



Third Quarter 2006 Letter To Investors: January – September 2006: Hurley composite rises 10.1% net of fees vs 8.6% for S&P 500

During the most recent quarter, a composite of accounts managed at Hurley Capital accrued its largest gains in Enbridge Energy Management LLP (NYSE: EEQ), Vanguard Health Care VIPERs (NYSE: VHT), and Magellan Midstream Partners LLP (NYSE: MMP). Computer Horizons (NASDAQ: CHRZ), Dell, Inc. (NASDAQ: DELL) and Jacada (NASDAQ: JCDA) were the largest loss generators during the July-September quarter.

*“We look for companies generating or holding a lot of cash, trading at reasonable prices, **where we can’t figure out how we can fundamentally lose**, and that are run by smart, honest people with great records who have their money where their mouth is.” – Bruce Berkowitz, President, Fairholme Capital Management*

How Can We Lose?

Prior to initiating a new investment, we ask ourselves, “How can we lose?” Put differently, what fundamentally would have to happen to make this seemingly inexpensive investment, suddenly quite expensive and subject to fall? If we can become comfortable with the risk associated with adverse events occurring, then we proceed. With Dell, the investment discussed in our last [Letter To Investors](#), losses would be caused by shrinking margins and market share and continued sinking customer satisfaction. We are comfortable with that risk, as we believe that Dell’s direct-to-consumer business model has structural margin advantages over its competition, and, with renewed investment in service, in customer satisfaction.

New Investment: Discovery Holdings

With our latest investment, Discovery Holdings (NASDAQ: DISCA), it’s also difficult for us to figure how we can lose. DISCA is a holding company principally made up a 50% share of Discovery International, the owner of cable networks including Discovery, TLC, Travel Channel and Animal Planet. Discovery and TLC are two very profitable domestic cable/satellite channels generating significant cash flow, while Travel Channel and Animal Planet are about breakeven. International markets are the principal growth driver as much of the programming content is easily translated; safaris and shark watching sell in Stuttgart and Singapore as well as it does in Seattle.

We estimate that Discovery Holdings trades at an 8.5% free cash flow yield, which includes spending on international growth initiatives, High-Def channels, and an education-focused initiative. DISCA is trading at a 35% discount to its peers due to an unorthodox holding company structure where the other 50% of Discovery International is owned by two private companies who (1) limit the amount of publicly available corporate data, and (2) have expressed no interest in converting their stake into publicly-traded shares. We think this issue will be resolved eventually, and get the internal growth and free cash flow yield while we wait.

How can we lose? We may have to wait for this “holding company discount” to disappear. But, we believe change may be closer than the market thinks. Two clues may be: (1) Discovery International just hired a new CFO from a \$3 billion public company. Why would someone

leave a simple job for a company with a strange holding structure without some chance of resolution? And (2) as of October 2005, Discovery International employees are receiving DISCA stock appreciation rights (like options, but different). Hopefully, the private business owners do not intend their employees to suffer a 30% holding company discount forever.

Moving Forward

Hurley Capital remains focused on providing clients with value-oriented asset management and a high level of personal service. We believe our client accounts are well positioned for continued solid returns with below market risk. We are committed to our goal of presenting clients positive returns and protection in all market conditions. Thanks again for your continued interest and patronage.

Charles Goldblum
October 2006

Performance of Hurley Capital Investments

	Action	Initial Investment Date	Symbol	Name	Total Return to Date*	Transaction Price	Market Price 9/30/06**	
2006 Transactions								
Hedging Long Position	Bought	28-Sep-06	DISCA	Discovery Holdings 'A'	0.3%	14.40	14.46	
	Sold Call	15-Sep-06	DE AP	Deere & Co. Jan07 \$80 Call	-42.3%	3.88	8.20	
	Bought	12-May-06	DELL	Dell Inc.	-6.0%	24.33	22.84	
Closed 7/10/06	Bought	28-Apr-06	DMCX	Datamirror Corp.	16.7%	8.98	10.50	
	Bought	16-Mar-06	POS	Catalina Marketing Corp	19.6%	23.23	27.50	
	Bought	01-Mar-06	565011AB9	Manugistics Group 5%'07 Cvt	9.8%	94.18	100.00	
	Bought	21-Feb-06	JCDA	Jacada Ltd	-11.4%	2.56	2.27	
	Bought	14-Feb-06	CHK	Chesapeake Energy	2.7%	28.38	28.98	
Hedge Expired 6/17/06	Bought	04-Jan-06	NWSA	News Corp Ltd Cl A	27.7%	15.37	19.65	
	Bought	23-Feb-06	PTFRD	Put Petrofund Energy Trust	-100.0%	1.30	-	
2005 Transactions								
Closed 7/26/06	Bought	27-Dec-05	NXR	Nuveen Select Tax Free	6.0%	13.19	13.60	
	Bought	15-Dec-05	DE	Deere & Co.	21.1%	70.09	83.91	
	Bought	12-Dec-05	COST	Costco	2.9%	48.60	49.68	
	Bought	28-Nov-05	CHRZ	Computer Horizons Inc.	-1.4%	4.03	4.00	
	Bought	03-Oct-05	WMT	Wal-Mart	13.2%	44.03	49.32	
	Bought	17-Aug-05	MMP	Magellan Midstream Partners LP	23.4%	31.70	36.90	
	Bought	22-Jul-05	SKM	SK Telecom Ltd ADR	19.3%	20.65	23.63	
	Bought	23-Jun-05	TPP	Teppco Partners LP	-1.4%	41.06	37.16	
	Bought	17-Jun-05	465754AF6	i2 Technologies 5.25% Cvt Bond	11.4%	93.00	99.95	
	Bought	27-May-05	GXM	General Motors Pfd 'A'	11.7%	23.65	24.75	
	Bought	18-Apr-05	KO	Coca-Cola	12.9%	40.87	44.68	
	Bought	10-Mar-05	T	AT&T Corp.	32.7%	24.92	29.19	
	Bought	25-Jan-05	CVX	Chevron Texaco	29.7%	52.51	64.86	
	2004 Transactions							
	Closed 9/27/06	Bought	28-Oct-04	VHT	Vanguard Health Care VIPERs	22.7%	46.56	56.63
		Bought	06-Oct-04	EEQ	Enbridge Energy Mgt LLC	17.8%	44.95	46.25
		Bought	13-Sep-04	BMN	Blackrock Muni Trust	1.6%	10.67	10.05
Bought		03-Sep-04	PTF / PWE	Petrofund / Penn West Energy Trust	78.7%	19.57 ***	36.06	

*Total returns include transaction fees, dividends, interest and trading proceeds

** Final transaction price indicated for closed transactions

*** Purchase price adjusted for PWE share acquisition of PTF (0.6 shares PWE for each share PTF)

Important Disclosure

The Hurley Capital Managed Accounts Composite represents all actual client accounts invested in this strategy. The Hurley Capital Managed Accounts Composite allocates client portfolios in equity and fixed income investments, weighted according to Hurley Capital's proprietary investment strategy. Actual client accounts utilizing the Hurley Capital Managed Accounts Composite may have varying allocations between equities and fixed income investments based on individual investment preferences. The results of the Hurley Capital Managed Accounts Composite are net-of-fees, brokerage commissions, and other expenses. Hurley Capital's investment advisory fees are described in the disclosure statement of Part II of the Form ADV which is available upon request. The results of the Hurley Capital Managed Accounts Composite include the reinvestment of dividends. Comparison of the Hurley Capital Managed Accounts Composite to the S&P 500 and NASDAQ Composite is for illustrative purposes only and the volatility of the indices used for comparison may be materially different from the volatility of the Hurley Capital Managed Accounts Composite due to varying degrees of diversification and/or other factors. Past performance of the Hurley Capital Managed Accounts Composite may not be indicative of future results and the performance of a specific individual client account may vary substantially from the composite results above in part because client accounts may be allocated among several portfolios. Different types of investments involve varying degrees of risk, and there can be no assurance that any specific investment will be profitable.