Lesjak Planning CORPORATION

The Advisor

FALL 2006

Market Comment

This summer has been much like those before, in that it has provided plenty of volatility. We were pretty much fighting back from the May-June decline brought on by interest rate and inflation fears, when the Middle East conflict began and threw a whole new round of negative scenarios at investors. Stock prices fell for a few weeks on speculation of oil shortages and even the possibility of a third world war.

Whenever market fundamentals are healthy, attention must eventually turn to them...

As usual, it took the refocusing on the better than expected earnings reports from corporate America to turn the markets in the positive direction. The fact that the inflation numbers leveled off, which prompted the Federal Reserve Board to not raise interest rates in August, also helped. Whenever market fundamentals are healthy, attention must eventually turn to them and the markets will rise accordingly.

Small cap issues, which have lead all asset classes since 1999, have started losing investors

The current corporate earnings environment should continue to promote the already robust spending on equipment, inventories, structures and employment. This quarter marks the 12th consecutive quarter that profits have grown at least by ten percent. If this double digit growth persists until the end of the year, it will be the longest period of such growth since records began in 1950.

The stock market responds to such growth periods and its current recovery since 2002 is a testament to that. Good profits also help lay a good foundation for stocks in turbulent times such as these past 4-5 months.

Going forward, interest rates, inflation, cost of energy and higher labor costs all can have an effect on future earnings. Our economy in the States is showing signs of slowing and we know increasing margins are affected by the factors above and can not go on indefinitely. If, as expected, profit margins experience a gradual decline well into 2007, then we can assume that a foundation will stay in place to allow for continued equity performance in the future.

Negative news also affects market prices and short term trends. Take, for example, the rise in oil prices prompted by the battle in Lebanon and threatened sanctions against Iran over their nuclear program. Prices rose in anticipation of disrupted flow, which in turn lead to talks of higher inflation and reduced corporate earnings as our economy started slowing. Stocks fell in sympathy of all these negative expert opinions. BP Oil then came out with the news it had to close its pipeline from Alaska due to corrosion problems. Experts predicted $100 per barrel oil by year end. With all

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Market Comment

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of the negative commentary on oil, we have seen the price steadily decline to its lowest level in months. Just like the stock market, commodities like oil revert to their real value once you look past the hype. One noted energy analyst calculates that the fear premium has added at least $30 to the price of oil per barrel. Take away the fear factor and oil is at $40 per barrel. This same analyst says proven oil reserves worldwide in 1980 amounted to 29.6 years of consumption at 1980 usage rates. In 2005, the world had 40.6 years of consumption at the 2005 rates. We have a larger cushion of reserves now than we did in 1980 due to better technology and more oil exploration. Oil is being priced with the higher risk premium today because of fear that we are vulnerable to various world events or threats. In reality, there have always been risks of oil supplies in Iran, Iraq, Nigeria and other mideast countries. Avoid the negative news.

This spring we have seen investors begin the transition of accepting less risk exposure than in the prior couple years in both the U.S. and world markets. Small cap issues, which have lead all asset classes since 1999, have started losing investors to the more attractive large cap issues; especially those with a value bias. This transition from the growth sector, both large and small, to the value style is illustrated in the graph below. We think the trend towards the more undervalued large cap equities will continue into the near future as investors reduce their appetites for risk. One such value manager, Chris Davis, is highlighted later in this newsletter. A well balanced allocation will allow participation in these various sectors as they become desirable.

Bailing Out Affects Long Term Returns

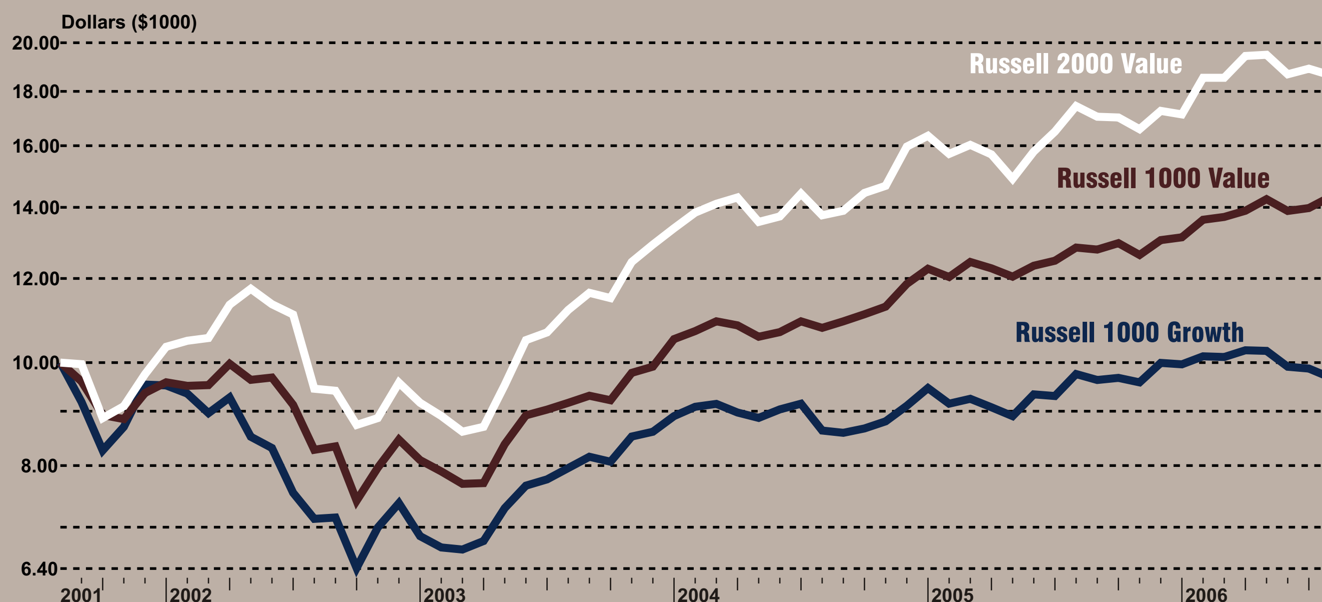
It is inevitable. The market, at some point, will decline sharply for a short period of time. The decline in the market this past spring is a perfect example. Many investors gravitated towards emotional comfort and headed for the sidelines. However, such a reaction may not prevail over the long run versus a diversified portfolio. Recent studies show that overreacting to short term dips in the market has significant long term consequences.

The studies compare one investor who stays invested throughout market ups and downs against another investor who goes to cash when there are declines of 10 percent or more. What they found was not surprising. The investor who stayed invested from June 1990 to June of 1996 averaged 10.3% per year while the investor who

Market Summary
Year to Date

Index	Change
Dow Industrials	+ 6.19%
Dow Transportation	+ 2.07%
S&P 500 Index	+ 4.45%
NASDAQ Composite	- 0.98%
Russell 2000	+ 7.79%
International	+ 12.22%

Investment Growth



bailed to cash and then tried to reinvest later average 8% annually. In other words, if both investors started out with $100,000 the one who "stayed the course" ended up with $517,499 and the one who "bounced around" ended up with $360,659.

As the chart illustrates, the majority of months in each of the asset classes have positive returns. The main culprit for the underperformance of those who sell during short term dips is trying to decide when to buy back. Considering the majority of recoveries occur relatively quickly after a drop, those who sell due to emotion usual miss the ride back up. Whereas, those with a diversified portfolio are able to weather the short term dips and then participate in the subsequent gains of the market.

Number of Positive and Negative Monthly Returns For Each Asset Class in Market Timing Study June 1990 - June 2006

Equity Asset Class	No. of Positive Monthly Returns	No. of Negative Monthly Returns	% of Positive Monthly Returns
Large Cap	124	68	65%
Small Cap	118	74	61%
International	118	74	61%
Emerging Markets	120	72	63%

Selected American

Every so often we like to highlight one of the money managers we trust to invest your money with. As you all know, our process for selecting money managers begins with several criteria based on performance, risk, expenses, and manager experience to name a few. We then take those remaining money managers and apply subjective screening to choose those we feel are best for you in the long term. While you see these money managers on your statements or pie charts, let's take a deeper look into what one of them is really all about.

The Selected American mutual fund is managed by Chris Davis and Ken Feinberg of Davis Advisors which was founded in 1969. The firm's philosophy centers on its belief in patient, long term investment practices and avoiding investment "fads." They pay careful attention to invest in high quality companies that are currently trading at a price below their actual value.

One of the reasons Davis Advisors is unique is their approach towards valuing companies. Throughout their process they implement a "margin of error" because they recognize that there are always unexpected circumstances in the future or that mistakes are possible. This helps to protect your monies by adding a cushion in the event there are unexpected losses.

Another attribute to these managers is their long term perspective. In today's world, an investment is owned on average less than one year. However, the Selected American mutual fund has an average holding period of around 5 years. Through their strict discipline towards avoiding short term fads, they are able to avoid the emotional sell triggers that come with a down market.

In short, their philosophy works very well. Over the past eleven years, the fund has outpaced the S&P 500 nine times and landed in its category's top quartile seven times. It ranks in the top 4 percent of all the funds in its category for last ten years. The average rate of return for the fund over the past 10 years is 12.3 percent, versus 8.8 percent for the S&P 500. A sound philosophy, experienced money managers, and a strict adherence to their process have resulted in excellent returns over the years for this fund.

New Pension Reform Bill

Congress and President Bush have enacted a new pension reform bill designed to give millions of workers a better chance of getting the retirement benefits they have earned. The new legislation encourages companies to automatically enroll 401k eligible employees and also to automatically increase their contributions each year. Based on current studies, almost 40 percent of workers over the age of 40 don't participate in their 401k. It is expected the automatic enrollment will raise that figure to roughly 90 percent.

The new law also changes some of the rules for pension plans. Companies have up to seven years to shore up their pension plans, and those companies that are severely under funded have to do so even faster. This will go a long way in securing promised retirement benefits to workers when then retire.

However, the new law will also lead to a decline in the number of pension plans available to employees. Since the new rules are more stringent, many companies are expected to freeze their current pension plans in favor of 401k type retirement plans. This will put even more emphasis on participant's ability to identify with their goals and comfort level and choose their investment options appropriately.

The other major highlight of the legislation is permanent changes to the college 529 Plans. The tax-free status of qualified 529 Plan withdrawals was set to expire in 2011. Now, under extreme pressure from the public and plan sponsors, congress and the President made the tax-free status a permanent feature to all 529 Plans. With that in mind, it is widely expected that monies flowing into the college plans will increase significantly over the next several years.

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