current Allocation:** Based on current market conditions, the suggested equity/fixed-income allocation is 93/7%.

Aggressive Portfolio:

- **Best For:** Appropriate for investors who have a high tolerance for enduring market fluctuations and who seek above-average returns over the long term. Investors who are further from retirement will find this portfolio suitable to their needs. Only investors who have in excess of $100,000 to invest, and who are not close to retirement, should consider this asset allocation.
- **Fair Value Allocation:** When the stock market is considered to be at "fair value," the Conservative Portfolio will have a 90%/10% equity/fixed-income split.
- **Current Allocation:** Based on current market conditions, the suggested equity/fixed-income allocation is 125%/0%. (A number greater than 100% for equities means the portfolio will be leveraged.)

Table 3: Asset Allocation Models

Category	Mutual Fund Symbol	Mutual Fund Name	Conservative Portfolio		Moderate Portfolio		Aggressive Portfolio	
			"Fair Value" Target	Current Target	"Fair Value" Target	Current Target	"Fair Value" Target	Current Target
Percentage in Equities			**60%**	**78%**	**75%**	**93%**	**90%**	**125%**
Large Cap	RSP	Rydex S&P 500 Equal Weight	15.0%	19.4%	18.8%	23.1%	22.5%	31.3%
Mid Cap	VIMSX	Vanguard Mid-Cap Index	12.0%	15.5%	15.0%	18.5%	18.0%	25.0%
Small Cap	VISVX	Vanguard Small-Cap Value Index	18.0%	23.3%	22.5%	27.8%	27.0%	37.5%
REITS	VGSIX	Vanguard REIT Index	6.0%	7.8%	7.5%	9.3%	9.0%	12.5%
International	VEIEX	Vanguard Emerging Markets Index	9.0%	11.6%	11.3%	13.9%	13.5%	18.8%
Percentage in Fixed Income			**40%**	**22%**	**25%**	**7%**	**10%**	**0%**
Long Term Bonds	VBLTX	Vanguard Long-Term Bond Index	10.0%	5.6%	6.3%	1.9%	2.5%	0.0%
Medium Term Govt	VIPSX	Vanguard Inflation-Protected Sec.	20.0%	11.2%	12.5%	3.7%	5.0%	0.0%
High Yield Bonds	VWEHX	Vanguard High-Yield Corp.	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
International Bonds	FNMIX	Fidelity New Markets Income	8.0%	4.5%	5.0%	1.5%	2.0%	0.0%
Cash (Money Market)	VSGBX	Vanguard Short-Term Federal	2.0%	1.1%	1.3%	0.4%	0.5%	0.0%

From the Editor's Desk

Investment Conundrum

Well, the "R" word is finally in the mainstream media. Talk of recession is now becoming more popular, if "popular" is a fitting word for something so unpopular. In a recession, one generally would be better off in cash and fixed income than in stocks. That would seem like a logical move now if that is indeed where we are headed. But what about the Fed Model that we've discussed many times in this newsletter? As of the end of November, it was suggesting a stock market that is ***undervalued*** by 35%. That's the lowest we've seen in a very long time. By itself, the Fed Model would sound like a screaming "buy!"

Granted, one could argue that the Fed Model is distorted right now because the US Treasury market is a bit out of whack. With 10 year Treasury Notes now yielding under 4%, one could argue not that the stock market is cheap, but that Treasury Notes are expensive (giving a correspondingly low yield).

So is it time to buy with gusto or sell and sit on some cash? Our emotions tell us that it may be time to take some money off the table, especially until we can start to see a true bottom to the credit crunch and related deteriorating housing market. When things are the worst, that is the time to jump in as an investor with boldness, because the markets have usually hit bottom at that point. And yet, that is the very hardest time to invest.

As we have said in the past, it's best to stick to your investment discipline and not try to time the market, even when everyone is so sure that the "r" word is coming. That means continue to take advantage of market dips to add to your investment portfolio. However, now is definitely not the time to take any risk with funds that may be needed in the next one to three years. Park those funds in a good money market and sleep well at night.

Tax Loss Selling

December is a busy month for tax-related selling. Stocks that are down on a year-to-date basis are easy targets for selling before year-end in order to capture a tax write-off. Microcap stocks like NTRZ can especially be hit hard because it doesn't take many sellers to swing the stock price. This is a stock that we think is time to remove from our portfolio, but we'll probably wait until at least January to give it a chance to recover from tax-loss selling pressures. The company has a great story, but management has not yet proved they can steer the company to profitability as they grow. Though we plan to sell this one early next year, we may be buyers again if management does a good job in delivering robust earnings in 2008.

Pausing for '08

At present your editor of *The Prudent Investor* has made no plans to continue the newsletter in 2008. This may not be a permanent decision, but as you can certainly understand, the time demands of a newsletter can be considerable at times, and as a free service it is hard to justify the effort some months. We would prefer to end on a strong note, but alas our second half of 2007 has been very weak. This is not the motivating reason for hibernating the newsletter, for we still believe very strongly in the investment strategy we follow of letting corporate insiders guide our stock selection.

For those of you who currently own one or more stocks in our Model Stock Portfolio, we would like to offer some guidance on when to successfully exit those stocks in 2008. If you would like to receive notice on when to exit the individual stocks in our model, please email info@pruinvestor.com and we will make arrangements with you to keep you informed on when each stock no longer passes our criteria for owning.

SMI

We'd like to suggest our readers consider subscribing to a faith-based newsletter called *Sound Mind Investing* (SMI). SMI has an excellent track record for investment recommendations that have consistently beat the overall stock market for the past 10+ years. They do not purchase individual stocks but instead recommend mutual funds. It's a simple strategy to follow and one that takes only minutes each month to implement. As a bonus, the newsletter is full of excellent advice on money management from a Christian perspective.