

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

International Equities at Bargain Prices



PAUL SUTHERLAND, Chairman

Paul Sutherland has worked in the investment and financial advisory business since 1975. As a Senior Portfolio Manager, he has been managing global total return investment portfolios (under the "investing without borders" style) for more than 25 years. In 1984, Mr. Sutherland formed the Financial & Investment Management Group, Ltd. (FIM Group) – a Traverse City, Michigan-based registered investment adviser that manages investment portfolios on a discretionary basis for individuals, trusts, foundations and retirement plans. He currently serves as the company's President and Chief Investment Officer.

Beyond his extensive investment experience, Mr. Sutherland is the author of numerous books on financial planning and money management, including *The Virtue of Wealth*, *Creating Life Success the Zenvesting Way*, *Zenvesting: The Art of Abundance & Managing Money*, *12 Steps to a Care-Free Retirement* and the *AMA Guide to Financial Planning*. Mr. Sutherland began his

writing career in 1979 with an article on international investing that was published by *Physician's Management Magazine*. Over the past 27 years he has had academic and consumer articles published in magazines, newsletters and other publications on subjects such as benchmarking global portfolios, asset allocation, retirement investing, income investing, forecasting and global investing. His work has been published in *Business Ethics*, *Financial Planner*, *Dental Management* and *NAPFA News*. He is a regular columnist for *Spirituality & Health* magazine and has been interviewed by *Bloomberg News*, *Barrons*, *The Wall Street Journal*, *The Wall Street Transcript*, *Investors Business Daily (IBD)*, *Investment News*, *Money Magazine* and others.

Mr. Sutherland received his M.B.A. from Lake Superior State University. In addition, he is a Certified Financial Planner and has completed the College of Financial Planning's Advanced Studies Course: *Investment Strategies and Portfolio Management*.

Individuals and corporations from across the United States have sought his advice on estate and tax planning, retirement and investment management. He has spoken to professional groups nationally and internationally – including Singapore, Beijing, Sydney and Toronto – on topics such as international investing, investment economics and portfolio management.

Mr. Sutherland is Co-founder of the Children of the World Foundation, past Chairman of the Traverse City Rotary Club's World Community Service Committee, past Chairman of Safe Passage and current board member, as well as Founder and Chairman of the Board of the Utopia Foundation.

SECTOR – GENERAL INVESTING

TWST: Please start with a brief overview of your firm and your investment philosophy.

Mr. Sutherland: FIM Group became 25 years old this year, so we've been around a while. We've always been global money managers. We primarily work for individuals and trusts, retirees, entrepreneurs, business people and regular folks that have accumulated some wealth. Most all of our clients live in the U.S. As investors we believe price matters, and that we look to make sure our portfolios are full of sustainable investments that are risk-adjusted bargains. We believe that it's appropriate and important to be proactive and forward-looking

in order to spot trends. For example, it's obvious that the world is no longer dominated by the United States from an economic point of view. We think that the U.S. will probably be stable in its GDP while significant growth will happen over the next 10 or 15 years in emerging countries that become strong, sustainable economic powers in their own right.

Consider Singapore, China, emerging Europe, emerging South and Central America, and India. It is obvious that these countries are no longer dependent on America, Europe or the developed dominant countries of old, and realize that they can acquire the necessary technology and skills to be hyper-competitive without help from the U.S. and developed world. That's a huge shift for U.S. investors but most

still seem stubbornly domestically oriented. That's never been the way we've managed money. Rather, we've managed money on a global basis, not caring where a company's home office was located. Naturally you have to be forward-looking and look at business practices, government regulations, currencies and cultures in any country you invest in. I think indexing is a loser's strategy. That's why most investors fail. Accepting the mediocre oriented indexing or benchmarking silliness is why people don't often meet their goals. They don't hire money managers with any significant track record of success. They hire them off a brochure or a great telephone pitch. We've been around a long time, and our clients are happy because we've kept our forward-looking orientation as well as a global view.

TWST: There was a lot of talk about decoupling several years ago, and then the global markets crashed following the United States and there was no more talk of decoupling. But now the global markets are all doing very well and even better than the United States. What are your views on that?

Mr. Sutherland: The whole idea of decoupling is kind of like saying, "You know what, everybody's stock market went down, so therefore the markets are in sync. Everybody's stock market went up, so therefore markets are in sync." All you have to do is take a common-sense look at what has happened this year with the performance of the world markets. With the currency adjusted to date, the Dow Jones was up about 17% as of last night, whereas the Hong Kong market was up 56%. So surely both went up, but Hong Kong nearly tripled the U.S. market. Often people want to oversimplify and believe the U.S. market affects all other markets, but the Dow Jones EURO STOXX 50, which is comprised of the larger European companies, was up significantly more than S&P or the Dow. Naturally within those groups, there is significant growth in certain sectors. We believe that it is rational to invest in areas where we think the excess is going to be and not in areas that are going to do poorly. So the countries that have a lot of finance and insurance companies haven't had a very strong recovery this year. The companies that are really building wealth, however, are involved in other areas and have had a pretty good year. Decoupling, I think, is oversimplifying a complex subject, and I think people need to examine investments much more closely. Chatting about decoupling or throwing darts at indexes is a way for mediocre investors to justify their mediocre performance.

TWST: One of the main features of the last 12 months has been the extreme swings of volatility in the market at home and abroad. How does that impact your investment?

Mr. Sutherland: We're long-term investors; any common sense-oriented, realistic, long-term investor has to embrace the fact that there is going to be volatility in their portfolio. We tell the clients that hire

us that they should have a minimum of about a four-year commitment to our portfolio strategy. Any investment manager who says that they can provide very long-term returns without volatility is probably not being as straightforward as they could, or else they are extremely naïve. The reason that longer-dated investments like stocks or long-term bonds or corporate bonds tend to have better long-term performance is because they are volatile and, especially in times like now, people are addicted to having their capital not fluctuate. That's why you see Treasury bills and CDs and short-term money market instruments near 0%. That's because people want no volatility. But what investors often don't realize is that to achieve their goals you have to worry about inflation, which could be quite significant in the future. You also need to make sure that your portfolio is growing, so that you can retire at 65, not 90. Investors have to embrace that volatility is going to be a side effect of good long-term performance.

TWST: Did volatility bring about some great bargains in the stock markets that you snapped up?

Mr. Sutherland: Yes, naturally. The key is that, with investing,

you need a long-term time horizon. As long as people want to be happy and as long as people don't want to suffer, there will be economic activity. Teachers are still going to teach, bakers are still going to bake bread and people are still going to drive, so there's always going to be economic activity and profits to capture from that. That creates a huge opportunity for anybody who realizes that basically the sun will come up tomorrow and that the economic systems basically depend on people being involved in activities. As long as they are involved in activities there will be profits to be had, and cash flows from that in exchange of resources. And so the crisis of this last year was one of the biggest buying opportunities of my lifetime. Of course you have to believe in human nature to be able to buy or hold during tough times. I guess you need to be a long-term, optimistic investor. Naturally, I've have had a few other crises to gain profits from, back when we experienced a big currency crisis meltdown in the late 1990s in Asia.

That was also a huge buying opportunity that was very wonderful for us as a global manager. Another was in October 1987, but most money managers were not even born then or not yet graduated from high school, so their experience with crises and crashes has not been very extensive. Successful people will tend to hire people who have a history. Most money managers who have positive track records have been through many crises and realize that those opportunities are significant. At such times you need to back up the truck and buy very good investments in order to have great performance. You can't sit on your hands and wait.

TWST: What are the steps that you take within your investment process? What criteria do you look for? Does the criteria vary in different areas of the world?

Highlights

Paul Sutherland is a long-term investor who identifies global companies selling at bargain prices. This year he was able to purchase many great companies at incredible bargains. Areas that he likes at this time include energy, health care, pharmaceuticals and agriculture. Because of his "investing without borders" philosophy, he also has no market cap bias, no geographic borders and no percentage of an index bias. Areas that he doesn't favor include banking, housing and retail. He believes that every risk has significant opportunity on the other side. He thinks people who invest in general indexes are irrational because they are investing in areas that are going to perform poorly. He prefers to make his investment where he believes there is a reasonable chance of having good returns.

Companies include: Pargesa Holdings; Chunghwa Telecom (CHT); Xcel Energy (XEL); Terna; EDP; Total Produce; Swiss Water Decaf; Lonrho Africa; Cheung Kong Holdings.

Mr. Sutherland: First of all, we want to buy investments at bargain prices. Often there are great companies that we like, but they are just priced really badly. They're just too expensive. It's important that as an investor we must realize that just because a company is great, it doesn't mean it's a great investment. We love great companies, we love companies with great franchises, we love companies that have good management and high ethical standards, that are value-driven and have sustainable businesses. However, we do not want to pay high prices for them. What was wonderful about this last year and even today is

We want to own companies that are sustainable businesses with ethical, honest, talented management and are in good industries.

TWST: What about the composition of your portfolio? Do you invest mostly in large caps?

Mr. Sutherland: No, because of our "investing without borders" philosophy, we have no market cap bias, we have no geographic borders and we have no percentage of an index bias. We own companies that are the largest in their markets, and we own companies that are probably the tiniest in their markets that are public. So we have no real bias toward size.

"Pargesa basically is a holding company with significant insider ownership, and it is involved in energy, water and waste services, specialty materials and building materials. It owns very large chunks of Total (TOT), the large French energy company, as well as Suez energy utility. When you take the value of all of its holdings, you're basically ending up with some very great companies"

that you can buy many great companies at incredible bargain prices. I have a strong bias toward companies that have good balance sheets and appropriate capital structure. One of the first things I do when we identify a company that we think looks interesting is look at its capital structure to make sure it doesn't have too much debt. We also look to make sure that we are not paying too much money for a dollar's worth of earnings, cash flow or profits. Whether the company is really building wealth is another area we look at. It's easy to grow a company that sells \$1 bills for \$0.90. A lot of companies, especially in hot, popular industries, can do that for a while and attract capital, but that's not a sustainable model. You saw that model in the real estate business for the last few years. You also saw

In certain industries, however, a large size makes a difference — for example, in the energy and telecommunications areas. Other areas, like the middle-sized niche software or food companies, can be very, very successful as they grow that niche.

TWST: How diversified are you? How many holdings do you have generally, and does the number fluctuate?

Mr. Sutherland: Yes, the number fluctuates. We tend to own between 50 and 120 positions in a portfolio, depending on how we see the market, how we assess the unsystematic risk constraints of the market or how the market growth looks. We put our portfolios together one at a time. When considering whether or not to include a company

"[Chunghwa Telecom is] Taiwan's main telephone company. This actually does have an ADR in the United States and pays a nice dividend yield. We think that Taiwan is going to have stronger and stronger ties with Mainland China, and that it's a good way to leverage the growth of that area with less risk than you might have investing directly in China."

that model in the Internet business and a little bit in the banking industry. We look at a company very closely to make sure it really is building net worth. We also ask ourselves, "Would common sense dictate that it's an appropriate investment? Would Warren Buffett buy it?" We are very theme-oriented. For example, today we really think that energy is a good area to invest in. We also like health care and pharmaceuticals, as well as agriculture, and we believe that the real action from an economic point of view is going to be in emerging Asia, emerging Europe and Africa, and in Southern and Central America. That's really where the real growth is going to be. The problem is, of course, that we want to buy companies in these sectors, but we have to do a lot of work to make sure we're buying companies at the right price, that the companies are real and that the companies are appropriately valued. But that's part of our process.

in a portfolio, I like to think about it in terms of, "If this were the only company in my portfolio, would I be comfortable with it?" When you have portfolios like ours, it especially gives us a bias toward owning companies that have significant insider ownership. So a lot of companies we own, especially overseas, have significant insider management or ownership by a family or an individual.

TWST: Do you buy foreign companies or are they mostly ADRs?

Mr. Sutherland: We tend to buy wherever it's cheapest. Usually we end up buying in the natural market of the company just because it's cheaper to buy there than to have to pay for ADRs. Also the number of ADRs is very limited. The problem with ADRs, although there are some inexpensive ADRs, is that they often tend to be way overpriced in the emerging market companies.

They go up because people say, “I want to own something in India,” or “I want to own something in Taiwan.” We will tend to go right to the domestic market and buy the shares on behalf of our clients. So it’s just very less expensive, and we don’t want to limit our investment opportunities by dumbing down our portfolios with ETFs or ADRs as a primary conduit to global opportunities.

TWST: Would you tell us about some of the companies you find attractive, exploiting the themes you mentioned and the reasons they were attractive to you?

Mr. Sutherland: Our largest holding is a company called **Pargesa Holdings (PARG.SWF)**. **Pargesa** basically is a holding company with significant insider ownership, and it is involved in energy, water and waste services, specialty materials and building materials. It owns very

1-Year Daily Chart of Xcel Energy



Chart provided by www.BigCharts.com

large chunks of **Total (TOT)**, the large French energy company, as well as Suez energy utility. When you take the value of all of its holdings, you’re basically ending up with some very great companies. Because of the holding company structure, **Pargesa** probably sells for around 20% to 30% less than its breakup value. Since **Pargesa** is a Swiss-based company, there are a lot of other things that have been helpful, like its currency being in Swiss francs, which has been helpful in providing us with some currency returns.

Another company that we like is **Chunghwa Telecom (CHT)**, Taiwan’s main telephone company. This actually does have an ADR in the United States and pays a nice dividend yield. We think that Taiwan is going to have stronger and stronger ties with Mainland China, and that

“We like Xcel Energy (XEL), which has a nice dividend. They are in the Midwest and are really committed to being a wind and energy producer. They also have good management that is very forward-looking. We think that they will grow well in their markets. It’s more of a conservative name that we don’t own in our growth portfolios, but we own them in most of our income-oriented portfolios.”

it’s a good way to leverage the growth of that area with less risk than you might have investing directly in China. We own this company even in our more conservative income-oriented portfolios. We also own some utility companies in Europe and United States.

We own **Terna (TRN.BIT)**, which is an Italian energy company that basically owns the extra-high-voltage grid in Italy and pays out a

very nice dividend, which has grown over time. They’ve got very savvy management and good cost controls, and realize that the energy area is going to be moving more and more toward renewables like solar, wind or hydro. We own **EDP**, which is the largest seller of electricity in Portugal, and they’ve got 10 million customers. They are basically the fourth largest wind energy operator in the world, pay a nice dividend and also own some assets in Brazil, which is another emerging country we like. We like the energy utility area a lot, especially ones that are forward-looking and realize that the world is moving away from coal, and toward wind, solar and hydro.

In the United States, we like **Xcel Energy (XEL)**, which has a nice dividend. They are in the Midwest and are really committed to being a wind and energy producer. They also have good management that I think is very forward-looking. We think that they will grow well in their markets. It’s more of a conservative name that we don’t own in our growth portfolios, but we own them in most of our income-oriented portfolios.

TWST: What companies are exciting to you in that field?

Mr. Sutherland: In agriculture, we own **DuPont (DFT)**, a very large company that pays nice dividends. They have a big seed business and also provide chemicals for that industry. Another company we like a lot is **Swiss Water Decaf (SWS-UN.TO)**, a Canadian company that also pays a nice dividend. They’re a very tiny niche company that decaffeinate coffee. We think they can grow over time.

1-Year Daily Chart of Chungwa Telecom



Chart provided by www.BigCharts.com

We also like **Total Produce (T70.BE)**, an Ireland-based fresh fruit and vegetable distributor that serves most of Europe. They pay a nice dividend and are inexpensive. The company is managed well and has a good balance sheet. They also provide worldwide distribution for **Fyffes**, which is why you’ll see **Fyffes**-brand bananas, melons or fresh fruit in your grocery store. Those are the companies that we like a lot in

that space. We also have some smaller companies, but we tend to not chat about those because if everybody starts to buy them before we have the names in all of our portfolios, then we'll have disadvantaged our clients.

TWST: You mentioned Central and South America as an emerging market that you find interesting. Do you have any companies in that area?

Mr. Sutherland: We don't have anything directly in that area just because when you look at the individual securities, they seem a little bit expensive. We've been less enthusiastic about directly investing in

positions. One of the advantages of owning holding companies is many times, mutual funds or trusts or managers are not allowed to own more than 10% or over a certain percent in those assets, which often means that there is significant value in those businesses because the mutual fund companies can't invest in them. Companies like **Cheung Kong** and **Pargesa**, and some of the other holding companies can tend to have much better value. Most individuals and investors tend to invest through mutual funds or some kind of trusts, and often they don't realize that those mutual fund or trust companies that they're investing in through

"One of our largest Chinese holdings is Cheung Kong Holdings.... We like Chinese companies, and we like Cheung Kong because they're involved in ports and real estate. We think that there will be deflation throughout the world, and that some of that deflation will end up in Hong Kong and Chinese real estate."

Brazil. We've done it indirectly through some of the utilities that we own and other holding companies. We have concerns about the rest of South America in terms of the risk that the companies could be nationalized. We are concerned about this significant political risk, so we tend to want to have our investments in those countries through holding companies.

In Africa, we own a company called **Lonrho Africa** (LNAFF.PK), which has significant interest in agricultural and transportation and ports all over Africa. We are sure that Africa will grow. I have been there a number of times and the people are great, and there is such exciting, raw, untapped potential there.

TWST: You mentioned Taiwan Chunghwa. What about Chinese companies? Is that important in your investing process?

Mr. Sutherland: One of our largest Chinese holdings is **Cheung Kong Holdings** (CHE.SG), which I think is the largest company listed in Hong Kong. We like Chinese companies, and we like **Cheung Kong** because they're involved in ports and real estate. We think that there will be deflation throughout the world, and that some of that

liquidity constraints, board influence, charter, benchmarking, regulations and such are excluded from investing in certain investments, which can limit opportunity and affect returns. Even many financial advisers don't realize the issues around the mutual funds they recommend to clients.

TWST: What is the sell discipline? What triggers an exit from your portfolio?

Mr. Sutherland: There are two main things that trigger us to sell. The first is what we call "squishing out," where we basically find a new company that we really like and we really want to own but have to sell a company we currently own in order to make room in the portfolio. The second reason is when a company has reached a point where we think it has pretty much reached its full value or when we are not compensated for the risk. Those are the two main reasons that cause us to sell. We think that for each asset that you own in a portfolio, you need to psychologically have the three decisions you could make on a stock or investment — which is buy, sell and hold — have the same emotional weight. Each has to have equal weighting. Selling something needs to be as easy as buying it or as easy as holding it.

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deflation will end up in Hong Kong and Chinese real estate. We also think that the world is going to survive the recent malaise, so that's really good for ports and the transportation businesses that **Cheung Kong** is involved in. They also have subsidiaries that are involved in energy.

Cheung Kong owns a part of **Hong Kong Electric**, a large electric provider in Southern China/Hong Kong area. That's one that we really feel good about, and that company sells for probably 20% or 30% less than its breakup value. **Cheung Kong** is one of our favorite

Behavioral economics has influence on the investor. Most of us tend to want to hold investments and then have a very hard time selling. Hence, you want to make sure that the reason you're holding something is not because you love the company or because it has made you so much money, but because it really has the investment merits. They are still intact and the company is going forward, expected to perform and grow as you had expected them to grow. We have quite a strong sell discipline, and thank goodness because that has helped us over the years to have good performance.

TWST: What is the average turnover? Has it been higher than usual in the past 12 months?

Mr. Sutherland: We do not monitor our portfolio turnover, largely because we think it gets us off track. What we found over our 25 years is that there were years where we tended to have little turnover, others where it was more. I would expect that this year and next, we'll probably have not very significant turnover, because we really like the companies that we've bought and feel really good about their prospects. Then you have years where the market is really getting fluffy, and then you tend to have more turnover because you're selling things off. They'll become way overvalued and then we'll end up having to sell them, which could maybe cause significant turnover in that year.

“Cheung Kong is one of our favorite positions. One of the advantages of owning holding companies is many times, mutual funds or trusts or managers are not allowed to own more than 10% or over a certain percent in those assets, which often means that there is significant value in those businesses because the mutual fund companies can't invest in them.”

TWST: You like to have a lot of freedom and flexibility in your active management of global stocks, but what about the risk-control factors? How do you incorporate risk management within your portfolio and stock level?

Mr. Sutherland: Darwin said that if you look at the history of who has survived, it's not been the biggest, it's not been the smallest, it's not been the smartest — it has tended to be the creatures that had the most flexibility. Flexibility is probably that number-one risk management tool that we have at our disposal. What's so amazing to me is even trustees or fiduciaries, when they hire money managers, expect good returns and add constraints to restrict a manager's flexibility. Then they wonder why their performance was so poor or basically matched the stock market. Look at Warren Buffett, who doesn't have any constraints on his investments. When he sees opportunities, he goes and seizes them. That's why on a risk-adjusted basis he's been such a great investor. He has flexibility. If you look at great managers, and I've talked to lots of them, they tend to have very flexible mandates. You're hiring a manager, so you want them to have flexibility so that they can execute. Flexibility is truly the number-one risk management tool that any investor has, otherwise you end up owning assets that can be very significantly overvalued, get risk all out of whack and such.

TWST: In addition to that flexibility of your investment approach, what other distinctive features differentiate your international equity approach from that of peer companies?

Mr. Sutherland: I think that we've spent a lot of time trying to assess what the cultural attributes and the values of that company are. Is that company managed and run by people who love the industry or the business? Or is it run by people who are basically just financial engineers that are going to manipulate things to make their stock go up, or on a short-term basis have the value go up? We want to own companies in really good industries run by really good people who love what they're doing, who are passionate about their businesses, who love showing up to work, who

love to talk about their companies and who are excited about it. One of the advantages of our firm is that we are smaller, and so we can buy a lot of those smaller companies that have significant insider ownership. We can own companies that have a \$100 million market cap or a \$50 million market cap, where half the companies are owned by one family or a few managers. Or we can own holding companies that are often significantly owned by a family, where often mutual funds are restricted to the amount of those kind of companies that they can own. So that gives us a significant advantage. But I think truly that our ability to go in and say, “Is this company really sustainable? Is it well-managed?” makes a big difference. It's not all about numbers, and the numbers on a company are really easy. What makes a great company are great people and great products, and then you want to

pay the right price for that. But you get good management in a company, and that company is going to succeed. You have bad management, even within a company with good products, and you are going to have trouble with that company making money, no matter what the numbers are.

We do try to assess those sorts of areas, and that's much more subjective. A computer can't do it. We spend a lot of time, Suzanne Stepan and I, thinking about whether or not we are seeing this company in the correct light, whereas a lot of people spend all their time staring at numbers. I think that's why the investment management industry has such a poor track record of success. People think it's only about numbers. It's partly about numbers, but the real value-add is really assessing management, products, product strategy and then buying them at the right price. Not getting caught up in the mania of the market. It's all about discipline.

TWST: What is your outlook for the global markets as we come into 2010? Are there any challenges or headwinds that investors should be wary of?

Mr. Sutherland: When you're successful and doing really well, that's when you really want to lose the most sleep, because you don't ever want to become complacent. Right now what worries me is that we've probably got some more asset bubbles being created with all of the liquidity in the markets that probably could cause significant inflation. We actually think that that's going to happen, and then all that money that's being put into economies by central banks or lent out by central banks at these low interest rates are going to create some asset bubbles. So we think that the areas that that money will probably end up going is energy, health care, emerging market real estate, gold, commodities and food. Take a look at health care and pharmaceuticals — you've got three billion people in the emerging world who would like to have better health care, and they are going to be big buyers of pharmaceutical products. And in United States, we're all getting older. In emerging Europe or in developed Europe, people are getting older. People are going to want to

have better life quality, so that requires better health care. Those areas should have significant growth, and I also think that they will attract significant investments.

The areas that we don't like include banking. We think banking is still going to have a terrible time going forward. We don't need as many banks as we have because there is excess capacity. There's going to be less economic activity going forward, especially in the United States. Housing is probably going to do really poorly. We think that the retail area is going to do very poorly as well. Consumers are going to be less likely to spend, and be more prudent and responsible, and realize that savings is important, especially for retirement.

We are looking forward. We see all of those things going on. Every risk has significant opportunity on the other side. So if you see lots of risks, you don't invest there. If you see opportunity, you invest there. But people who invest in general indexes are irrational because they're investing in areas that are really going to do poorly. Why would you do that? You want to invest where you're going to have good chance of having good investment returns.

TWST: Is there anything that we didn't touch on that you'd like to add?

Mr. Sutherland: A good question would be probably, "Why do you think so many investors do poorly?" I think a lot of it is because most investors are quite complacent, and really don't try to go out there and find excellence in companies that they own and the investments that they make.

TWST: Thank you. (PS)

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An investor should consider investment objectives, risk, charges and expenses carefully before investing.

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