Athena Capital Management Corp.

October 5, 2005

Greetings from beautiful Colorado Springs!

Hopefully, this client letter gives you a better idea of what to expect from future letters. In it, I briefly summarize how we're doing and update you on what I expect from the stock market over the next six years. After this, I comment on long term focus in an essay titled, "Take the Long Way Home." I hope you find this letter both informative and entertaining.

How are we doing?

From April 30, 2005 until the end of the third quarter, our growth accounts averaged returns of 4.34% versus 7.05% for the S&P 500 and 8.92% for the Wilshire 5000. From May 31, 2005 until the end of the third quarter, our equity income accounts returned 3.74% versus S&P-500-yield-plus-inflation returns of 2.83%. Please don't feel anxious or joyous about performance so far; our 4 to 5 month record is not long enough to be meaningful, yet.

So, what has done well and what has done poorly this quarter? As I mentioned in my note to you near the end of September, our energy and mining companies out-performed. In contrast, our insurance, retail and industrial companies under-performed. In my opinion, the investments I've selected for us continue to be backed by good fundamentals, and my assessments of valuation have not changed. In other words, I think our investments still represent good long term value.

What's likely to happen going forward?

When asked what the stock market would do in the short run, John Pierpont Morgan is famous for replying, "It will fluctuate." I couldn't agree more. Over the long run, however, I think it's possible to put a likely range on market returns. Below is my updated assessment for growth and equity income benchmarks over the next 6 years.

	Projected annualized returns over the next 6 years
S&P 500 (growth benchmark)	-6.7% to 7.9%
S&P-500-yield-plus-inflation (equity income benchmark)	3.4% to 6.4%

For those interested in my method for deriving these numbers, please visit www.athenacapital.biz (our website) and check under Free Articles for my 7/12/05 article.

As you can see, I continue to be unexcited about returns for the overall market going forward. Although I can make no guarantees, I think we have a good chance to do better than this.

In contrast to my projections, the average individual investor continues to be optimistic about future returns. The table below shows what individual investors expect going forward.

Long term annualized return expectations	**Percentage of people**
0% – 7%	23%
8% – 10%	42%
11% and higher	35%

Source: Rydex.

Please note that 77% of investors disagree with me about future returns. This is understandable because the stock market has generally provided 10%+ returns in the past. Unfortunately, that 10%+ number depends on where you start. Because we are not starting at average, lower stock market returns should be expected going forward. Please be cautious in your financial planning not to use overly optimistic assumptions.

With my comments about the past and future out of the way, here's my take on why long term focus is important for investing success.

Take the long way home

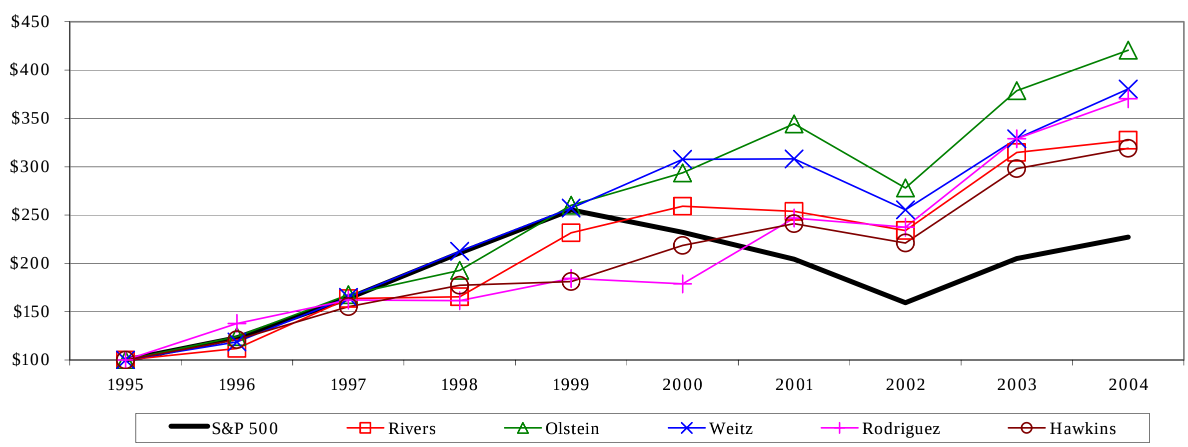
I'd be willing to bet some people in Louisiana and Mississippi are going to be laughing all the way to the bank. For the last 50 years or so, they chose to pay for flood insurance. Because so many people see this as a waste of money, their neighbors, friends and relatives have probably been laughing at them. I'm certain they've doubted their choice a hundred times. But now, they will be getting a check from their insurance company that will quickly put their lives back in order, while their uninsured neighbors wait for government aid.

This is a lucid illustration of why it's best to think long term and act on your own judgment. The stock market, too, richly rewards people who think this way. Numerous studies have shown that above average returns were consistently earned by those who focused on the long run and didn't follow the crowd.

Look at the record. Below is a table that shows the performance of some of my favorite investors (and me) over the last nine years. The first two columns show how the market and each investor did. The next five columns show the percentage of 1, 3, 5, 7 and 9 year periods over which these managers beat the S&P 500.

		% of the time managers beat the market over:				
	Annualized Returns	**1 year periods**	**3 year periods**	**5 year periods**	**7 year periods**	**9 year periods**
S&P 500	9.55%					
Rivers	14.09%	67%	71%	100%	100%	100%
Olstein	17.30%	89%	86%	100%	100%	100%
Weitz	16.00%	78%	100%	100%	100%	100%
Rodriguez	15.66%	67%	57%	80%	100%	100%
Hawkins	13.76%	44%	57%	80%	100%	100%

In this table, you can see my investors only *sometimes* beat the market in 1 to 3 year periods, but *almost always* won in 5+ year periods. Even better, look at the chart below that shows the same information in graphical format.



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As this graph illustrates, my investors frequently looked like slackers in 1 to 5 year periods, but, in the long run, they ended up with significantly more money.

Why is it that many investors with great long-term records frequently display mediocre-to-poor 1 to 5 year performance? Because it's almost impossible to be smarter than the market in the short run. The best way to beat the market is to think long term and act independently. Lucky for us, most people focus on the short term and follow the crowd.

If the record is so clear, why doesn't everybody think long term and act independently? Because it's hard. People will point and laugh at you for doing poorly in the short run. Your friends, family and co-workers will ask you, "what do you think you're doing?" You will even doubt yourself on many occasions. It's perfectly natural to feel this way—it's only human.

In fact, people seem to be wired to focus on less than 1 year periods. This makes some sense. Most of what we humans focus on happens within a year. The seasons go full circle, crops are planted and harvested, goods are produced and sold, and Christmas comes and goes.

But, there are many things in life that need long term focus. For instance, raising your kids, building a career, and planning for financial needs all require long range planning and action. I must acknowledge, however, that such long haul thinking is tough to keep in mind when you seem to be lagging everyone else. It's especially tough when you open your quarterly statements and want to be doing better, *right now!*

Stick to it, though, because using the right time frame to judge performance is critical to investing success. As support, countless studies show the leading reason why many people don't reach their financial goals is because they focus on monthly, quarterly, annual and 3-year performance. This short term focus causes many people to panic at some point, and then to move out of their under-performing investments right as they bottom and into out-performing investments just as they top. That is why they don't reach their goals.

I know this sounds preachy, but the record is clear. Focus on the long term and act independently. Don't let that nagging worry in the short term cause you to do something you will regret later. And, feel free to have the last laugh when you reach your goals sooner than those who were laughing at you.

How am I doing?

As usual, your comments, questions and suggestions are more than welcome. The best way for me to improve my service is for *you* to tell me what I'm doing well and poorly. Don't worry, I'm thick-skinned. Besides, I would much rather be doing a good job than deluding myself into thinking I am.

If you like my service and know other independent-minded, long-term-oriented investors who might benefit from my approach, feel free to pass my information along to them.

Until next quarter,

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