



MARYLAND CAPITAL ADVISORS INC.
◇ Registered Investment Advisory ◇

2006 Third Quarter Asset Class Report

October 2, 2006

As we began the 3rd Quarter, markets were grappling with fears of further Federal Reserve interest rate increases, higher commodity prices (especially oil), and a jittery stock market (see our June 14, 2006 *Investment Comment*). Three months later, the Fed has held the Funds Rate steady at 5 ¼%, commodities were the worst-performing asset class (crude oil -14.9%), and US Large Cap stocks turned-in a very strong quarter (S&P 500 Index ETF +5.35%). Balanced strategies (ex. Vanguard's 60/40 fund +4.23% Q3, +5.97% YTD) also performed very well. Even the level of "fear" priced into the stock market, as measured by the index called VIX, has fallen from 3-year high levels in mid-June to near all-time lows.

Interestingly, as the stock market is experiencing apparent nirvana and CNBC market reporters hyperventilate daily about the Dow Jones Industrial Average trading near an all-time closing high, the market for longer-term interest rates has declined significantly. Yields on 10-year US Treasury notes peaked at 5.25% in late-June and closed at 4.63% on Friday – indicating relaxed fears of future inflation and an expectation of slower economic activity. *These messages from the stock market and bond market are incongruent – one of them is wrong.* It is, in fact, somewhat unusual for long-term bond returns to move in tandem with stock returns (stock and bond returns are intuitively and historically *negatively* correlated).

Fortunately, investors with asset class-balanced portfolios need not be concerned with speculating which market is "right". Instead, we monitor and maintain targeted portfolio allocations to manage the various risk exposures. This means that we are likely to sell a portion of recent strong performing investments and buy recent underperformers – while constraining our overall equity market allocation to each client's target.

Within equities, US Large Cap Value (+5.96%) was the top-performer in the 3rd Quarter. Along the academically-defined factors (Small vs. Large Companies and Growth- vs. Value-priced), Large and Value were the drivers of Q3 portfolio returns (see bottom-right of data table). In bonds, the best-performing asset class was 20-30yr US Treasury bonds (+7.28%). As described in our 1st Quarter Report, we have only modest allocations to 20-30yr bonds "since longer maturity bonds offered no incremental yield for the additional risk" – and that continues to be the case. *Although the DJIA (+4.99% ETF, +5.35% Index) is the current media focus, the more interesting story is whether the US economy is in trouble (bond market is right) or there are no significant negative events ahead (stock market is right).*

[see attached Asset Class Report]

Maryland Capital Advisors Inc. is an independent, referral-only, investment advisor registered in Maryland. We provide investment management and advisory services to high net-worth individuals, families, foundations, trusts, and other select clients. We work with each client to design, build, implement, and manage a tax-efficient, low-cost investment portfolio designed to match each client's time-horizon, risk tolerance, liquidity needs, and cash flow.

Asset Class Report		Total Return						Risk		Yield	Valuation	
September 29, 2006		YTD	06Q3	06Q2	1YR	3YR	5YR	1YR	3YR	12mo	P/E	P/B
EQUITIES	Large Cap Growth	2.95	3.32	-3.84	6.19	7.69	4.18	7.82	9.04	1.00	21.58	4.01
	Large Cap Core	8.03	5.00	-1.84	10.59	12.28	7.47	6.77	7.83	1.67	17.79	2.81
	Large Cap Value	13.44	5.96	0.54	14.52	16.83	10.63	7.15	8.09	2.13	15.11	2.16
	Mid Cap Growth	3.37	0.75	-5.06	7.56	13.87	11.69	11.50	11.95	0.81	24.77	3.93
	Mid Cap Core	7.12	1.96	-2.72	9.99	17.81	14.63	9.36	10.22	1.42	21.44	2.72
	Mid Cap Value	10.82	3.44	-0.50	12.72	20.79	16.43	7.51	9.63	1.88	18.47	2.00
	Small Cap Growth	4.17	-1.42	-7.68	6.24	11.22	10.17	16.18	16.24	0.35	44.40	3.40
	Small Cap Core	8.67	0.70	-5.44	10.23	14.84	13.73	14.26	14.89	1.06	32.47	2.33
	Small Cap Value	13.16	2.41	-2.87	13.99	18.34	16.64	12.29	13.45	1.60	26.06	1.81
	Large Cap International	14.00	3.61	0.72	18.00	21.50	13.96	11.08	10.83	1.64	16.97	2.39
Emerging Markets	9.65	3.06	-5.15	15.08	29.83		23.91	19.57	1.02	13.29	2.54	
ALTS	Real Estate Investment Trusts	25.54	10.35	-1.59	31.28	28.50	23.20	12.61	16.66	3.05	43.48	3.33
	Commodities	-5.36	-4.81	5.31	-9.91	14.70		15.15	14.82			
	Precious Metals	15.30	-2.87	5.39	26.26			17.78		0.00		
	Hedge Fund Index	3.58	0.45	-0.66	5.08	4.01						
BONDS	Treasuries 1-3yr	2.93	1.90	0.63	3.52	1.84		1.01	1.42	3.89		
	Treasuries 7-10yr	1.88	4.64	-0.50	2.34	2.89		4.12	5.81	4.17		
	Treasuries 20-30yr	0.30	7.28	-1.79	1.32	5.88		8.94	9.51	4.68		
	Treasury IPS (TIPs)	1.76	3.52	0.44	1.57	4.87	7.06	3.76	5.06	6.08		
	Mortgage-Backed (MBS)	2.35	3.19	-0.70	3.67	3.64	4.35	2.73	2.72	4.97		
	Inv Grade Short Duration	3.27	1.93	0.79	4.29	2.88	3.43	1.04	1.56	4.09		
	Inv Grade Intermediate Duration	2.47	3.76	-0.30	3.08	3.56	5.07	3.18	4.08	4.95		
	Inv Grade Long Duration	0.95	6.76	-1.88	1.94	5.58	7.01	7.79	7.87	5.59		
	High Yield Intermediate Duration	4.00	2.91	-0.52	5.78	6.96	7.48	2.41	3.60	7.11		
	Municipals Short Duration	2.27	1.51	0.54	2.84	1.82	2.78	0.96	1.54	3.16		
	Municipals Intermediate Duration	3.00	2.87	-0.01	3.95	3.37	4.00	2.43	3.24	4.15		
	Municipals Long Duration	3.49	3.53	-0.19	4.64	4.35	4.92	3.03	4.17	4.55		
	International	4.19	0.58	3.10	2.30	4.53	8.33	5.65	7.79	3.00		
	Emerging Markets	5.56	5.79	-2.57	9.57	14.10	15.74	7.25	7.03	7.06		
Floating-Rate	3.80	1.39	0.69	4.88	4.63		0.75	0.73	5.19			
Money Market	3.11	0.86	1.17	4.09	2.47	2.08			4.29			
Balanced Portfolio Funds		YTD	06Q3	06Q2	1YR	3YR	5YR	1YR	3YR	Current	P/E	P/B
Vanguard 60/40		5.97	4.23	-1.27	7.64	9.05	7.05	4.62	5.10	2.82	18.42	2.65
DFA 60/40		7.55	2.83	-0.63	9.60			5.42		1.85		
DFA 25/75		4.86	2.06	0.29	5.85			2.35		1.97		
Market Index ETFs		YTD	06Q3	06Q2	1YR	3YR	5YR	1YR	3YR	Current	P/E	P/B
S&P 500		8.67	5.35	-1.41	10.90	11.80	6.92	6.67	7.72	1.63	17.33	2.81
DJIA		10.86	4.99	0.94	13.19	9.82	7.92	6.09	8.50	2.05	22.38	3.21
NASDAQ 100		0.79	4.91	-7.47	4.15	7.58	7.32	13.30	14.95	0.44		
US Domestic Bonds		2.72	4.04	-0.51	3.19	3.22		3.04		4.53		
US Dollar Index		-5.64	1.02	-5.09	-3.77	-7.57		7.74				

Source: Bloomberg L.P.

x.xx sub-asset class with highest period return

x.xx sub-asset class with lowest period return

Note: Asset Class returns are primarily investable benchmarks using selected mutual funds and ETFs, with dividends reinvested. Returns for periods greater than 1 year are compound annual returns. Risk is annualized standard deviation of returns.

Maryland Capital Advisors Inc. obtained the information from sources we believe to be reliable, but we do not guarantee its accuracy or completeness.

Equity Market Factors

	Growth	Core	Value	
Small Cap	-1.42	+0.70	+2.41	Q 3
Mid Cap	+0.75	+1.96	+3.44	
Large Cap	+3.32	+5.00	+5.96	
	Growth	Core	Value	
Small Cap	+10.17	+13.73	+16.64	Y R
Mid Cap	+11.69	+14.63	+16.43	
Large Cap	+4.18	+7.47	+10.63	