BRIAN D. LOWDER, INC.

QUARTERLY NEWSLETTER

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FINANCIAL MARKET OVERVIEW

The first quarter of 2006 was one of the better quarters in years. Both the Dow Jones Industrial Average and the S&P 500 were up 4% during the first quarter. The broad stock market as measured by the Wilshire 5000 was up over 5% and small-company stocks were up over 13%. International stocks posted 10% gains and precious metals were up approximately 15%. During the same three months, interest rates rose considerably and the Federal Reserve raised short-term interest rates one-quarter percent for the 15th time in a row since mid-2004. The net result was slightly negative returns for intermediate and long-term bonds because the decline in bond values was greater than the interest income.

In the following column are sample returns of various asset classes during the first quarter of 2006 and for the previous twelve months ending March 31, 2006:

Previous 12 Months	2006 1st Quarter	(includes dividends reinvested)
+ 8.3%	+ 4.25%	Dow Jones Industrial Average
+ 11.7%	+ 4.2%	Standard & Poor's 500 Index
+ 14.9%	+ 5.5%	Wilshire 5000
+ 14.3%	+ 2.8%	Large-company stock-Growth
+ 11.4%	+ 4.5%	Large-company stock-Value
+ 23.7%	+ 9.3%	Mid-Size Stocks – Growth
+ 16.9%	+ 6.7%	Mid-Size Stocks – Value
+ 26.1%	+ 13.0%	Small-company stock- Growth
+ 19.9%	+ 10.8%	Small-company stock- Value
+ 26.3%	+ 9.7%	International (excludes U.S.)
+ 46.7%	+ 12.7%	Emerging Markets
+ 13.9%	+ 36.7%	Real Estate
+ 24.6%	+ 8.0%	Science & Technology
+ 63.0%	+ 20.4%	Gold funds
+ 1.8%	+ 0.2%	Short-term U.S. Treasury *(includes appreciation)*
+ 1.6%	- 0.5%	Intermediate U.S. Treasury *(includes appreciation)*

ECONOMIC OUTLOOK: DECISIVELY INDECISIVE

Though the first quarter results for stocks were above-average, the daily, weekly and monthly fluctuations in market prices have been confusing, disjointed and seemingly random. During one week, seemingly positive economic news ushers in strong stock market performance immediately followed by a reversal in stock prices the following week. Conversely announcements of slower economic growth, rising oil prices and rising interest rates are followed by stock market rallies.

When the economic environment is characterized by mixed economic signals and uncertainty, the financial markets usually react in an unpredictable manner.

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In support of a positive economic outlook are the following: One, corporations are building up cash nicely as corporate profits continue to grow reasonably well. Two, increased profitability and excess cash flow allows for greater corporate capital spending and investment. Three, corporations are also using their excess cash to buy back their stock. Four, while interest rates have been rising lately, the current level is still relatively low compared to interest rates over the past thirty years. Five, stock market performance is up nicely thus far in 2006 and finally, investor sentiment or confidence is neutral (high consumer confidence is normally an adverse indicator because overconfidence leads to irrational behavior and expectations).

On the other hand, oil prices are still stubbornly high and many observers wonder when higher energy prices will adversely impact corporate profits and bring inflationary pressure on our economy. Gold prices hit a 25-year high in March. Corporate insiders (officers, directors etc.) have collectively sold four times as many shares compared to the number of shares purchased. Our state and federal budget deficits are growing, the value of the U.S dollar is falling, and consumer's net savings rate is *negative* for the first time in many decades. Consumer debt and mortgage balances have grown significantly. Add rising interest rates and concerns about overvalued real estate prices to the mix and it's just as plausible to arrive at a negative economic outlook.

EFFICIENT PORTFOLIO MANAGEMENT

During uncertain economic times, it is critical to maintain discipline, an efficient portfolio management style and minimize mistakes. During the previous 27 months, investment returns have been solidly in the normal to below-average range and positive investment performance was achieved over very short periods of time. During 2004, the overall U.S stock market was up 12.5% and all of that gain occurred during the last 60 days of the year. In 2005, the overall stock market was up 6.3% and most of the gain occurred during the final 30 days of the year. Finally, over one-half of the 5.5% stock market return thus far in 2006 occurred on the *first trading day* of the year. Maintaining a disciplined investment style with infrequent changes is a better approach to capturing equity returns during an uncertain economic environment. Missing just a few days, weeks or months of positive investment performance can have a significant impact on annual returns.

In a moderate to low-return environment, efficient portfolio management (minimizing costs) is crucial. Direct and indirect costs from buying and selling stocks and mutual funds (referred to as portfolio turnover) increase income taxes and transaction fees that can easily add up to more than 1% annually.

Investor mistakes are the most costly element of portfolio management. Normal investor behavior generally causes a timing penalty. Investors repeatedly have higher confidence and invest more money *after* the market has gone up and less *after* it has gone down – a self-inflicted timing penalty. During the late 1990's, investors poured money into equities, primarily technology, and these enormous inflows immediately preceded the worst two-year stock market returns in over thirty years. The same over-confidence can be seen today evidenced by the huge inflows of money into energy stocks and real estate.

All of the above explicit and indirect costs really add up during a moderate to low-return environment and can be especially costly during uncertain economic times. Our approach is to be mindful of costs by emphasizing infrequent trading and selecting only stock mutual funds with below average expenses and turnover ratios. Secondly, we maintain a disciplined approach in making investment changes. We implement our changes and make our shifts early in direct proportion to the level of our confidence.

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For example, we began shifting into international stocks in 2002 with a target goal of moving up to 5% of most clients' portfolio value into this area. Over the ensuing 18 months, the proportion allocated to international and emerging stocks increased from 5% of the total portfolio value to 10% to 25% range. Today, we are holding, but not adding to these positions because increasingly large inflows of funds are flowing into this sector.

Our disciplined management style and infrequent trading policy are cornerstones to our investment philosophy. However, we also recognize the elevated uncertainty in today's economic environment. In the event we feel compelled to act swiftly, we have also created and stored customized sell transactions for each client account to reduce stock exposure by 50%. Although the likelihood of implementing such a drastic change to our clients' equity positions is relatively small, we are prepared to execute these changes swiftly.

REAL ESTATE UPDATE

A combination of tighter lending standards, rising interest rates, affordability concerns, and lofty prices have had a cooling effect on the San Diego real estate market. Last month, DataQuick Information Systems reported a 6.4% price increase on the median sales price of San Diego real estate from January 2005 through January 2006. More recently, the median price dropped 5% during the month of January 2006.

The volume of sales transaction has slowed significantly. During the month of February, 2006, the number of sales transactions was down 17% from a year earlier and was the 20th consecutive month of lower sales volume. Presently, the number of unsold listings stands at their highest level in eight years with the average number of days to sell a single-family home moving up to nearly 70 days.

Affordability is a growing concern. Although home ownership stands at an all-time high at 70% for the nation as a whole, skyrocketing housing prices in California allows only 57% of the population to own a home. In San Diego, the homeownership rate is only 55%. Over the long run, San Diego County is in jeopardy of losing population as families and businesses relocate to other cities and states that are significantly less expensive and have home prices that are significantly lower. Two years ago, we suggested a similar scenario in our newsletter and some readers commented that limited open space and our growing population in San Diego would continue pushing housing prices up.

For the first time in more than three decades, the population of San Diego County declined last year. While the net population loss was very small, over 43,000 people left the county to other areas where housing prices are considerably lower. In addition, most of the new families moving into San Diego County do not have sufficient household incomes necessary to purchase and support the $565,000 median price home in San Diego.

In spite of all the growing evidence to the contrary, many realtors, homeowners and "housing analysts" are still predicting an upward trend in housing prices. We expect a continued downward trend in real estate values and a moderate increase in interest rates. Under this scenario, homeowners who expect to stay in their homes for the long-term should replace variable-rate financing in favor of fixed-rate mortgages. In addition, homeowners who are relying upon rising real estate values and equity lines of credit to supplement annual living expenses should either reduce their consumption or move down to a less-expensive home. Finally, real estate investors should focus on rental income as the primary source of investment return as price appreciation may not materialize for several years.

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YEAR 2005 INCOME TAX RETURNS

Please send us copies of your 2005 Federal and State income tax returns as soon as they are available. Our investment advice and long-term financial planning recommendations are most effective when we have current income tax information in our files. Our advice to you is greatly improved when we have current income tax bracket information and capital loss carryforward figures in our files. In addition, we may find opportunities to improve investment performance, implement new financial planning strategies and minimize income taxes. Your tax preparer will only send us this personal information upon your request. Please contact your accountant or send us copies at your earliest convenience.

ANNOUNCEMENTS

This summer, Brian D. Lowder, Inc. will celebrate our 20th anniversary of providing financial planning and investment advice to our clients and friends. We sincerely thank all of our clients and friends for your support, referrals, trust and confidence and we will work diligently to maintain that trust and confidence in the future. A special thanks goes to Remette Martinson and Pam Priest who will celebrate 10 years of dedicated service to Brian D. Lowder, Inc. later this year. Their dedication, loyalty and hard work is appreciated and has helped greatly in the success and growth of the firm.

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