

Courier Capital Corporation

INVESTMENT
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Market Review & Update

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Better than you think, better than you feel....

This should not be read as an exercise in cheerleading in as much as the year has been full of unsavory news. Fear over oil prices, inflation, Iraq, and U.S. corporate health divined from news items on troubled airline and other businesses with Ford and GM as the most notable examples. Heap on a good measure of seasonal political hyperbole and little wonder the moods of the country, the world, and the market have been a touch dour.

So, no cheerleading, but we should take a stone cold sober look at reality. As we enter the sixth straight year of economic expansion we can take stock of some of the significant areas of concerns and the milestones passed on this journey.

World economies continue to grow at a robust pace, redundantly led by well above-average growth in China & India. Add in Brazil and Russia for good measure and you get the market's acronym du jour "BRIC". The BRIC is indeed growing, and since it accounts for a fair share of global GDP, it gives the world an adrenal boost, smoothing the vagaries of single countries' economic ebbs and flows. It should be noted that several key developed economies, namely Japan and Germany are likewise on an improving trajectory. At least from an economic perspective, the world is a stable place.

As oil prices continue to retreat, natural gas has dropped to a 2 year low, and falling prices at the gas pump coupled with increased overseas production of iron, coal and aluminum (primarily China) have removed, for the time being, the inflation pot from the fire. Worries about weakening consumer spending have simultaneously eased as the above occurred, supported by subtle wage growth (Figure 1.) balancing what seems to be a softening trend in housing. That's all a bit better than what we view in the news.

Figure 1. Real Wage growth

Average hourly earnings
(year/year percent change)



Source: Bureau of Labor Statistics, Merrill Lynch

CIR U.S. Strategy

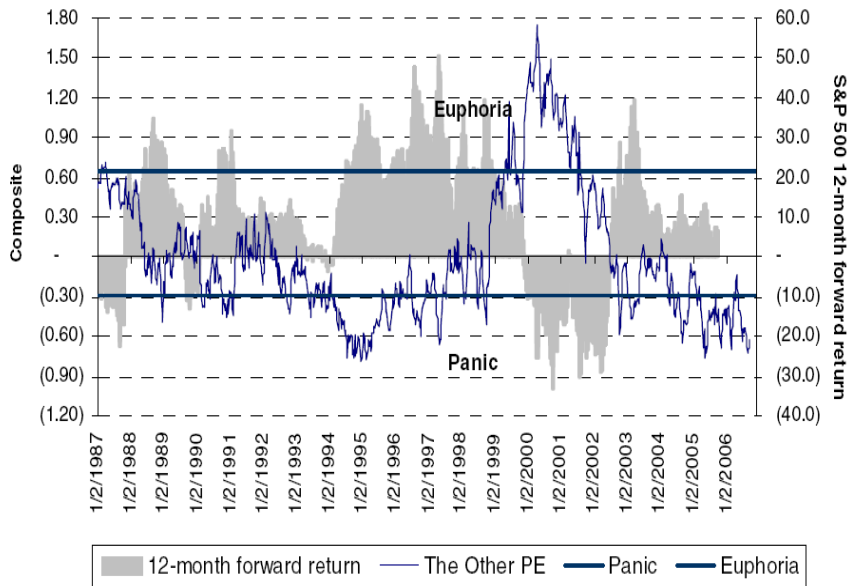
So, how do all the nebulous economic metrics manifest in my reality, you ask??? Let's take a peek at Corporate America first. The 3rd quarter of 2006 was the 13th consecutive period of double digit earnings growth. Since 2001, earnings for the S&P 500 have increased by over 111%, while stocks have appreciated 16%. Fear/sentiment played a huge role in this dislocation. It's not supposed to work like that in the long term. This divergence, coupled with our previous writings on record low P/E's and record high cash levels and we come to the now familiar refrain, large-cap U.S. equities (OK, Europe too...) appear cheap by many measures.



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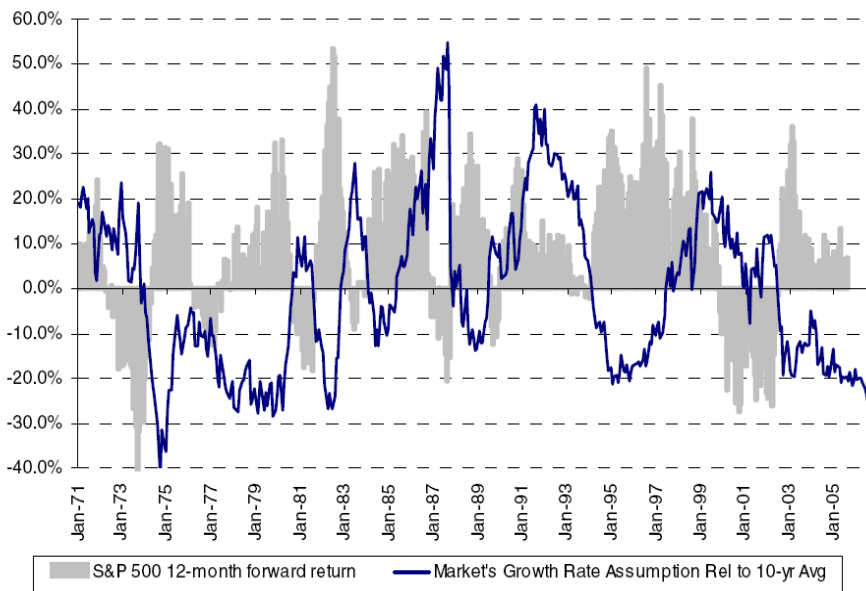
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Figure 2. Sentiment Readings below “Panic” level



Source: CIR U.S. Equity Strategy

Figure 3. S&P 500 Implied Long-Term Earnings Growth Expectations



Source: CIR U.S. Equity Strategy

better” condition. They have deemed used socks and underwear to never achieve this hurdle (perhaps an over-zealous legislator is still irked over a previous presidential deduction of \$18 for a used pair of jockeys?). Don, many thanks for the great information!

Summary

In summary, for the time being economic growth is evidencing worldwide momentum, consumers are offered a reprieve by an inflation muting decline in commodity prices, and the markets resilience is supported by very solid fundamentals. This good environment has produced strong portfolio results and absent exogenous events, these trends show persistent strength.

We’ll talk to you soon.

Tobias Levkovich, Chief Strategist at Citigroup, looked at a 20 year history where sentiment readings reached current levels (Figure 2.) and notes that such readings below the “Panic” level have resulted in higher stock prices in 97% of all past occurrences. On average, the gains were 19% over the course of the next year. Additionally, implied forward Returns on Earnings have reached multi-decade lows, an unusually rare environment. Levkovich also found that when earnings expectations are at steep discounts to average earnings growth (as we find today), stock prices usually rally. (Figure 3.)

Will the markets, or more correctly, will the vox populi get it??? Perhaps they have already begun... In spite of the sentiment millstone, the Dow Industrial Average has pushed to an all time high and the S&P 500 is at a 5 1/2 year high. Large cap stocks now lead other sectors in valuation, balance sheet cleanliness, earnings production and now, performance. As much as this advance snuck up on investors, it is indeed better than it felt.

Good Advice

More often than we admit, clients bring us valuable things, other clients, candy, and good ideas. Recently, a client called to request a novel charitable gift made directly from an IRA. He explained to us that this was part of new legislation. We did a bit of research on the new pension legislation and indeed, the IRS in a grand gesture of simplicity will allow a charitable gift of up to \$100,000 to be made directly from an IRA without a tax consequence. Kudos to the IRS for embracing simplicity. Additionally, the measure also creates tighter record keeping requirements for all cash and in-kind gifts made to charitable recipients. Keep good records, and get good receipts for all gifts. The humorous post script is that they require in-kind gifts to be in “good or

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