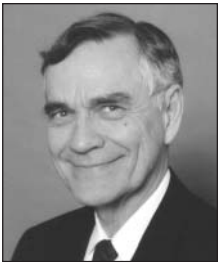


THE QUARTERLY NEWSLETTER OF CARTER FINANCIAL
MANAGEMENT AND CARTER ADVISORY SERVICES

2005 MARKET OVERVIEW

By Joe B. Mattei, CFP®



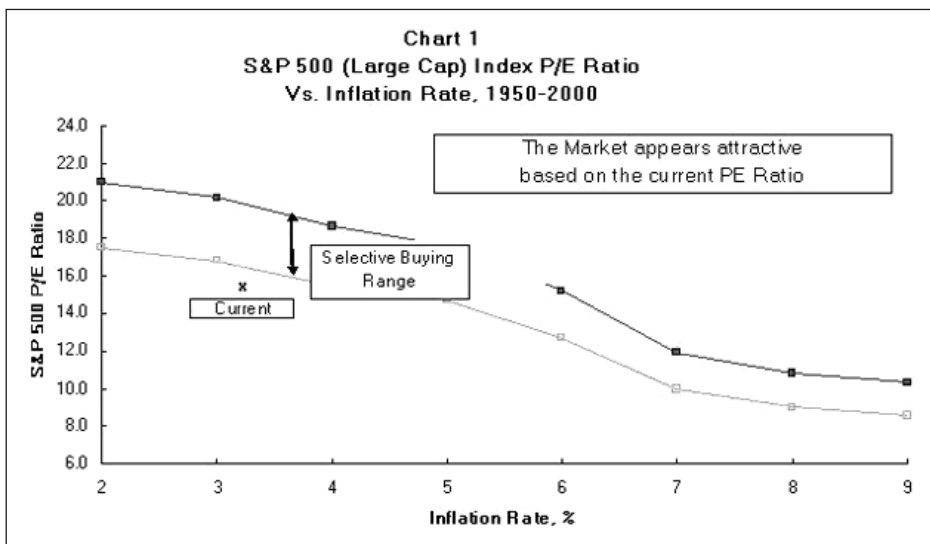
Joe B. Mattei, CFP®

The attached charts are intended to provide a framework for where the domestic market stands today, and a quantitative guide for future investment decisions.

Chart 1 shows the norm for the S&P 500 P/E (Price/Earnings) ratio versus inflation. The S&P 500 is an unmanaged index of 500 widely held stocks generally considered representative of the U.S. stock market. When inflation is low, such as today, the P/E ratio is normally higher than the average. When inflation increases, the market demands a lower P/E ratio, primarily because increasing costs caused by inflation may not be recoverable in the price of the products sold. Currently, at an inflation rate of about 3 percent, the historical norm for the S&P 500 P/E ratio has been between 17 and 20.

Chart 2 is an operating earnings forecast for the S&P 500, based on data from *Business Week* and *First Call*. From 1999 until mid 2000, the S&P 500 earnings outlook and the market were up. Starting in the April to July 2000 time frame, the earnings outlook and the market peaked, and then declined, initiating the bear market. The earnings decline continued until the end of 2001. During 2002, the earnings outlook was mixed to slightly up, but the bear market continued, because of a P/E ratio decline.

Chart 3 is a monthly plot of the S&P 500 Forward Looking P/E ratio since the start of 2000. During 2001, the P/E ratio averaged about 21. Starting in 2002, the average P/E ratio declined to about 17, almost a 20 percent drop. The 2002 bear market was the result of the P/E ratio reverting to the norm – not a reflection of earnings. In February 2003, the P/E ratio was down to 14, *continued on page 5*



10 TIPS TO MINIMIZE IDENTIFY THEFT

By Mark Opdahl



Mark Opdahl

The rash of identity theft incidents in recent news headlines probably has you concerned about the safety of your own personal information.

Although the media reports may have given the impression that this phenomenon is widespread, a recent Federal Trade Commission's survey found that only 3.39 percent (10 million) of the population of the United States have been victims of identity theft.

The low percentage is surprising considering the numerous places you can find someone's personal information. However, the number of people with access to personal information is increasing every day, so we could see an increase in the number of people affected in the future.

Identity theft can cause issues ranging from loss job opportunities to being arrested for crimes you did not commit. The ramifications can take months or years to clean up. However, you do not have to stand by and become a victim. You can take action to protect yourself and prevent prying eyes from taking advantage of your personal information. Here are 10 easy tips to help you minimize your chances of having your identity stolen.

Tips to Minimize Identity Theft

1. **Shred receipts, credit applications, bank statements** and other documents that might have personal information. The goal is to make the information as

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PRESIDENT'S LETTER

Second Quarter 2005



“Real Estate Bubble?”

“Is there a real estate bubble?” is probably the most frequent question you hear in today’s investment circles.

Bill E. Carter, CFP®, ChFC, CLU While there has been much discussion on this topic for some period of time, I have not written about it because I did not think the problem was urgent. I am not sure we are at that point today, but it does appear there is a bubble building in certain geographical locations.

However, let’s establish some basic facts.

First of all, real estate prices are very local in nature. There are certain markets today, even in Texas, that without question, are not overpriced, or at least not overpriced by historical standards. However, if you look at certain markets, such as in the Northeast, Florida, parts of Arizona and California, housing prices seem to be increasing at an unsustainable pace.

Let’s examine the drivers that have contributed to the increase in the areas I just referred to that may be creating a real estate bubble. The first driver is low interest rates. After the stock market bubble burst and the economic slowdown following 9/11, the Federal Reserve began lowering rates in a very aggressive manner in an attempt to provide a catalyst to get the economy growing again. This led to very low mortgage rates. With mortgage prices being so low, there was a whole new set of first-time home buyers that could now afford to purchase a home as opposed to spending their money renting. As this group began to buy houses, the people who owned those starter homes bought larger properties that were more expensive than what they previously owned. This trend continued all the way up the pricing hierarchy, resulting in overall higher prices.

The second driver was lending institutions that became very aggressive in their lending policies. They continue to be very innovative and very aggressive. This has resulted in many marginal consumers purchasing homes they may not have been able to afford under more conventional financing. In fact, I have never seen so many creative financing methods and mortgages in my career as we have seen in the last few years, as banks and mortgage companies continue to aggressively market to increase market share.

The third driver, after the stock market burst, many people became disenchanted with the equities markets and sold out completely. While much of this cash sat on the sidelines, and in fact, much is still sitting on the sidelines, there were many people who were simply not satisfied with the 1 percent return they were receiving in certificates of deposits or money market funds. They began looking at ways to invest this money creating more growth in their total portfolio, and real estate looked attractive.

So, if you have lower interest rates, creative and aggressive financing, the continuation of buy-up in hierarchy of bigger and more expensive homes, and investment dollars looking for a place to earn more than money market rates, you can see why prices began to increase. From an investment perspective, as more real estate investors come into the market in the locations referenced earlier, we are seeing investors buying real estate before the actual building is built, and then flipping it once the property is completed. This speculation may have created a bubble in certain markets.

And so the spiral continues upward. As a result, the question becomes “Does the bubble already exist, and if so, how *severe* is this bubble?”

Information published in the June 18 issue of *The Economist* is somewhat alarming.

“According to the estimates by *The Economist*, the total value of residential property in developed economies rose by more than \$30 trillion over the past five years, to over \$70 trillion, an increase equivalent to 100 percent of those countries’ combined GDPs. Not only does this dwarf any previous house-price boom, it is larger than

the global stock market bubble in the late 1990s (an increase over five years of 80 percent of GDP) or America’s stock market bubble in the late 1920s (55 percent of GDP). In other words, it looks like the biggest bubble in history.”

This article is not only saying there is a bubble developing; it says one has already developed and it appears to be the worst in history.

Just like the bubble in the stock market, you are never sure it is developing because you generally do not see it, except in hindsight. The other difficult thing about a bubble is that it may go on for some period of time. Again, we saw this in the stock market, as stocks remained overpriced for a considerable period.

Let’s assume for a minute there is a bubble at least in certain areas. If that is the case, we need to address the questions, “what will burst the bubble and what will the effect be?”

I think some answers are relatively obvious. One, if interest rates were to increase and people could not afford to buy new homes, then this buying hierarchy I mentioned earlier could happen in reverse.

You can also see the same effect if there was an overall slowdown in the economy, where people begin to lose jobs and cannot afford to make their mortgage payments.

In any of these scenarios, we would see that a large number of people “bought in over their heads” with low interest rates and aggressive lending practices, and now cannot afford their mortgage payments.

The same article in *The Economist* points out the housing market in Britain, Australia and The Netherlands have already begun to slow.

“Some housing booms have now fizzled out. In Australia, according to official figures, the 12-month rate of increase in housing prices slowed sharply to only 0.4 percent in the first quarter of this year, down from almost 20 percent in late 2003. Wishful thinkers call this a soft landing, but another index, calculated by the Commonwealth Bank of Australia, which is based on prices when contracts are agreed rather than at settlement, shows that average house prices have actually fallen by 7 percent since 2003; prices in once-hot Sydney have plunged by 16 percent.

“Britain’s housing market has also cooled rapidly. The Nationwide index, which we use, rose by 5.5 percent in the year to May, down from 20 percent growth in July 2004. But once again, other surveys offer a gloomier picture. The Royal Institution of Chartered Surveyors (RICS) reports that prices have fallen for 10 consecutive months, with a net balance of 49 percent of surveyors reporting falling prices in May, the weakest number since 1992 during Britain’s previous house-price bust. The volume of sales has slumped by one-third compared with a year ago as both sellers and buyers have lost confidence in house valuations. House-price inflation has also slowed significantly in Ireland, the Netherlands and New Zealand over the past year.”

“Since 1997, home prices in most countries have risen by much more in real terms (i.e., after adjusting for inflation) than during any previous boom. (The glaring exceptions are Germany and Japan, where prices have been falling). American prices have risen by less than those in Britain, yet this is still by far the biggest boom in American history, with real gains more than three times bigger than in previous housing booms in the 1970s or the 1980s.”

Now to the second question: “How severe would the impact be if this bubble were to burst?” Trying to determine the impact is just as difficult as trying to determine if there is a bubble in the first place, and trying to determine the time it will burst is nearly impossible. One scenario is the overall impact would not be that great. The only areas that would

be impacted to any major degree would be in those markets in the geographical areas where prices have really been speculated upward. Another scenario is that when the bubble bursts, it will be similar to the stock market burst, with a dramatic effect in housing prices all over the country.

In my opinion, it will be somewhere in between. If the markets continue to increase at the rates they are increasing for an extended period of time, then there will definitely be a true bubble and prices will decline substantially. I think this bubble would have an effect nationwide. However, I also think in those areas that have not been overpriced, general pricing may come down for awhile, but the prices would rebound in a reasonable period of time, probably one to three years. In those markets where the speculation has been the greatest, the people who bought in toward the end will probably have to wait many years before they see prices recover to those highs.

This is not the first time I have seen an increase in prices like this. We have seen them in California several times, and I remember a time in Dallas where prices in Highland Park were moving up, literally, on a weekly basis.

How do you protect yourself in this situation? First, **avoid buying in these highly speculative markets**, unless you are purchasing to own a property you plan to live in. If you plan to live there for an extended period of time, at some point, the prices will come back. Second, **place yourself in a position where you**

do not have to sell the real estate if the market declines. Just like the stock market, if you can hold through a decline, markets will generally rebound and go even higher. You do not want to be holding a note on one of these overpriced properties when the bottom falls out and be forced to sell.

As with all bubbles, we really do not know how severe the impact will be until it ends. While we can speculate on what the effect will be, we really do not know until the bubble bursts and we see where prices finally settle. The other thing to keep in mind is that there are always other circumstances that can exacerbate the problem and make it much worse. We saw this with the market decline that began in 2000. The impact of 9/11 extended the decline in the market and certainly made it worse.

So let me sum it up. I am not positive we are in a real estate bubble; however, there appears to be one developing in certain geographical areas. If a bubble does not already exist, but speculation continues to drive prices higher and higher, a bubble will be created. I am not saying you should not buy real estate; I am just suggesting caution. If you are buying in one of those really “hot” areas, be prepared to hold that real estate for an extended period of time in case the market turns south.



Bill E. Carter, CFP®, ChFC, CLU
President

FINANCIAL TRENDS	6/30/04	9/30/04	12/31/04	3/31/05	6/30/05
Dow Jones Industrial	10,435.48	10,080.27	10,783.01	10,503.76	10,274.97
NASDAQ	2,047.79	1,896.84	2,175.44	1,999.23	2,056.96
NAREIT Composite	125.64	134.00	150.94	137.88	137.88
Russell 2000	591.52	572.94	651.57	615.07	639.66
MSCI-EAFE	1,327.98	1,318.03	1,515.48	1,503.85	1,473.72
Prime Rate	4.00%	4.75%	5.25%	5.75%	6.25%
Gold	395.80	415.65	435.60	427.50	437.10
10-Year U.S. Treasury	4.59%	4.12%	4.22%	4.49%	3.92%
30-Year U.S. Treasury	5.31%	4.89%	4.82%	4.77%	4.22%
1-Year Certificate of Deposit	1.85%*	2.0%*	2.25%*	2.75%*	3.05%*

Past performance may not be indicative of future results. Source of Information: Issues of the Investment Book and The Wall Street Journal. *Bank of Texas rate

*“10 Tips to Minimize Identity Theft”
continued from page 1*

unusable as possible, preventing someone from picking through your trash and stealing personal information.

2. **Keep your Social Security card in a safe place** and only carry it when the card is needed. Do not carry the card around with you in your wallet or purse. If you are robbed or lose your wallet, the thief can easily take advantage of readily available information by using your number.

3. **Give your Social Security number only when absolutely necessary.** If someone asks you for your number, find out if you can provide them with some other form of identification. The less you use your Social Security number, the better.

4. **Do not give out personal information over the phone**, such as bank account numbers or credit card numbers, especially if you did not initiate the contact or if you do not know the person. A perfect example of this danger was in the news recently when a con man called a person and explained that the person had won a gift certificate for \$500 from a well-known company. The con man said the only way to receive the gift certificate was if the person pays a small shipping fee. Of course, the only way to pay for the shipping fee was to give a checking account number or credit card number. If you receive such a call, you should hang up the phone immediately.

5. **Be cautious when responding to promotions.** Identity thieves create fake promotional materials so that you can give them your personal information. This is called “phishing” and is more widely done through e-mail.

6. **Make sure you have adequate protection** on your home computer and laptops, including anti-virus protection software, spy ware protection and a firewall program. Microsoft Windows’ users should ensure they have the latest system and security updates. Adequate computer protection can protect your personal information from hackers and other outside sources.

7. **Do not save personal information like passwords and credit card information on the Internet.** More and more companies want you to save this type of information in their databases for easier use in the future. However, hackers can access this information through temporary files on your computer in the “cookies” and history files in your Web browser.

8. If you are in the military and are on active duty, **put an active duty alert on your credit report.** The active duty alert will remove you from the credit reporting companies’ marketing list of pre-screened credit card offers for up to two years.

9. **Have the credit bureaus notify you** when an application for new credit is made in your name. By having this in place, you will know immediately if

someone tried to steal your identity. Make sure the credit bureaus have your cell phone number so you can respond quickly to such an incident.

10. **Check your credit report at least once a year.** In the past, the only way to see a copy of your credit report was if your credit application was denied or if you purchased from one of the three major consumer reporting companies. Starting in January 2005, the Federal Fair Credit Reporting Act required that each of the major consumer reporting companies provide a free copy of your credit report, at your request, once every 12 months. Due to the size of the U.S. population, the free reports were phased in over a nine-month period, rolling from the states in the West to the states in the East. Texas phased in June 1. However, in September 2005, everyone will have access to the free reports. If you would like more information about the reports and to see when you are eligible to receive them go to www.annualcreditreport.com.

Minimize your chances of becoming a victim of identity theft by taking these preventive actions. If you have any other questions or concerns about identity theft, consider discussing the topic with your financial planner.

Mark Opdahl is a financial analyst with Carter Advisory Services. He is working toward his CFP® designation. Contact him at 214/363-4200 or mopdahl@cascfm.com. ■

CARTER FINANCIAL HIGHLIGHTS

- Bill Carter and Tara Scottino attended the FPA Retreat May 14-17.
- Taylor Steele got married to Merrick and honeymooned in Washington, D.C. Taylor also passed his Series 7 and 66 exams.
- We welcome Sarah Cassida to our team as Bob Berg’s new assistant.
- CFM held another successful Emerging Investors seminar June 7. Justin Cassida, Tara Scottino and Taylor Steele presented to a great group of high school/college age students. Remember to mark your calendars for next year’s event!
- Tom McIntire attended the PIMCO Due Diligence meeting in Newport Beach, April 28-29; the Davis Funds Due Diligence meeting in New York City, April 14-15; the NAIFA-Dallas Annual Conference May 2; the Financial Planning Association (FPA) North Texas Financial Planning Symposium June 3; the RJFS Alternative Investment Group Summit in Las Vegas, June 16-17; and the RJ National Conference in Chicago, July 17-21.
- William and Cally Taylor had a little dominator named Whit May 23 - 8lbs, 2oz and 20 inches of toughness!!
- Bill Carter attended the Coldwell Banker Texas Synergy Meeting in San Antonio on July 22; and the Allianz Global Investors Due Diligence Meeting in Newport Beach, July 27-29. Upcoming meetings include the RJFS Regional Sales Conference in Dallas, Sept. 11-13; the FPA National Meeting, in San Diego, Sept. 15-18; and the Private Enterprise Research Center Meeting in College Station on Sept. 30.
- CFM/CAS held its semi-annual Company Planning Day July 26.

*“2005 Market Overview”
continued from page 1*

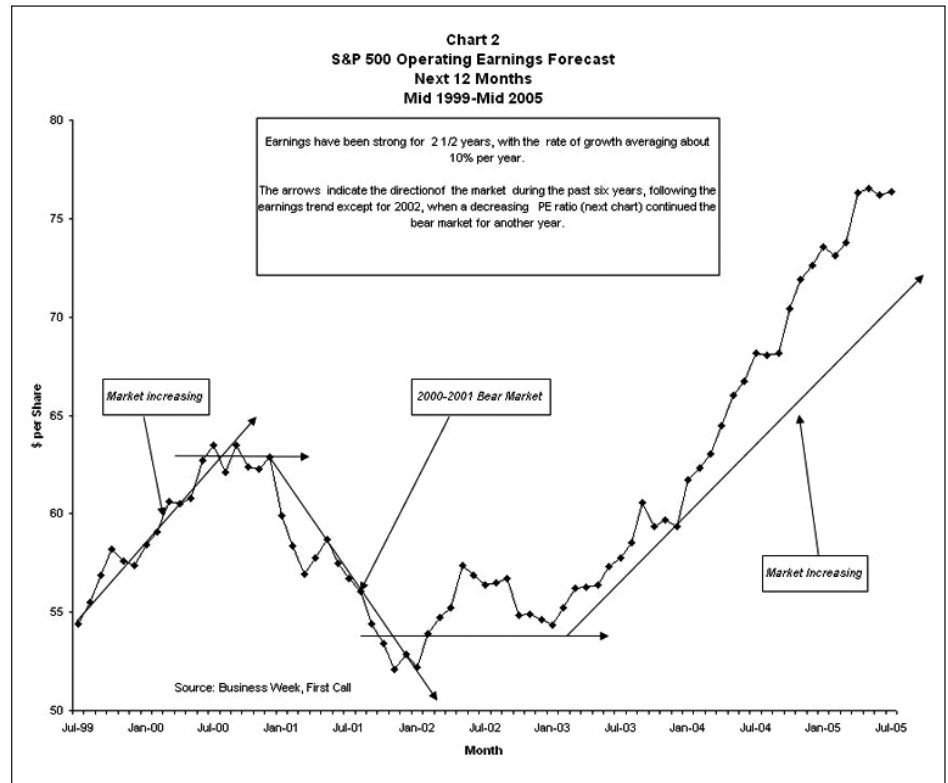
representing a buying opportunity. Since then, the P/E ratio has risen, leveled out, and more recently, declined. Currently the Forward Looking P/E ratio is about 15 1/2.

The domestic stock market had a great year in 2003 because of a combination of increasing earnings (Chart 2) and a rising P/E ratio (Chart 3).

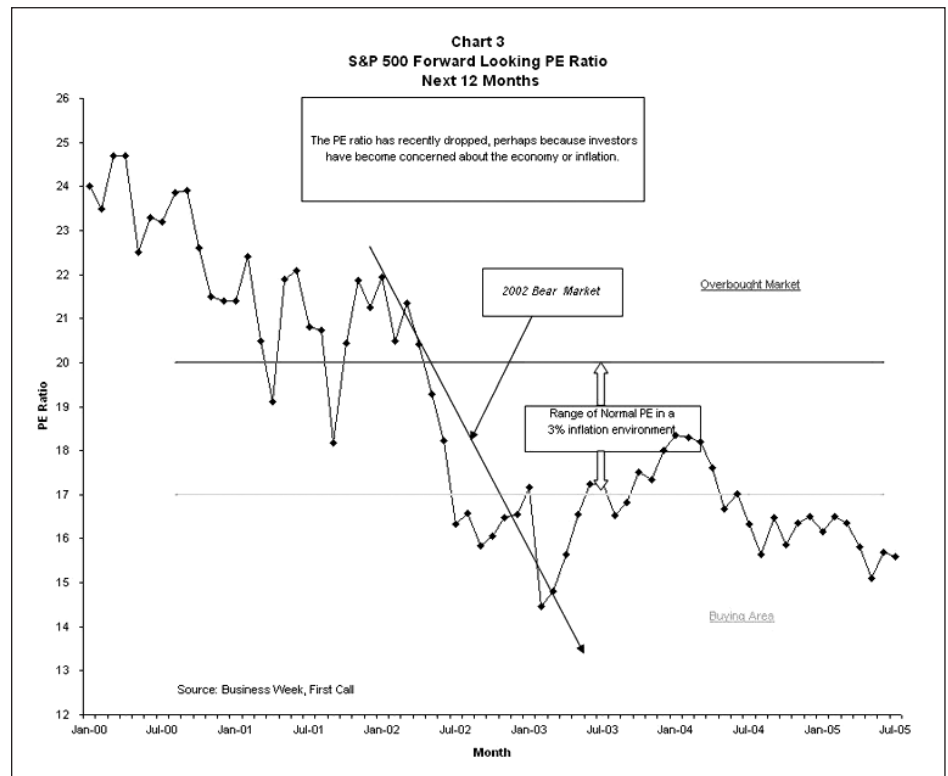
2004, and 2005 year-to-date, have been mixed, with increasing earnings being somewhat offset by a decline in the P/E ratio. Late in 2004, a nice rally was generated as the election was resolved and crude prices started to come down for a short while. This resulted in an overall 9 percent rise in the S&P 500 index for the year. For 2005 year-to-date, the market has essentially been flat.

Based on these data, the market currently appears to be in a buying range, with some stocks overpriced relative to the norm, while others could be attractive. The key is to continue to look for stocks and mutual funds that are reasonably priced relative to the norm and have a good outlook with strong management, **remembering that past performance may not be indicative of future results.**

Joe B. Mattei, CFP®, is vice president of the Houston Office of Carter Financial Management. He is a comprehensive financial planner and a registered representative of Raymond James Financial Services. Joe may be reached at 713-266-3919 or jmattei@rjfs.com. ■



The key is to continue to look for stocks and mutual funds that are reasonably priced relative to the norm and have a good outlook with strong management, remembering that past performance may not be indicative of future results.



CARTER FINANCIAL MANAGEMENT

12222 Merit Drive, Suite 1800
Dallas, Texas 75251

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2005 CALENDAR OF EVENTS

Nov. 19 — CIC XXVI
MARK YOUR CALENDARS NOW!

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RJFS Deadlines

Cutoffs:
Trades/Mutual Funds3:00 CST
No Load Mutual FundsBuys: 1:00 CST
No Load Mutual Funds.....Sells: 2:30 CST
Nuveen Munis10:00 CST
Government Bonds4:00 CST
Wires-From Customer Accts.12:30 CST

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Our mission is to become our client's trusted advisor by providing superior financial planning services that enable our clients to define and achieve their financial and life goals.

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