

January 1, 2008

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| <b><i>INVESTMENT STRATEGY OVERVIEW</i></b> |
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The stock market was lower in the fourth quarter as fears of a “credit crunch” worried investors. The financial stocks led the downdraft, however, the sell-off was fairly broad as the DJIA, Russell 2000, and Value Line all saw their averages decrease by over 4% as indicated below.

|                 | <u>Value</u> | <u>December</u> | <u>3 Months</u> | <u>2007 YTD</u> |
|-----------------|--------------|-----------------|-----------------|-----------------|
| DJIA            | 13264.82     | -0.8%           | -4.5%           | 6.4%            |
| S&P 500         | 1468.36      | -0.9%           | -3.8%           | 3.5%            |
| NASDAQ Comp.    | 2652.28      | -0.3%           | -1.8%           | 9.8%            |
| Value Line 1700 | 440.28       | -1.5%           | -6.9%           | -3.8%           |
| Russell 2000    | 766.03       | -0.2%           | -4.9%           | -2.7%           |

The financial markets have continued to focus on the problems in the residential mortgage market spreading throughout the domestic economy. In addition, the rise in oil prices, into the mid-nineties, has raised the fear of stagflation (rising inflation and sub par economic growth). While third quarter economic growth was a robust 4.9%, economist have continued to lower growth estimates for the next several quarters. GDP is forecast to grow between 1.0% and 1.5% in the fourth quarter. At this time we continue to expect growth to remain positive, thereby avoiding a recession according to the classic definition of two negative quarters of growth.

The slowdown will also impact corporate profit growth both this year and in 2008. The S&P profit growth for 2007 is expected to rise between 5.0% and 6.0% and slow further in 2008 to around 4.0%. The financial sector is impacting overall profit growth as earnings fell in this sector by 5.0% year over year. The decline should be more severe in the fourth quarter as banks and investment banks continue to write off non performing assets.

Housing has remained weak as new home sales and prices continue to decline. The weakness is expected to continue well into this year. Fortunately for the overall economy export growth has remained strong and has helped offset the weak housing sector. Consumer spending has held up relatively well, although Christmas sales were moderately below expectation. We expect the consumer to become more cautious as the combination of negative housing news and high oil prices impact future spending decisions.

We anticipate that inflation will be higher over the next several quarters. Oil prices and many commodity prices have been at or near record highs. Likewise, gold has been strong and the dollar has been weak versus most foreign currencies. We suspect the bias on future inflation is to move beyond the Federal Reserves desired range, however, restoring confidence and lessening the “credit crisis” is far more important than a short term increase in inflation. We feel the Fed will err on the side of avoiding a recession and returning normalcy to the credit markets, rather than worrying about aggravating inflation over the short term.



## Stock Market Outlook/Strategy

The market returns in the fourth quarter were negative as the S&P 500 and the DJIA declined 3.8% and 4.5% respectively. The markets showed weakness throughout the quarter despite a couple of cuts in the Fed Fund rate by the Federal Reserve. The general feeling has been that the banks and investment banks have more significant write-downs to take in the fourth quarter, although we have already seen some significant ones. Furthermore, the weakness in the housing market and the fear that it will get worse before it gets better has some analysts believing the consumer will lessen their spending habits. The Russell 2000, a small capitalization index, fell 4.9% during the quarter. The market made returns in 2007 slightly below historical averages. The sectors that outperformed were commodities, energy, technologies, and utilities. The weakest performing sectors have been and continue to be financials and consumer discretion.

We believe valuation levels for large companies remain the most compelling when compared to other sectors of the market. In addition, larger companies who have more international exposure should continue to perform better than domestic companies who are dependent on the U.S. consumer. We are approaching the point where valuation levels for selective consumer discretionary stocks are becoming attractive; however, we need to see further evidence that the consumer will have both the ability and willingness to spend. We also believe that the point to increase our investment in the financial sector is drawing closer, however, we feel that time may be another three to six months away.

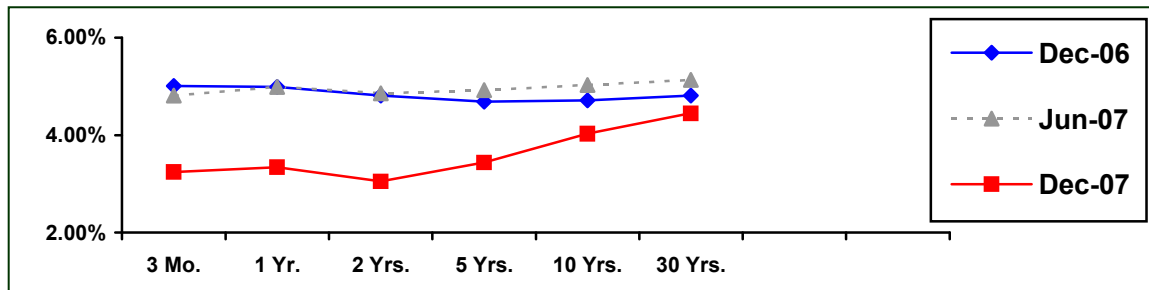
During the fourth quarter we made several changes to the portfolios. The stocks that were sold from the portfolios were Amdocs (DOX), American Int'l Group (AIG), Electronic Data Systems (EDS), Genworth Financial (GNW), and Walgreen's (WAG). We also cut back the position of BHP Billiton (BHP) as the stock increased over 50% in a relatively short time. The stocks that were added during the quarter were Ameriprise Financial (AMP), Express Scripts (ESRX), IBM (IBM), Kimberly-Clark (KMB), and Peabody Energy (BTU). Our purchases were concentrated in economic industries that we view constructively such as consumer staples, energy (coal), and generic prescription drugs. We continue to hold modest cash levels that will enable us to take advantage of attractive new opportunities that present themselves in the coming months.

We are very pleased with our relative performance in the fourth quarter as our returns were generally ahead of the S&P 500. The returns for 2007 are also ahead of the S&P 500. Those accounts with large low cost basis in selective financial services (mostly bank stocks) will have lagged the returns of our other accounts due to the "credit crunch" that we spoke about earlier. Our investment style has served our clients well over the long term and our investment returns since the peak in the market in 2000 have been very good. We preserved our client's assets in the Bear market and continue to increase client's assets in a prudent and consistent manner. We remain committed to our investment style of large-cap core investing in growing companies.



### Fixed Income Outlook

The Federal Reserve has responded to the mortgage mess by lowering the Federal Funds Rate by 0.75% to 4.50% and adding short term liquidity to the market. These trends of lower rates and increased liquidity have also occurred in the major European countries. The world central banks are working together to resolve the current “credit crisis.” Given the recent weaker economic news we expect the Federal Reserve will continue to lower the key lending rate in the first quarter. The yield curve has dropped sharply in the past six months, with the short end of the Treasury curve approaching yields of 3.0%. The longer end has fallen less as market participants fear higher inflation in the months ahead. The reaction of the short end of the market indicates market participants anticipate further easing the Federal Reserve.



|         | <u>12/31/06</u> | <u>06/30/07</u> | <u>12/31/07</u> | <u>2007 Change</u> |
|---------|-----------------|-----------------|-----------------|--------------------|
| 3 Mos.  | 5.01%           | 4.81%           | 3.24%           | -1.77 %            |
| 1 Yr.   | 4.99%           | 4.99%           | 3.34%           | -1.65 %            |
| 2 Yrs.  | 4.81%           | 4.86%           | 3.05%           | -1.76 %            |
| 5 Yrs.  | 4.69%           | 4.92%           | 3.44%           | -1.25 %            |
| 10 Yrs. | 4.71%           | 5.03%           | 4.03%           | -0.68 %            |
| 30 Yrs. | 4.81%           | 5.13 %          | 4.45%           | -0.36 %            |

The yield curve shown above has become significantly more positively sloped as a result of the recent rate cuts. The yield curve, beyond 2 years, has a more normal positive slope. The policy action of the Federal Reserve can dictate the level of short term interest rates; however, market participant’s action will determine the direction of longer term interest rates. As of this writing investors are worried that as the economy slows and inflation remains elevated that there could be a period of stagflation.

