TRIVANT
CUSTOM PORTFOLIO GROUP, LLC

January 2007

quarterly INSIGHTS

Fourth Quarter 2006

In This Issue

3 Equity Market Review
8 Bond Market Review
9 2007 Market Forecast
14 2007 Portfolio Strategy
16 Closing Thoughts
17 Appendix

EXECUTIVE SUMMARY

Europe, Emerging Markets, Energy and Materials Lead Q4 2006

In the Fourth Quarter, the domestic S&P 500 Index rose 6.70% while the MSCI EAFE Index (foreign) returned 10.40%. The Fourth Quarter 2006 US midterm election rally drove performance globally.

Three primary trends occurred:

- European markets, buoyed by a currency appreciation, led the developed countries
- Emerging markets benefited from increased investor "risk appetite"
- The Energy and Materials sectors surged with returns in excess of 10%

Our 2006 Equity Market Forecast Was Conservative

We expected global equity markets would advance 9%-13% in 2006 (2006 Market Forecast, Quarterly Insights, January 2006). From a quantitative perspective, our forecast was conservative (the S&P 500 Index rose 15.80% and the MSCI World Index rose 20.65% in 2006). The factor we did not anticipate was the surprisingly strong performance of Europe and the Emerging Markets. (See Appendix: Our 2006 Report Card for a detailed discussion).

Our 2006 Equity Performance Was In Line With the Market

The equity component of our portfolio closely resembled the performance of the S&P 500 Index.

Our 2007 Forecast: Global Equity Markets Will Advance 11%-15%

We believe that global equity markets will advance 11%-15% in 2007. Our rationale includes the following:

- The 2007 S&P 500 Index consensus forecast return of 7% is conservative
- Stable US interest rates should positively impact the market
- The current equity Price Earnings ratio (17.40) is attractive

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EXECUTIVE SUMMARY

Continued from Page 1

TriVant 2007

2007 Portfolio Strategy Considerations	2007 Portfolio Position (Anticipated)	2006 Portfolio Position (End of Year)
Equity		
Domestic versus Foreign	Increase Domestic, Reduce Foreign	78% Domestic, 22% Foreign
Sector Weighting	*Over-weight* (*to S&P 500 Index*) - Consumer Staples - Health Care - Technology *Under-weight* (*to S&P 500 Index*) - Financials - Energy	*Over-weight* (*to S&P 500 Index*) - Telecom - Health Care - Technology *Under-weight* (*to S&P 500 Index*) - Financials - Utilities
Average Market Cap	Maintain current level	$40 Billion
Style (Growth versus Value)	Maintain current level	Weighted - Emphasis towards growth stocks
Portfolio Beta Level (Risk)	Maintain current level	Above Market (greater than 1.0)
Fixed Income		
Desirable Securities	Shorter term government bonds and Treasury Inflation Protected Securities (TIPS) Average Duration = 4.5 years	Shorter term government bonds and Treasury Inflation Protected Securities (TIPS) Average Duration = 5.5 years
Securities with less emphasis	Longer term government bonds, corporate bonds	Longer term government bonds, corporate bonds

TRIVANT CUSTOM PORTFOLIO GROUP, LLC Fourth Quarter 2006 Review

Commentary in this review reflects our portfolio strategy. Many of our clients have different objectives and circumstances which are reflected in unique portfolio considerations. Please note that accounts may not contain all elements of the strategy discussed here. Additionally, individual client customizations and start dates may preclude certain elements of this strategy from being implemented. Past performance is no guarantee of future results. A risk of loss is involved with investments in stock markets.

John Barber, CFA
Chief Investment Officer

Dan Laimon, MBA
President

Equity Market Review

Europe, Emerging Markets, Energy and Materials Lead Q4 2006

In the Fourth Quarter, the domestic S&P 500 Index rose 6.70% while the MSCI EAFE Index (foreign) returned 10.40%. The Fourth Quarter 2006 US midterm election rally drove performance globally. Three primary trends occurred:

- European markets, buoyed by a currency appreciation, led the developed countries
- Emerging markets benefited from increased investor "risk appetite"
- The Energy and Materials sectors surged with returns in excess of 10%

Equity Index Performance

Index	Q4 2006	2006
S&P 500 (Domestic)	6.70%	15.80%
MSCI EAFE (Foreign)**	10.40%	26.86%
MSCI World	8.47%	20.65%
MSCI Emerging Markets	17.37%	32.59%
Russell 2000 (Small Cap)*	8.55%	17.00%
MSCI Japan	5.01%	6.33%
MSCI UK (United Kingdom)	10.29%	30.67%
MSCI EMU (European Monetary Union)	12.08%	37.28%

* Performance data does not include dividends ** Europe, Australia and the Far East

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- Stable US interest rates should positively impact the market
- The current equity Price Earnings ratio (17.40) is attractive

Currency, Country, Sector & Market Cap Performance at a Glance

The US Dollar

The US Dollar depreciated versus the Euro and British Pound in the Fourth Quarter, and slightly appreciated versus the Japanese Yen. We believe the dollar has reached an appropriate level and expect a relatively flat currency market in 2007.

U.S Dollar Appreciation vs. Foreign Currencies

Currency	Q4 2006	2006
US Dollar/Euro	(4.01%)	(11.79%)
US Dollar/Japanese Yen	0.92%	0.94%
US Dollar/British Pound	(4.77%)	(14.00%)

Source: MSCI

In 2006, the dollar fell 8.49% against a basket of diversified currencies.

The amount of depreciation of the US Dollar versus the Euro and British Pound in 2006 surprised us. We stated the following in our Quarterly Insights, January 2006 page 4:

"We believe that the US Dollar appreciation may end in 2006 for the following reasons:

- Mr. Greenspan's replacement (Federal Reserve Board Chairman Ben Bernanke) may be less "hawkish" regarding inflation (see our Third Quarter 2005 Review, page 8, "Greenspan Reign Comes To An End And So Might Interest Rate Hikes")
- Considerable US Dollar appreciation in 2005
- Jean-Claude Trichet, the President of the European Central Bank (ECB), may feel pressure to raise interest rates with the fall of the Euro
- The American Jobs Creation Act of 2004 (2004 Jobs Act) has expired. To benefit from special temporary tax incentives, American companies previously moved profits from their foreign subsidiaries to the US, which strengthened the dollar."

We believe the US Dollar will not fluctuate significantly in 2007 for the following reasons:

- Stable Federal Reserve interest rates (the last rate change occurred August 8, 2006)
- Falling oil prices may reduce inflationary pressures and help to improve the US trade deficit
- The moderate US Dollar decline in 2006 should inhibit further potential declines

The US Dollar: Portfolio Strategy Considerations

Since we do not believe the US Dollar will fluctuate dramatically in 2007, we do not currently view the US Dollar as an important factor to determine portfolio style, country or sector decisions.

Japan

Japan trailed global markets all year and finished as the worst performing developed market with a return of 5.01% for the Fourth Quarter (6.33% for the year). Concerns over a reform-minded new Prime Minister and North Korean intentions continue to negatively impact Japanese stocks. Top government officials continue to warn the Bank of Japan not to raise its benchmark interest rate (0.25%) too quickly. The perception of political meddling in monetary policy could make international investors reluctant to commit money to Japan.

Japanese trade with China and other nearby emerging markets remains strong. However, if the Chinese government enacts policies to slow down China's economic growth, this would hurt Japan. The Bank of Japan's Tankan survey shows that business confidence remains strong.[1]

Japan: Portfolio Strategy Considerations

We view Japan as neutral at this time and will maintain our current portfolio position.

Emerging Markets

Emerging markets finished a stellar 2006 (32.59%) with a robust Fourth Quarter (17.37%). This strong performance includes a dramatic Second Quarter sell-off which saw the Emerging Markets Index decline by 26.24% in barely five weeks. This illustrates the high volatility of emerging markets exposure.

We see an increasing investor appetite for risky investments while political risks are growing. This may result in substantial future downward market corrections. Venezuela, Russia, and the Ukraine have all threatened to nationalize companies and/or industries. New investors have been attracted to strong returns. A disastrous investment return in one region of emerging markets could easily prompt investors to flee from all regions of emerging markets (a situation called "contagion").

Emerging Markets: Portfolio Strategy Considerations

Strong returns have increased our portfolio weighting. We will keep our target weight at around 3% and will rebalance should levels increase due to appreciation.

Europe

Europe and the UK both returned over 10% for the quarter and over 30% for the year. No market surprised us more than Europe. The European Central Bank (ECB) and the Bank of England (BOE) both raised interest rates (the ECB reached 3.5% and the BOE reached 5.25% as of January 11, 2007). The current Consumer Price Index (CPI) is at 3%, which exceeds the stated 2% target rate. Strong currency appreciation in 2006 may slow the economy. Both the ECB and BOE may raise interest rates again if inflation continues to exceed the target.

Europe: Portfolio Strategy Considerations

Higher interest rates and taxes, coupled with stronger currencies, may impede returns. We believe that Europe will lag US performance, and that it is prudent to pare back European exposure to raise US exposure.

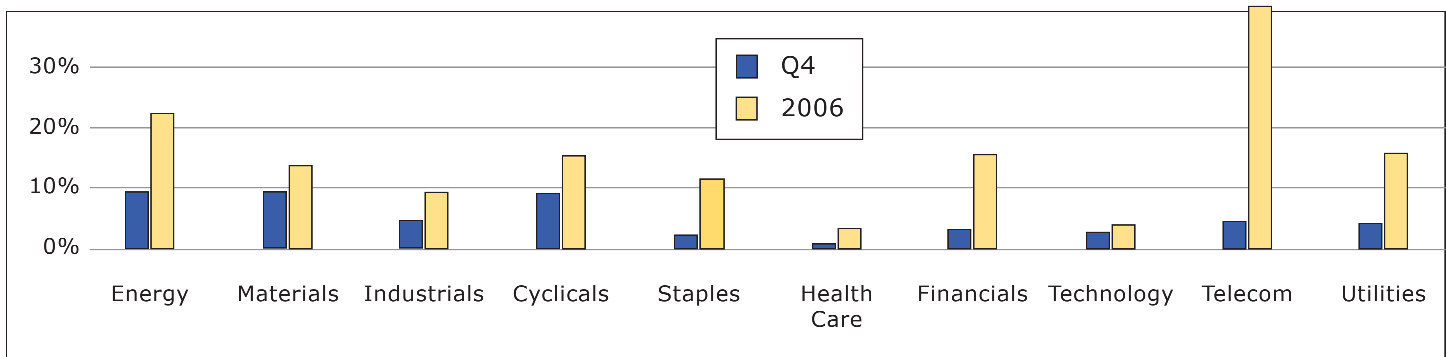
[1] The Tankan is a short-term economic survey of Japanese enterprises published four times a year by the Bank of Japan. It gives an overall impression of the business climate in Japan.

Sector Performance

Telecom was the best performing sector in 2006 with an impressive 32% return. Industry consolidation and new technology, along with improved balance sheets, drove Telecom returns. Energy continued its streak of out-performance by rising 22%, primarily driven by higher oil prices.

Spare oil production capacity has been growing over the last year, but the market has not discounted this increased capacity. Estimates are that spare capacity could reach three million barrels per day by the end of 2007. We believe that spare capacity will cap oil prices on the upside and possibly eliminate the "terrorism" premium (which has been estimated as up to $10 per barrel). The new Democratic-controlled Congress may eliminate previously-granted Federal tax breaks for energy companies.

S&P 500 Index Sector Performance



Source: Standard & Poor's

Sectors: Portfolio Strategy Considerations

Telecom valuations are not nearly as attractive as a year ago, but we believe it is prudent to maintain our current over-weight position in the sector. The Energy sector appears to have more downside than upside potential. Consequently, we will maintain our current under-weight position. The Staples sector will likely benefit from a slowing economy, and should be over-weighted at this time.

We continue to over-weight Health Care and Technology (as compared to its weightings in the S&P 500 Index). Health Care should flourish in a slower growth environment, although pharmaceutical companies are now challenged by reduced drug pipelines. Technology should gain from healthy corporate balance sheets and global product demand. Since Technology is becoming an export-driven industry (the US is a world leader in this area), it may benefit from the weaker US Dollar.

An inverted yield curve causes us to maintain our current portfolio under-weight to Financials (specifically regional banks dependent on interest rate spreads).

Market Cap Performance

Small cap stocks slightly out-performed large cap stocks in the Fourth Quarter 2006. This was not the case for the full year as large cap stocks out-performed small cap. We anticipate continued large cap out-performance in 2007, as out-performance tends to occur in multi-year streaks. The last period of noteworthy large cap excess annual returns lasted five years (from 1994 through 1998).

Political "gridlock" should favor large cap stocks (Quarterly Insights, October 2006, page 9).

Market Cap Performance

	Fourth Quarter 2006	2006
Large Cap Performance		
World	8.47%	20.65%
Foreign	10.40%	26.86%
USA	6.75%	15.32%
Small Cap Performance		
World	9.91%	17.56%
Foreign	11.75%	19.67%
USA	7.50%	14.67%

Source: MSCI

Market Cap: Portfolio Strategy Considerations

We continue to believe that large cap stocks are better positioned from a risk/reward standpoint and will maintain our large cap focus. Our current average market cap is approximately $40 billion, which is slightly smaller than the S&P 500 Index and larger than the MSCI EAFE Index. Our interest rate model predicts that the S&P 500 Index will beat the Russell 2000 Index by 9% in 2007.

Style Performance

Led by the Energy and Telecom sectors, value stocks out-performed growth stocks for the Fourth Quarter 2006 and for the year. Accelerating economic expansion favors cyclical value companies. Declining economic expansion favors companies with strong market positions and healthy balance sheets.

Style Performance

	Fourth Quarter 2006	2006
US Growth	5.77%	8.90%
US Value	7.74%	21.97%
Foreign Growth	9.43%	22.69%
Foreign Value	13.34%	31.05%

Source: MSCI

Style: Portfolio Strategy Considerations

We will maintain our growth bias due to our expectaton of a flat yield curve and slowing (yet positive) economic growth.

Bond Market Review

We believe the Fed rate hikes experienced in 2006 (+100 basis points) will cease (the last rate hike occurred August 8, 2006). The Lehman Brothers Government/Corporate Bond Index (widely considered the broadest of the major US bond indices) rose 1.06% for the Fourth Quarter and 3.77% for the year. Modestly rising interest rates and deteriorating credit quality held back bond returns.

Key US Interest Rates

	31 Dec 2005	31 Dec 2006	Change
Federal Reserve Board Funds Rate	4.25%	5.25%	+100 basis points
2-Yr Treasury (Constant Maturity)	4.39%	4.79%	+ 40 basis points
5-Yr Treasury (Constant Maturity)	4.35%	4.68%	+ 33 basis points
10-Yr Treasury (Constant Maturity)	4.39%	4.68%	+ 29 basis points

Note: 100 basis points (bp) = 1.00% Source: Bloomberg

During the year, interest rates rose and bond prices fell (yields increased) as investors continued to shift money from bonds to stocks.

The yield curve, which compares the 2-Year Treasury rate (Constant Maturity) versus the 10-Year Treasury rate, inverted as the rise of longer yields did not match the rise of shorter yields. This implies that future inflation will not be an issue. Core inflation has been minimal in 2006. Should energy prices fall as we expect, inflationary pressures could be reduced to the point of providing flexibility for the Federal Reserve. The Fed may finally be in a position to cut rates should the predicted "soft landing" of the slowing economy become more difficult than forecast.

We view current US and foreign interest rates as stable, although we believe that foreign rates may rise modestly. In our opinion, there is reasonable economic growth and minimal inflation risk. Even if interest rates rise, we would expect a modest increase in yields at best.

Corporations have used strong earnings and balance sheets to buy back shares and assume debt in an effort to increase equity returns. Very strong credit quality was weakened last year, as evidenced by the growing yield spread between corporate bond and treasuries. All in all, these factors point to a 2007 bond market that should be relatively uneventful.

Bond Market: Portfolio Strategy Considerations

We continue to maintain our fixed income portfolio position in shorter term maturity bonds (average duration of 4.5 years) and Treasury Inflation Protected Securities (TIPS). Shorter term bonds provide higher yields while protecting the portfolio from a larger than expected increase in interest rates.

Although we do not view inflation as a large risk at this time, TIPS offer protection in the event inflation becomes more prominent. This can be especially important for investors who require portfolio income.

2007 Market Forecast

In 2007, we believe global equity markets will advance 11%-15%. Market momentum will carry forward from the 2006 midterm elections.

Our 2007 Equity Market Prediction
"Global Markets Will Advance in the Range of 11%-15%"

RATIONALE				
Domestic Considerations		**Positive**	**Neutral**	**Negative**
Market Sentiment	The 2007 S&P 500 consensus forecast return of 7% is conservative.	◆		
Leading Economic Indicators	The index will continue to grow at an annualized rate of 3%-4%, consistent with moderate economic growth.		◆	
Monetary Policy	Stable interest rates should positively impact the equity market.	◆		
Fiscal Policy	Current fiscal policy (tax policy and deficit levels) will neither help nor hinder the equity market.		◆	
Market Momentum	Market momentum will continue.	◆		
History	The third year of the Presidential cycle has historically been the strongest for the market.	◆		
Equity Valuations	The current equity price/earnings ratio remains attractive.	◆		
Corporate Profitability	Profitability will show average gains in 2006.		◆	
Foreign Considerations				
Currency Translation	Exchange rates will stabilize.		◆	
GDP Growth, Monetary & Fiscal Policy	Relative to the USA, foreign GDP growth should lag, interest rates should rise, deficit levels comparable.		◆	

Our 2007 Bond Market Prediction
"Longer-term bond yields will slightly increase."

RATIONALE				
Domestic Considerations		**Correct**	**Neutral**	**Incorrect**
Interest Rate Expectations	The currently inverted yield curve will slightly flatten. The FRB will maintain the current level of interest rates.		◆	
Inflation Rate Expectations	Future inflation expectations will be minor and only slightly discounted into the longer maturity bond yields.		◆	

Global Equity Markets Should Rise in 2007

We predict that global equity markets will advance between 11%-15% in 2007. Our rationale is as follows:

Domestic Considerations

Market Sentiment

The 2007 S&P 500 consensus forecast of 7% (BusinessWeek, December 25, 2006), in our opinion, underestimates market potential given the other factors we will discuss shortly. The consensus forecasts were accurate from 2003 to 2005. Last year's forecast (10%) proved conservative (the S&P 500 index rose 15.80% in 2006).

Leading Economic Indicators

The Index of Leading Economic Indicators (LEI) rose at an annualized rate of only 0.2% for the last half of 2006. As Q4 2006 stock market growth is factored into the LEI, we anticipate the index will rise in the range of 3%-4% for 2007. This is a level that would be consistent with moderate economic growth. A reasonably rising LEI index could equate to stock market growth in the range of 11%-15%.

Monetary Policy

The Fed Funds Rate is currently 5.25%, a level we believe is accommodative to business. We do not foresee a rate adjustment in 2007 that would hinder economic growth. If there is a rate adjustment, we believe it would be downward. This should benefit the equity markets.

Currently, there is an "inverted yield curve".[2] Many investors believe this implies that we are headed towards a recession. We disagree. While it is true that inverted yield curves have preceded most recessions, we view the global economy as healthy.

In general, longer term interest rates are determined by expectations of future inflation. When investors believe inflation is ahead of us, interest rates rise. When slower economic growth is on the horizon, interest rates fall. We believe that inflation expectations will not significantly factor into longer term interest rates. Consequently, we anticipate a very slight "flattening" of the yield curve. This bodes well for the economy and the equity markets.

[2] A scenario where the 2-Year Treasury Rate exceeds the 10-Year Treasury Rate.

Fiscal Policy

Federal income tax cuts have continued to spur economic growth. Tax receipts have risen, even with the lower rates, setting an all-time high in 2006. However, government spending increased at a rate greater than revenue growth in 2006. The Bush administration's original forecast of a $319 billion deficit was substantially surpassed, reaching $423 billion.

The war in Iraq greatly exceeded original cost estimates. This situation continues to fester and was the major issue in the 2006 midterm elections.

Federal Deficit Levels ($ billions)

Year	Receipts	Outlays	Surplus/Deficit
2003	1,782	2,160	(377)
2004	1,880	2,293	(412)
2005	2,153	2,472	(318)
2006 (Est.)	2,285	2,708	(423)
2007 (Est.)	2,415	2,770	(354)

Source: Bureau of Economic Analysis

We believe the federal deficit level is within an acceptable boundary at this time, but remain concerned for the longer term.

In 2006, there was a surplus cash flow of $185 billion collected by Social Security that was included in federal government revenues. As baby boomers retire in the next few years, this surplus will likely evolve into a considerable deficit as the federal government meets Social Security obligations.

The cost of the Iraq war ($95 billion in the fiscal year ending in October, 2006) is “off-budget” — it is accounted under “Special Emergency Spending Bills” versus the budget of the United States Government. Therefore, the current budget deficit level underestimates reality.

Persistently large deficits can lead to higher long-term interest rates, essentially rule out the possibility of additional tax cuts, and put increasing pressure on Congress to make hard decisions about maintaining tax cuts, raising taxes, and/or cutting federal programs and benefits.

Market Momentum

There is considerable market momentum to carry over from Q4 2006. Market momentum should continue in 2007, although there will likely be short periods of market declines.

History

The third year of the Presidential cycle has historically been the strongest for the stock market.

Presidential Cycle — Annual Returns Since World War II

First Year	Second Year	Third Year	Fourth Year
6.1%	6.9%	24.1%	12.2%

Source: Standard & Poor's

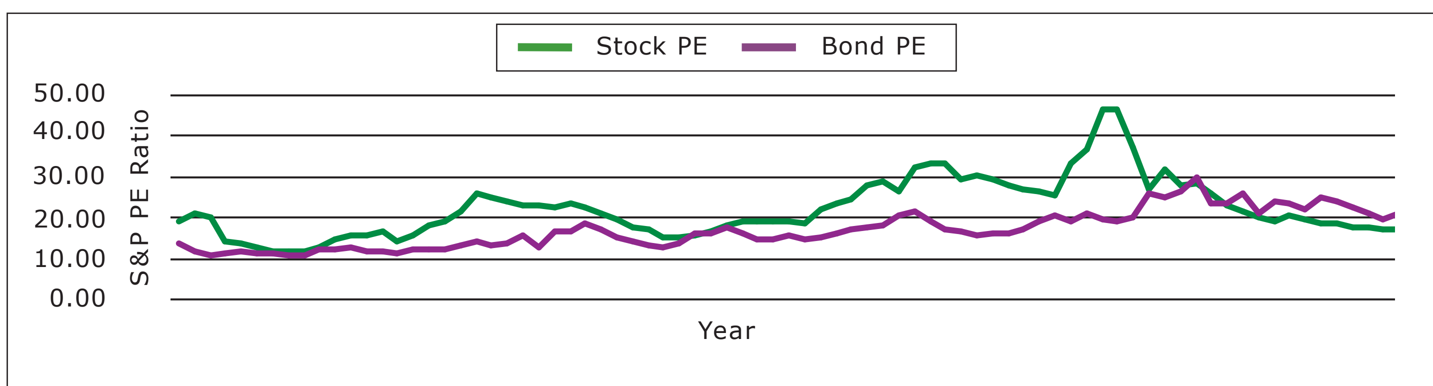
Corporate Profitability

Economic growth rates may be slowing, but corporate profits remain healthy. Standard and Poor's forecasts corporate profit growth of 9.5% in 2007. We anticipate this will be a catalyst for healthy market performance.

Equity Valuations

Due to its higher expected future earnings, we believe that a stock PE should theoretically exceed a bond PE.[3] Indeed, this was the case from 1987-2003. However, from 2004 to date, the 10-Year Treasury PE has exceeded the S&P 500 PE.

S&P 500 Price Earnings (PE) Versus 10-Year Treasury Price Earnings (1987—2006)



Source: Standard & Poor's

The S&P 500 PE Ratio is 17.40 (as of December 31, 2006). The 10-Year Treasury PE Ratio is 21.93 (as of December 31, 2006). There are three primary ways to interpret why the stock PE does not exceed the bond PE:

1. Bonds are over-priced
2. Stocks are under-priced
3. A combination of the above two points

We believe that bond pricing will be stable in 2007 (see Bond Market Review, page 8). Therefore, we conclude that stocks are under-priced.

The main factors that affect stock valuation levels are interest rates, expected growth, and risk.

We expect the Fed Rate (5.25%) to be stable in 2007. The interest rate environment should allow for expanding PE ratios.

Standard and Poor's forecasts corporate profit growth at 9.5% in 2007 for S&P 500 companies. US GDP growth is expected to lead the developed countries. Favorable expected growth should benefit stock PE values.

Politics, oil supply shocks, and terrorism are risk factors that are hard to qualify. Because the midterm elections have passed, we do not view politics as a 2007 risk. We do not believe oil supply poses a 2007 risk (see Sectors: Portfolio Strategy Considerations, page 6). Terrorism is a constant risk, but in itself should not negatively impact stock PE values.

[3] A stock Price Earnings (PE) ratio is calculated as stock price/company earnings (over the last 12 months). A bond PE ratio is the inverse of the bond yield.

Corporate balance sheets remain strong. The price earnings ratio (PE ratio = stock price/company earnings) of the S&P 500 Index should expand in 2007 because of the following:

- We anticipate stock prices will rise 11% to 15%, and
- Standard & Poor's forecasts 2007 profit growth to rise 9.5%

The PE ratio numerator (stock price) should rise at a relatively higher rate than the ratio denominator (company earnings), causing the ratio to increase.

Foreign Considerations

We do not believe the US Dollar will fluctuate dramatically in 2007 (see page 4), and consequently do not currently view the US Dollar as an important factor to determine US versus foreign equity exposure. We will increase our US equity exposure (and reduce foreign exposure) because of relatively higher projected US GDP growth and our expectation of increased foreign interest rates (coupled with stable US interest rates).

Longer-Term Bond Yields Should Slightly Increase in 2007

We view current US interest rates as stable, and believe that foreign interest rates will rise modestly. In our opinion, there is reasonable economic growth and minimal inflation risk. We anticipate that demand for US bonds from China and Japan will not waiver as these countries need US consumers to buy their exports. The US deficit level should not significantly impact the bond market (see page 11). All in all, these factors point to a 2007 bond market that should be relatively uneventful.

2007 Portfolio Strategy

Our 2007 outlook is more optimistic for the equity market than the fixed income market. We anticipate three portfolio adjustments from our current position:

- Increase domestic exposure and reduce foreign exposure
- Increase consumer staples exposure
- Reduce foreign health care exposure (but still maintain over-weight to the sector)

TriVant 2007

2007 Portfolio Strategy Considerations	2007 Portfolio Position (Anticipated)	2006 Portfolio Position (End of Year)
Equity		
Domestic versus Foreign	Increase Domestic, Reduce Foreign	78% Domestic, 22% Foreign
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Average Market Cap	Maintain current level	$40 Billion
Style (Growth versus Value)	Maintain current level	Weighted - Emphasis towards growth stocks
Portfolio Beta Level (Risk)	Maintain current level	Above Market (greater than 1.0)
Fixed Income		
Desirable Securities	Shorter term government bonds and Treasury Inflation Protected Securities (TIPS) Average Duration = 4.5 years	Shorter term government bonds and Treasury Inflation Protected Securities (TIPS) Average Duration = 5.5 years
Securities with less emphasis	Longer term government bonds, corporate bonds	Longer term government bonds, corporate bonds

Equity

Domestic vs. Foreign

We are raising domestic equity exposure and lowering foreign equity exposure because US GDP growth is forecast to exceed European GDP growth. Additionally, we anticipate that foreign interest rates will rise while US interest rates remain stable. Regarding foreign equity regional exposure, we will:

- Maintain Japan
- Maintain Emerging Markets
- Reduce Europe

For detailed discussion, see Portfolio Strategy Considerations, page 5.

Sector Weighting

We continue to over-weight Health Care and Technology, and under-weight Financials and Energy. The Consumer Staples sector has become more attractive and consequently, we will increase exposure in this area. For detailed discussion, see Sectors: Portfolio Strategy Considerations, page 6.

Average Market Cap

We will maintain the average market cap of our equity portfolios at $40 billion because we believe it lowers our portfolio risk without sacrificing performance. For detailed discussion, see Market Cap Performance, page 7.

Style (Growth vs. Value)

We continue to moderately weight our equity portfolio towards growth stocks because:

- Growth stocks have more attractive valuations versus value stocks at this time
- An inverted yield curve should favor growth versus value stocks
- Given a slower profit growth outlook, investors will likely seek large growth companies with solid historical earnings

Portfolio Beta Level (Risk)

We have a current portfolio beta above the market (greater than 1.0) and anticipate maintaining this level throughout 2007.[4]

Fixed Income

We will maintain our fixed income strategy, but slightly lower the average duration of the portfolio from 5.5 years to 4.5 years.[5] We believe there is a greater likelihood of an interest rate decrease (versus increase) in 2007.

[4] The beta of an individual stock is a measure of its risk in relation to the market. By definition, the market has a beta of 1.0. Portfolio beta describes the relative volatility of an individual securities portfolio, taken as a whole, as measured by the individual stock betas of the securities making it up.

[5] Duration measures the sensitivity of bond prices to a 1% change in interest rates. As interest rates increase (decrease), bond prices decrease (increase). For example, the average duration of 4.5 years would mean that if interest rates decrease by 1%, the bond portfolio value would be expected to increase by 4.5%.

Closing Thoughts

In 2006, we were successful regarding our equity strategy and selection. The equity component of our portfolio closely resembled the performance of the S&P 500 Index.

The fixed income component of our portfolio also performed well in relation to the market. (See Appendix: Our 2006 Report Card for a detailed discussion regarding our 2006 strategy and results.)

Our 2007 outlook is more optimistic for the equity market than the fixed income market.

We will continue to closely monitor the market and adjust your portfolio as needed. Please feel free to contact us anytime to discuss questions or comments you may have. We will keep you informed of portfolio progress.

Respectfully submitted,

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"A bank is a place that will lend you money if you can prove that you don't need it."
Bob Hope

Disclaimer: The information presented herein is intended for informational purposes only. All views are subject to change based on updated indicators. The recommendations made in this publication are made without regard to individual suitability. Investors should consider their own needs and objectives before making any investment decision. A risk of loss is involved with investments in stock markets.

Our 2006 Report Card

In this section, we re-visit our 2006 Market Forecast and Portfolio Strategy. How accurate was our forecast? How successful were our strategy decisions?

Our 2006 Equity Market Prediction

"Global Equity Markets Will Advance 9%-13%." **Conservative**

RATIONALE				
Domestic Considerations		**Correct**	**Neutral**	**Incorrect**
Market Sentiment	The 2006 S&P 500 consensus forecast return of 10% is reasonable.		◆	
Leading Economic Indicators	The index will continue to grow at an annualized rate of 3%-4%, consistent with moderate economic growth.		◆	
Monetary Policy	Stable interest rates should positively impact the equity market.	◆		
Fiscal Policy	Current fiscal policy (tax policy and deficit levels) will neither help nor hinder the equity market.	◆		
Market Momentum	Market momentum will be a factor in the second half of the year.	◆		
History	The second year of the Presidential cycle has historically been stronger for the stock market than the first.	◆		
Equity Valuations	The current equity price/earnings ratio remains attractive.	◆		
Corporate Profitability	Profitability will show average gains in 2006.	◆		
Foreign Considerations				
Currency Translation	Exchange rates will stabilize.		◆	
GDP Growth, Monetary & Fiscal Policy	Relative to the USA, foreign GDP growth should lag, monetary & fiscal policy is comparable.		◆	

Our 2006 Bond Market Prediction

"Bond Yields Will Stabilize." **Correct**

RATIONALE				
Domestic Considerations		**Correct**	**Neutral**	**Incorrect**
Interest Rate Expectations	The yield curve will remain flat, and has the potential to slightly invert. The FRB will likely maintain the current level of interest rates.		◆	
Inflation Rate Expectations	Future inflation expectations will be moderate and be discounted into the longer maturity bond yields.		◆	

Our 2006 Portfolio Strategy Considerations

PORTFOLIO POSITIONING				
Equity		**Correct**	**Neutral**	**Incorrect**
Domestic versus Foreign	The foreign component of a properly diversified equity portfolio should not exceed 21%. Domestic exposure was increased from 74% to 79%.			◆
Sector Weighting	*Over-weight (to S&P 500 Index)* - Telecom - Health Care - Technology *Under-weight (to S&P 500 Index)* - Financials - Utilities			◆
Average Market Cap	Average market cap was increased to $42 billion (from $35 billion).	◆		
Style (Growth versus Value)	We maintained a slight emphasis on growth stocks.			◆
Portfolio Beta Level	Portfolio beta level was increased from "below the market" (less than 1.0) to "above the market" (greater than 1.0).	◆		
Fixed Income				
Desirable Securities	Shorter term government bonds and Treasury Inflation Protected Securities (TIPS). Average Duration = 5.5 years.		◆	
Securities with Less Emphasis	Longer term government bonds, corporate bonds.	◆		

2006 Equity Market Prediction – How We Fared

Our overall prediction of a 9%-13% advance in equity market growth proved to be conservative (see Equity Market Review, page 3), as did domestic market sentiment (the consensus forecast was a 10% return on the S&P 500 Index). The Leading Economic Indicators index was flat (0.2%) for the six months spanning May through November.

We correctly anticipated the effects of monetary policy, fiscal policy, market momentum, history, corporate profitability, and equity valuations. Of these factors, monetary policy and market momentum likely had the most significant impact on the equity market.

The US Dollar depreciated against the Euro and British Pound at a rate higher than we expected, although the Dollar slightly appreciated versus the Yen. Overall, we do not view currency translation as an important factor in our 2006 portfolio performance, nor did we anticipate that it would. Although foreign GDP growth lagged US GDP growth, the foreign markets out-performed at a rate greater than their relative currency appreciation. This was an occurrence we did not foresee.

2006 Fixed Income Market Prediction – How We Fared

We anticipated that the Federal Reserve Board would maintain the 2005 year-end level of interest rates. Rates increased a total of 1.00% (100 basis points) in 2006, so our interest rate prediction was not accurate.

Despite the slight rise in interest rates, we were correct in predicting that the yield curve would remain flat and have the potential to slightly invert. The 2-Year Treasury yield rose 0.40% (40 basis points) to 4.79%. The 10-Year Treasury yield rose just 0.29% (29 basis points) to 4.68%. Consequently, the yield curve is now slightly inverted (see page 8 for detailed discussion). Inflation and expected inflation, for the third consecutive year, did not factor into the rate of longer term interest rates to the degree we anticipated.

2006 Portfolio Strategy Considerations – How We Fared

Equity

We were moderately successful regarding our equity strategy and selection. The equity component in some of our customized portfolios slightly lagged the S&P 500 index in 2006. Overall, our portfolio has out-performed the S&P 500 index since our inception[6].

In our opinion, 2006 was a year where our equity strategy decisions had greater performance attribution than our equity selection. Strategy considerations included the following factors:

- Domestic versus foreign weighting
- Sector weighting
- Average market cap
- Style (growth versus value) weighting
- Portfolio beta level (risk)

Overall, we assess our 2006 decisions in the above areas to be satisfactory, but not excellent.

Domestic vs. Foreign

Our research concludes that an equity portfolio (for a USA-based investor) comprised of 79% domestic (USA) stocks and 21% foreign (non-USA) stocks carries the least amount of risk (see Quarterly Insights, July 2006, page 10). We reduced our 2006 foreign exposure (from 26% to 21%) in our equity portfolio because we felt it was a time to be conservative versus aggressive in terms of portfolio risk (standard deviation).

[6] Composite data is available upon request.

Foreign stocks out-performed (with the exception of Japan), partially due to relatively strengthened currencies. The small reduction in foreign exposure slightly hindered our portfolio performance. However, reducing foreign exposure enabled us to implement desired positioning regarding portfolio sector weighting, average market cap, style and beta.

Sector Weighting

In 2006, our portfolio was over-weighted to Telecom, Health Care and Technology. It was under-weighted to Financials, Energy and Utilities. Portfolio performance would have improved had we over-weighted Energy and under-weighted Health Care and Technology. Telecom and Energy significantly out-performed the S&P 500 Index. Health Care and Technology significantly lagged the S&P 500 Index.

We increased our Telecom exposure early in 2006, but since Telecom comprises less than 5% of the S&P 500 Index, the positive performance attribution of this sector was not significant. Since we did not adjust our Energy weighting as the sector rose (at the time, we did not believe this was a worthwhile risk/reward tradeoff), our slight market-underweight portfolio position soon became more pronounced. This caused a performance lag.

Our over-weight positions in Technology and Health Care also impacted portfolio performance. However, we believe these two sectors are well-positioned for 2007 and will consequently maintain the over-weight positions (see page 6).

Most other sectors performed within a narrow band in 2006, and our positioning in these sectors neither helped nor hindered portfolio performance.

Average Market Cap

We raised the average market cap of our equity portfolio from $35 billion to $42 billion because we believed it would lower our portfolio risk without sacrificing performance. In 2006, large cap US stocks slightly out-performed small cap US stocks (see page 7). Our positioning proved correct.

Style: Growth vs. Value

We slightly weighted our equity portfolio towards growth stocks in 2006 because:

- Growth stocks had more attractive valuations versus value stocks at that time
- A flatter yield curve should, theoretically, favor growth versus value stocks
- Given a slower profit growth outlook, investors would likely seek large growth companies with solid historical earnings.

For these same reasons, we continue to weight our equity portfolio towards growth stocks. Value stocks out-performed growth stocks in 2006 (see page 7). The Energy sector was the driving force for value stocks. The Technology sector hurt growth stocks. Our growth bias slightly hindered the portfolio.

Portfolio Beta Level (Risk)

The beta of an individual stock is a measure of its risk in relation to the market. By definition, the market has a beta of 1.0. Portfolio beta describes the relative volatility of an individual securities portfolio, taken as a whole, as measured by the individual stock betas of the securities making it up.

We increased our portfolio beta from "below the market" (less than 1.0) to "above the market" (greater than 1.0) in anticipation of an above-average equity market return (9%-13%). In 2006, the S&P 500 Index performance (15.80%) exceeded our expectation. The move towards a higher portfolio beta level was successful.

Fixed Income

The fixed income component of our portfolio performed reasonably well in relation to the market. Given our expectation that the yield curve would flatten, we held shorter term government bonds and Treasury Inflation Protected Securities (TIPS). The average duration of our fixed income holdings was 5.5 years.

In 2005, we reduced our corporate bond exposure when the spread between corporate and treasury bonds became very narrow. In 2006, we maintained our level of corporate bond exposure as the spread widened. This neither helped nor hindered the bond portfolio, although we will consider adjusting the level of corporate bond exposure in 2007.

We could have slightly benefited from higher average bond duration. The yield curve flattened more than we anticipated. Bearing in mind our clients' specific portfolio income needs, we felt the potential risk in having average bond duration greater than 5.5 years, given our interest rate and inflation rate expectations, would have been too great.