Taylor Investment Services LLC
2006 Q1 Letter

INTRODUCTION

The stock market was higher at the end of Q1, with smaller stocks doing better than larger stocks. On a consolidated basis, TIS performance was better than our large company index benchmark. Please note that consolidated performance represents a blended fee rate and individual accounts, especially those under $100,000, may differ significantly.

LOWER RETURNS ON MY WEBSITE

You've seen consolidated returns referenced in past quarterly reports and can find current numbers on my website www.taylorinv.com under the performance tab. I revised these numbers in March and this section explains why.

In early 2006 a routine cross-check of performance returns revealed a discrepancy. Extensive discussions with Captool concluded that program updates may have caused some differences. Also, TIS has historically presented consolidated performance by including all transactions for all accounts (excluding only family bank and money market accounts). In some cases (especially 2000), return data for clients with less than 30 days of history was annualized. I re-ran the numbers and when there was any doubt between non-annualized returns and annualized returns, I chose the lowest number listed. Finally, to ensure absolute conservatism, I reduced every yearly return by 0.225% (or a 0.9% yearly return) to account for a Q4 fee which was incurred but not yet paid.

Because past TIS quarterly reports were written at the time Captool reported higher returns, previous references to consolidated returns are at times slightly inaccurate. I'm embarrassed this happened but believe the current presentation is extremely conservative. Consider that consolidated returns also include fixed income and money market positions mandated at times by certain client accounts. In most years this dampened returns. Plus, in the final analysis, overall returns remain favorable versus our S&P 500 benchmark.

I do not believe these issues impacted client returns. Some of this was caused by a file merging issue with Captool that I've avoided by temporarily hand-merging client data with multiple accounts. While TIS does not include the impact of the latest incurred but unpaid fee, this fact is noted on the cover page of your report. Finally, the partial period issues are not a problem once a client is with TIS for more than 30 days and I've never presented annualized data on your cover sheet for periods less than one year.

Here are the previous and revised figures:

Annualized Returns to 2005

	PREVIOUS	REVISED
1YR	10.5%	10.2%
3YR	16.5%	15.8%
5YR	16.8%	15.6%
7YR	24.0%	22.6%
9YR	22.2%	21.8%
11YR	21.6%	20.2%

Single Year Returns

	PREVIOUS	REVISED
2005	10.5%	10.2%
2004	11.4%	11.2%
2003	28.5%	26.7%
2002	0.5%	-1.0%
2001	36.8%	34.5%
2000	42.5%	38.3%
1999	45.8%	45.7%
1998	14.7%	13.7%
1997	25.9%	24.4%
1996	13.6%	13.1%
1995	16.5%	14.1%

MAJOR CHANGES

Here is a briefing on the major changes in the portfolio. These are consolidated changes, and some of these trades may not have appeared in your specific account. These are listed roughly in chronological order.

- Eliminated Pet-Med Express (PETS). I eliminated shares in PETS as the valuation escalated. In hindsight, our gain would have been bigger with a more gradual reduction of this position but for all its charms PETS operates a business with few competitive advantages.

- Reduced Federated Investors (FII). While prospects for FII's money market business remained favorable, continued outflows in the company's fixed income and equity products could mute earnings progress.

- Added to Robert Half International (RHI). While the stock is not cheap, there is near term earnings momentum and the company has much to recommend it as a long-term holding, including a strong balance sheet and high free cash flow (the amount of money the company generates that doesn't need to be reinvested back in the business)

- Added to IMS Health (RX). The announcement of a substantial buyback plan provides more assurance that this management team will use its free cash flow in an appropriate manner so I increased the position.

- Added to American Express (AXP). The stock's reasonable valuation suggested a higher position size.

- Liquidated Talbot's (TLB). TLB's appears to be paying top dollar for new acquisition J Jill Group (JILL), a company that often struggles to make money consistently but who always pays management top dollar. Instead of paying $500 million for JILL, TLB could buy the company it knows the best by purchasing its own shares instead. Maybe this wasn't exciting enough, but I don't want to retain a negative impression here for too long – maybe JILL will be a true growth vehicle, in which case TLB could reappear in the portfolio again.

- Eliminated Cheesecake Factory (CAKE). I sold based on concerns that the company's valuation didn't reflect high costs for CAKE's generous option plan.

- Added to Abercrombie and Fitch (ANF). A questionable purchase in hindsight, especially since I've steadily reduced the stock since 2005, but the latest same store sales reports (which measure how well sales for stores open for a year did versus the year before) show few signs of weakness and the stock's reaction to what could be a weather-induced slowdown (but still good) in February seemed overdone.

- Added to Staples (SPLS). Added to SPLS when it fell slightly, as I've been actively looking to make the stock a bigger holding.

- Sold Pepsico (PEP). Stalwart PEP reached the upper range of its historical price to earnings ratio with little change to the story so I sharply reduced the position.

- Added to Dollar Tree (DLTR). DLTR's latest earnings report contained some positive signs: good inventory control, significant cash levels, and a new acquisition that will increase square footage growth to 13% next year. Plus, the company's capital expenditure budget remains muted, leaving excess available for buybacks, though higher gas and utility prices could impair earnings prospects in the short-term.

CONCLUSION

I hope this review has given you a better understanding of my investment philosophy and your portfolio composition. I appreciate the trust you have placed in my firm to manage your assets.

Paul E. Taylor