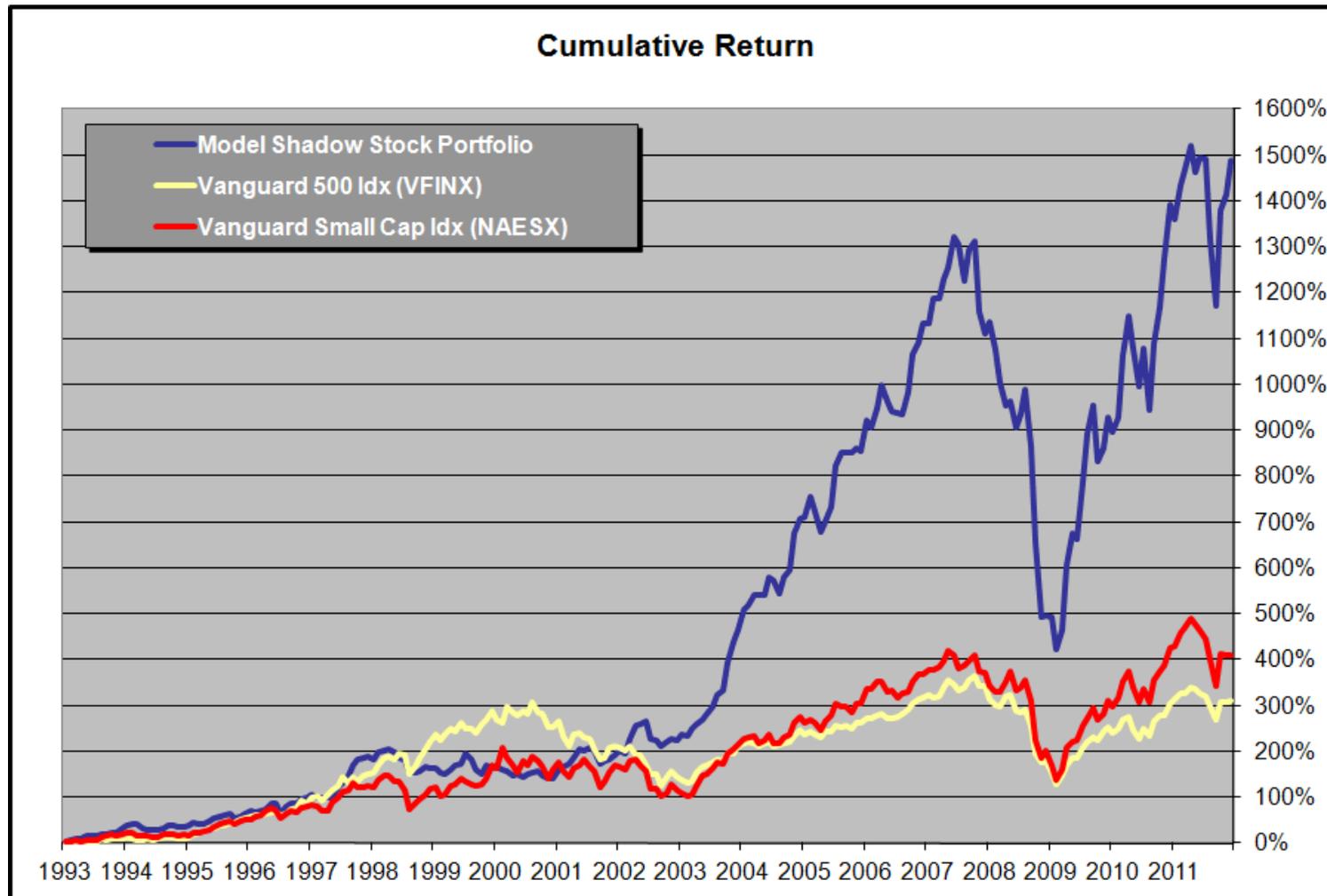


Model Shadow Stock Portfolio Historical Returns 1993-2011



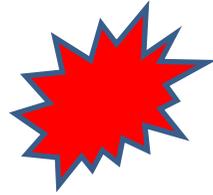
Shadow Stock Portfolio Principles

The best stocks for individual investors are not the same stocks that are best for institutions.

Over the long run, research indicates that value stocks outpace the market, as do small (and micro-cap) stocks.

Excessive trading of small-cap stocks hurts your bottom line; you can achieve solid returns by simply adjusting your portfolio quarterly.

Ultimately, the best returns come from giving major consideration to risk. Success comes more from concern for the overall portfolio than for individual stocks.



RISK !!!



The stocks in the AAll Model Shadow Stock Portfolio are largely risky stocks when evaluated separately. But when taken together as a portfolio, most of that individual stock risk has been **diversified** away. In fact, the average risk of the individual stocks has been reduced by about 70%.

The central point of our Model Shadow Stock Portfolio is that the risk of any individual stock is not important if your portfolio is well **diversified**. What is important is how the addition of that stock affects the risk of your overall portfolio.

Portfolio Management Criteria

It is our belief that a quarterly review of the following purchase, sale and management criteria is all that is needed to build your own Shadow Stock Portfolio.

Simply review your holdings on a quarterly basis to see if any fundamental changes make them candidates for sale. If you have new investment funds available or cash from sales, you can look at AAI's online list of Passing Companies (www.aai.com/stockportfolio) to see if any companies meet your needs for inclusion in your Shadow Stock Portfolio.

Stock Purchase Criteria

Price-to-book-value ratio must be less than 0.80.*

Market capitalization must be between \$17 million and \$200 million.*

Price-to-sales ratio must be less than 1.2.*

The firm's last quarter and last 12 months' earnings from continuing operations must be positive.

The share price must be greater than \$4.

**These figures will change gradually as market values change. Any changes will be noted in the Journal and online.*

Stock Purchase Criteria Con't

No bulletin board or pink sheet stocks will be purchased.

No financial stocks or limited partnerships will be purchased.

No foreign stocks will be purchased because of different accounting and/or withholding tax on dividends.

Any stock that was sold within two years will not be rebought.

See quoted bid/ask spread rules on Stock Order Guidance (slide).

Eliminate any company that failed to file a 10-Q (quarterly) report in the last six months.

Stock Sale Criteria

The stock reports a string of negative earnings:

—If last 12 months' earnings from continuing operations are negative, the stock is put on probation;

— if a subsequent quarter has negative earnings prior to 12-month earnings from continuing operations becoming positive, the stock is sold.

Stock Sale Criteria Con't

The stock's price increases so that it is no longer considered a small/micro-cap value stock:

- The stock's price-to-book-value ratio goes above three times the initial criterion.
- Market capitalization goes above three times the initial maximum criterion.

In summary, we sell when the market recognizes the value of one of our holdings, thus driving up the price so that it no longer remains in the “shadows” of Wall Street.

Stock Order Guidance

These rules are for general guidance. Your own experience, market conditions and size of position will impact decisions.

Market orders are not used. Instead, if the quoted bid/ask spread is less than 2% (ask price minus bid price, divided by ask price), place a limit order at the ask price for a buy and at the bid price for a sell. If the bid/ask spread is more than 2%, try to place a limit order between the bid and ask prices to keep transaction costs low. If necessary, build a position gradually. With low commissions, it is often better to place partial orders than to try to establish a large position all at once. Be patient.

Stock Order Guidance Con't

The average daily dollar volume should be at least four times the amount needed for your position. This will ensure liquidity to get in and out of the position, even if you need to grow the position gradually and sell gradually. This will result in a varying number of qualifying stocks for each investor.

Stock Order Guidance Con't

For NASDAQ stocks, it appears to be better to use day orders. If the order is not filled, it is placed again with a slight adjustment. For NYSE and Amex stocks, good-till-canceled (GTC) orders are used to keep a place in line in the specialists' books. If the market isn't close to the desired price, the price is adjusted in a few days with a new GTC order.

If price changes cause a stock to become ineligible (due to changes in the price-to-book-value ratio or market capitalization) when only part of the order has been filled, shares already purchased are kept but the balance of the order is canceled.

Building Your Own Portfolio

Follow the printed guidance provided here and issued in the AAI Model Portfolios columns in the January, April, July and October AAI Journals—remember, this portfolio was designed to require only simple modifications on a quarterly basis when company fundamentals change.

OR

Utilize the online resources we offer at www.aai.com/stockportfolio where we provide monthly updates on the “Passing Companies” that meet our criteria for inclusion in the Shadow Stock Portfolio. We run this screen monthly, so please seek out our online information for the most current list of stocks.

Management Rules

Equal dollar amounts are invested in each stock initially.

Decisions are made only at the end of each quarter. In order to react to the majority of earnings reports as soon as possible, quarterly reviews are made early in February, May, August, and November.

Best judgment is used for tenders or mergers, but all criteria must be obeyed.

Management Rules Con't

At the end of a quarter, if receipts from stocks sold exceed requirements for new purchases, the excess receipts—up to 5% of the portfolio's value—are kept in cash until the next quarter. If the excess receipts are greater than 5% of the total portfolio value, the amount above 5% is distributed to smaller holdings that still qualify as buys. Efficient quantities are purchased: If over 10% of the portfolio is in cash, the price-to-book-value ratio can be moved up, but never over 0.90.

At the end of a quarter, if receipts from stock sales are insufficient to buy all newly qualifying stocks, purchases are made in order of lowest bid/ask spreads.

Management Rules Con't

If you are managing your own portfolio, it should consist of at least 10 stocks. If you are developing the portfolio gradually you can do it stock by stock, but don't put more than 10% of your funds in each additional stock. More than 20 stocks are not needed until the portfolio exceeds \$1 million.

Modification Results

Lowering the price metric to \$3 from \$4 yielded a total of 35 stocks.

Raising the market capitalization to \$300 yielded 26 stocks.