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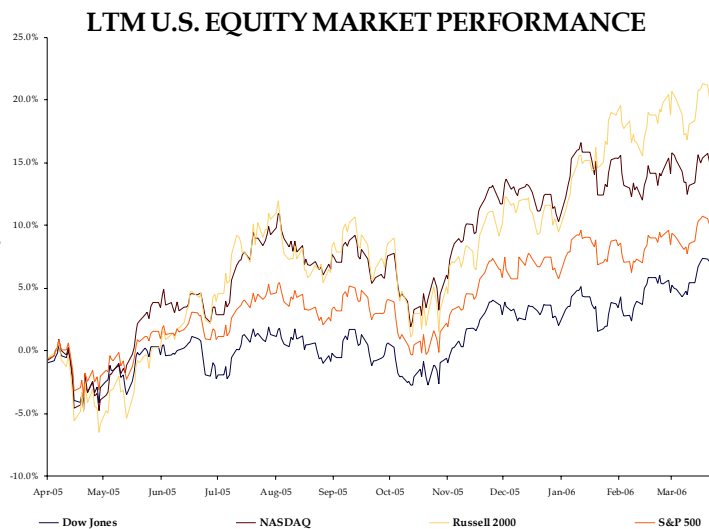
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## ECONOMIC COMMENTARY BY A. MARSHALL ACUFF

For stock investors, happiness is a market that rises persistently, especially in the face of adversity. Based upon this premise, the strength of the market year-to-date should be producing growing enthusiasm for equities. In fact, the market's strength is pulling more cash off the sidelines which in turn is supporting the market's persistent rising trend. It appears that few investors want to miss the boat. Virtually all of Jim Cramer's nightly tips rise in price the next day.

Clearly, the market wants to move higher and that has become increasingly recognized. The positives outweigh the negatives. On the plus side, profits for most companies continue to rise nicely, the individual investor has returned to the stock market, hedge funds have raised the long side of their exposure in recent months, merger activity continues at a high level, liquidity remains abundant, and hope is sustained that the Fed will cease raising rates after its May meeting. The negatives include: valuations are high for many stocks at a time of rising interest rates, the potential exists for both short and long rates to rise further than now anticipated, profit margins are historically high and may be peaking in the months ahead with resulting moderation of earnings growth and the possibility that the return of individual investors to the stock market may lead to a period of unsustainable exuberance.



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A conundrum could be developing for the stock market. Much of the current move in stocks is predicated upon the expected end in the rate hikes by the Fed in May. If the market continues to rise into May, the end of rate increases, if it occurs then, may be fully discounted. Thus, some set-back in the market is possible going into the summer – a normal seasonal occurrence in a typical year. On the other hand, if the Fed continues to raise rates after May, the market is also likely to suffer some relapse from the disappointment that rates are not stabilizing. Between now and the summer, it will be interesting to see how the rate scenario plays out and how the markets react given the rising expectations currently for a cessation of rate increases.

One of the sobering characteristics of public and private investment is that most asset classes do not represent unusually good value. Warren Buffet understands this and backs up his understanding by holding \$40 billion in relatively liquid assets. Because of the unusual setting of relative value among most asset classes, investors are advised to remain diversified and like Mr. Buffet to hold some liquidity for future opportunities. Consequently, unlike most investors, Cary Street Partners is reluctant to chase the momentum driven public equity markets at this time. Mr. Buffet may have more staying power than Mr. Cramer.

## FINANCIAL PLANNING

### PLANNING IDEAS FOR THE PRIVATELY-HELD BUSINESS OWNER

Successful entrepreneurs' approaches to business and management succession can vary greatly. A common theme for these business owners who have worked a lifetime to accumulate substantial wealth in their business is that they want the proceeds to end up in their designated beneficiaries' hands not the IRS'.

An effective tax planning strategy for owners desiring partial or full liquidity for their private business interests is the Grantor Retained Annuity Trust, or GRAT. A GRAT is a trust established by the business owner who can retain a stream of annuity payments. The assets remaining in the trust, after making all of the annuity payments, are distributed to the beneficiaries designated by the business owner. If the trust and the annuity payments are structured in accordance with IRS regulations, the appreciation of the trust's assets can pass to the beneficiaries free of gift and estate tax.

To be most effective, a GRAT needs to be established well in advance of any possible change in control or other liquidity event to permit the full use of other valid tax planning techniques such as discounts for lack of marketability and minority interests. At a minimum, a GRAT should be formed at least six months before beginning work on a possible transaction. A GRAT is irrevocable and trust interests cannot be reassigned once granted so the business owner needs to be very thoughtful about designating beneficiaries. Family members are often the beneficiaries of choice for this type of strategy. If a GRAT is properly executed, the estate and gift tax savings can be substantial,

potentially adding up to millions for the typical middle market business owner.

As always, tax strategies should never be analyzed in a vacuum. Please consult your own tax or financial advisor before implementing, or contact one of Cary Street Partners' wealth advisors to discuss in more detail.

## DEAL MARKETS

### MERGERS AND ACQUISITIONS

The strength of the U.S. M&A markets continued in the first quarter of 2006 with 2,492 transactions announced with an aggregate deal value of \$273.1 billion, compared to 2,536 deals generating \$253.3 billion in aggregate deal value during the same period in 2005. Middle market M&A activity, encompassing deals disclosing a deal value between \$1 million and \$500 million, was also very robust with \$57.5 billion in deal value created from 2,415 announcements.

The market consensus is that the current M&A wave will continue because of the huge pools of capital chasing targets and the stock market's willingness to accept acquisition announcements. In 2005, private equity and venture capital firms raised record amounts of capital which they now must put to work. The first quarter of 2006 saw a continuing of the trend of new fund commitments. Many corporations also have healthy balance sheets due to strong cash flows in recent years and view acquisitions as a way to grow earnings quickly and efficiently.

Middle market deals are likely to remain attractive to buyers as the economy continues to help operating results and

capital providers look across a broad spectrum of companies to put money to work. The wide swath of the middle market capital providers that we regularly speak with continue to aggressively pursue attractive companies in which to invest.

### FINANCING MARKETS

*Venture Capital* - The steady pace of venture capital investing continued in the first quarter of 2006 with \$5.6 billion raised in 761 deals. This quarter marked the 16<sup>th</sup> consecutive quarter that venture capitalists have placed between \$4 and \$6 billion in U.S. based emerging growth companies. Another good sign for entrepreneurs is that for full year 2005 valuations continued to rise. For example, post-money valuations for later stage companies hit a four-year high of over \$92 million which compares favorably to the \$71 million mark set during the twelve months ending Q3 2005. The first quarter of 2006 was the most robust in terms of M&A volume for venture backed companies in over two years, with 95 announced deals (43 with disclosed values) generating over \$4.8 billion and an average deal size of \$112 million. The only real downside in the quarter was the disappointing IPO market for venture backed companies. In Q1 2006 only 10 companies came to market raising an aggregate \$540.8 million with an average offering size of \$54.1 million, the lowest since Q3 2002.

*Debt* - Thanks to some very large M&A deals, 2006 has started like no other year on record for the leveraged loan market. Loan volume for Q1 was \$109 billion, a 36% increase over last year's first quarter and 47% above Q4 of 2005. M&A loan activity represented just over 50% of the first quarter volume, while private equity sponsored loans

represented roughly one-third of the total first quarter loan volume.

Average leverage multiples have begun to flatten after increasing every year since 2001. At the end of Q1, average total debt / EBITDA was 4.2x, down slightly from 4.3x at the end of 2005.

While the available market data is sparse, anecdotal evidence seems to indicate that middle market credit remains widely available. Many normally conservative lenders who usually will only consider loans backed by hard assets for small and mid-sized businesses are being pushed by market forces to offer cash flow based loans at attractive spreads to keep their best customers. Traditional asset based lenders are also having to increase their advance rates to win business.

*Equity* - In the first quarter, 43 companies raised \$9.7 billion, which is less than the \$10.2 billion raised by 41 offerings in the same quarter of 2005. The average size IPO declined from \$245 million in Q1 2005 to \$221 million this quarter. The largest IPO of the quarter came from Dallas, TX based Exco Resources, Inc. which raised \$650 million. The best performing IPO was Chipotle Mexican Grill Inc., a Denver based burrito chain that was spun out of McDonald's Corp., which delivered a 152% increase from its offer price.

### Domestic Equity Markets

<i>(Returns)</i>	Q1 2006	LTM
Dow Jones	3.7%	6.8%
NASDAQ	6.1%	17.9%
S&P 500 <sup>(1)</sup>	3.7%	10.4%
Russell 2000 <sup>(1)</sup>	13.7%	25.1%

(1) Return includes dividends.

### International and Emerging Equity Markets

<i>(Returns)</i>	Q1 2006	LTM
EAFE	8.8%	21.5%
Europe	10.1%	17.5%
Pacific ex Japan	5.7%	16.9%
Japan	11.4%	35.8%
BRIC (Brazil, Russia, India, China)	22.7%	74.0%

### Hedge Funds

<i>(Returns)</i>	Q1 2006	LTM
CSFB Tremont Hedge Fund Index	5.5%	13.6%
MSCI Hedge Fund Composite Index	5.3%	13.3%

Source: Morgan Stanley Capital International and The Wall Street Journal.

### Interest Rates

	3/31/2006	12/30/2005	3/31/2005
Federal Funds	4.75%	4.25%	2.75%
30 Year Treasury	4.89%	4.55%	4.76%
10 Year Treasury	4.85%	4.39%	4.49%
LIBOR - 6 Month	5.14%	4.70%	3.40%

Source: The Wall Street Journal.

### Key Economic Indicators

Unemployment Rate		4.7%
Capacity Utilization		81.3%
	<u><i>S&amp;P Earnings Growth<sup>(2)</sup></i></u>	<u><i>GDP Outlook<sup>(2)</sup></i></u>
Q1 06	11.6%	<b>4.8%</b>
Q2 06	9.6%	3.6%
2004	<b>21.0%</b>	<b>4.2%</b>
2005	<b>13.7%</b>	<b>3.5%</b>
2006	7.6%	3.5%

(2) Statistics represent average of analyst estimates as of the end of Q1 2006 and are derived from various sources. Figures subject to change. Actual figures are in **Bold** and estimates are *italicized*.

### Initial Public Offerings

<i>Totals</i>	Q1 2006	Q4 2005	Q1 2005
Number of Deals	43	49	41
Aggregate Volume (\$MM)	\$9,660	\$7,533	\$10,158
<i>Q4 Notable Deals:</i>	Date	Amt (\$MM) <sup>(1)</sup>	Return <sup>(2)</sup>
Exco Resources	2/9/2006	\$650	(3.6%)
Western Refining	1/19/2006	\$383	27.2%
Chipotle Mexican Grill	1/26/2006	\$174	152.3%
Thomas Weisel Partners	2/2/2006	\$90	46.0%

(1) Excludes underwriter over allotment.

(2) Represents performance from IPO date through March 31, 2006.

### Venture Capital

<i>Totals</i>	Q1 2006	Q4 2005	Q1 2005
Number of Deals	761	781	710
Aggregate Volume (\$MM)	\$5,625	\$5,664	\$5,011
<i>Q4 Notable Deals:</i>	Date	Amt (\$MM)	Industry
ITA Software	1/23/2006	\$100	Info. Tech
Microbia Inc.	2/28/2006	\$75	Pharma.
Optasite Inc.	3/16/2006	\$60	Telecom.

Source: PwC MoneyTree and The VC Deal.

### High Yield New Issuances

<i>Totals</i>	Q1 2006	Q4 2005	Q1 2005
Number of Deals	62	73	100
Aggregate Volume (\$MM)	\$25,948	\$18,736	\$24,710

### Mergers & Acquisitions

<i>Totals</i>	Q1 2006	Q4 2005	Q1 2005
Number of Deals	2,492	2,342	2,536
Aggregate Volume (\$MM)	\$273,100	\$281,900	\$253,300
<i>Q4 Notable Deals:</i>	Ann. Date	Amt (\$MM)	
BellSouth, acquired by AT&T	3/5/2005	\$83,761	
Albertsons, acquired by Investor Group	1/23/2006	\$17,400	
North Fork Banc., acquired by Capital One	3/13/2006	\$14,600	
Pixar, acquired by Walt Disney	1/24/2006	\$7,400	

Source: Mergerstat, The Wall Street Journal, and Capital IQ.