NORTH ★ STAR
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FOURTH QUARTER 2006

The stock market rally that began in mid-July continued virtually uninterrupted through the fourth quarter of the year. The S&P 500 rose 6.20% in price and provided a total return of 6.70% including dividends for the quarter. There were a number of factors that continued to provide a tailwind for stocks during this period. Earnings continued to surprise on the upside. It now looks like the operating earnings for the S&P 500 grew an impressive 16% in 2006. Interest rates remained relatively stable during the quarter as inflationary pressures moderated. The ten-year Treasury note began the fourth quarter at a 4.64% yield and finished the year at 4.71%. The most recent reading on the Fed's favorite inflation indicator, the core personal consumption expenditures index, showed no change in November and was up 2.2% on a year over year basis. This rate of inflation has fallen in the last several months and is now very close to the Fed's stated comfort zone of 1½%-2%. Thus far, the Federal Reserve appears to be successfully engineering the elusive "soft landing" for the economy. The progression in real GDP growth in 2006 was as follows; 1st Q +5.6%, 2nd Q +2.6%, 3rd Q +2.0%, and 4th Q estimate +2-2.2%. With the understanding that the stock market cannot continue to rise indefinitely without some corrections along the way, and also noting the extended nature of some short-term technical indicators, we are still of the opinion that the current environment is conducive for further gains in equities this year.

THE IMPORTANCE OF BEING GREEN

Sometimes we are surprised when an idea that has been around for awhile suddenly takes center stage. As investment managers, we are students of this phenomenon, yet we can be caught off guard, too. It appears that the concept of global climate change is gaining wide acceptance. Over the past few years, much scientific research has been devoted to this subject. It ranges from alarmist to dismissive; with what is probably a lot of good science in between. As investors and citizens, we will all reach our own conclusions; it is not our place or intention to argue for or against. Regardless of the science, we are aware that the subject of climate change is moving into the main stream and will increasingly demand a bigger share of the world's attention and investment dollars. The social, economic and political consequences of global climate change are potentially enormous. As might be expected, investors have a name for the broad study of this developing theme on the world's financial markets. That name is clean technology.

Clean technology is not just about developing alternative energy sources, as it touches on all aspects of efficiency, lower emissions of greenhouse gases and the smart use of resources. A company is considered to be part of the clean technology industry if it produces any product or service that improves operation, performance, productivity or efficiency while reducing costs, inputs, energy consumption, waste or pollution.

In September of last year, California Governor Arnold Schwarzenegger signed into law a bill that requires the state to reduce its greenhouse gas emissions to 2000 levels by 2010 and to 1990 levels by 2020. This ambitious plan will require California to heat, cool, transport and employ in the year 2020 an estimated 44 million people while keeping emissions at 1990 levels - when the population was 30 million. Eleven other states are following California's example for aggressively curbing greenhouse gases in a variety of ways. Nationally, both political parties are weighing in on this issue as we prepare for the change in legislative leadership this month.

The rest of the world has been taking notice of these issues for a number of years and reacting in a variety of innovative ways. One example is the creation of a market for the trading of emission credits, whereby companies that pollute beyond an allowed level are able to buy credits from those who pollute less than their allowances. Also contemplated for wider use are carbon taxes which levy taxes directly on those industries that produce CO^2.

As in other endeavors, the application of market forces tends to produce more economically beneficial results. Most promising in our opinion are incentives that encourage adoption of cleaner power production, such as those that benefit installation of solar panels. Japan, the second largest solar market in the world (after Germany), is now a self-sustaining and growing market where solar power is competitive with minimal subsidies. After having supported consumers' investments in solar power installations since 1994, the Japanese subsidy

scheme has now been phased out for residential installations, yet sales have not dipped. (It must be pointed out that Japan has among the highest electricity prices in the world). The problem in the U.S. is that very few states have consistently offered incentives. Those that have are seeing a growing number of installations. Carbon sequestration describes the process where carbon dioxide is recycled back into trees, plants and the soil. The U.S. Department of Energy and others are also researching long-term storage of carbon underground, or deep in the ocean so that the buildup of carbon dioxide concentration in the atmosphere will reduce or slow. At this time, the associated technology is unproven and expensive. An obvious beneficiary of success in this area will be our own coal industry.

Indeed, it may take some time to sort it all out, but if the amount of money flowing toward clean technology from venture capital is any indication, the future is bright. Many pundits are calling the move to clean technology the biggest (or bigger still) thing since the internet. While we hope that this coming boom will not end in similar fashion, we understand the risks that come from too many dollars chasing too few good or economically viable ideas. Many of the companies that we invest in for your benefit are leaders in this emerging discipline. Several exchange traded funds that focus their investments on clean technology are being introduced as well.

Great investment ideas often come after analyzing emerging themes. Clean technology has joined our working list of themes along with trends in health care, demographics and information technology to name a few. An important part of what we do for you involves identifying investments that will benefit as our society progresses. We wish you a prosperous New Year.

Bob Van Wetter Timothy J. Waymire, CFA Richard P. Kopp, CFA
Moses Taylor Frederick B. Taylor

Cynthia Sack Gina Spencer

Northstar Investment Advisors, LLC
700 17th Street
Suite 2350
Denver, CO. 80202
303-832-2300
800-204-6199
www.northstarinvest.com

to save for your retirement years, won't be paying FICA tax, and the kids should be out of the house.

Here are the Savings to Income Ratios

Age	Savings to Income Ratio
30	0.1
35	0.9
40	1.7
45	3.0
50	4.5
55	6.5
60	8.8
65	12

To use the chart, take your current income and then multiply it by the Savings to Income Ratio that corresponds with your age. For instance, if your income is $150,000 and you are 50 years old, your Savings to Income Ratio should be 4.5. Thus, you should have approximately $675,000 in investable assets ($150,000 X 4.5).

If you would like to explore these concepts in greater detail as they may relate to your personal finances, please feel free to call your portfolio manager. Charlie's ratios were originally published in an article he wrote for the Journal of Financial Planning in January 2006, and have also appeared numerous times in the Wall Street Journal.

Richard P. Kopp, CFA Moses Taylor Frederick B. Taylor

Bob Van Wetter Charlie Farrell, J.D. LL.M. Timothy J. Waymire, CFA

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