



Fourth Quarter 2006 Letter To Investors:

January – December 2006: Hurley composite rises 16.1% net of fees vs. 15.8% for S&P 500

Performance Review

In 2006, a composite of accounts managed by Hurley Capital rose 16.1% net of fees, as compared to the S&P 500, which rose 15.8%. We delivered market-beating returns in 2006 at below market risk, as most clients carried non-equity balances (cash and pipeline partnerships) of about 25% during the year. During 2006, the largest winners were News Corp., PennWest Energy Trust, SK Telecom, and DataMirror Corp., while fractional losers included Jacada Corp. and recent purchase Canadian Natural Resources.

Value Investing Concept: Ugly Ducklings

From the point of view of value investors, negative investor sentiment is great – pushing stocks down and creating opportunity. A reversal in sentiment often provides a commensurate upside boost. Wide price swings of individual stocks are often due to sentiment changes as much as fundamental ones. For instance, Apple (AAPL) trades at \$85/share about the same as a year ago, but last July it was down to \$50/share. Last year, investment performance was buffeted by dissipating negative sentiment toward: oil prices (Chevron, PennWest), a slowing economy (Deere), and GM's financial stability (General Motors Pfd 'A').

A Recent Investment: Jacada Corp.

Jacada (JCDA, \$2.56/share on 1/8/07) has plenty of what we like -- a good valuation and lots of negative sentiment. Jacada makes software that makes call center representatives more efficient. More efficient means shorter call times and fewer required call center representatives, in some cases 40% fewer. Clients including Vodafone, Qwest and UBS are paying over \$1 million each for this technology. Valuation-wise, Jacada is among the cheapest in software, trading below our estimation of the value of current client maintenance agreements (i.e. if they were to basically shut down today). A similar-sized software company was sold recently at a valuation 30% higher than JCDA currently.

JCDA is cheap because of rampant negative sentiment (with our rebuttal):

1. Too risky (over 70% of market value is in cash on the balance sheet and is not burning cash),
2. Company is in decline (more than counterbalanced by growth of these new call center sales),
3. Company is irrelevant and invisible (good performance increases relevance & visibility)

As Jacada begins to show revenue growth in 2007 and begins to publicize its story through its first investor relations campaign in years, we believe Jacada could reach \$4/share in a year. Finally, management believes in its prospects too, as both the CEO and head of European sales have each bought Jacada stock over the past few months.

In Summary

2006 was a successful year in terms of both absolute and relative performance. We believe that client accounts are well positioned for solid returns at below market risk levels. For further information on specific holdings, please see our year-end portfolio review at the end of this letter. We reiterate our goal to provide clients with positive returns at below market risk regardless of market conditions and target annual returns of 8-10%. We pledge to continue investing your capital in a conservative fashion by pursuing value-oriented investments that offer attractive upside potential.

Year-End 2006 Commentary on Client Holdings

Canadian Natural Resources (CNQ): A fourth quarter '06 purchase, CNQ is a lower-valued, but higher volatility replacement for Chevron Corp. We like the high inside ownership, upcoming oil sands production, and debt pay-down via excess asset sales. Additionally, we take comfort in CNQ's assets being located primarily in Canada, free from the risks of wars (Nigeria), nationalization (Venezuela), and expropriation (Russia) found with Chevron and other large multi-nationals. The big risk for CNQ is, if winter '07 never comes, this investment will surely suffer.

Catalina Marketing (POS): Negative sentiment here focuses on high corporate spending to upgrade their supermarket coupon technology from black & white to color. While earnings will suffer during the transition, early success is apparent and when rollout is done by year-end, profit margins (and sentiment) should recover. Also, private equity acquirers have expressed interest in buying POS at \$30/share and company is reviewing its strategic options.

Chesapeake Energy (CHK): Fast-growing domestic U.S. natural gas producer should do well so long as winter arrives and summer follows with typical temperatures. It's getting harder for the major oil & gas companies to find growth, hence the large acquisitions over the past few years, including Kerr McGee, Unocal, Burlington Resources, etc. We suspect acquisitions will continue, buffeting sentiment.

Coca-Cola (KO): High asset value, high earnings power, low business momentum. This defensive investment has paid off due to operational improvements (and a strong stock market). Our hoped for pullback in commodity prices (aluminum for cans and oil for plastic bottles) didn't happen, but could provide upside for 2007 if current commodity weakness continues. Coke also pays a 2.5% dividend and continues to buyback its own stock.

Computer Horizons (CHRZ): We thought this IT staffing and consulting firm would sell itself for \$5-7/share. Looks like the sum of the sales will be closer to \$4.70/share as the company winds down operations in first half 2007. While a modest winner for our investors, not as fast or lucrative as we expected.

Costco/Wal*Mart (CSCO/WMT): Income growth (i.e. from your job, not your house) for the average American has been stagnant for years. With a softer housing market, more people will shop at the 'big box' stores. Wal*Mart has lowered 2007 store opening goals, which ought to increase focus on company's cash generation capability.

DataMirror (DMCX) is another small software company selling for around salvage value with growth opportunity. DMCX was up over 40% in 2006 as the company bought back over 30% of outstanding shares.

Dell (DELL) still has a better mousetrap than Hewlett-Packard via direct-to-customer relationships with consumers and enterprises. Its growing international business should be the key to unlocking value here. Are computers going out of style? Maybe, but not as fast as naysayers would have you believe.

Discovery Holdings (DISCA): We discussed DISCA extensively in our last investor letter. Since then, DISCA's parent company Liberty has acquired a controlling stake in Direct TV, implying wider carriage for Discovery Holdings' cable channels. We still anticipate that ownership structure and limited financial disclosure issues will disappear at some time, allowing for the valuation discount versus its peers to evaporate. Our target is over \$20/share.

Enbridge Energy Management (EEQ) / Enbridge Energy Partners (EEP) / Magellan Midstream Partners (MMP) / Teppco Partners LP (TPP): These stocks are limited partnerships that own oil/gas pipelines. They are a nice substitute for fixed income investments for many portfolios, with the relative advantages of increased tax efficiency, rates of payment, which are typically over 2 percentage points higher than the 10-year Treasury bond, and potential dividend growth. The risk here is a rise in long-term rates.

General Motors Preferred "A" (GXM): Our bet that GM would not go bankrupt by mid-March 2007 paid off -- producing a 27% return in 2006. This position will be sold shortly.

News Corp. 'A' (NWS-A): We like News Corp for its Italian pay TV business, Fox News contract renewals with cable companies and the launch of the Fox Business Channel. MySpace and the rest of the online businesses are icing on the cake. Its recent deal with Liberty amounts to a 17% buyback of stock.

Nuveen Select Tax-Free Income (NXR): This exchange-traded fund pays 4.625% tax-free to investors, which is equivalent to a 7.7% return on a taxable bond for those in the top tax-bracket. If long-term interest rates stay steady investors will collect this return, but if interest rates rise, this investment will decline.

SK Telecom (SKM) is the #1 wireless telecom operator in Korea, with a free cash flow yield of about 9%. As domestic telecom regulations promoting competition (i.e. helping SKM's competitors) are rolled back, SKM should continue to benefit. A 2006 \$1 billion investment in and partnership with China Unicom may provide a lucrative growth opportunity. Other growth initiatives include a domestic music download site, an online gaming site, wireless transaction processing, wireless telecom services in Vietnam, and a partnership with Earthlink to provide high-end wireless services to tech

savvy youth in the U.S. called Helio (we wish they'd shut this down!). Where the 2006 risk was how they will find growth opportunities, the 2007 risk is how the China opportunity will work out. We don't know how the China Unicom relationship will develop, but if it doesn't, SKM can get their \$1 billion back in 2009.

Vanguard Health Care VIPERs (VHT): Demographics deem this industry the place to be for the next 20 years in our country. We're no healthcare experts here, so we used the cheapest way to place a bet on the whole industry, paying just 0.26% in annual fees. Up 7% in 2006 -- so far, so good.

Performance of Hurley Capital Investments

	<u>Action</u>	<u>Initial Investment</u> Date	<u>Symbol</u>	<u>Name</u>	<u>Total Return to</u> Date*	<u>Transaction</u> Price	<u>12/31/2006</u>
<u>2006 Transactions</u>							
	Bought	30-Nov-06	CNQ	Canadian Natural Resources	-2.3%	54.33	53.23
	Bought	28-Sep-06	DISCA	Discovery Holdings 'A'	11.6%	14.40	16.09
Hedge closed 10/6/06	Sold Call	15-Sep-06	DE AP	Deere & Co. Jan07 \$80 Call	-86.0%	3.88	10.71
	Bought	12-May-06	DELL	Dell Inc.	3.2%	24.33	25.09
	Bought	28-Apr-06	DMCX	Datamirror Corp.	44.5%	8.98	13.00
	Bought	16-Mar-06	POS	Catalina Marketing Corp	19.6%	23.23	27.50
	Bought	21-Feb-06	JCDA	Jacada Ltd	-1.6%	2.56	2.52
	Bought	14-Feb-06	CHK	Chesapeake Energy	3.1%	28.38	29.05
	Bought	04-Jan-06	NWSA	News Corp Ltd Cl A	39.9%	15.37	21.48
<u>2005 Transactions</u>							
	Bought	27-Dec-05	NXR	Nuveen Select Tax Free	8.7%	13.19	13.90
Sold 10/6/06	Bought	15-Dec-05	DE	Deere & Co.	23.0%	70.09	84.81
	Bought	12-Dec-05	COST	Costco	9.7%	48.60	52.87
	Bought	28-Nov-05	CHRZ	Computer Horizons Inc.	11.4%	4.03	4.52
	Bought	03-Oct-05	WMT	Wai-Mart	6.1%	44.03	46.18
	Bought	17-Aug-05	MMP	Magellan Midstream Partners LP	30.6%	31.70	38.60
	Bought	22-Jul-05	SKM	SK Telecom Ltd ADR	33.1%	20.65	26.48
	Bought	23-Jun-05	TPP	Teppco Partners LP	8.8%	41.06	40.31
Redeemed 12/20/06	Bought	17-Jun-05	465754AF6	i2 Technologies 5.25% Cvt Bond	11.7%	93.00	100.00
	Bought	27-May-05	GXM	General Motors Pfd "A"	14.0%	23.65	25.28
	Bought	18-Apr-05	KO	Coca-Cola	22.3%	40.87	48.25
Sold 12/4/06	Bought	25-Jan-05	CVX	Chevron Texaco	44.9%	52.51	73.53
<u>2004 Transactions</u>							
	Bought	28-Oct-04	VHT	Vanguard Health Care VIPERs	24.7%	46.56	56.94
	Bought	06-Oct-04	EEQ	Enbridge Energy Mgt LLC	25.9%	44.95	48.50
Redeemed 12/31/06	Bought	13-Sep-04	BMN	Blackrock Muni Trust	5.9%	10.67	10.00

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

Important Disclosure

The Hurley Capital Managed Accounts Composite represents all actual client accounts invested in this strategy for the entire year. 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.