Moose Pond Investors
Annual Report for 2005

Happy New Year to all! We are especially grateful that David Wake is home safely from Iraq and back with his family. We thank David for all that he has done for our country, the people of Iraq, and his fellow soldiers through his ministry. We also thank David's family for the sacrifices they made while he was serving in the Middle East.

We started Moose Pond Investors a little over five years ago. It is hard to believe that five years have gone by. We now have 18 partners made up of family and friends. Looking at our 5-year total return, we are well ahead the S&P 500 (large stock index) and almost even with the Russell 2000 (small stock index). While our return has been respectable, two of our underlying goals are to achieve a 15% annual return and to consistently outperform the major indices by several percentage points each year. We need to keep working in 2006 to achieve these goals.

Internet technology has made it easy to stay in touch with our partners who are literally all across the United States. Bivio.com has done a great job with its club accounting software. Our brokerage account at http://buyandhold.com/ automatically updates the club records on Bivio.com. This system works so well that we are able to get out the partnership tax return early each year.

As you may have noticed, we have migrated most of our investment discussions to our weblog at http://tyhughes.net/moosepond/. The weblog serves as a journal for our investment ideas and it documents our buy and sell decisions. Using the search feature on weblog we can find the stock selection guides and assumptions we used to make our buy and sell decisions. As time goes on, this ability to look back and learn from past decisions will be more useful.

Those who have been investing regularly in Moose Pond understand the advantages of dollar cost averaging. The annualized returns for these investors range from 4.9% to 8.4%. It is impossible – even for the so-called "experts" – to time the market. Investing regularly is the only way to compensate for the ups and downs of the market. Investing regularly (monthly or quarterly) will provide much better results over the long run than sporadically investing the same amount.

Portfolio Performance

Given the amount of effort that went into research and analysis this year, the results for 2005 were a little disappointing. On a cash flow basis, we finished with a very small gain. While that is better than losing money, we did not beat either the S&P 500 or the Russell 2000. They were up 4.9% and 4.6% respectively. On a positive note, we have soundly beaten the S&P 500 over the past five years and we are almost even with the Russell 2000.

The table and chart below show the annual return for Moose Pond Investors over the past five years. The "Stocks Only" column only shows the return of the stocks we held. The next column, "Stocks & Cash," includes cash awaiting investment and monthly brokerage fees. As a result, the return is slightly lower. As our portfolio holdings grow larger, cash on the sidelines and fees will have less of an impact on overall portfolio return.

The annual returns for Moose Pond Investors are calculated using internal rate of return (IRR). This method is more precise because it looks at actual cash flows. It better accounts for partner investments and market fluctuations throughout the year. We could have calculated annual return using the change in unit value from year to year. However, we opted for the more accurate IRR method.

The two indices that we have been using for comparison, the S&P 500 and Russell 2000, show the total return for each year including dividends. These return calculations do not take into account the actual cash flows for Moose Pond Investors.

Annualized Returns for 2001-2005

Year	Stocks Only	Stocks, & Cash	S&P 500	Russell 2000	Value of one unit
2005	0.3%	0.1%	4.9%	4.6%	$13.097
2004	16.1%	13.8%	10.9%	17.0%	$13.256
2003	35.1%	23.1%	28.7%	47.3%	$11.802
3-year	*10.4%*	*9.3%*	*12.4%*	*22.1%*	
2002	(23.4%)	(19.1%)	(22.1%)	(20.5%)	$9.707
2001	37.9%	13.8%	(11.9%)	2.5%	$11.970
5-year	*8.1%*	*7.1%*	*0.5%*	*8.2%*	

Moose Pond Investors Portfolio

At year end, our portfolio had a market value of $33,656. One unit in Moose Pond Investors is worth $13.097. We currently hold 24 stocks in our portfolio. Our cash position is $2,107 or 6.3%.

Portfolio Holdings

Current Holdings	Shares	Market Value	Pct of Portfolio	Date Bought	Gain or (Loss)	Annual-ized IRR
Brown & Brown Inc	41.9	$1,280	4.1	9-Mar-04	$480	30.4
Commerce Bancorp Inc	55.3	$1,902	6.0	26-Aug-03	$563	28.8
FactSet Research Systems	30.0	$1,233	3.9	12-Mar-04	$433	27.8
Lowe's Companies Inc	20.1	$1,338	4.2	1-Dec-00	$932	27.0
Amgen Co	15.9	$1,253	4.0	5-Aug-04	$353	26.5
Capital One Financial Corp	11.5	$997	3.2	14-Feb-02	$445	16.7
Marsh & McLennan Cos	32.6	$1,036	3.3	10-Nov-04	$133	15.4
Cardinal Health Inc	18.4	$1,264	4.0	11-Nov-03	$445	14.5
Affiliated Computer Services	29.7	$1,760	5.6	11-Nov-03	$255	12.9
Patterson Co	23.6	$789	2.5	7-Mar-03	$214	12.9
Chevron	29.2	$1,655	5.3	13-Jan-05	$77	11.3
Jack Henry & Associates Inc	85.4	$1,630	5.2	11-Aug-05	$44	10.7
Johnson & Johnson	17.0	$1,024	3.3	21-Nov-03	$126	9.5
Harley-Davidson Inc	19.9	$1,027	3.3	26-Aug-03	$23	2.2
Intel Corp	44.8	$1,118	3.5	1-Feb-01	($98)	-2.2
Bed, Bath & Beyond Inc	39.2	$1,417	4.5	11-May-04	($58)	-3.4
Wal-Mart Stores Inc	38.1	$1,785	5.7	17-Aug-05	($26)	-4.8
Maxim Integrated Prod Inc	34.1	$1,235	3.9	2-Feb-05	($97)	-7.4
Investors Financial Services	36.0	$1,327	4.2	7-Jul-04	($134)	-8.1
Pfizer Inc	72.9	$1,700	5.4	25-Jul-02	($332)	-9.6
Fifth Third Bancorp	39.1	$1,476	4.7	24-Mar-05	($184)	-14.1
UTStarcom Inc	49.1	$396	1.3	7-Jul-04	($754)	-51.8
Synovus Financial Corp	50.8	$1,372	4.4	15-Nov-05	($28)	NMF
Occidental Petroleum Corp	19.2	$1,537	4.9	15-Nov-05	$87	NMF
Cash		$2,107	6.3			
Total		*$33,656*			*$2,897*	

Winners and Losers

For the year, 18 of our stocks advanced while 12 declined. Our realized and unrealized losses totaled $167. This was offset by dividend income of $259 for a net gain of $93. Our worst performing stock was UTStarcom (UTSI).

UTSI underscores the market risk associated with stocks with extraordinarily high growth. The drop in UTSI value reduced the overall return for the portfolio by about 2.3%. Without UTSI, we would have come close to beating the S&P 500. Oh well.

The following tables show our top 5 winners and losers.

Top Five Winners and Losers in 2005

Top 5 Gainers	Percent Change	Dollar Change
Brown & Brown	41.2%	$367
O'Reilly Auto[1]	32.8%	$234
Amgen	22.9%	$266
Cardinal Health	18.6%	$195
Lowe's Co.	16.1%	$182
Total		*$1,244*
[1] We sold O'Reilly on 11/15/2005.		

Bottom 5 Losers	Percent Change	Dollar Change
UTStarcom	(63.6%)	($686)
Fannie Mae[2]	(23.5%)	($181)
Patterson Dental	(23.0%)	($236)
Investors Fin	(21.2%)	($296)
Harley Davidson	(11.3%)	($133)
Total		*($1,532)*
[2] We sold Fannie Mae on 3/24/2005.		

Portfolio Turnover

Our sales for the year totaled $5,935. We sold six stocks: QQQ, Fannie Mae (FNM), O'Reilly Automotive (ORLY), Lincare Holdings (LNCR), Johnson Controls (JCI), and Fiserve (FISV). Our total purchases for the year were $14,777. We took new positions in Chevron (CVX), Maxim (MXIM), Fifth Third Bancorp (FITB), Wal-Mart Stores (WMT), Synovus (SNV), and Occidental Petroleum (OXY). The rest of our new cash was reinvested in existing stocks.

Portfolio turnover is the rate of trading activity in a portfolio. It is equal to the lesser of purchases or sales, for a year, divided by average total assets during that year. Our average net asset value for 2005 was $29,509. Thus our portfolio turnover is calculated as follows:

Turnover = (Sales / avg. NAV) = ($5,935 / $29,509) = 20.1%

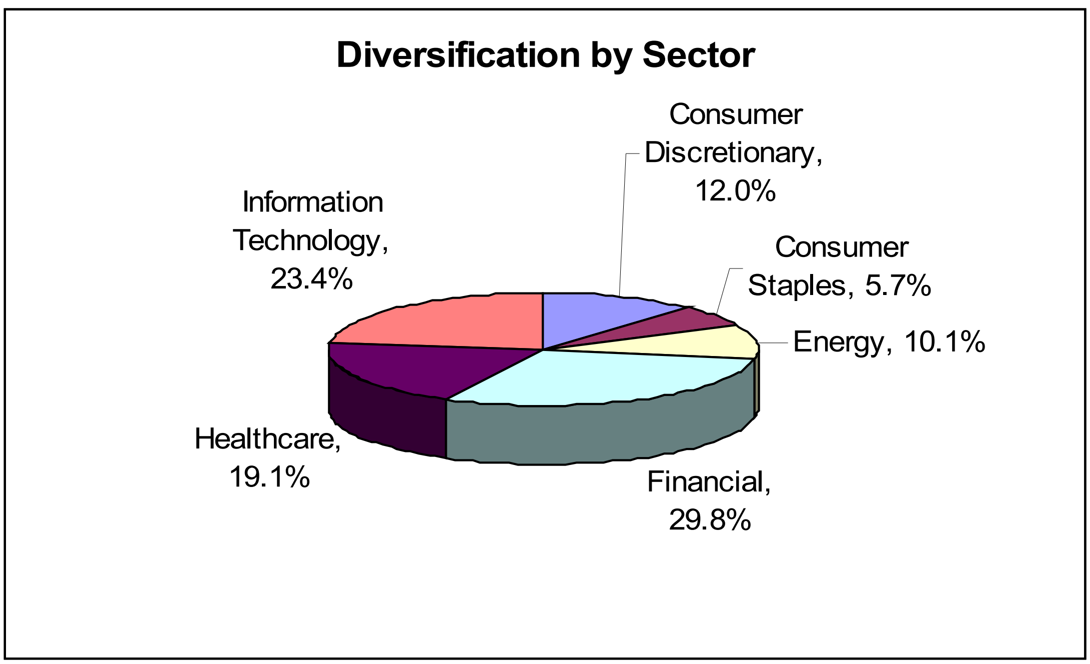
Stocks Sold in 2005

Sold in 2005	Date Sold	Net Gain or (Loss)	Annual-ized Rtn
O'Reilly Automotive Inc	15-Nov-05	$645	39.1%
Johnson Controls Inc	15-Nov-05	$628	22.6%
Lincare Holdings Inc	15-Nov-05	$323	22.1%
NASDAQ-100 (QQQ)	13-Jan-05	$111	18.6%
Fiserv Inc	15-Nov-05	$213	11.9%
Fannie Mae	24-Mar-05	($236)	(15.3%)
Total		*$1,684*	

Portfolio Diversification.

The portfolio contains 24 stocks in six sectors. This provides sufficient diversification to eliminate most of unsystematic risk in the portfolio. The portfolio has a RiskGrade of 48. (See RiskGrades.com for more information about unsystematic risk.)

The sector diversification does not mirror any particular index. We achieved this diversification by purchasing quality growth stocks when were selling at an attractive valuation. For more information, see the portfolio diversification report on the weblog.



Our Investing Philosophy

We invest in **quality** companies that **grow their earnings** based on a sound business model. We buy these stocks when they are priced to provide **superior long term returns**. While many investors and mutual funds invest in either "growth" or "value" stocks, we look for companies that have both attributes. Growth, quality, and value are interrelated.

A company should have a sound business model that has demonstrated consistent growth in revenue and earnings over the past 3 to 5 years. The company also should have the potential to sustain growth in revenue and earnings into the foreseeable future.

The **quality** of a company, which usually reflects strong management, manifests itself in several ways, including: (1) consistent historical growth in revenue and earnings, (2) steady or increasing pre-tax profit margins, (3) steady or increasing return on equity that is greater than the industry median and is generally greater than 15%, and (4) a strong balance sheet.

Value Line ratings of B++ or better for Financial Strength and 85 or better for Earnings Predictability correlate well with quality and good management. We also compare each company's prospects for future growth and net profit margins with other companies in the same industry. The Manifest Investing quality rating combines these four factors into a single 100 point rating.

Superior long term returns can be assessed in two ways – (1) by calculating intrinsic value for a company using discounted cash flow or (2) estimating the projected average return using a stock selection guide or similar calculation. Using the stock selection guide, we look for a projected average return (PAR) greater than 15%. We also look for quality stocks that sell below their intrinsic value. Morningstar uses a discounted cash flow analysis to determine the fair market (or intrinsic) value of a stock. Stocks rated 4 and 5 stars sell below their intrinsic value. It is generally easier – although not as precise – to compare stocks using their projected average return from the stock selection guide.

We prefer companies that, if purchased, offer the possibility of price earnings (PE) ratio expansion. We generally avoid companies with high PEs, particularly when the PEs have been contracting in recent years. High growth stocks with high PEs are particularly vulnerable to large downward price adjustments if the growth outlook for the company slows down.

Portfolio management is as important, perhaps more important, as selecting good stocks. Several general principles guide our portfolio management:

- We try to stay fully invested and to keep our cash position below 5%.
- We don't try to time the market.
- We maintain about 20 stocks in our portfolio +/- 5. We reinvest all of our dividends in the companies paying the dividends or in the portfolio.
- We will replace a holding if the company's fundamentals deteriorate or if the company becomes overvalued.
- We will replace an individual stock if the replacement company will improve the overall projected average return or the quality of the portfolio.
- We consider diversification when making purchases and try to stay invested in at least five different sectors but we do not have any strict rules about sector weighting or company size.

Summary

We wish all the partners of Moose Pond Investors and their families a prosperous and happy New Year.

Ty Hughes
December 31, 2005

Corrected: 10 Jan 2005