Investment Report and Market Commentary

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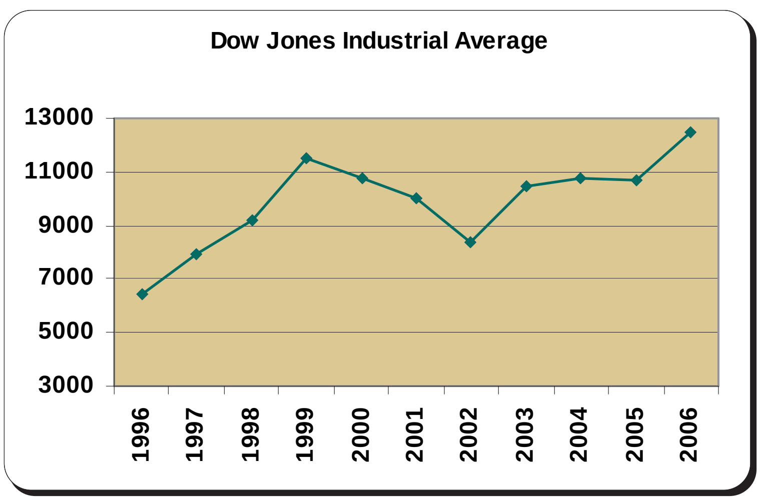
Fourth Quarter 2006

Market Index Total Returns as of December 31, 2006

Market Index	Fourth Quarter	1 Year	3-Year Annualized	5-Year Annualized
Standard & Poor's 500 (Large Cap)	6.7	15.8	10.4	6.2
Standard & Poor's 400 (Mid Cap)	6.9	10.3	13.1	10.9
Russell 2000 (Small Cap)	8.9	18.4	13.6	11.4
MSCI EAFE (Foreign)	10.4	26.3	19.9	14.9
Lehman Bros. Aggregate Bond	1.2	4.3	3.7	5.1
Lehman 3-Year Municipal	0.6	3.1	1.9	3.0

Stocks finished 2006 with a real knockout quarter. Building on the momentum from the third quarter, all equity asset classes participated in the rally that resulted in the fourth consecutive year of positive market returns. There was lots of good economic news underpinning these festive results. On December 15 the Federal Reserve Open Market Committee decided against an interest rate hike for the fourth consecutive time since last raising rates on June 29. Inflation appeared firmly in check as the year drew to a close. Employment continued strong and GDP growth moderate. Corporate earnings continued to rack up impressive double-digit gains. Consumer confidence ended the year with a jaunty surge, reflected in strong holiday sales for electronics retailers, discount chains and internet sales outlets. Even the trade deficit and the federal budget deficit, those twin grinches, narrowed a bit as the year ended. Worries about continued high energy prices, the ongoing struggle in Iraq, and a slumping domestic housing market were not enough to rattle a market that obviously knew only one direction as the year came to a close.



A New Record… Finally! The Dow Jones Industrial Average hit a record high in December. Since bottoming out just over four years ago in October of 2002, the Dow is up over 71% excluding dividends. For the ten-year period ending 12/3/2006, the Dow is up over 93% excluding dividends. These are fantastic returns but we can't ignore the great bear market of 2000-2002. Since the last peak in January of 2000, the Dow is up only 6% excluding dividends. Indeed, we have enjoyed a great market for the last four years, a just reward for having endured a terrible market at the start of the decade.

Move over small caps, it is time for foreign stocks to shine. The table at the top of the page makes it clear that foreign stocks (MSCI EAFE) easily won the asset class "beauty contest" in 2006 returning over 26% for the year and beating the other equity asset classes by a wide margin. This is a welcome change after three years of dominance by mid cap and small cap stocks. Perhaps this will continue; perhaps not. By now, you are starting to see a pattern. One asset class (like small cap or foreign) will dominate for a while and then it will lag as another asset class takes the lead. Sometimes these periods of dominance are short lived, while other times we see an asset class stay on top for a long period of time. Over the long term, one thing is certain: <u>asset class returns regress to the mean</u>. Each asset class will do well over long periods of time but during shorter periods of time, something will always be leading and something will always be lagging. I liken it to the traffic jam I endure each day going north on I-77. There is always a teenager, constantly changing lanes, trying to find an easier, faster route to his destination. He'll see an opening, stomp the gas and zoom past me at the Sunset exit only

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to be frustrated when I catch up with him again at Harris Boulevard. Now I, being wise beyond my years, am staying safely in my lane, patiently waiting to get to my exit, often arriving before the young lane-changer. Asset classes and even sectors are the same way. Something will zoom ahead for a time (think small cap, energy, real estate) while others lag (think large caps or tech stocks) and then at some point leadership will reverse. Said another way, today's obvious winner may likely be tomorrow's loser. Now if we knew which asset class was going to be on top next year, we would easily earn 35% annually and never think about money again. But since we don't know (and no one does… especially not that "expert" quoted on CNBC), we will maintain exposure to all of these asset classes and sectors and when one runs ahead for a time, we will trim it back and add to the ones that have lagged. This buying low and selling high (rebalancing) will get us to our destination a lot faster than trying to load up on what has been hot or on what we think might be hot next year.

Our portfolios have a relatively large allocation to US large cap stocks and we have been pleased to see that large caps are stirring to life after a few years of trailing other asset classes. In addition to owning US large caps, all of our portfolios have exposure to foreign stocks, both developed markets and emerging markets. While most of our foreign exposure comes through owing mutual funds that invest directly in the shares of foreign companies (like Sony, Royal Dutch Petroleum, Nestle and Nokia), you may not realize that you get great exposure to foreign markets through the US large cap portion of the portfolio. This is because most of the large companies we own (either directly or through mutual funds) are truly global companies. Perhaps surprisingly, companies like Proctor & Gamble, Intel, McDonald's, Caterpillar and Exxon Mobil derive more than half their sales from overseas. (see table). Did you know that Wal-Mart has over 2,700 stores outside the US? And that the majority of McDonald's 30,000 franchises are located outside the US and are spread over 110 different countries? **Fully 41% of the revenues of the S&P 500 companies came from overseas in 2005, up from 32% in 2000.** These large companies have the capital, resources and management depth to take advantage of opportunities in developed and developing markets worldwide, offering investors the many benefits of investing outside the US while owning American companies with proven track records.

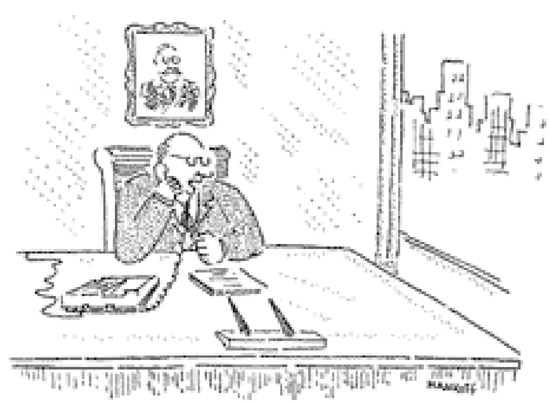
Company	2005 Sales from Outside the US
Becton Dickinson	52%
Caterpillar	48%
Colgate Palmolive	64%*
ConocoPhillips	27%
Danaher	47%
Dow Chemical	62%
Exxon Mobil	69%
Intel	81%
McDonald's	53%
News Corp.	46%
Proctor & Gamble	52%*
UPS	19%
Wal-Mart	18%
Source: S&P Stock Reports	* outside North America

We hope your Holidays were wonderful and we wish you a safe, happy and prosperous new year. Thank you for trusting Bragg Financial Advisors for your planning and investing.

Sincerely,

Benton S. Bragg, CFP, CFA

Suzanne Wittebort, CFS contributed to this report.



"A billion is a thousand million? Why wasn't I informed of this?"

Source: Cartoon Bank used with permission