BRIAN D. LOWDER, INC.

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FINANCIAL MARKET OVERVIEW

The popular adage that stock market performance during the first month of the year is an indicator of what to expect for the full calendar year is once again troubling investors. January 2005 began in the same manner as the beginning of 2004. The major stock indexes declined during the first quarter of 2005 with the broad market down over 2.3% and the Dow Jones Industrial Average down nearly 2.1%. The NASDAQ was the worst performing index ending the first quarter down 8.1%. Concerns about sharply rising oil prices and overall inflation, rising interest rates, higher borrowing costs, and the risk of further decline in the value of the U.S. dollar due to our massive current-account deficit have all weighed heavily on the financial markets. Even safe fixed-income (bonds) holdings were down during the first quarter due to rising interest rates.

With oil prices temporarily spiking 30% during the first quarter, energy-focused mutual funds and individual stocks led the way, rising an average 12.5% during the first quarter. Value-oriented stocks outperformed growth stocks and international stocks continued to post positive performance compared to U.S. stocks. Real estate investment trusts declined an average 7% and technology oriented mutual funds declined an average 9% during the first quarter. Below are sample returns of various asset classes during the first quarter of 2005 and for the previous twelve months ending March 31, 2005:

Previous 12 Months	2005 1st Quarter	(includes dividends reinvested)
+ 3.6%	- 2.1%	**Dow Jones Industrial Average**
+ 6.7%	- 2.2%	**Standard & Poor's 500 Index**
+ 0.3%	- 8.1%	**NASDAQ**
+ 1.2%	- 4.6%	**Large-company stock-Growth**
+ 8.5%	- 0.8%	**Large-company stock-Value**
+ 5.2%	- 2.9%	**Mid-Size Stocks – Growth**
+ 12.8%	- 0.4%	**Mid-Size Stocks – Value**
+ 1.6%	- 5.4%	**Small-company stock- Growth**
+ 11.4%	- 2.1%	**Small-company stock- Value**
+ 12.6%	- 0.4%	**International (excludes U.S.)**
+ 18.5%	+ 3.3%	**International Small Companies**
+ 15.5%	1.3%	**Emerging Markets**
+ 10.1%	- 6.9%	**Real Estate**
- 6.6%	- 9.0%	**Science & Technology**
- 10.7%	- 4.2%	**Gold funds**
- 0.5%	- 0.3%	**Short-term U.S. Treasury** *(includes appreciation)*
- 0.1%	- 0.5%	**Intermediate U.S. Treasury** *(includes appreciation)*

Comments & Expectations

During 2004, external factors such as the Iraq war and the presidential elections dominated the financial headlines. In 2005, the focus has shifted back to economic factors including oil prices, rising interest rates, the weak U.S. dollar, sluggish new job growth, and the potential for inflation (due to increased prices associated with energy costs). As expected, the *possibility* of potentially negative outcomes and expressions of concern dominate the financial press. Yet the higher probability of experiencing steady economic

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growth receives less attention and is actually a beneficial path to maintain. Even sluggish growth prevents imbalances and sudden adjustments.

Consumer confidence has held steady measuring 84.5 compared to 84.8 a year ago. This benchmark index is slightly lower compared to a 100 index value in January 2002. Overall, consumers are reasonably confident about our economy despite higher oil prices, a slowdown in new job creation and rising interest rates.

Employers who have been hit the hardest by increased energy costs have added less than half of the 243,000 new jobs created in February. In March employers added only 110,000 new jobs. The previous two month’s growth in new employment is the lowest rate of growth in eight months and underscores what we still consider to be a bumpy and slow-growth economy.

Surprisingly, the overall economy grew by an estimated 4.0% in the first quarter; the actual figures are to be released later this month. Some economists suggest that the 4% growth rate is higher than normal due to a temporary increase in disposable income (extra cash) buoyed by taxpayers filing early and receiving larger than anticipated refunds. We believe the 4% rate of economic growth in the first quarter to be short-lived and income levels are expected to drop or at least flatten for the remainder of 2005.

The Consumer Price Index, or the government’s measure of inflation, showed an increase of .3% and .4% in January and February, respectively. The inflation rates for the first two months in 2005 represent the largest increases since October 2004. If the rate of inflation were to continue for one full year, the 2005 annualized inflation rate would be above 4% compared to nearly 3% last year.

Stay The Course

Overall, we expect the economy to continue improving at a slow-to- moderate 3% to 3.5% growth rate in 2005. The financial markets will continue to move up and down in reaction to daily news events, but year-end performance should be similar to the moderate results achieved in 2004.

Interest rates (federal funds rate) have already increased twice during the first quarter of this year and we continue to expect another one-half percent increase by the end of 2005. The current federal funds rate is 2.75% compared to a 1% rate approximately one year ago. We continue to believe that large U.S. and global companies with high stable returns and quality valuations will remain in favor as well as international companies benefiting from the explosive growth in India and China. Aside from energy companies and real estate, we find most asset classes to be fairly valued. Some appear attractive with both long-term and above-average growth opportunities, and larger value-oriented domestic companies appear more attractive than smaller growth-oriented companies. From a macro economic perspective, we continue to view international and emerging markets as having superior long-term return potential.

Rising interest rates should give the U.S dollar more strength, by making it more attractive than other currencies.

Interest Rates

As suggested in our previous newsletters, the movement toward a rising interest rate environment is still underway. On February 2nd and March 22nd the Federal Reserve raised short-term interest rates another quarter percent after each meeting and Alan Greenspan is expected to keep boosting rates at a “measured pace”. Over one year ago, Alan Greenspan signaled his intention to raise the federal funds rate back to the 3% to 5% range we were accustomed to prior to the terrorist attacks in 2001. Today, the overnight lending rate or federal funds rate is 2.75% - up from 2.25% at the beginning of the year. Presently, the federal funds rate has reached its highest level since the September 11 attacks in

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2001. Even after seven one-quarter percent increases, we expect borrowing costs to increase another one-half percent before year-end, but still remain at bargain levels relative to the borrowing costs experienced during the 1970's through the 1990's. Long-term interest rates (such as home mortgage rates) haven't increased as much and have remained lower than anticipated, but are expected to move higher as well.

During the first quarter of 2005, the interest rate for the 5-year Treasury Note increased from 3.61% to 4.17% , the 10-year Treasury Note increased from 4.22% to 4.5% while the 30-year Treasury Bond actually decreased from 4.82% to 4.77%.

Thus far, the Fed has been successful in raising short-term borrowing costs without adversely impacting our economy. However, the Fed faces a tough balancing act, particularly if officials see signs that energy price increases are being passed on to other sectors of the consumer economy. Together, higher prices (inflation) and continued interest rate hikes could slow the economy or even reverse the progress we've made since September 2001. If this scenario begins to unfold, Greenspan and his colleagues will have to decide how aggressively to raise rates at a time when the economy already might be at risk of a sharp slowdown.

We continue to recommend short-term fixed income investments. This strategy has been in place for several years and we will continue to favor short-term maturities over long-term bonds until we are confident that the risk of declining bond prices and loss of principal caused by rising interest rates has subsided.

Typically, it takes six to 12 months for interest rate changes to work their way through the economy, but a new business loan at 5.75% (prime rate) is certainly not the bargain rate of 4.0% last summer. Similarly, fixed-rate home mortgages have increased nearly 1% over the past twelve months.

Energy Prices

According to predictions by the Energy Information Administration, "The run-up at the pump isn't over and Americans will pay more this summer." In a recent report, the energy administration warned that worldwide demand for oil would continue through this summer and perhaps into next year. The major contributing factors are disruptions in oil production in the Middle East, reduced refinery capacity, and the increase in energy demand from China and India.

There is much disagreement amongst analysts regarding long-term trend in oil prices. Some analysts believe that prices will reach $100 per barrel, while others see the return of $20 per barrel. One side predicts that energy demand will out pace production and refinery capacity resulting in $100 per barrel prices for oil, while other analysts who predict the return of the $20 per barrel see production and capacity increasing as refineries refurbish and expand their facilities with their newly found profits. In addition, if the price of oil remains at current levels, many expect competition from alternative fuel sources will finally reach economic viability.

Is the demand for energy truly increasing? Yes. Globally the world burned 3.4% more oil in 2004 compared to 2003 and estimates suggest the world will consume 2.6% more oil in 2005 and 2006. Is the current spike in oil prices different from others? Yes. During most of the 1970s, the inflation-adjusted cost of oil hovered around $20 per barrel. In 1979, the seizure of the U.S. Embassy in Iran triggered a petroleum crisis. In 1981, President Reagan lifted oil price controls. At that time, prices jumped and reached an annual inflation-adjusted average cost above $53 per barrel. The higher energy costs quickly reduced demand and helped trigger a recession. The current spike in energy prices hasn't forced the U.S. or other world economies into a recession, but the true impact will eventually be revealed. In the meantime, expect

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to pay higher prices at the pump this summer during peak travel time.

ALTERNATIVE MINIMUM TAX

The AMT will affect three million filers this year and if the current exemptions are allowed to expire as scheduled after 2005, an estimated 11.6 million taxpayers will be trapped in 2006. Sadly, Congress is doing little to reform this inequity. What is the AMT tax? Basically, it is a two-tiered flat tax that subjects joint filers to a 26% tax on the first $175,000 of AMT income and a 28% tax on the excess above $175,000 after a $58,000 exemption. First, taxpayers compute their income tax bill under the regular rules. After all deductions are considered, taxpayers pay a 10% tax on some income, then 15%, 25%, 28%, 33% and 35% on income above $326,450. The average or effective tax rate under this graduated tax rate system is often between 22% and 30%. The resulting "regular' tax is then compared to a second income tax computation method using the AMT rules.

Under the AMT computation method, many deductions are disallowed such as personal exemptions, state and local income taxes, property taxes, any discount when exercising incentive stock options and most miscellaneous write-offs. Then the entire (alternative) taxable income is subject to the 26% and 28% tax rates. Often, the average or effective rate of tax is near 27%.

The two resulting tax computations are compared to each other and the higher amount is the resulting tax owed. Taxpayers with large state (i.e. Calif.) income tax bills, property taxes, discounts on incentive stock option exercises etc. are punished harshly. The primary problem is that unlike the regular income tax brackets, the AMT tax brackets and exemptions are fixed – in other words they do not increase (for inflation) over time even though most taxpayers' income and deductions do increase over time. Middle and upper-income taxpayers living in high state income tax states (such as Calif.) find themselves subject to AMT tax solely because of rather large state income tax bills.

Very little can be done to avoid the AMT tax, although taxpayers may be able to defer the tax bite one additional year. For example, for those taxpayers who make estimated income tax payments (self-employed or high-income employees) on a quarterly basis, they can defer making the final 4th quarter state estimated tax payment until January 15th of the following year. Since state income taxes are a disallowed deduction, deferring the final payment into another tax year may help reduce or eliminate AMT. Defer exercising incentive stock options. Also, defer more wages into qualified and nonqualified retirement plans to reduce reported income. Take the deferred income out later after retirement or during a tax year when you are not subject to AMT taxes. In most cases, the only hope to avoid or reduce AMT tax is to wait for bold action by Congress to eliminate or amend the AMT laws.

Credit Reports

A new federal law provides consumers with one free annual credit report from each of the three major credit bureaus (Experian, Equifax and Trans Union). To order your credit reports, you can go to www.annualcreditreport.com, call 1-877-322-8228, or you can fill out a form and mail it to Annual Credit Report Request Service, P.O. Box 105281, Atlanta, Georgia 30348-5281. These credit reports are free and no purchase is required. Be aware, however, that the website may try to sell you additional services such as credit scores or monthly credit monitoring services. These additional services, **which do cost money, are not required to obtain your free report**. We encourage all our clients to check their credit reports regularly. It is not unusual to find errors in the information reported by the credit bureaus. In addition, in this era of increasing identity theft, it is a good idea to check your credit report for unauthorized activity.

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Reduced Trading Fees at Schwab with eConfirm

In June 2004, Schwab reduced the commissions for ***electronic*** equity trades from $29.95 to $19.95 for the first 1,000 shares of stock ($9.95 for clients with accounts totaling over $1 million). Beginning May 1, 2005, clients who sign-up for Schwab's eConfirm can receive a reduced rate of $12.95 per trade. eConfirms are electronic trade confirmations delivered through email. If you sign up for this service, you will continue to receive your Schwab account statement by regular mail, however, you will no longer receive paper copies of your trade confirmations. If you are interested in receiving a $7 - $10 reduction in trading fees in exchange for accepting trade confirmations by email, please call our office and ask to speak to Clint.

Year 2004 Income Tax Returns

Please send us copies of your 2004 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 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.

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Best regards

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