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**HOW WE MAKE  
DECISIONS ABOUT  
INVESTING OUR  
CLIENTS' MONEY**

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**Quote of the Quarter**

*“Over the long term, earnings and confidence in earnings move valuations and the markets. We are seeing indications of improving earnings and improving confidence.”*

**Godsey & Gibb  
Investment Research Group**

**What criteria do we use in deciding how to invest our clients' funds? We'll take a look at the “top” of the process, the “bottom” of the process, then we'll put it all together for you.**

**G**odsey & Gibb's primary mission is to protect the wealth you've worked so hard to accumulate. We also want to increase the probability that your money will grow, enabling you to create additional wealth to accomplish your life goals.

We view stocks as part of a portfolio, not as individual components. With this view in mind, we work to structure a diversified portfolio of stocks for our clients, to mitigate overall risk by owning a number of carefully selected companies in a broad cross section of industries that strictly meet our criteria and style requirements.

How do we do this? What is the process we use? We approach our choice of companies from two directions. First, from a macro view of economic strengths and weaknesses, called a “top down” approach. Second, from the more micro view of selecting specific companies that are appropriate for your portfolio, which is called the “bottom up” approach. Let's take a brief look at each.

**Top Down – The Economic View**

The first step in our analysis consists of studying the economic indicators and formulating a view of the economic environment, analyzing directional trends and the magnitude of growth. Next, we study the market indicators that provide the primary forces of strength in the markets. After we have assessed the economic backdrop and market environment, we study price strength and movement within the S&P's Defined Business Sectors, and the industry groups within those sectors. This process provides a guide to asset allocation and appropriate weighting within those industry sectors.

**Bottom Up – Specific Stock Selection**

We begin the stock selection process by examining a universe of the leading 1000 businesses contained in the S&P 500, S&P 400, and the NASDAQ 100. We then apply a filter to this list. We screen based on a cross section of leading fundamental, business, valuation, and market criteria. This narrows the focus to about 100 companies. We analyze each of those companies in depth. We look at the individual businesses, focusing on favorable or improving business conditions. We search for rising or improving earnings and analysts' estimates. We make a “reasonable price” evaluation, and we monitor the trend of the technical measures. We study business and price risk on a continual basis. This is how we develop a guide for selecting individual stocks that make up our portfolio.

## Putting It All Together

We take all the information we've gathered from our "top down" and "bottom up" approaches and we develop a portfolio of companies with strong characteristics such as:

- Favorable or improving fundamentals
- Rising or improving earnings and estimates
- A reasonable price for purchasing the security

Most importantly, we continuously monitor the portfolio's performance. We use a number of criteria including the following:

- Past earnings performance
- Current earnings growth
- Expected future earnings growth
- Market capitalization
- The company's financial rating

We do provide for exceptions to these criteria, but these determine our "core" positions.

## When Is It Time to Sell?

Our objective is not only to protect the wealth you've already accumulated, but also to maximize the probabilities your current wealth will create even greater wealth. To this end, there can be both desirable and less desirable reasons to sell a stock.

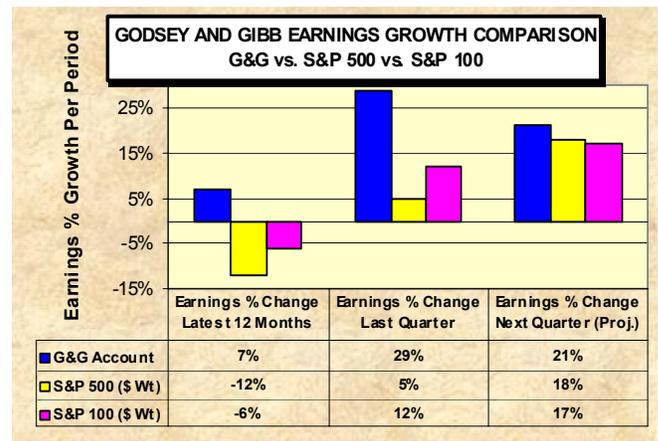
There are times, especially in an "up" market, that a stock's price may run too high, too fast. A rising price is generally good, but price appreciation that occurs too rapidly can increase holding risk beyond acceptable levels. Prudent actions in such a case would include trimming or reducing the size of the position to lower the extended price risk and lock in some of the profits. That is a desirable reason to sell.

Sometimes a company simply does not perform as well as expected, creating a less desirable reason to sell. How do we decide when it's time? We strongly believe that positive earnings are important. If a company warns that earnings or revenue will be significantly less than estimated or experiences negative earnings revisions, this would prompt a review of the company, which may result in the removal of its stock from client portfolios.

Even if the company has been doing well, the sustainability of that growth (or of its industry group) may come into question. One of the criteria we use for selection may change. The company may announce a merger, an acquisition, or a divestiture that could change its direction, vision or goals and thus, the expectations we had at the time of purchase.

Changes in the long-term fundamentals of the company, causing lower earnings, revenue, and price prospects than originally expected could also be considered selling criteria. Negative relative performance compared to a market index like the S&P 500 with no apparent negative news is a warning sign as well.

By monitoring our portfolios on a continual basis, we evaluate such events as they occur and we eliminate a position as soon as our selling criteria have been met. This process allows us to make our best efforts at eliminating further risk and maintaining the strength of the overall portfolio.



## Conclusion

To sum it up, we build our clients' portfolios of securities using the strict guidelines and parameters of our investment discipline. Our goal is to structure a diversified portfolio of high quality securities with strong fundamental characteristics. The performance of the portfolio is continuously monitored and securities are removed when sell criteria are met. By strictly adhering to these disciplines, we aim to protect the wealth our clients have accumulated and increase the prospects for its further growth.

This analysis is from proprietary sources and is not an offering to buy or sell securities. All charts are proprietary unless otherwise noted.