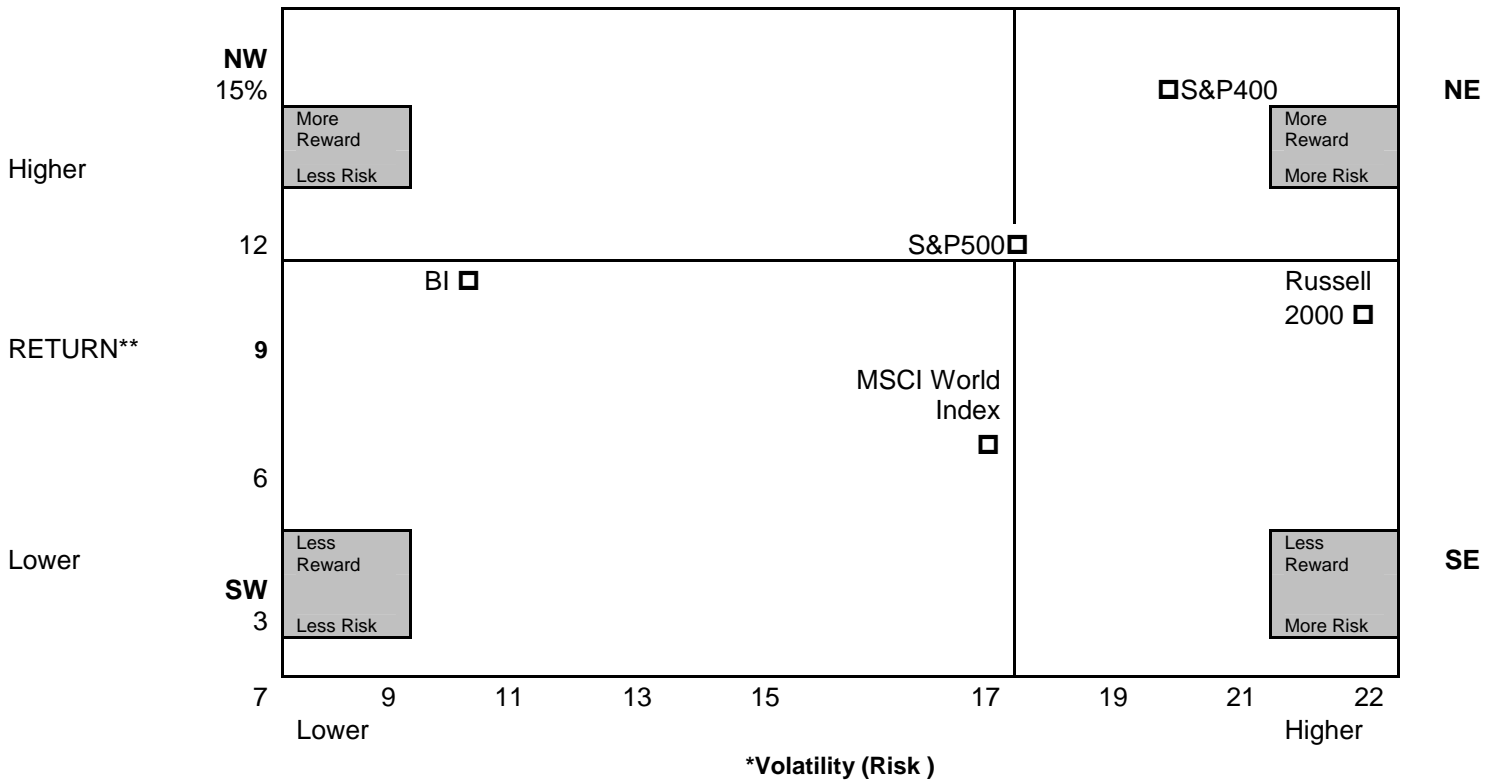


Krosnowski & Scott, LLC
 Financial Fitness Newsletter
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I. “The Great Northwest” - Let’s take a trip back in time and reflect on the financial markets over the past ten years. If we are lucky, we just might find ourselves in the same beautiful country that Lewis & Clarke discovered back in the early 1800’s. The first part of our journey is to learn more about risk so we can try to avoid some of the pitfalls along the road to financial prosperity. Standard deviation is a measure of risk or volatility. The lower the standard deviation of an investment, the lower the risk. An ideal investment provides investors with below average risk and above average return. The chart below is known as a scattergram. This chart is very useful in educating investors so they can understand the risk/reward relationship between various investment vehicles. Becoming more knowledgeable about these investments will enable you to make better, more informed decisions regarding the investment of your assets.



*Standard Deviation (a measure of risk or volatility) for the 10 year period ended June 30, 2004

** 10 Year Average Annual Return

	<u>Standard Deviation</u>	<u>10 Year Return</u>
<u>US Large Company:</u>		
S&P 500 Index (SP)	17.90	12.07
<u>US Medium Companies:</u>		
S&P 400 Index (SPM)	16.54	16.10
<u>US Small Companies:</u>		
Russell 2000 Index (R2)	22.04	11.54
<u>Global Companies:</u>		
*Global Stock Portfolio (GS)	17.48	8.52
<u>Balanced / Equity Income:</u>		
60% S&P 500/ 40% LB Int Index (BI)	10.29	10.57

(10 year rates of return and standard deviations as of 12/31/04)

*Please contact us if you would like information on professionally managed portfolios, that invest in the above mentioned asset classes and whose risk/return characteristics fall in the northwest quadrant.

The optimal area of the scattergram is the northwest quadrant. Investments that fall into this category are characterized as having “greater return and less risk” than a well known financial yardstick (such as the S&P 500 stock index). An ideal investment portfolio is constructed by incorporating the following asset classes (baskets):

- An asset allocation (stock and bond) mix that meets your investment objectives and comfort level (i.e. determining what percentage of your assets you wish to invest in stocks and what percentage you wish to invest in bonds).
- Fixed income securities such as quality individual bonds adjust maturities based on the ever changing interest rates. Individual bonds are attractive because they have no annual fees. (A good information source for bonds that we are currently recommending to our clients can be found at www.lasallebonds.com.)

- Overweight the stock portion of your portfolio with northwest quadrant Large Cap money managers (versus the S&P 500 Index).
- In moderation, blend into portfolio domestic medium and small capitalization stock portfolios that exhibit northwest quadrant statistics versus the S&P 400 Mid Cap and Russell 2000 Small Cap stock indices, respectively.
- A blend of both value and growth styles with an emphasis on value across all stock investment categories (i.e. US Large, Medium, Small Cap, Global, etc.).
- In similar fashion, globally diversifying your assets by selecting a northwest quadrant money manager (versus the MSCI World Index) in your portfolio. We continue to emphasize global stock exposure in client portfolios since stock valuations remain attractive abroad. Currently, companies outside the United States have higher stock dividend yields, and lower P/E ratios.

Simplicity - Northwest quadrant “balanced” and “equity income” portfolios are attractive in that they provide exposure to many of the asset categories listed above. We have access to managers of these portfolios that have outperformed the S&P 500 over the past 10 years with approximately fifty percent less risk. This concept is known as “one stop shopping”. One stop shopping is attractive because it can make investing simple and easy.

Minimize your fees - Over the past year, the big Wall Street investment firms and insurance companies have been launching age based and asset allocation products in the form of variable annuities and funds. Beware of excessive fees in these investments (annual fees of 2.0% (+)) and no performance history. These firms attempt to justify higher fees with unnecessary investment features such as guaranteeing a minimum balance or income withdrawals. We have money management solutions that are available to investors at substantially lower fees (50% to 75% lower in some cases) and have superior performance records over the past 15 to 30 years. Remember, when reviewing annual fees, if there is a number in front of the decimal that is not good. Seek out investment solutions where your annual fees are less than 1.0%.

In addition to asset allocation northwest quadrant characteristics and low fees, additional investment efficiency can be achieved by selecting portfolio managers that have low portfolio turnover. Not only are low turnover portfolios tax efficient, they also keep transaction costs down, which enhances long term performance.

Hopefully you have enjoyed your visit to a very scenic part of the financial world and you have learned strategies to invest more efficiently. Lewis & Clark discovered valuable territory in the “Northwest” and hopefully you will too.

II. Fixed Income Investing: “How to thrive in a rising interest rate environment”.

For bond investors, a rising interest rate environment is like swimming in shark infested waters – it is treacherous!

The two main types of risk associated with bond investing are interest rate risk and credit or default risk. Interest rate risk occurs if you have to sell a bond prior to maturity. If interest rates rise, and a bond is liquidated prior to maturity, a loss of principal normally occurs. Two methods to combat interest rate risk are holding bonds to maturity and shortening bond maturities. Shorter term (1 to 10 years) bond prices fluctuate much less than longer term (10 to 30 years) bond prices. Unfortunately, longer term bonds normally pay higher rates of interest. When a bond is held to maturity, the owner of the bond receives the return of their principal at par value. Credit risk occurs when the issuer of a bond goes into bankruptcy before the bond matures and the owner’s principal is lost. The best ways to avoid exposure to credit risk are to diversify the number of bond positions and to invest in high quality bonds (ranked in the top three categories by major credit rating institutions).

Due to inflationary fears, the Fed is currently raising interest rates. This is a concern for bond investors because inflation reduces purchasing power and rising interest rates has an adverse effect on the value of fixed income securities. The following is a review of defensive investment strategies to confront both concerns:

1. Inflation Protected Securities – Issued by the US Treasury (TIPS) or as FDIC insured CDs, the principal value of these securities adjusts for inflation on a

monthly basis. A fixed coupon is paid semi-annually. Upon maturity, the inflation adjusted amount is paid to investors, thus having the same real value as when originally invested.

2. Step Up Investments – These securities pay a pre-determined rate of interest that periodically “steps up” or increases over specified time periods. Step-ups normally become callable on the first date the coupon resets (increases). Step-ups provide more protection during periods of rising interest rates than conventional callable fixed income securities. They also offer more attractive yields than comparable non-callable bonds. Many Step-ups are also “estate” friendly in that they offer a death put feature. Should the beneficial owner become deceased prior to maturity, the beneficiaries can redeem the bond at its par value prior to maturity. For example, a five year FDIC insured “Step-up” CD could pay 3.0% in year 1 and then 3.5%, 4.0%, 5.0% and 6.0%, increasing the interest paid each year toward maturity.
3. Floating Rate Securities – The interest coupon “floats” or adjusts periodically (quite often monthly) based on the rate of an underlying index such as CPI , LIBOR or the yield of 10 year US Treasury notes within a specific range. A “floor” provides investors with a minimum rate of interest, while a “cap” limits how high rates can increase. These investments provide a higher level of current income than most short term bonds. The market value of these securities is less sensitive to changes in interest rates than fixed-rate bonds. For example, a ten year FDIC insured “Floating Rate” CD could pay 4.0% interest initially and then adjust monthly based on CPI to maturity.
4. Bond Ladder – This strategy allocates fixed equal amounts of assets to different maturities over a specified time period (for example: a \$100,000 portfolio structured as a 10 year ladder would invest \$10,000 for each year maturing from 1 through 10 years). As investments mature, reinvest in bonds with maturities at the long end of the ladder. The laddered strategy enables investors to reinvest assets at higher rates of interest if rates are rising. If rates are falling, longer term bonds should provide investors with above average returns.

Summary –

To protect the value of fixed income securities against rising interest rates, the following strategies may be attractive depending on your financial situations.

Consider the following:

- Avoid long term maturities (10(+) years)
- Invest in quality bonds (safety ratings of A or better)
- Invest in fixed income securities whose principal (TIPS) or interest (Step-up, Ladder and Floating Rate), may increase to help you keep pace with inflation.

III. Fitness & Health – “Go Big Blue”. No we are not talking about the Michigan Wolverines, we are talking about blueberries. Recent research supports the centuries-old belief that these berries have unique health properties and may help protect against cancer, cardiovascular disease, stroke, urinary tract infections, muscular degeneration and Alzheimer’s disease. No matter how you swallow it, the blueberry shows promise as an important tool for personal health.

High in cholesterol-lowering fiber, the anti-cancer agent ellagic acid, and rich in antioxidants, including Vitamins A, E, and C compounds that aid in the fight against disease, this unlikely little superhero draws power from its deeper blue color.

Dr, James Joseph, Chief of the Neuroscience Lab at USDA Human Nutrition Research Center on Aging, explains “anthocyanins are pigments in blueberries that provide the blue color. While they themselves are very potent antioxidants, there are other groups of chemicals that work in synergy with anthocyanins to provide health benefits.”

Blueberries are ranked number one in antioxidant activity against 40 other fruits and vegetables. This vigorous performer appears to work its magic in specific ways – by helping to prevent the formation of blood clots that cause heart attacks. Additional evidence suggests blueberries stop the growth of bacteria that promote urinary tract infection, reduce “bad” cholesterol levels responsible for stroke and strengthen blood vessels in the eye, possibly slowing down the effects of macular degeneration.

Dr. Joseph thinks blueberries also help reverse age-related short term memory loss, creating hope for Alzheimer’s victims. Apparently, blueberries directly affect the way neurons in the brain communicate with one another. Preliminary results from his current studies suggest that test subjects who consume a cup of blueberries a day have better motor skills than those who don’t.

We hope you and your family had a Happy Holiday season. Remember, the key to good health is not depending your doctor or pharmacist. It is taking control of your own destiny and balancing exercise with a nutritious diet. We look forward to advising you on efficient investment strategies in the near future.

Sincerely,

Andrew J. Krosnowski
Senior Financial Consultant

Melissa A. Scott
Financial Consultant

P.S. Affiliated Financial Services – Our primary area of investment expertise is investment and retirement planning. We also provide advice on the topics mentioned below. Please contact us should you need advice on the following:

- Estate Planning _____
- College Education _____
- Long Term Care _____
- Life Insurance _____
- Tax Planning _____
- Income Distribution Planning _____
- Free Retirement Planning Reports _____
- Retirement Plans (IRA, 401 (k), Roth, etc.) _____

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