



Quarterly Commentary: October 3, 2005

Greetings from San Mateo! We hope you enjoyed the last days of summer and have exciting plans for the fall. The summer quarter is typically characterized by little news and slow market activity, but the summer of 2005 was certainly atypical. A significant amount of genuinely impactful news contributed to considerable volatility in the equity and fixed income markets. While this volatility can be frustrating, we remind you that short-term volatility provides investors with long-term opportunity and that, ultimately, the market rewards companies with strong business models and improving fundamentals – exactly the kind of companies we own on your behalf.

For the third quarter, the Dow Jones Industrial Average gained 2.9% but is still down 2.0% for the year, and the NASDAQ gained 4.6% but remains down 1.1% year-to-date. The S&P 500, our primary benchmark, gained 3.1%, helping it move 1.4% into the black for the year. We are pleased to note that most of your portfolios continue to outperform year-to-date.

We would be remiss if we did not mention the past month's events along the U.S. Gulf Coast. Like all Americans, we are saddened by the devastation and can only hope that your families were not directly impacted by Hurricanes Katrina or Rita. As investment managers, it is our responsibility to analyze how major events like these will affect your portfolios, both in the near- and long-term. For example, the two hurricanes wreaked incredible destruction on the Gulf's oil and gas infrastructure, which has had the slightly perverse effect of driving up the share prices of your energy-related holdings. While companies like Chevron and Royal Dutch Shell will have to engage in significant reconstruction of some drilling platforms and pipelines, the decreased production volumes should support energy prices that will more than offset the repair costs. As such, your energy holdings were some of the strongest performers this quarter.

On a more macroeconomic basis, the effects of the hurricanes will be mixed. First, the overall health of the economy was strong before the hurricanes hit, and it should remain so as the Gulf states recover and rebuild. For example, national unemployment is now below 5% for the first time since 2001 – a level many economists consider “full employment.” Second, GDP growth may slow slightly for the balance of 2005, but the massive reconstruction efforts, coupled with the large highway bill passed in August, should add to growth in 2006. There is simply no data to suggest that the hurricanes will cause our economy to stall.

In the face of rising energy prices, some market watchers are voicing concern over possible inflation. With a few targeted exceptions (*e.g.* energy), we believe inflation is likely to remain in check, especially as the Federal Reserve continues its measured pace of short-term interest rate increases. For one, Fed Chairman Greenspan has built up the political capital over his tenure to continue raising rates for some time – a luxury the new Chairman will not have. Thus, we expect the Fed to continue raising rates at least until January 2006, when Greenspan's term expires. Your portfolios remain well positioned despite this continued increase in short-term rates.

As the economic climate continues to change, many of our clients have asked us whether we feel it is appropriate to get “more aggressive” or, conversely, “more defensive” with their portfolios. Indeed, we are doing both. On balance, your portfolios are prototypically defensive: you own a well-diversified collection of blue-chip companies in stable industries such as consumer staples, health care, financial services, REITs and energy. That said, we also look for opportunities where more quickly-growing

companies are trading well under their intrinsic values. Either way, we are confident that equities remain particularly attractive. In support of this belief, we point to the fact that the range of valuations within the S&P 500 has tightened substantially over the past 5 years. Back in 2000, one might have focused merely on cheap stocks because they were much easier to identify. That is, expensive stocks were very expensive, and cheap ones were very cheap. Now, with the range between high and low valuations tightened, the best investment opportunities exist where the best businesses exist. In other words, many pundits believe we are now in a classic “stock pickers’ market.” We prefer to think we’re in a classic *business-pickers’* market – something which we do best.

As further evidence of the business strength of your equity holdings, we’ll note some recent fundamental characteristics of the Golub Group’s aggregate stock portfolio. Collectively, our portfolio companies enjoyed a 15% annual increase in revenues, a 30% annual increase in net income, a 17% annual increase in operating profit, and a 12% annual increase in shareholders’ equity. These are impressive numbers, and we believe that the companies’ stock prices will ultimately reflect the strength of this data.

Recent growth of the Golub Group has led us in the past few quarters to devote some of our quarterly discussion to new employees, new clients, and a new office. This quarter, we’d like to recognize an anniversary. It was just over one year ago that the Golub Group began working with Charles Schwab as a member of its Schwab Advisor Network. While we have had a longer working relationship with Schwab, we truly appreciate the support and commitment that comes from the Schwab Advisor Network. In particular, we would like to recognize Gage Gilham, Scot Kobashigawa, Lance Oman and Mariah Byrne, as well as the numerous Schwab Financial Consultants across northern California, for their support. Thank you for all that you do!

We close with a few operational notes. First, as we move into the fourth quarter, we begin to think about 2005 tax considerations. Although April 15th might seem far away, we may make tax-related adjustments to your portfolios during the coming quarter. As a result, we encourage you to introduce us to your tax advisers so we can best minimize your overall tax bill. Second, many clients are entrusting us with more of their assets to manage and are often curious as to where they should send a check. Please make your checks payable to our custodian, Charles Schwab & Co., not the Golub Group. In your check’s memo line, note your name and account number, preceded by the term “For the Benefit of,” or simply “FBO”. You can mail those checks to us, and we’ll take care of the rest.

As always, included with this commentary are your account performance figures, management fee invoice(s), and a copy of your portfolio allocation as of 9/30/05. You are also welcome to access your accounts online at www.golubgroup.com. Finally, as we mail this letter, we look forward to hosting our annual Open House celebrating the Golub Group’s second anniversary as an independent firm. We are delighted to see so many old friends and new faces planning to attend. If you are not able to make it – or even if you are – please know that we always look forward to hearing from you. Please don’t hesitate to write, call, or visit!

With Warm Regards,

The Golub Group

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