SARA-BAY FINANCIAL CORP.

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When a popular index like the Dow Industrials pushes to new high, a lot of investors appear enormously pleased. Making money in the market seems like a piece of cake. The formula is remarkable simple: buy a few stocks with popular names and hang on to them. Broadcasters like CNBC tend to exacerbate these buoyant emotions and further fuel the passion. No longer content to simply report the advance, they now flash numbers on the screen showing how many points before the Dow reaches a new high, or how much it is above it. The media loves to sensationalize this recurring theme of "breaking news," even though after reaching a new high, it takes less than a point to set another new record. We believe the real danger created by this atmosphere is that it engenders a sense of complacency and overconfidence on the part of many investors. This feeling of invulnerability will ultimately result in increased carelessness in the selection of investments, and generally leads to a bad end.

In May of 2005 we wrote a client letter both discussing and warning of the rapid increase in real estate prices. We believed that the rate of gain was entirely unsustainable, and therefore posed a substantial threat to new investors entering that market. That letter was greeted less than enthusiastically by a few of our customers, and a couple of people reminded us that we were not experts in real estate (which is emphatically true). But the fact is that extreme price advances, regardless of the asset class, have certain characteristics in common. In sending that letter, we were wrong with our timing. The real estate market did not hit the wall until October of that year. However, had you made an investment anywhere near that time, you are likely still under water, and may remain so for some time. This assertion is not intended to be universally applicable. There are always selected pieces of real estate as well as individual stock selections, which continue to thrive, but they are the exception, not the rule.

Major price advances, or bubbles, do not typically correct themselves in a year. By their very definition, they are long-term in nature. The bubble is created as more and more people quietly begin to enter the market. The pinnacle is finally reached when the majority concludes that prices can only move in one direction - up. After a top of this magnitude, it may take several years, or even more than a decade for normalization to occur. During these long periods of correction, there are major waves up and down, and many opportunities will present themselves. The important thing is to remember not to become overly enthusiastic during these interim advances. There is a good possibility we may have not fully recovered from the aftermath of the stock market bubble of the '80s and '90s, which ended in early 2000.

Approximately two months ago the Dow Jones Industrial Average established a new record high. Keep in mind, the Dow is comprised of only thirty stocks. The S&P 500 is made up of 500 major companies, and the NASDAQ Composite contains over 3000, thus being more accurate measures of the true market. All three of these indices hit their all-time highs early in the year 2000. As of December 31st, 2006, the Dow was 4.4% over that high, but the S&P was 8.6% below, and NASDAQ ended the year a whopping 53.0% below.

When managing accounts, we have two primary goals: 1) Achieve a superior long-term return, and 2) Guard the capital. Number two is just as important as number one. For the last several months we have been increasing the money market positions in our managed

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accounts. The stock market made an important low four years ago, and, as referenced above, the rate of climb has been escalating. Make no mistake about it; there is more danger in being fully invested in the market now than a couple of years ago.

It is never easy holding a larger than normal position in money markets or staying on the sidelines, as stock markets rapidly advance. This is especially true when the popular media is trumpeting, "Come on in, the water's fine!" But, we have been there before. It is somewhat reminiscent of 1999 and 2000, when the trumpets blared even louder. Where are WorldCom and Enron today?

Falling stock markets are not necessarily bad, as the media might have you believe, nor are they the harbinger of the end of western civilization as we know it. As prices fall, and bad news begins to roll like thunderheads on the horizon, opportunities begin to quietly arise. Declining markets have always provided us with our best investments, that will, in time, deliver our best gains. Downward cycles have been with us since the first stock was traded, and it is likely we will see one again. When this occurs, don't get discouraged. We have funds available and dropping prices will give us our chance.

Again, we thank you for your continued confidence in us.

Sincerely,

Mike

Mike Hard

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