

<b>INVESTMENT STRATEGY OVERVIEW</b>
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The hope of a strong finish in the final quarter of 2005 failed to materialize as the market limped along in December. The stock market managed to generate modest progress during the fourth quarter, and the returns for the year among the major averages listed below were mostly positive.

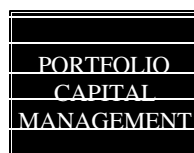
	<u>Value</u>	<u>December</u>	<u>3 Months</u>	<u>2005 YTD</u>
DJIA	10717.50	-0.8%	1.4%	-0.6%
S&P 500	1248.29	-0.1%	1.6%	3.0%
NASDAQ Comp.	2205.32	-1.2%	2.5%	1.4%
Value Line 1700	412.50	0.3%	0.7%	2.0%
Russell 2000	673.22	-0.6%	0.8%	3.3%

Market participants continued to worry about the same concerns that have been over hanging the market for the past six months, oil prices, interest rates, and economic growth. Energy prices remain high although prices retreated briefly as warmer weather in December eased fears of an inventory shortage. The Federal Reserve continued to raise interest rates therefore market pundits predict one or two more increases are likely in early 2006. Retail sales in the Holiday season were good, but not so robust as to spur investor enthusiasm for stocks.

In the third quarter hurricane Katrina and Rita dominated the economic and political news. However, the economic impact on GDP has proven to be far less worrisome than initially anticipated, which is good news. Most economists have indicated higher energy prices should reduce GDP growth by 1% in 2005. In addition, lower consumer confidence coupled with higher energy prices will continue to be a mild drag on the economy over the next several quarters.

Economic growth should remain near 3% in 2006, following the expected 3.5% for this year. Housing activity will slow next year as higher interest rates will reduce demand, however, a collapse in housing activity is likely to be avoided so long as interest rates do not soar or a major decline in employment levels occurs. There are significant risks in current mortgage lending practices that have magnified the housing boom. The use of "payment option" adjustable-rate mortgages along with other more risky lending practices has risen to over 50% of mortgages in some high-cost areas. As a result, regulators proposed more stringent guidelines for loan terms, underwriting criteria, and risk management practices for such nontraditional mortgage loan products.

The core inflation rate for both the CPI and PPI has remained near 2.0%. We anticipate a modest pick-up in the rate to 2.25% - 2.5% over the next several quarters. We expect winter heating cost will be one of the catalysts to the forecasted pickup of inflation over the next several months. If a pickup in inflation remains below 2.5% the fear of higher labor rates and the possibility of energy cost pass-through may be avoided in 2006. Historically manufacturers have passed higher energy costs in the form of higher prices. The speed at which this occurs will determine the future inflation rate.



Corporate profits have remained strong as S&P 500 earnings rose nearly 11% in the last year through the September quarter. Profit growth should slow and fourth quarter comparisons will decelerate. The combination of higher commodity prices and rising labor cost will affect margins and earnings. Profit growth will also slow to around 7% for the balance of this year and 2006.

### **Stock Market Outlook/Strategy**

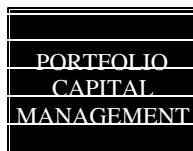
The market returns in 2005 were below a modest forecast of mid-single digits (5-7% for 2005). The sub par returns reflect the lack of compelling valuation in the market and more importantly the uncertain outlook concerning energy prices, inflation and future interest rates. Bond returns were in the 1.6 to 2.3% range as rising short term rates impacted the total return from bonds as prices of bonds fell. The best fixed income returns came from cash as U. S. Treasury Bills returned 3.0% for the year. We are confident that investment returns in 2006 will exceed those of the pass year.

We continue to view our near-term outlook as cautious, but our longer-term outlook (3-5 years) as positive. We expected large capitalization stocks to provide above average returns in 2005, however, that expectation failed to materialize as mid and small capitalization stocks and international stocks outperformed. We remain convinced that the most under valued sector of the stock market is large capitalization stocks. Our emphasis in this sector should prove rewarding to investors in 2006.

Our equity returns trailed the returns for the S&P 500 for the year 2005. The shortfall in performance was concentrated in our exposure in the technology sector as well as having an underweighted position in the energy sector. The shortfall in performance occurred mostly in a single month, September. During the 4<sup>th</sup> quarter we sold Symantec and Sonoco Products and established new positions in Baker Hughes, General Mills and Texas Instruments.

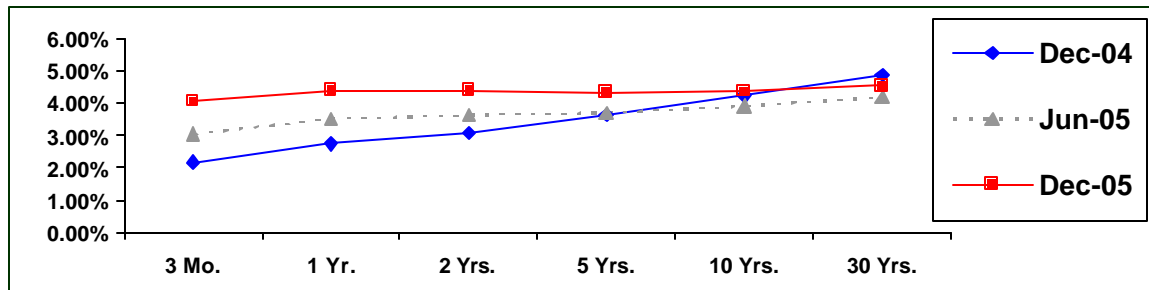
We have added a research analyst to our staff, Robert Fontana. We are confident this addition will prove rewarding to our clients as Bob's excellent credentials and track record should help enhance our stock selection and performance in the future.

Over the last five years, the majority of our accounts have fared better than the S&P 500. We have been very pleased with our relative performance on a long term basis. Although our performance on a one and three year basis is currently underperforming we feel our focus on high quality growing companies will translate into superior investment returns going forward. We remain committed to our investment style of value investing in growing companies. This strategy has proven itself over the last 20+ years and we feel as strongly as ever that it will continue to do so in the future.



### Fixed Income Outlook

The Federal Reserve has increased short term interest rates thirteen times and the Federal Funds rate is currently at 4.25%. We believe we are nearing the end of the interest rate hikes by the Federal Reserve. The language of the Fed has changed indicating they believe their action is accomplishing the gradual slowing of growth and containing inflation before it becomes troublesome. The Federal Reserve has left themselves a good deal of latitude to adjust future changes in the Federal Funds Rate based on economic conditions as they view them in the future. The core rate for both the PPI and CPI has increased over the past twelve months. In addition, evidence continues to demonstrate that corporations, for the first time in several years, have been able to pass along their higher raw material costs to the consumer.



	<u>12/31/04</u>	<u>06/30/05</u>	<u>12/31/05</u>	<u>2005 Change</u>
3 Mos.	2.18%	3.05%	4.08%	+1.90%
1 Yr.	2.74%	3.51%	4.40%	+1.66%
2 Yrs.	3.08%	3.63%	4.40%	+1.32%
5 Yrs.	3.63%	3.70%	4.35%	+0.72%
10 Yrs.	4.25%	3.91%	4.39%	+0.14%
30 Yrs.	4.87%	4.19%	4.54%	- 0.33%

The yield curve shown above has become virtually flat, and during December we witnessed a brief inversion of the yield curve as two year rates moved above the ten year rate. Frequently, an inversion in the yield curve has preceded the onset of an economic recession. The inversion does not insure a recession and we, as well as most economists, are not anticipating a recession in 2006. We believe the flattening reflects an overly optimistic bond market that believes the Federal Reserve will be completely successful in controlling inflation. With inflation likely to move higher and the dollar weakening, we anticipate a moderate increase in longer term interest rates over the next several quarters.

