Schaper, Benz & Wise
INVESTMENT COUNSEL, INC.

Economic and Market Summary
January 2007

U.S. economic growth has moderated to about 3.0%. While lower than 3.2% in 2005 and 3.9% in 2004, this is still a healthy growth rate. Consumer spending has been resilient despite significant weakness in the housing market, defying pessimists who believe that "equity withdrawal" from rising home values is the main driver of economic growth during the current expansion. Wage and salary growth, which has a much greater impact on spending than home equity, has accelerated to 6.3% and unemployment has dropped to 4.5% during 2006. Due to the vibrancy of the labor market and to attractive borrowing rates, housing is likely to be less of a drag on 2007 economic growth than commonly believed. Business spending is growing 8% and, supported by robust corporate profits and healthy balance sheets, should contribute to economic growth again in 2007. Other key variables that appear supportive of continued economic expansion are accessible and inexpensive credit and strong economic conditions of most major trading partners, driving strong export growth.

Tempering our outlook, however, are cautious signals from two fairly reliable forward-looking indicators. The Manufacturing ISM (Institute for Supply Management) Index broke slightly below 50 in November indicating contracting conditions in the manufacturing sector. A recovery in December to 51.4 is encouraging, but still signals only moderate growth. The yield curve is slightly inverted (long-term bond yields are lower than short-term money market yields), which has been a precursor to previous economic slowdowns. Also, favorable fiscal policy has facilitated economic growth in recent years. We're monitoring closely the sometimes disturbing rhetoric coming from newly elected congressional leaders. Protectionism, increased government regulation and involvement in health care, and tax increases would be damaging to the economy. At this point, we remain confident that sound judgment, and the President's veto pen, will prevent any palpably harmful measures from becoming law. Overall, we expect U.S. economic growth to remain in the vicinity of 3% throughout 2007.

Inflation remains a potential concern for the U.S. economy. Stubbornly high commodity prices, accelerating wage and salary growth, decelerating productivity, large budget deficits, and a weakening dollar could fuel inflation. Despite these developments and warnings from the Federal Reserve, bond investors seem unmindful of the possibility that inflation could reaccelerate after moderating in recent months. The Consumer Price Index has been distorted the past 3 years by wild swings in energy prices. Core inflation, however, appears to be trending upward. We remain uncomfortable investing in all but very short maturity bonds. The general consensus expects the Federal Reserve to begin lowering interest rates by mid-year 2007. We do not expect the Federal Reserve to ease in 2007.

Corporate profits increased about 14% in 2006, again exceeding expectations. Profit growth could slow in 2007 because of a partial reversal of unsustainably high profits earned by energy and commodity producers. Since the last cyclical peak in 2000, profits for companies in the S&P 500 are 54% higher while the S&P 500 index is about flat, resulting in PE ratio contraction from 26x to 16x. Steady economic and corporate profit growth, reasonable valuations, and accommodative interest rates and credit conditions are supportive of further stock price appreciation. Despite continued investor enthusiasm for cyclical investments such as real estate, commodities, and energy, we believe that high quality consistent growth companies will continue to provide attractive long-term returns with limited volatility.

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To request our SEC Form ADV Part II, please contact Michael L. Wise, Chief Compliance Officer, at the address below.

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