

PEARSON Investment Letter

Published Monthly Since 1982

www.pearsoncapitalinc.com**FEATURED STOCKS**

Bed Bath & Beyond	Quest Diagnostics
Community Bancorp	Sportsman's Guide
Escala Group	Tenaris S.A.
The Home Depot	Unit Corporation

GROWTH & INCOME STOCKS

American Capital	Vineyard Nat. Banc
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2006 - STRATEGY FOR SUCCESS**BY DONALD PEARSON**

In 2005 stocks have held their own despite high energy prices, rising

interest rates, and hurricanes. This has to be viewed as good news because it portrays a reasonably strong economy as this year is coming to an end. What have we learned from this, and where are we headed next year?

The upcoming year has the possibility of higher inflation augured by the recent spike in energy prices. The other specter we face is a recession brought on by too-high interest rates that dampen economic activity and pop the housing bubble. How does one prepare for inflation and recession at the same time? Because we can't predict with any certainty which hazard to prepare for, we don't. We can, though, insulate our portfolios properly so that in either case, if we must face one of these scenarios, the negative effect will be minimal.

Something else to consider is the market's position on news and events today. We have already seen mildly discouraging news for 2006 factored into share prices. If the economy continues to grow enough to keep unemployment low, yet stay tame enough to allow the Fed to stop worrying about inflation and ease up on rates, the stage will be set for a much stronger 2007. If that occurs, the market might pick up long before that calendar year begins.

A strategy for success simply means being prepared for the obstacles we may have to overcome, while at the same time being prepared for good news. Now that a strategy has been somewhat outlined, how can we develop it further? As an advisory service that builds portfolios rather than purchase mutual funds, we believe there are two ways one can improve a portfolio significantly.

Adding quality growth companies that increase their dividends every year is one strategy for long-range success. In 1982 the S&P 500 average dividend yield was a lofty 5.8%. By 2000, that yield was reduced to 1.2%. It appears today, because of the 2003 tax cut which slashed the rate on dividends to a maximum of 15% (the lowest level in the last 50 years), yields are again on the rise. The yield for Dow Jones stocks has increased from 2.1% to 2.6% in the last year, and the S&P 500 is now yielding 1.9%, the highest since 1996. Unlike stock price gains, dividend income is reliable. Once companies start paying dividends, they are reluctant to curtail payments. Dividends are expected to rise by 12% or more for 2005 over 2004. Once a company begins any reduction, it is seen as a sign of serious problems and many investors immediately begin dumping the stock. As we see many quality companies leading their sectors, making record profits, and shoring up their balance sheets with unheard of hoards of cash (and in many cases buying back their shares and increasing their dividends), we consider them for acquisition. Companies paying healthy dividends afford us the opportunity to collect additional income while we are waiting for their stock to appreciate. Industry and sector leaders many times provide an extra layer of safety when times become volatile. The S&P web site (www.standardpoors.com) lists 57 companies that have increased dividends for 25 consecutive years.

A second way to improve our opportunity for success is to become better diversified with ETFs (Exchange Traded Funds). With ETFs we can better diversify when pursuing a specific sector or area of the world when we believe it's the place to be at any given time. As we continue our research of the near two hundred ETFs available, we've found they can provide us better diversification in other parts of the world where information historically lags performance, by days in many cases. In our opinion, having many stocks built into an ETF within a portfolio, compliments exactly what we are doing with individual stocks.

Continued On Page 6

Walter D. Pearson
Chairman



Donald E. Pearson
President



Sandra Alberti
Publishing President

Investment Letters are complimentary to our clients with managed accounts!

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Adding quality growth companies that increase their dividends every year is one strategy for long-range

ONE MORE TIME

By Walter Pearson

It seems that there are still some people who do not understand the market vs. inflation. Many, many years ago this country was founded by a number of people who had lived through the same financial problems that we are experiencing today, and when they wrote the Constitution, they included a statement which said only Congress had the authority to issue money and regulate the value thereof, and that each paper dollar which was issued would be backed by gold or other specie. These people had lived through similar periods such as we are experiencing today and they wanted to make sure it did not happen to us.

When I was a boy, I can remember the sayings, the dollar is as "good as gold" or "sound as a dollar." These were true statements. One could take a United States Dollar, walk into any bank, and exchange it for gold. Today we do not even have a United States Dollar. It has been changed to a Federal Reserve Note. These notes are issued by the Federal Reserve Bank and can be turned in for other notes which have no intrinsic value.

If I were to tell a client that I had an investment opportunity which was backed by the government and would turn \$10,000 into \$7500 within a five-year period, I am sure he would look at me as if I had holes running through my head, but this is what is happening to numerous people today who actually believe they are taking the right road to safety. Can it be safe because your loss is guaranteed? Using my figures, I calculate today's inflation rate to be at a figure of about 8 percent. I believe, along with some other people who study the situation, that it will eventually hit 12 percent. I also believe it will continue to rise as the government continues excessive spending.

The Federal Reserve bankers tried to get established years ago and were fought off time after time by different patriots, but, in 1913, they barreled through and the Federal Reserve was formed. Nothing happened for a while, but little by little the Fed took over until today we do not even have a United States paper dollar. When the U.S. government needs more cash, it turns to the Fed who will obligingly lend whatever is needed. The Fed may not have the money but, no problem, they just print it up, lend it to us, and charge interest. As more and more ersatz currency is printed, the debt rises to the point where there is more debt than there is currency. Some years back one of our financial gurus figured out that if no new currency was created, and the people paid only the interest on the debts outstanding with no payments on the principal, within six months there would be no money in circulation. The banks would have it all. This is why your government must find the ways and means of borrowing greater and greater amounts of currency as time goes on. Think about it! Wars are a great way of spending money.

How do you bet on inflation? It is a simple matter. Get out of currency. Get out of any investments that move only with currency. This means no CDs, no bonds, or anything of similar nature. Buying gold or silver will afford protection. Buying real estate that produces an income will give income and protection. Buying stocks will give growth and protection as well. Price is important. Do not pay too much or you may then find yourself on the other side of the street.

One of the problems in the stock market is the view some people have that it is very risk oriented. Nothing of the sort. The stock market can be the safest haven one can find for one's investments. It is simply a matter of selection. The stock market is composed of thousands of companies. One can choose highly speculative companies that may turn up dead in the water after a period of time. On the other hand, there are numerous companies that have been paying dividends for twenty-five years. There are a good number that have dividend records that go back fifty years or more. If you are interested in safety, it is simply a matter of selecting an ultra conservative direction and everything should work out well for you.

Think of it this way: Suppose you invested \$10,000 in McDonald's ten years ago, which would not have been the best investment you could have made at the time, but neither was it the worst. Your \$10,000 would now be worth in the neighborhood of \$20,000. In spite of the fact that your dollar value has doubled, you can probably buy just about the same amount of gasoline with the twenty grand as you could back then with the ten.

Walter Pearson is the former President of First New England Securities, Co., Inc. and at that time, also managed the Statistical Department. He is the author of the book, "Investing for the Millions" and Publisher Emeritus for the Pearson Investment Letter. At this time, Mr. Pearson is Chairman of the Board of Pearson Capital, Inc. He is a contributing columnist for various publications and is listed in Who's Who in America.

"Remember the Lord your God, for it is He who gives you the ability to produce wealth. Deut. 8:18"

PEARSON CAPITAL'S RECOMMENDED STOCKS FOR DECEMBER 2005

BED BATH & BEYOND, INC (BBBY) NASDAQ PRICE: \$42.60

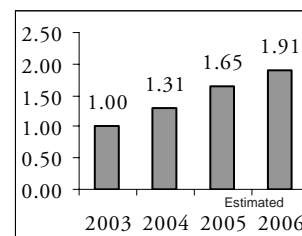
BBBY operates specialty retail stores in the U.S., including stores of Bed Bath & Beyond (BBB), Harmon Stores, Inc. (Harmon) and Christmas Tree Shops, Inc. (CTS). BBB stores are of a big box format. BBB offers an assortment of merchandise at everyday low prices. Its domestics merchandise line includes items, such as bed linens, bath accessories and kitchen textiles, and BBB's home furnishings line includes items, such as cookware, dinnerware, glassware and basic housewares. As of 02/26/05, BBB operated 660 stores in 44 states and one territory. CTS is a retailer of giftware and household items selling an assortment of domestics merchandise and home furnishings at value prices in many categories, including home décor, giftware, housewares, food, paper goods and seasonal products.

Type: Growth
Sector: Retail

Institutional Holdings: 426
Industry: Home Furnishing

Ratings & Recommendations Earnings per share

Current P/E Ratio: **23.8**
Annual Yield: **0%**
Annual Dividend: **\$0**
Investor's Bus. Daily: **C**
Pearson Growth Rating: **B+**
Pearson Value Rating: **A-**
Stand.&Poor Rating: **A+**
Value Line Rating: **1-2-3**



COMMUNITY BANCORP, INC (CMBC) NASDAQ PRICE: \$34.30

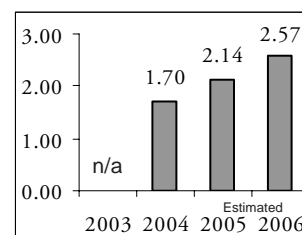
CMBC serves as the holding company for its wholly owned subsidiary, Community National Bank (the Bank). The Bank provides commercial banking services to businesses and individuals in the communities along the one to 15 corridor in Riverside and San Diego counties of Southern California. Community National Bank has 10 branches offices in the communities of Bonsall, El Cajon, Encinitas, Fallbrook, La Mesa, Santee, and Vista in San Diego County, and in the communities of Temecula and Murrieta in southwest Riverside County. The Bank also has additional Small Business Administration (SBA) loan production offices that originate loans in California, Arizona, Nevada and Oregon. On October 1, 2004, the Company acquired Cuyamaca Bank, N.A., a commercial bank and merged it into Community National Bank

Type: Growth
Sector: Financial

Institutional Holdings: 6
Industry: Regional Banks

Ratings & Recommendations Earnings per share

Current P/E Ratio: **17.2**
Annual Yield: **1.10%**
Annual Dividend: **\$0.40**
Investor's Bus. Daily: **C+**
Pearson Growth Rating: **B**
Pearson Value Rating: **B+**
Stand.&Poor Rating: **C+**
Value Line Rating: **N/R**



ESCALA GROUP, INC (ESCL) NASDAQ PRICE: \$16.55

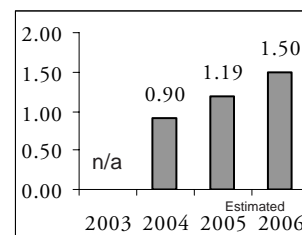
Escala Group Inc., formerly Greg Manning Auctions, Inc. (GMAI), is a global collectibles merchant and auction house network with operations in North America, Europe and Asia and on the Internet. In September 2003, the Company and Auctentia, S.L. (Auctentia), integrated their auction businesses, creating a global collectibles auction network. Auctentia is the wholly owned subsidiary of Afinsa Bienes Tangibles, S.A. (Afinsa), the Company's major customer. Afinsa and Auctentia collectively own approximately 69% of the Company's outstanding common stock. In North America, the Company is a traditional and e-commerce-Internet, interactive telephone, and Internet and live simulcast-auctioneer and merchant/dealer of collectibles, including rare stamps, stamp collections and stocks, coins, sports trading cards and memorabilia, and fine art.

Type: Emerging Growth
Sector: Services

Institutional Holdings: 29
Industry: Business Services

Ratings & Recommendations Earnings per share

Current P/E Ratio: **11.3**
Annual Yield: **0%**
Annual Dividend: **\$0**
Investor's Bus. Daily: **B+**
Pearson Growth Rating: **A**
Pearson Value Rating: **A**
Stand.&Poor Rating: **B-**
Value Line Rating: **3-2-3**



THE HOME DEPOT, INC (HD) NYSE PRICE: \$41.78

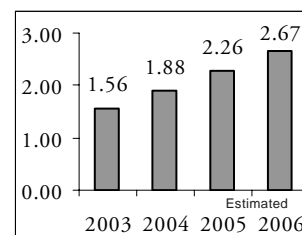
HD is a home improvement retailer. During the fiscal year ended January 30, 2005 (fiscal 2004), the Company was operating 1,890 stores. Most of the stores are either Home Depot stores or EXPO Design Center stores. Home Depot stores sell a wide assortment of building materials, home improvement and lawn and garden products and provide a number of services. Home Depot stores average approximately 106,000 square feet of enclosed space, with approximately 22,000 additional square feet in the outside garden area. EXPO Design Center stores sell products and services primarily for home decorating and remodeling projects. EXPO Design Center stores offer interior design products, such as kitchen and bathroom cabinetry, soft and hard flooring, window treatments and lighting fixtures.

Type: Growth
Sector: Services

Institutional Holdings: 770
Industry: Home Improvement

Ratings & Recommendations Earnings per share

Current P/E Ratio: **16.1**
Annual Yield: **0.90%**
Annual Dividend: **\$0.40**
Investor's Bus. Daily: **C+**
Pearson Growth Rating: **B+**
Pearson Value Rating: **A-**
Stand.&Poor Rating: **A+**
Value Line Rating: **2-3-4**



PEARSON CAPITAL'S RECOMMENDED STOCKS FOR DECEMBER 2005

QUEST DIAGNOSTICS, INC (DGX) NYSE PRICE: \$50.09

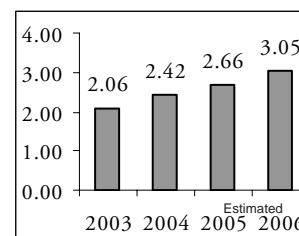
DGX is a provider of diagnostic testing, information and services, providing insights that enable physicians and other healthcare professionals to make decisions to improve health. The Company offers patients and physicians access to diagnostic laboratory services through its nation-wide network of laboratories and patient service centers. It provides interpretive consultation through its medical and scientific staff. DGX provides esoteric testing, including gene-based testing and testing for drugs of abuse. The Company offers healthcare organizations and clinicians with information technology solutions that can improve patient care and medical practice. Customers include patients, physicians, hospitals, healthcare insurers, employers, governmental institutions and other commercial clinical laboratories.

Type: Growth
Sector: Financial

Institutional Holdings: 365
Industry: Regional Banks

Ratings & Recommendations Earnings per share

Current P/E Ratio: **19.1**
Annual Yield: **0.70%**
Annual Dividend: **\$0.36**
Investor's Bus. Daily: **B**
Pearson Growth Rating: **A**
Pearson Value Rating: **A-**
Stand.&Poor Rating: **D**
Value Line Rating: **3-3-3**



THE SPORTSMAN'S GUIDE, INC. (SGDE) NASDAQ PRICE: \$26.24

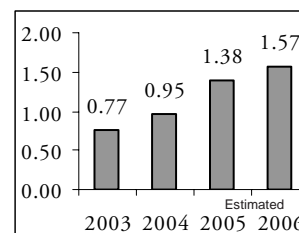
The Sportsman's Guide, Inc. is a marketer of outdoor gear and general merchandise, with a special emphasis on outdoor clothing, equipment and footwear. The Company markets and sells its merchandise through two primary channels: catalogs and e-commerce Websites. The Company's catalogs and its Websites offer products at low prices. Its catalogs are advertised as the fun-to-read Catalog, and its primary Website is advertised as the fun-to-browse Website. The Websites include its online retail store modeled on its print catalogs, featuring e-commerce and content, and www.bargainoutfitters.com, the Company's online liquidation outlet. The company was formed by Gary Olen in 1970 and is based in South St. Paul, Minnesota.

Type: Growth
Sector: Services

Institutional Holdings: 31
Industry: Catalog/Mail Order

Ratings & Recommendations Earnings per share

Current P/E Ratio: **20.2**
Annual Yield: **0%**
Annual Dividend: **\$0**
Investor's Bus. Daily: **B**
Pearson Growth Rating: **A-**
Pearson Value Rating: **B+**
Stand.&Poor Rating: **A**
Value Line Rating: **1-2-4**



TENARIS S.A. (TS) NYSE PRICE: \$111.80

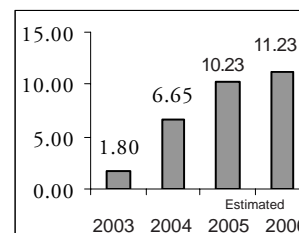
Tenaris S.A. is a global manufacturer of seamless steel pipes for the oil and gas industry and a global supplier of seamless steel pipes for process and power plants and for industrial and automotive applications. It is also a regional supplier of welded steel pipes for oil and gas pipelines in South America. Tenaris focus on providing end-user customers a service that integrates manufacturing, procurement, distribution and on-time delivery of products throughout the world. Incorporated in Luxembourg, the Company has manufacturing facilities in Argentina, Brazil, Canada, Italy, Japan, Mexico, Romania and Venezuela. It also has a proprietary global service and distribution network in over 20 countries. Tenaris' customers include many of the world's major oil and gas companies, as well as a large number of engineering and industrial companies.

Type: Growth
Sector: Basic Materials

Institutional Holdings: 89
Industry: Steel & Iron

Ratings & Recommendations Earnings per share

Current P/E Ratio: **9.7**
Annual Yield: **1.50%**
Annual Dividend: **\$1.69**
Investor's Bus. Daily: **A**
Pearson Growth Rating: **B**
Pearson Value Rating: **A**
Stand.&Poor Rating: **N/R**
Value Line Rating: **N/R**



UNIT CORPORATION (UNT) NYSE PRICE: \$54.16

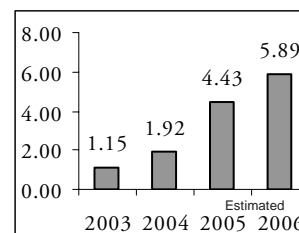
UNT has three principal business segments: contract drilling, which involves contracting to drill onshore oil and natural gas wells; oil and natural gas exploration, which involves the exploration, development, acquisition and production of oil and natural gas properties, and natural gas purchasing, gathering and processing, which involves the purchase, gathering, processing and treatment of natural gas. The Company's businesses are carried out by its three principal wholly owned subsidiaries: Unit Drilling Company, for contract drilling; Unit Petroleum Company, for oil and natural gas exploration, and Superior Pipeline Company, L.L.C., for natural gas purchasing, gathering and processing. As of 12/31/04, the company had 8,561 Mbbls of oil reserves and 295,406 MMcf of natural gas reserves. UNT was founded in 1963 and is based in Tulsa, OK.

Type: Emerging Growth
Sector: Basic Materials

Institutional Holdings: 185
Industry: Oil & Gas Drilling

Ratings & Recommendations Earnings per share

Current P/E Ratio: **15.7**
Annual Yield: **0%**
Annual Dividend: **\$0**
Investor's Bus. Daily: **A+**
Pearson Growth Rating: **A+**
Pearson Value Rating: **A+**
Stand.&Poor Rating: **A**
Value Line Rating: **3-3-3**



WALL STREET INDEXES

Indexes	1999	2000	2001	2002	2003	2004	05/YTD
S&P 500	21.1%	(10.1%)	(13.3%)	(23.4%)	26.4%	9.0%	3.1%
Dow Jones	25.2%	(6.2%)	(7.1%)	(16.8%)	25.3%	3.2%	0.2%
Nasdaq	85.6%	(39.3%)	(21.1%)	(31.5%)	50.0%	8.6%	2.6%
Russell 2000	21.3%	(4.2%)	1.0%	(21.6%)	45.4%	17.0%	3.9%
Our CD Buster	Data available on our website			8.1%	56.7%	22.8%	(In Dispute)
CD Annual Average	4.9%	5.4%	3.0%	2.3%	1.5%	1.5%	3.5%

MARKET VIEW

Christopher Carothers - PCI's Stock Analyst

ECONOMIC FLOWS:

Expect another increase at the next Fed meeting on December 13th. This is the 13th meeting in which the Fed will have a continued bias toward raising interest rates. Standard and Poors has suggested that this next meeting may end the bias with a 50-point increase. This will allow the new Fed chief Bernanke to do his own thing when he begins his tenure, instead of stringing it out over the next few months.



Key point: *I hate the number 13.*

EARNINGS FLOWS:

At the end of the third quarter earnings season, it turns out that stocks have done very well. In fact, there is very little bad news throughout each sector. The surge in the S&P 500 has set the market for a great year end run. Gas prices have retreated, leaving retail stocks to take the lead as shoppers return in droves for the Christmas season. Money is starting to move away from energy and into other sectors leading to a broad move upward.

Key point: *Retail takes the lead toward the year end tally.*

CASH FLOWS:

Housing prices continue to rise! Even with the surge in the stock market, the housing market is taking money off the table for stocks leaving excellent bargains. Once again, dividend stocks have marched on, many with dividend increases. According to Standard and Poors, up until November, dividend stocks in the S&P 500 posted a total return of 5.3 percent vs. 3.8 percent for the nonpaying ones.

Key point: *These stocks post a better return with far less risk!*

ADDITIONAL NOTES:

Even though short term interest rates will rise, the long term interest rates will remain cool leading to a good 2006 for equities.

General Motor's stock moved recently to an eighteen-year low.

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for accounts of \$25,000 or more
(2% for smaller accounts)

Free consultation
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DECEMBERS'S RECOMMENDED GROWTH & INCOME STOCKS

AMERICAN CAPITAL STRATEGIES, LTD (ACAS) NASDAQ PRICE: \$38.36

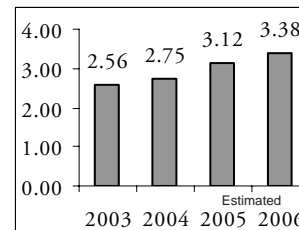
American Capital Strategies, Ltd. is a buyout and mezzanine fund that provides investment capital to middle market companies, which it generally considers to be companies with sales between \$10 million and \$750 million. The Company invests in senior and mezzanine (subordinated) debt and equity of companies in need of capital for buyouts, growth, acquisitions and recapitalizations. Its wholly owned operating subsidiary, American Capital Financial Services, Inc. (ACFS), provides financial advisory services to the Company's portfolio companies. ACFS arranges and secures capital for large transactions, particularly buyouts that the Company sponsors. American Capital Strategies was incorporated in 1986 and is headquartered in Bethesda, Maryland.

Type: Growth & Income
Sector: Financial

Institutional Holdings: 101
Industry: Diversified Invest.

Ratings & Recommendations Earnings per share

Current P/E Ratio: **9.4**
Annual Yield: **8.2%**
Annual Dividend: **\$3.16**
Investor's Bus. Daily: **C+**
Pearson Growth Rating: **B**
Pearson Value Rating: **A**
Stand.&Poor Rating: **D**
Value Line Rating: **3-3-2**



VINEYARD NATIONAL BANCORP (VNBC) NASDAQ PRICE: \$29.17

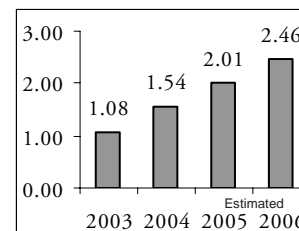
VNBC serves as a holding company for Vineyard Bank (the Bank) and for other banking or banking-related subsidiaries that it may establish or acquire. As a wholly owned subsidiary, the Bank is a community bank that operates nine banking centers, which are located in each of the communities of Rancho Cucamonga, Chino, Diamond Bar, La Verne, Crestline, Lake Arrowhead, Irwindale, Manhattan Beach and Corona, all of which are located in Los Angeles, Riverside and San Bernardino counties in California. The Bank is involved in attracting deposits from individuals and businesses, and using those deposits, together with borrowed funds to originate commercial business and commercial real estate loans, primarily to small businesses, churches and private schools, single-family construction loans, and Small Business Administration (SBA) loans.

Type: Growth & Income
Sector: Financial

Institutional Holdings: 36
Industry: Regional Banks

Ratings & Recommendations Earnings per share

Current P/E Ratio: **15.5**
Annual Yield: **1.10%**
Annual Dividend: **\$0.32**
Investor's Bus. Daily: **B**
Pearson Growth Rating: **A**
Pearson Value Rating: **A-**
Stand.&Poor Rating: **B**
Value Line Rating: **N/R**



2006 - Strategy For Success Continued From Page 1

A well-balanced portfolio can now be in Asia, Europe, Australia, and the Americas and still have another fifty well-diversified companies of our choice. Besides selecting from different countries, we can also purchase different sectors. Once into a sector or country, we can monitor these companies more closely, and, as we begin to see who the real winners are, we may choose to buy an individual company based upon its performance. We began using selected ETFs in 2004, and we expect to see an increase within our portfolios in the upcoming years.

I believe using these strategies, coupled with safety every time a key decision must be made, will prove successful. Knowing when to sell a stock in our opinion is more difficult than when to buy. A valuable lesson we've learned over and over again is to err on the side of safety. One will never be right all the time, but making these tough decisions can add to the bottom line.

This being our last investment letter of 2005, I would like to close the year by again saying thank you from our entire staff for your trust and confidence in Pearson Capital, Inc. This has been another tough and challenging year. We are happy to report above-average returns once again for our clients, and we look forward to being your investment advisory firm of choice again next year. Please continue to call, email, and write to speak with any of us, as we believe our service and our availability for you is as important as **our** portfolio management.

Merry Christmas



Happy New Year

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Source Rating Key for PCI's featured stocks: Pearson Investment Growth Rating measures long-term past and future growth.

Pearson Value Rating measures current value in terms of potential for the dollar. Investors Business Daily measures growth and relative price strength. S&P measures financial quality and growth potential. Value Line measures timeliness, value and safety.