The third quarter of 2006 has relieved many of the uncertainties that the markets were facing during the second quarter. The result has been gains in the major market indices. This quarter, the large cap S&P 500 gained 5.67%, again outperforming the S&P Mid Cap 400 which lost 1.08%. This was the second quarter in a row and only the second time in over two years that large cap stocks outperformed mid cap stocks. Additionally, growth stocks, represented by the S&P 500/ Citigroup Growth Index again outperformed value stocks represented by the S&P 500/ Citigroup Value Index, returning 6.06% and 5.28% respectively. The best performing sectors during the quarter were Telecommunications Services and Technology, returning 9.63% and 8.33% while the worst performing sectors were Energy and Basic Materials, losing 2.14% and 1.13% respectively.

We indicated in our last letter that much of the recent market volatility was due to the uncertainty concerning the next move by the Federal Reserve. This was resolved when, at both of the Federal Open Market Committee meetings during the quarter, members decided to keep rates constant at 5.25%.

Unemployment has remained relatively steady with the rate climbing slightly to 4.7%. Initial indications are that 121 thousand and 128 thousand jobs were added in July and August. Final reports for the second quarter show that 346 thousand jobs were added. Final readings for domestic economic growth indicate that growth moderated in the second quarter with GDP up just 2.6%, 3% less than in the first quarter.

There were also some notable developments that have contributed to the recent market rallies. The price of energy related commodities such as oil, natural gas and coal have all fallen since mid quarter. Oil, for example, which reached a peak near $80, now is priced around $60. Additionally, military tensions in the Middle East, most notably in Lebanon between Israel and Hamas, have resolved relatively quickly.

Despite the attractive gains that equities have seen there have been notable slowdowns in the earnings and sales momentum of numerous sectors. It will still take some time to discern whether the Fed has engineered a “soft landing” or if recession is a possibility. Many market participants seem to be expecting the “soft landing” outcome. We continue to monitor these fundamental, bottom-up indicators and have been seeking out investment opportunities in somewhat defensive areas. Over the last quarter we added names in healthcare as well as stronger names in the technology sector. As always we are continuing to look for stocks that are financially strong and that can perform independently of economic changes. We are optimistic going forward as the market seems to be playing to our strengths; namely rewarding companies with solid fundamentals, good growth prospects and that are priced attractively considering their future cash flows.

We hope you are enjoying the beginning of fall and appreciate your continued trust in us. Please don’t hesitate to contact us if you have questions or concerns about your accounts.