MITCHELL CAPITAL MANAGEMENT

MCM Market Outlook

NOVEMBER 2006

Equity Markets

Here is before fee performance information through the first ten months of this year.

	YTD	12/31/2002-10/31/2006 Annualized RR
Representative Client	2.1%	16.8%
S&P 500	12.1%	14.4%
Russell 3000 Growth	7.0%	12.6%

A review of the numbers leads to the following three observations.

1) MCM's performance significantly lags our benchmark, the Russell 3000 Growth Index, and the broad market so far this year.

2) MCM has significantly out performed both our benchmark and the broad market since the current bull market began almost four years ago.

3) The growth sector of the stock market has underperformed during the entire bull market.

Regarding our results so far this year, our representative portfolio is 30% invested in large capitalization companies. The popular market indices like the Dow and S&P 500 are dominated by large capitalization companies and our benchmark index is over 50% large capitalization companies. This year the large companies have been the market leaders. Our underweighting in that sector is the primary reason for the shortfall so far this year.

While you wouldn't know it from the way the stocks are behaving, the companies in the portfolio are actually doing quite well and their earnings will be up over 20% again this year. Similar increases are forecasted for next year. Earnings performance ultimately determines stock price performance. While we don't like it when stock prices temporarily disconnect from the underlying earnings trends, it does happen from time to time and this is one of those periods. We monitor the business performance of the companies closely and like what we are seeing. We expect continued superior earnings performance will be reflected in share prices. Perhaps we don't have long to wait and more on that in a later paragraph.

As noted in observation #2, despite investing in the lagging sector of the market, MCM's results since the beginning of the bull market have substantially exceeded not only the growth benchmark, but also the broad market as measured by the S&P 500. That period covers almost four years now and confirms our underlying core principal, which superior earnings performance leads to superior stock performance.

Because the growth sector has lagged for so long, it is clearly the most undervalued sector of the market. That observation has been made many times recently in articles written for the various investment and business magazines. The relative attractiveness of growth stocks can be illustrated with the following numbers. The MCM portfolio is now priced at an average of 19 times earnings. The portfolio's earnings growth rate and the price earnings ratio are essentially the same. Contrast that with the S&P 500, which is currently trading at about 15 times earnings and the longer term earnings growth rate is in the 7 to 8% range. The price earnings ratio for that broad market index is almost twice its underlying growth rate. These numbers clearly indicate the growth sector is far and away the most undervalued part of the market, but that has been true for a long time. So the question becomes "What might cause that to change?"

Here is the answer. There is one extremely unusual characteristic about this economic expansion. The growth in corporate profits has been extraordinary. The companies in the S&P 500 have been increasing their earnings at about a 15% annual rate for close to four years now. Typically when a business expansion begins corporate profits accelerate for the first 18 to 24 months and then tapers off to the more sustainable 7% long-term growth rate. In this cycle that has not happened and corporations have enjoyed a record level of profitability. However, that above trend profit growth for the corporate sector is ending. We expect fourth quarter profit growth for the corporate sector will be in the 10% range and then decline to the traditional area of 7%. The reason for that is economic growth is slowing to a sustainable 2 ½ % rate.

Over the last four years your companies have been growing their earnings at a 20% rate. Corporate America generally has stayed pretty close to that with a 15% growth rate. Going forward your companies are expected to grow their earnings at or close to 20% a year, while corporate America will be growing earnings at a single digit rate. That substantial variation in growth rates could be the catalyst to begin drawing attention back to the relatively better opportunities offered investors by growth companies. We don't have long to wait to test this idea. A widening in the gap between earnings growth rates in favor of your companies is going to occur in the current quarter and become even more obvious as 2007 unfolds.

We are confident our disciplined and unrelenting emphasis on rapidly growing financially strong businesses will continue to meet investment objectives of our clients.

Sincerely,

Fred Mitchell, CFA
President