



January 13, 2006

**RE: 2005 in Review & 2006 Outlook**

**Dear Valued Client:**

With the stock market “stuck” in a tight trading range, and the bond market posting its first loss since 1999, most investors will want to forget about 2005. From a money management standpoint, I found 2005 especially tricky to navigate between investment valuation concerns and possible client tax ramifications caused by profit taking transactions. Yet 2005 was a defining investment year. In an environment of rising interest rates, high oil prices, terrorist attacks, auto industry problems, and devastating hurricanes the S&P 500 index managed to finish in positive territory, and the bond market’s decline was minor. In other words, stocks and bonds ignored a lot of bad news and held most of the gains made over the last several years.

**2006 should be an interesting year for the following reasons:**

1. Sideways moving markets are usually followed by strong advances (1984, 1% vs. 1985, 26%, and 1994, -1.7% vs. 1995, 31%). Will history prevail in 2006?
2. The Federal Reserve is expected to stop raising interest rates soon and bond prices typically “snap back” quickly when this occurs as new bond purchases are made by yield-hungry investors.
3. As evidenced by the recent price decline in home building stocks, the three-year real estate rally has stalled and housing prices will probably be soft for several years to come.
4. The U.S. dollar posted a 13% increase over the last 12 months. Foreign stocks and mutual funds don’t perform well in a strong dollar environment. In fact, Chinese stocks have declined for the second year in a row.

**Growth Investment Outlook: S&P 500 should finish the year near 1370!**

Our research indicates a strong possibility of a 9% to 12% rally in the S&P 500 during this year, if there are no widespread earnings disappointments during this month and the Federal Reserve stops raising interest rates soon.

Last fall we were actively rotating out of lagging investments into companies with strong prospects for 2006. It is important to note that in this “stock picker’s market,” investment selection is an important key to success and our tolerance for any stock falling below its 200-day moving average is low. Stock market history is full of examples of once-popular stocks trading sideways for many years.

**Income Investment Outlook: The best buying opportunity in 3 years!**

When bond prices decline, it is a mixed blessing for “buy and hold” investors. While it hurts to see the liquidation value of bonds decline on brokerage statements, there is an increase in the availability of new bonds at higher yields.

It is important to remember that the primary objective of income investments is to provide steady cash flow with near certainty of principle returned at a future date. In other words, a bond investor knows how much interest is paid annually, when the bonds comes due, and that principle will be repaid most of the time.

As higher-yielding bonds recently appeared in higher numbers, we were actively adding bonds as well as selected equity income investments to the portfolios we manage. Once the Federal Reserve stops raising interest rates, bond prices typically “snap back” quickly and bond inventories “dry up” as new bond purchases are made by yield-hungry investors.

**Other Items:**

**Tax Loss Carry-forwards (TLC):** Our policy has been to sell losing investments near year-end and to use those losses against current or future profits in order to reduce capital gains taxes. When you complete your 2005 tax returns, please check with your accountant to see if you have TLC left to offset gains in 2006 and forward the information to us.

**Client Restricted Investments:** Please keep in mind that any investments listed under “Client Holdings” on your Portfolio Overview report have not met our selection requirements and therefore are not treated in the same manner as those we select. Please let us know what your objectives are for these holdings. In general, we find these investments inferior to the holdings we select, and we recommend that you allow us to remove them from the portfolio. Also, you can call the brokerage house directly on trading these investments if we are not available to help you.

**Out-of-Office Client Meetings:** Due to the growth of our business, I have decided to limit the amount of traveling I do to January through April, and to use in-office meetings, conference calls, and video conferencing for the remainder of the year. Please try our free video conferencing service. We believe that this “easy to use” system will greatly increase our ability to communicate with our clients by being able to see each other on computer screens during phone calls. The internet address used for our conference calls is <http://people.sightspeed.com/ken@winansintl.com/>. FYI, you do not need a computer video camera to use this service. Give it a try; it is the future!

As we enter our 14<sup>th</sup> year of operation, I want to thank you for your continued business. Please let me know how we can better serve you in the future.

Sincerely,

**Kenneth G. Winans**  
**President & Founder**