Pacific Asset Management Group

Market Commentary

"Creating Efficient Strategies to Build and Preserve Wealth"

Pacific Asset Management Group

Securities offered through First Allied Securities, Inc.
Member NASD/SIPC
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Fourth Quarter 2006 Outlook – 12,000 and beyond:

After a notable summer slump in equities, especially the technology laden NASDAQ market during July, stocks have enthusiastically rallied to push the Dow Jones Industrial average above the 12,000 mark for the first time in history. Coincidently, this milestone was reached on the 19th anniversary of the 1987 stock market crash which has historically cast a shadow on the prospects for stocks during October. With only a few days remaining, this October will likely instead be remembered as one of the best on record.

Though we are very bullish on stocks over the long term, the question is, have equities in the short term become overextended? To answer this question we first need to understand the current rally is basically a by-product of a simultaneous 23% decline in oil prices from $77 highs and a realization that the Fed is finished raising rates for the foreseeable future. The decline in oil prices were mainly attributed to a milder than anticipated hurricane season and a secession of major hostilities between Israel and Lebanon. We welcome further increases in equities however it is not likely the same catalysts will continue to influence stocks as they did in the last quarter. First, oil prices won't decline another 23% in the face of an approaching winter home heating season. Second, after a large run up in equities, some on Wall Street could be anxious to shift a portion of their profits to the sidelines. This shift could be justified by any sign of softer than anticipated declines in housing or any number of other economic indicators. Despite the chances for a short term pull back we believe the underpinnings of our economy are stronger now than at any time in the last 5 years. Corporate profits are growing, the job market is improving and consumers will likely turn this holiday season into one of the best retailers have seen in years.

About:

Pacific Asset Management Group

We are registered investment advisors headquartered in the San Francisco-Silicon Valley, Bay Area. Pacific Asset Management Group develops and manages portfolios for individuals, trusts, estates, and retirement funds. Each portfolio is positioned to take into consideration our clients current needs, long-term goals, risk profile and other more personal issues including economic and social values. Our ongoing reviews and personal meetings help us to make adjustments and take advantage of trends in the financial markets while at the same time striving to keep our clients on a steady, long-term course towards their goals.

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Outlook for Equities:

Despite the Dow hitting record highs, the overall stock market advance this year has been anything but equally balanced. For one thing, since 2003 the much anticipated advance in technology and more aggressive growth stocks has yet to materialize (see chart below). These shares have improved noticeably since 9/30/06 and could shift back into the limelight in 2007. Paradoxically, despite near record revenue and profit growth investors just haven't been willing to pay as much for these companies as they did in the 1990's. This illustrates the importance of dividing your investments into each of the major asset classes in order to benefit when one class performs well and limit the downside when another asset class does poorly.

Multi-Year Morningstar Index Performance

Morningstar Index's	**2003**	**2004**	**2005**	**9/30/06**
Large Cap Growth	30.65%	0.19%	3.43%	0.10%
Large Cap Blend	24.71%	13.99%	3.82%	8.75%
Large Cap Value	26.26%	14.05%	7.05%	16.45%
Mid Cap Growth	40.02%	15.45%	16.27%	2.56%
Mid Cap Blend	38.68%	19.05%	10.05%	5.95%
Mid Cap Value	35.94%	24.30%	11.54%	9.10%
Small Cap Growth	52.65%	13.48%	5.77%	2.66%
Small Cap Blend	42.59%	23.61%	6.30%	11.50%
Small Cap Value	48.87%	24.03%	5.12%	10.16%
Standard & Poor's 500 Index	28.69%	10.88%	4.91%	8.53%
NASDAQ Composite Index	29.28%	12.16%	6.95%	9.23%

(Data complied from Morningstar Principia 9/30/06)

Outlook for Fixed Income:

There are concerns among a chorus of economists that the Federal Reserve will or has already increased interest rates to the point of hindering economic growth in 2007. If correct this could cause the Fed to reduce rates next year. After reviewing the last Federal Reserve statement and taking into consideration the strength of the most recently released corporate earnings reports it appears clear to us that the Fed is intent on maintaining a neutral stance and could actually be induced to raise rates if oil prices start to rise again.

From an investment standpoint, in the fixed income market we are starting to see some activity in preferred stocks, FDIC insured Certificates of Deposits and high yielding common stocks. For more details please call us.

Quote for the Quarter:

"Perhaps the most common mistake investors make is to let emotions drive their investment decisions. It's easy to get caught up in the euphoria when everything is going up. But buying at the top of the market when stocks are at their most expensive or selling after prices have already fallen creates a frustrating investment experience and can lead to a failure to reach your financial goals." *John Hancock Mutual Funds 5/06*

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