The Compass™

The Appleton Group, LLC
100 W. Lawrence Street, Third Floor
Appleton, WI 54911

July, 2006

The Appleton Group was founded to fulfill an investor's desire to participate in the U.S. equity markets while simultaneously addressing the need to manage investment risk. Our firm was founded in April of 2002 by Mark C. Scheffler who serves as Senior Portfolio Manager.

The Appleton Group currently serves 60 clients, and manages $51 million of investable assets. We serve individuals, families, corporations, institutions, endowments, trusts and company sponsored retirement plans.

The Appleton Group is an independent Registered Investment Advisor.

"The Compass" is published quarterly, and is produced by The Appleton Group which is solely responsible for its content.

Confessions of an Equity Zealot

Mark C. Scheffler
Senior Portfolio Manager,
Founder

In the wealth management trade, I am bombarded every day with a barrage of information, market data, and analyst opinions, much of which come from individuals whom I have never personally met. Trust me when I say that my filter gets a pretty good daily workout. Knowing the difference between what is truly important and what is trivial is something I struggle with, though. My greatest fear is overlooking something, some critical piece of information that could make all of the difference.

Knowing what is important in my line of work really comes down to two simple (but not easy) needs: The need to produce consistently beneficial returns over time, balanced against the need to accept only as much risk as is absolutely necessary to get those returns. Everything else is less important. In fact, it is clear to me that much of what gets filtered out every day is truly trivial.

The hard part is keeping my filter clean! I mean, there's so much to consider: earnings, momentum, interest rates, geopolitical events, money flow, sentiment, investor psychology, taxes, liquidity factors, currency translations, and so on. Truly, wealth management is a complicated endeavor. Striving for perfection can be truly maddening, and settling for less than perfect is sloth.

I confess that I do struggle with what is important in life (who doesn't). Knowing my craft, understanding my clients and living a good life all need to be in balance, and I expect these qualities to be present at all times. Doing more in any one area requires that I do less in another, throwing the mix out of balance and creating stress. Four years ago I founded The Appleton Group on a set of core beliefs which hold true to this day. I'd be surprised if those of you who know me would find any of these beliefs to be a surprise. But I find it useful to revisit these core beliefs from time to time, and I'd like to take this opportunity to share them with you.

Core Beliefs 101

1. *I believe the fundamental issue of successful investing is getting a high enough return over time so that you can maintain your standard of living*

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The Appleton Group Receives 2006 Rising Star Award

Pictured from left to right: Mark Scheffler, Wendy Hoeft, Peter Mutschler, Cherie Wirth Not Pictured: Karen Anderson

The Appleton Group is the proud recipient of the 2006 Rising Star award. This award was presented by the Fox Cities Chamber of Commerce and Industry at the annual small business award banquet to a company that displays early success and innovation. The award is given to those ventures that have gotten off to a strong start and exhibit the potential for continued growth in the future.

"Being recognized by the Fox Cities Chamber of Commerce and Industry is humbling, but we are just getting started," said Mark Scheffler, senior portfolio manager and founder of The Appleton Group.

We appreciate the support of all of our clients and business associates. This award would not have been possible without you.

-BPH

Inside this issue:

Retirement Plan Corner - FAQ's

Wendy Hoeft
Director - Retirement Plan Relations

The following in an excerpt from an interview Cherie Wirth conducted with Wendy Hoeft, Director - Retirement Plan Relations. If you have any specific questions that you would like to see addressed in this column, please feel free to contact Wendy at 920.993.7727 or whoeft@appletongrouponline.com.

Q: What has been the impact of interest rates on DB pension plans?
A: Persistently low long-term interest rates combined with recent reform initiatives have led many pension plan sponsors to review liability-oriented strategies. Plan sponsors may increasingly look for ways to minimize the volatility of their funding gap.

Q: Can you explain in what ways this might be accomplished?
A: There are a number of alternative approaches plan sponsors may take in an effort to better match the characteristics of plan assets and liabilities being discussed in the industry such as through interest rate swaps or shifts in asset allocation. An important point with regard to this exhibit is that there is no "one size fits all" answer. The appropriate actions taken by a particular plan will depend on a variety of factors, such as the current funded status of the plan and the duration of the pension liability.

Q: Aren't pension plans well suited to invest in equities and other long-dated assets?
A: Ah, therein lays the rub facing plan sponsors: minimizing the volatility of the funding gap while at the same time achieving high portfolio returns. No matter what the regulatory or accounting rules are, plan sponsors will always have an incentive to maintain exposure to assets with high expected returns.

Q: Then what strategies should plan sponsors consider to better match assets and liabilities?
A: A dramatic shift in asset allocation may not be the suitable answer for most plan sponsors. Beyond the transaction costs and other disruptions, a large shift to fixed income implies lower plan returns over time and therefore higher costs and contributions for the plan sponsor.

Q: How can the plan sponsor effectively add to or subtract from their portfolio duration without decreasing or eliminating exposure to asset classes with high expected returns?
A: A potential alternative often proposed over the last year has been the use of an interest rate swap to hedge the liability from interest rate movements. Although such a strategy provides no disruption to the plan's current asset allocation, when rates rise 100 basis points then the swap value would be a liability.

Q: Would plan sponsors rather be subjected to funding gap volatility due to fluctuations in the long-term interest rate environment, or would they rather hedge that risk and effectively forgo any potential improvement to the funding gap from rising long-term interest rates?
A: With many of the potential pension reform initiatives having negative consequences resulting from funding gap volatility, many plans will likely consider the hedging approach. Such an approach allows them to focus solely on the performance of the assets in the plan.

Nonetheless, there may be situations where a shift from volatile assets like equities to less volatile assets may be appropriate.

Q: What impact would focusing on absolute, as opposed to relative returns, have on a plan?
A: Such a strategy would minimize volatility due to changes in interest rates and equity market volatility like last month's topsy-turvy ride; while at the same time aiming for a consistent and stable positive return on plan assets. The use of tactical management can provide plan sponsors with reduced risk, yet still allow for participation in favorable markets. Some plans have shown an increased willingness to explore alternative asset classes.

Q: Considering that May was a month in which most of the major financial indexes were jarred, what implications does this unprecedented correlation of asset classes have for plan sponsors?
A: As I mentioned in last quarter's newsletter, sponsors are concerned about fiduciary issues, protecting themselves and offering a meaningful, competitive and cost effective benefit to participants. In May, the Standard & Poor's 500 Stock Index declined 2.88%, the NASDAQ Composite Index fell 6.19%, the Dow Jones Europe STOXX Index dropped 4.25% and the Lehman Brothers Aggregate Bond Index declined 0.11%. The Dow Jones Equity All REIT Index was down 2.64% and even the Dow Jones AIG-Commodity Index was only up 0.96%.

This means that traditional asset allocation models based on Modern Portfolio Theory and its Efficient Frontier may not be as completely "prudent" as we've always believed, if the underlying correlation assumptions no longer apply.

Q: Huh? I think you lost me when you lapsed into "Wall Streetese"…
A: Okay, let me give you the Reader's Digest Condensed Version in English. If, for whatever reason, asset classes which have typically moved in opposite directions (e.g. stocks and bonds) begin to move in lock step with each other, are we really achieving true diversification? Many plan sponsors tell me that they "diversify" the plan assets among multiple investment managers and some even employ additional consultants to oversee the due diligence process. But the unfortunate result is that many times the various managers have positioned those dollars in the same assets (if not the exact same funds, many of the same underlying securities). And due to a strict Investment Policy, they all use identical allocation strategies. Our role is to guide the plan sponsor through a process of properly managing their fiduciary responsibility through thoughtful investment policy development, allocation & diversification advice, comprehensive investment analysis, due diligence and fee analysis. -CW

Confessions of an Equity Zealot (continued from page 1)

without running out of money during retirement.

For many investors who've had the luxury of being able to save for retirement, quality of life hasn't been an issue. As Americans, many of us live comfortable, safe, secure lives. Maintaining this lifestyle over many decades is truly a luxury, one that no other generation in our nation's history has been able to accomplish. Think of it: we have at our disposal practically everything we want and certainly everything we need to live, but losing this station in life is downright frightening.

2. *I believe the stress of running out of money during one's lifetime is the mother of all financial stresses.*

Most investors are in a race against time. For many retirees, income will need to be generated for upwards of thirty years, over which time consumer prices could triple. Worse yet, many retirees face high levels of inflation due to rising healthcare costs, higher property taxes, and higher energy costs. So the real risk in investing is the risk of losing purchasing power while you're still alive.

3. *I believe the only long-term safety, therefore, lies in the sustainability of purchasing power.*

If risk is the consistent loss of purchasing power, security can only be defined as the building up of purchasing power. I define the growth of purchasing power as a positive return on investments, net of inflation and taxes. Selecting securities that give an investor the highest net return over time are therefore the safest in the long run.

4. *I believe the best way to sustain purchasing power lies in a lifetime of exposure to equities, either through public markets or through a privately held business.*

Owning a company, either through a privately held business or through publicly traded stock ownership (including mutual funds) have historically generated the highest net returns compared to many other forms of securities ownership. However, because equity investing involves risk, the ability to actually experience a high enough return to sustain purchasing power requires the investor to both recognize and manage investment risk so as to not get scared out of them.

5. *I believe the key in being able to maintain equity ownership throughout one's lifetime is to manage investment risk in a way that will minimize the worst possible outcome in equity investing: bear markets occurring at the worst possible time.*

Recognizing and being prepared for uncooperative markets ahead of time is smart. There is an old saying: "A bear market returns a stock to its intended owner." Over the course of time, investors who are exposed to significant risks often are most likely to cash in at exactly the worst time, near the bottom of the market downturn. Being proactive in managing investment risk means that the likelihood of getting to that point of unbearable stress is minimized. It also has the potential to place the investor in a position to benefit from normal and significant market downturns.

6. *I believe that being prepared for both good and bad markets is smart, and that preparing for only one of these is not.*

The ultimate benefit of managing investment risk is the potential for higher returns over time. For many investors, full participation in market downturns means having to dig out of a big hole just to get back to breakeven. Not enjoyable in anyone's book! Working to keep investment losses to single digits is significantly useful as it enables you to buy stocks (and mutual funds) at significant discounts during normal market downturns. This can be powerful, and can lead to building purchasing power over an entire lifetime.

7. *I believe the worst mistake any investor can make is to succumb to fear during market downturns or to succumb to greed during market upturns.*

Call it the narrow path if you will, but the twin problems of fear and greed cannot be understated. Both lead to emotional decision making, both lead to unplanned changes in course, and both have

the potential to result in lower returns than necessary to sustain purchasing power. Too much participation in market downturns leads to fear, too little participation in market advances inevitably can lead to greed. Recognizing these emotions in yourself (and in myself, truth be told) can be truly liberating!

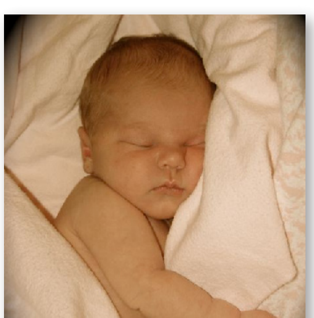
Getting to Work

As core beliefs, these seven principles of investing are put into practice every day both in our wealth management discipline and in our financial planning process. Not much has changed over the past four years, except for a more flexible approach to implementing them. Over the course of our firm's history, we've introduced more portfolio options to help make the ride as smooth and stress-free as possible. From The Appleton Group Portfolios, The Appleton Group Composite Portfolios, The Appleton Group 401(k) to our own mutual fund family, we have a host of low-cost investment solutions that work to help build and sustain purchasing power over an entire lifetime.

-MCS

New Additions

The Appleton Group would like to welcome two new additions this summer. Bryan and Cherie Wirth had a healthy baby girl named Sierra Rae Wirth. She was born on Friday June 23 at 7:00 A.M. Cherie is on maternity leave and will return to work in mid-August.



Brent Heiges has also joined the firm for the summer as our Operations Specialist intern. He will be filling in for Cherie Wirth while she is out on maternity leave. Brent is a senior Business Administration with a Finance emphasis and German major at the University of Wisconsin in Green Bay.

Data as of June 30, 2006

The Appleton Group Portfolios	Morningstar Category	Q2 - 2006 Total Return	3 Year Total Return (Annualized)	5 Year Total Return (Annualized)
Appleton Group Portfolio	Large Cap Blend	-2.79%	+9.58%	+8.03%
Appleton Group Plus Portfolio	Large Cap Blend	-5.74%	+5.76%	+8.82%
Appleton Group - Balanced Income Portfolio	Moderate Allocation	-4.55%	+5.13%	+6.63%
Appleton Group - Tax Managed Growth Portfolio	Large Cap Blend	-4.74%	+7.98%	+8.63%
	S&P 500 Index	*-1.44%*	*+9.24%*	*+0.74%*

The Appleton Group Composites: Historic Performance Summary**

Data as of June 30, 2006

The Appleton Group Composites	Investment Objective	Q2 - 2006 Total Return	3 Year Total Return (Annualized)	5 Year Total Return (Annualized)
Appleton Group Conservative Composite	Conservative Growth	-4.38%	+7.41%	+6.86%
Appleton Group Moderate Composite	Moderate Growth	-4.31%	+8.91%	+7.89%
Appleton Group Assertive Composite	Aggressive Growth	-5.10%	+10.26%	+8.45%
	S&P 500 Index	*-1.44%*	*+9.24%*	*+0.74%*

Performance quoted represents past performance and is no guarantee of future results.

*The Appleton Group Portfolio performance information provided indicates what effect the portfolio adjustments generated by the Appleton Group Wealth Management Discipline, strictly implemented, have had on a model portfolio as such portfolio adjustments were implemented. Although the portfolio adjustments are actual recommendations which have been generated by the Appleton Group Portfolio Management Discipline since December 31, 1999, the performance results are for a model portfolio and do not represent the actual performance of accounts managed using the Appleton Group Portfolio Management Discipline.

**The Appleton Group Composite performance information reflects weighted historic performance, uses the benefit of hindsight, and does not represent the actual performance of accounts managed by The Appleton Group LLC.

Performance statistics have been calculated net of management fees, net of applicable expenses and net of brokerage costs using the internal iterative rate of return (dollar weighted) calculation method. While performance is compared to the benchmark indicated, client accounts may be fully invested, partially invested in cash equivalents, or invested in inverse ("bear market") funds, depending on the portfolio selected. The actual amount of time invested in the market will vary with economic conditions. Unlike an actual performance record, these performance results do not reflect the impact a client's economic circumstances might have had on the investment adviser's decision making if the investment adviser were managing a client's money. Investors should not consider the performance data a substitute for the performance of actual client accounts, nor should investors consider this data as an indication of future performance. A complete history of our performance analysis is available upon request.

The principal value and return of exchange traded mutual funds and other mutual funds will fluctuate with changing market conditions, and may be worth more or less than your initial investment. All dividend, interest, and capital gain distributions assume reinvestment into the targeted investment. Performance statistics do not consider potential tax liabilities as a result of management activity. Please consult your tax advisor for further information. The Appleton Group, LLC became the investment advisor for The Appleton Group Portfolios on April 5, 2002, with Mark C. Scheffler serving as the sole portfolio manager. Prior to that date, Mr. Scheffler managed The Appleton Group Portfolios on a non-discretionary basis while employed as a broker with Robert W. Baird & Company, Inc.

Deviation from the models will produce substantially different results.

September 2006 Advisor Lunch and Learn

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September 19-21, 11:00 AM - 1:00 PM

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