The Outlook

A.R.Schmeidler & Co., Inc.

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As of September 30, 2005		
Index	**YTD % Change**	**Market Value**
Dow Jones Industrials	-2.0%	10,568.70
S&P 500	+1.4%	1,228.81
Nasdaq Composite	-1.1%	2,151.69

The financial markets are responding to rising energy prices and hurricane damage in the Gulf of Mexico. **From a sector perspective, we continue to invest in energy, defense, transportation, metals, basic materials, heavy equipment and insurance companies shares**. The hurricane season has shut in as much as 20% of U.S. petroleum refining capacity and a much larger percentage of natural gas production. This comes at a time when the global market for refined petroleum products has never been tighter. On a national level we expect consumers' disposable income to be seriously impacted by higher electric, heating and fuel prices. Along the Gulf Coast the shipping, manufacturing, agriculture, housing and tourism industries will suffer dislocations which will have negative implications for the U.S. economy and the federal budget deficit.

Inflation and Rising Interest Rates

The Central Bank raised interest rates for the eleventh consecutive time this month. The Federal Reserve is more concerned about the potential for rising inflation caused by high-energy prices and the severe hurricane damage in the Gulf of Mexico than from the fallout of a slowing U.S. economy. The decision to raise the federal funds interest-rate target to 3.75% from 3.50% indicates that Chairman Alan Greenspan appears willing to accept the political risk of economic slowing by raising interest rates, rather than run the risk of letting inflation get out of control by not taking action. In response to the Federal Reserve move, commercial banks raised their prime-lending rate to 6.75% from 6.50%. **The Federal Reserve's work may not be complete and we could see further interest rate hikes in 2006**. Moreover the central bank can't be comfortable with a fiscal deficit that is rising dramatically. **Accordingly we expect the fixed-income markets to weaken from current levels**.

Oil and Natural Gas Prices Surge

Oil and natural gas prices surged this month because of hurricanes in the Gulf of Mexico and because OPEC ministers meeting in Vienna admitted they have no real means to increase oil production to meet growing global demand. The U.S. economy is dependent on the Gulf of Mexico region's oil and natural gas production. The region is not only home to about a quarter of the nation's oil and natural gas production but also to a large number of refineries and pipelines. The hurricane damage to the Gulf comes on the heels of rising global demand for oil and natural gas from China and India. The price of U.S. benchmark crude oil is now settling at about $65 a barrel.

The World's Thirst For Oil

The world's spare oil capacity has been drawn down to about one million barrels a day from three million barrels a day in recent years. As a consequence, oil prices remain high as demand continues to swell along with the ever-present threat of supply shortages. The demand for oil from China and India has clearly raised the price of petroleum resources. Expectations that Russia would provide additional supplies of oil have not been realized. The imprisonment of former oil executive Mikhail Khodorkovsky and the dismantling of his company Yukos have made Russia an unappealing place for the industry to do business. OPEC's key player, Saudia Arabia, has committed to increasing production, but in reality has little spare capacity to produce. **The U.S. petroleum industry is attempting to produce oil from places in the U.S. that have been traditionally difficult and uneconomic to develop. However, not enough drilling is likely to take place in the U.S. to make a significant difference in supply owing to the environmental restrictions currently in place and strong political opposition in the U.S. Congress to change our energy policy.** New techniques and advanced technologies are opening up development of supplies in Africa, Asia, Canada and South America. Unfortunately, it will be several years before the new fields will actually start producing significant volumes. In the meantime the world's thirst for oil continues to increase while many of the large fields are mature and in decline.

Natural Gas

As we move into autumn, concerns are concentrated on the hurricane damage to the production facilities in the Gulf of Mexico. The natural gas exploration and production companies in the Gulf are now facing significant repairs on their facilities, and production is not likely to be fully restored for many months. **Despite a modest increase in inventory levels, natural gas futures peaked above $13.00 per thousand cubic feet (mcf) this month following the hurricane damage and the upward trend of crude oil prices. A decade ago**

natural gas futures were trading for less than $2.00 per mcf. For the remainder of the current year we believe natural gas prices on average will likely continue to trade in the double digit per mcf range. The companies that we favor in the natural gas industry are performing extraordinarily well. Higher profits and raised earnings forecasts should likely continue to support equity valuations. The industry is reaping the benefits of the high commodity prices and rapidly accelerating earnings and cash flows. We expect further positive earnings surprises from the companies that we favor. They are in a position to raise their dividends, buyback shares, pay down debt and hedge a portion of future production in order to lock in high natural gas prices.

Coal

The coal mining industry is currently enjoying a secular upturn, which has caused the average spot price per ton for coal to increase considerably over the last several years. From 1990 to 2004 coal consumption in the U.S. increased by 22% from 904 million tons to 1,104 million tons. The main driver of increased coal consumption has been demand from the U.S. electric power producers. Coal's primary advantage to electric power producers is its relatively low cost compared to the other fuels that can be used for generating electricity. The average total production costs (per megawatt hour) of electricity, using coal verses competing generation fuel alternatives, in the first quarter of 2004 was as follows: Coal $19.41, Natural Gas $59.14, and Oil $57.18. We believe that domestic coal use will continue to rise in the future as the demand for electricity and the cost of competing fuels increases.

Petroleum Refineries and Interstate Pipelines

As we previously indicated Katrina and Rita damaged and shut in a significant amount of U.S. petroleum refining capacity at a time when the global market for refined products was already tight. It now appears that some of the damage is extensive and the recovery will be slow. The loss of electric power in the region also shut down major interstate pipelines that deliver petroleum products to Midwest and East Coast refineries. As a result, many of the U.S. refineries must now operate at reduced levels. This has created shortages of gasoline, heating oil and various other refined products in states outside of the Gulf Region. Unfortunately many global refiners lack the ability to process the abundant supply of heavy, high sulfur crude that is more readily available. It will be some time before refiners are able to upgrade facilities to process the entire supply of heavy, high sulfur crude currently accessible to the market. Finally, the implementation of ultra-low sulfur fuel standards in the U.S. starting in 2006 is likely to further exacerbate refined petroleum product shortages. The U.S. relies on importing rising amounts of refined petroleum product, but many of the foreign refineries are not properly configured to efficiently meet the U.S. ultra-low sulfur fuel standards that are approaching. **In almost any other industry, strong business demand would prompt the building of new capacity. However, that is not the case in the U.S oil refining business. The red tape associated with the permitting process to build a new refinery in the U.S. time and again has represented an overwhelming challenge to the construction of new refining capacity. In the mean time, global economic growth is likely to continue to sustain strong demand for refined petroleum products.**

Cement and Aggregates

An upsurge in economic activity in the U.S. and Asia has made the global demand for cement very strong. The availability of cement in most regions of the U.S. remains limited, and imports are restricted by high fuel costs and limited rail and vessel availability. Shortages existed in Texas and Florida before the recent hurricanes. **The price of cement has been rising steadily since the economic recovery in the U.S. took hold. Cement manufacturers increased prices at the beginning of this year, and we look for significant price increases over the next several months.** The recently passed $286 billion Highway Transportation Act will accelerate the demand for cement and aggregates. A large portion of the cement and aggregates that the industry produces is directly tied to public highway spending.

Heavy Machinery

Heavy machinery demand is noteworthy in the transportation, industrial, energy, power generation, mining, and construction industries. The companies that comprise this industry are recording record sales. **Worldwide infrastructure improvement needs are enormous, and the industry is positioned to capitalize on the increases in government and business spending for the foreseeable future.** Moreover China and India are solid growth drivers for the industry. The improved sales volumes have enabled the industry to offset high steel, energy, and labor expenses with price hikes, and managements have made significant productivity improvements that supported margins through cost-containment. Earnings and cash flows continue to improve throughout the industry. The cash is being used to reward shareholders with stock buybacks and dividend increases. However, the industry's first priority for cash has been to finance expansion in order to meet demand.

Copper

Copper mining companies continue to generate strong results. This largely reflects high prices for copper made possible by solid world demand. Copper prices are being supported especially by strong demand from China. However, strong economic conditions in the U.S. have also supported demand. This positive backdrop has accelerated profits and cash flows in the industry. It has provided the opportunity for the industry to bring down debt, buy back stock, and increase dividends. **The copper industry is a major beneficiary of future demand due to further global industrialization.** Improvements in technology and operating efficiencies are also benefiting the industry's profit margins.

Steel

For many years when steel companies were awash in red ink, there was a question about the group's ability to fashion a durable recovery under even the best of conditions. The doubts of even the most vocal skeptics have now been put to rest. The industry has prospered and is likely to continue to prosper if our projection of global demand is near its mark. The Federal Reserve interest-rate hikes seem likely to limit some U.S. economic growth, but the recently passed energy and highway bills should absorb any weakness in overall product demand. The hurricane damage in the Gulf of Mexico should also increase demand for steel. The increased sales volumes and operating efficiencies should produce continuing profit improvement. **We do not expect the solid pace of global demand for steel products to subside near-term, and the improved cash flows and balance sheets should benefit shareholders.**

Railroads

We expect the demand for railroad services, the lowest-cost means of land transportation, to remain strong and generate substantial earnings for the industry. **The earnings improvement is driven by the absence of excess capacity, volume growth across a variety of railroad business segments and price increases.** The two most profitable segments of the railroad industry are traffic generated by imported goods entering the U.S. through West Coast area seaports and coal transportation to electric power utilities. Imported goods are entering the U.S. in increasing quantities through West Coast area seaports. They are then loaded on railcars and shipped across the country to central distribution points; goods are sent from the central distribution points by trucks to their final destination. Coal transportation utilizing the rails has also remained robust, as both the Powder River Basin (Wyoming) and the Illinois Basin are fully exploited to support the increasing amount of coal-fired electric power generation. Coal shipments are the railroads most profitable cargo. Moreover the railroads have recently announced important projects to modernize and improve service. The industry is funding these projects from strong profits and improved cash flows. Demand for rail services is growing and should remain strong for the foreseeable future.

Property/Casualty Insurance

In the late 1990's the insurance industry fell on difficult times. Intense competition severely held back the ability of the industry to underwrite profitable business. Not only was pricing power weak in the industry, but also companies pursued marketing strategies in an attempt to increase market share that attracted marginally profitable policies. The marginally profitable policies later turned unprofitable and generated substantial losses for the industry. The industry has since consolidated and the weaker players are now gone. **The insurers are using more stringent underwriting standards, and pricing has shifted in their favor.** Companies are unwilling to renew policies that are considered too risky or potentially unprofitable. The high-quality book of business in the industry today is evidenced by their improved loss ratios and bottom line profits over the past several quarters. The hurricane losses on the Gulf Coast are manageable and should not have a material financial impact on the companies that we favor. Any weakness in the share prices of the companies we favor will represent a buying opportunity.

The Defense Industry

We believe the U.S. defense procurement and research and development budgets will see additional funding in 2006. In our view, the equities we favor are attractively valued given their strong positions in a number of critically important defense programs. Procurement programs such as the modernization of armored fighting vehicles, infrared sighting and night vision and container and cargo security are just a few of the programs considered to be of vital importance to the departments of Defense and Homeland Security. In addition, their business in the operations and maintenance (O&M) portion of the defense budget continues to grow. The fiscal 2006 O&M budget is expected to represent over $145 billion in defense spending.

Gold

Monetary policy in the U.S. has become less accommodative in recent months as the U.S. Federal Reserve Bank raised interest rates in order to slow the U.S. economy and prevent inflation. Although these actions generally would weaken the demand for gold, the U.S.'s large and growing fiscal deficit and trade imbalance of goods and services are providing support for gold prices. The supply and demand for gold continues to provide price support. **Total gold production in 2004 declined 5%, the largest drop in decades. Demand that same year increased approximately 7%, with China, India and the Middle East being the principal drivers.** A recent development in the demand for gold is now coming from trading in exchange-traded gold funds. Exchange-traded gold funds have gained a considerable amount of investor interest.

Conclusion

Katrina and Rita damaged important assets in the U.S. petroleum and natural gas production and delivery chain. The storms have damaged offshore production platforms, pipelines, natural gas processing facilities, and oil refinery operations. The Gulf Coast is also home to major shipping ports and thus a gateway into the U.S. economy. The hurricane damage to the Gulf Coast ports has snarled the flow of bulk cargos like grain, steel, copper, cement, forest products and chemicals. We believe the impact of the hurricane shock in the Gulf will be significant to the national economy, even if its impact is temporary. Recovery will probably take several weeks to commence and months to complete.

On a long-term basis according to the American Society of Civil Engineers' report card for 2005 on America's infrastructure, aviation, bridges, dams, drinking water, energy, hazardous waste, navigable waterways, parks and recreation, roads, schools, solid waste, transit, all received quality ratings of C's and D's. Since there has been little improvement since 2001 we expect the approximately $950 billion earmarked to be spent over the next five years to be insufficient. The required investment should be more like $1.6 trillion. **Many of the companies that we favor have recently increased sharply in market value, but still remain worthwhile investments in our view. The market sectors in which we are most interested should be major beneficiaries of U.S. and global infrastructure needs.**