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Welcome to the Fall edition of Market Thoughts. The year is quickly coming to a close and investors are wondering what the future will bring. Nick's comments this quarter focus on the shift in investor expectations over the quarter and provides us with some insight into his thoughts about future markets.

In this issue of Market Thoughts, we are pleased to feature an article written by our Small Cap Growth investment team. Please see the middle pages of this publication for their discussion of growth versus value investment styles and why they think growth is poised to outperform value.

It has been a busy quarter for the small cap team. Earlier this month, Touchstone Investments (also a member of Western & Southern Financial Group®) launched the Touchstone Diversified Small Cap Growth Fund, a mutual fund sub-advised by our team. We are very excited to be able to make this fund available to our institutional and wealth management clients. For more information, please refer to www.touchstoneinvestments.com.

We've updated our 2004 paper titled "Investing in Private Equity Through a Fund of Funds; Important Considerations in Portfolio Allocation to Private Equity". Please visit our website to read more about our thoughts on investing in the private equity asset class. It can be found on the home page at www.fortwashington.com. All research papers written by our professionals can be found on the website in the Media Center under Research and Commentary.

Fort Washington continues to add investment professionals and staff throughout the various departments in the company. This quarter, we welcomed five new employees. All the media and hiring activity around Fort Washington for the quarter can be found on the back of the publication. As always, please let us know how we are doing!

Topsy-Turvy Markets

Following a surge in oil prices and bond yields in the first half of this year, markets made an abrupt about face in the third quarter: Oil prices fell by about \$15 per barrel while bond yields declined by 70-basis points to a six-month low of 4.55%. Bond investors, who previously thought the Federal Reserve was poised to tighten monetary policy further, now expect the next move to be an easing: Euro-dollar forward rates are pricing in a 50-basis point decline in the federal funds rate to 4.75% by mid-2007.

What has happened to alter investor expectations so radically, and are these expectations likely to be realized?

To a large extent, the shift in investor sentiment reflects a slowing of the U.S. economy and a decline in inflation concerns. Real GDP growth moderated to 2.6% in the second quarter from 5.6% in the first quarter, and economists are now lowering their estimates for the third quarter to 2.0%-2.5%. This mirrors a downturn in residential housing, which is expected to detract a full percentage point or more from overall growth. The manufacturing sector has also begun to soften, spawned by weakness in the auto industry. Consumption has held up so far; however, some observers believe it will succumb eventually, as it becomes more difficult for households to extract equity from their homes.

Could these developments portend a recession in 2007? Econometric models based on the shape of the yield curve, which is now mildly inverted, assess the risks to be in the vicinity of 20%-30%. Thus, investors should not rule out the possibility entirely. At the same time, several recent developments will also help to revitalize the economy. The recent decline in oil prices, if sustained, will reduce headline inflation significantly and will also add roughly \$100 billion annualized to consumer spending power. In addition, the rally in stock and bond markets will boost household net worth, providing added support. Therefore, the economy could easily rebound next year from the current slowdown.

Finally, it is also important to realize that signals coming from the bond market are not uniform. Conditions in credit markets hardly point to fears of recession: Credit availability to households and businesses is ample, and credit spreads are near all-time lows. In this respect, the current environment is different from previous periods of yield-curve inversions.

In sum, economic developments and market signals paint a mixed picture about the economy's prospects. The most likely outcome is a "soft landing" that will keep the Federal Reserve on hold for a prolonged period. If so, we would expect bond yields to retrace some of their recent decline, as investors realize the Fed is not likely to ease policy anytime soon. At the same time, the lessening of inflation risks makes it more likely that interest rates have peaked.

Nicholas P. Sargen
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A Discussion on Growth versus Value or Why Growth is About to Turn the Corner

Investors in the growth style box have had a tough time ever since the Tech wreck of 2000. Growth has underperformed value in large, medium- and small-capitalization stocks for at least the last six years. As you can see from the table below (Figure 1), it does not matter which index you use, Russell or Standard & Poors, or what capitalization range you focus on, value has trounced growth. What is a growth investor to do? After a number of years in waiting, growth may be poised to outperform value.

Figure 1

Annualized Index Returns Ending 08/31/06

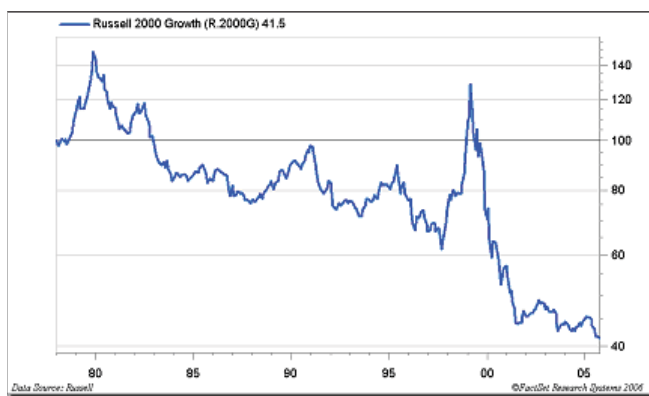
	1 Yr	3 Yr	5 Yr
Russell 1000 Growth Index	3.7%	7.0%	1.7%
Russell 1000 Value Index	14.0%	16.1%	8.7%
Russell 2000 Growth Index	6.0%	10.6%	16.2%
Russell 2000 Value Index	12.7%	18.2%	19.6%
S&P 500 Growth Index	4.2%	6.6%	8.2%
S&P 500 Value Index	13.8%	15.6%	14.4%
S&P 600 Growth Index	3.4%	14.8%	17.2%
S&P 600 Value Index	10.8%	17.0%	18.0%

Source: Zephyr StyleAdvisor

Market trends that fluctuate between growth and value cycles are not a new investment phenomenon. We know from past experience that growth cycles are typically shorter and more intense than value cycles. We also know that these style runs can be as short as twelve months or can last eight years or longer. As demonstrated in Figure 2 & 3, the current value run is getting a little long in the tooth in whatever cap range you compare. The current cycle favoring value is running over six years, making it one of the longest in recent memory.

Figure 2

Russell 2000 Growth Relative Strength vs. Russell 2000 Value



Source: FactSet

Figure 3

Russell 1000 Growth Relative Strength vs. Russell 1000 Value



Source: FactSet

There is a lot more behind these style moves than what at first may appear to be random swings. The intensity of the economic cycle, the valuation level of the market and the performance of the various industry groups all play a role in style moves. Forecasting which style is going to lead the market is not Fort Washington's primary focus. However, when we see major divergences in the market we make every effort to capitalize on them.

Why do we think we are on the cusp of a major style rotation? Let us outline the reasons. We believe first and foremost in bottom-up stock selection. However, we also believe that it is important to look at more than one aspect of any particular company. In our stock selection process, we evaluate and rank each security on the basis of valuation, fundamentals, price and risk, then assign a total score based on the weight of the evidence. Our call that growth has turned the corner goes through the same process.

Let's start with valuation first. We believe price to cash flow is a very important predictor of future stock performance. It is also an important valuation indicator. As seen in Figure 4, growth stocks are currently lower than value stocks on price to cash flow and growth is trading in-line with its historical average, while value is well above its average. This is the first time in the last 30 years that it has been possible to buy growth at a discount to value.

Figure 4

Price to Cash Flow (Large-Cap Growth vs. Large-Cap Value)



Source: Credit Suisse Quantitative Equity Research, Barra, Compustat.

As we dig deeper, the valuation story gets even better. In a review of price-to-book, price-to-earnings and price-to-sales ratios, growth stocks are also lower relative to value. As a matter of fact in small-cap stocks you can buy growth at the same price as value on price-to-earnings. This is the first time an investor has been able to do this since 1993.

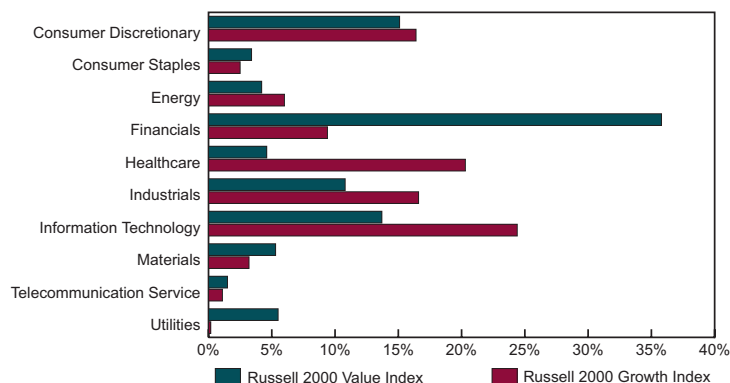
On almost every valuation measure, growth stocks are lower relative to their trading history versus value stocks. While growth stocks are not necessarily less expensive than value stocks on an absolute basis, growth is at or below its average valuation trading range, while value stocks are at or above their historical valuation trading ranges.

Finally, we will evaluate price. As discussed earlier, value has left growth in the dust since 2000. Can it get worse? Possibly, but at this time it seems that it is more likely we get some reversion to the mean. The spread in performance is almost unprecedented. We saw the same kind of spread in favor of growth just before it went off the cliff with the tech fiasco of 2000.

Fundamentals also seem likely to turn in favor of growth stocks. We have had five years in which GDP growth has averaged more than 3%. Given the Fed tightening and a significant escalation in commodity prices, including oil and raw materials, it seems like the economy may decelerate. While we do not look for a recession, a more temperate pace in GDP could be just what is needed for growth stocks to get back in favor. This is partly due to the difference in sector weightings between growth and value indices.

Figure 5

Russell Sector Weightings as of 09/20/06



Source: Frank Russell Company

Some of the dominance of value has been driven by its higher exposure to the metals, mining and commodity based industries. Now that prices have been driven sharply higher for almost all commodities, the real question is: can these pricing levels sustain themselves? Even if prices do maintain most of their gains, it is not likely that we see them move materially higher. Thus, one of the catalysts for the dominance of value appears to be behind us.

By comparison, the lagging performance of healthcare and technology stocks, which have the largest weights in the growth index, may be about to reverse itself. We think more investors will seek out the predictability of healthcare earnings as GDP cools, given their solid fundamentals and reasonable valuations. Technology should also come out if its slump as corporations that are flush with cash invest in IT infrastructure to keep up with competitive pressures which continue to plague almost every company in this globally competitive environment.

Technology continues to remain one of the best ways to foster increased productivity. Given corporate America's strong balance sheets it is not unreasonable to assume that a significant amount of capital spending remains on the horizon.

The table below (Figure 6) shows how small-cap growth stocks, as measured by the Russell 2000 Growth Index, have exhibited much higher historical sales and EPS growth (anywhere from 50%-80% higher growth than small-cap value) and are estimated to increase EPS at 50% more than value over the next five years. Yet, in spite of this significantly higher historical and estimated EPS and sales growth, the PE multiple on small cap growth is a modest 1.6 multiple points higher than value.

Figure 6

	3 Yr Median Historical EPS Growth	3 Yr Median Historical Sales Growth	Estimated Long Term EPS Growth	Price to 1 Yr Forward Earnings Est	PE to LT Est Growth
Russell 2000 Growth	20.8	15.8	18.0	16.7	0.93
Russell 2000 Value	11.5	10.9	12.5	15.1	1.39

Source: Compustat, Reuters, Factset

Last but not least, let us look at the risk of being wrong on favoring growth over value. At this juncture, from a valuation perspective, growth is cheaper than it has been over the last 10 to 30 years, depending upon which metric you choose to use. Clearly, from this perspective, maintaining a value overweight seems to be a risky strategy. On a fundamental basis, growth's predictability coupled with its attractive valuation level leaves little downside relative to the value alternative. From a pricing perspective growth also seems to have a lower risk profile. Given the substantial out performance of value for the last six years and its heightened valuation level, downside risk appears to be significantly higher in the value camp.

Summary & Conclusion

We will continue to make our stock selections on a bottom-up basis. However, at this time, it seems like investors are getting significant opportunity to buy growth at levels that have not been seen over the last 30 years. The weight of the evidence using our valuation, fundamental, risk and price models points to a turn in favor of growth. To us, it seems that the primary down side would be that growth performs only in line with value. With limited down side, it seems advantageous for investors to emphasize growth since the winds of change appear to be shifting. Rather than bucking strong headwaters, growth investors may finally have the opportunity to coast down stream.

A Footnote on Capitalization

After reading this paper, you may ask yourself, where in the spectrum should an investor currently be investing? The answer is where you have the most opportunity. Our own research does not support any specific cap range at this time. We do not see significant disparities between small, mid or large capitalization stocks on the growth side of the equation. Our conclusion is that growth, irrespective of capitalization, is poised to outperform value.

OUR CONCLUSION IS THAT GROWTH, IRRESPECTIVE OF CAPITALIZATION, IS POISED TO OUTPERFORM VALUE.

Market Summary for Third Quarter 2006

ECONOMY & EARNINGS

- ◆ Real GDP growth moderated to 2.6% in the second quarter from 5.6% in the first quarter and the consensus estimate for the third quarter stands at 2.0% to 2.5%.
- ◆ The downturn in residential housing and a decline in auto production with detract from economic growth in the second half of 2006.
- ◆ The recent decline in energy prices has made a “soft landing” the most likely outcome, but the risk of recession cannot be ruled out entirely.

STOCK MARKET

- ◆ Stock prices rebounded strongly from the summer lows with the S&P 500 Index advancing 5.7% during the third quarter.
- ◆ The Federal Reserve’s decision to hold policy steady since August, a drop in commodity prices and some encouraging economic statistics have contributed to the more bullish sentiment.
- ◆ Stocks appear reasonably valued relative to interest rates, especially if future earnings estimates prove attainable.

BOND MARKET

- ◆ Interest rates declined nearly 0.50% in the quarter driven by concerns over a housing-induced economic slowdown. It is clear that housing is weakening significantly, however, it remains to be clear that this will have a significant impact on consumer spending. Declining energy prices also provided fuel for lower interest rates, reducing inflation expectations.
- ◆ We are slightly defensive in terms of interest rate risk, anticipating rates may increase in the near-term. We believe the Fed will remain on hold through the first part of 2007.
- ◆ Our outlook is for relatively stable interest rates, which should bode well for the mortgage-backed securities sector. We recently increased our weighting to this sector. We remain conservatively positioned within corporate bonds.

A Note to Our Wealth Management Clients

The recently enacted Pension Protection Act of 2006 provides new charitable giving opportunities to taxpayers over age 70½. The new Act now allows donors to exclude from income up to \$100,000 in direct gifts to qualified charities from his or her IRA in each of 2006 and 2007. Please give us a call or consult your tax advisor for additional advice about giving opportunities.

Welcome to Fort Washington Investment Advisors!

Fort Washington Investment Advisors, Inc. is pleased to announce its latest client additions:

Weebetook Investments, Ltd. has selected Fort Washington Investment Advisors to manage \$1 million in its small cap growth strategy.

Fort Washington Investment Advisors, Inc. is excited to introduce its newest associates:

John Bessone,
Regional Director,
Private Equity (New Mexico)

Paul Cohn,
Regional Director,
Private Equity (Columbus)

Jessica Kupper,
Portfolio Analyst,
Fixed Income

Allyson Bosse,
Executive Assistant,
CIO & Marketing

Linda Fultz,
Manager,
Administration and LP Relations,
Private Equity

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In the News

Fort Washington Investment Advisors’ professionals have been featured in a number of publications throughout the quarter. Here is a sampling:

Newsday (New York), September 24, 2006, “This Week in Stocks” — Quotes by Nick Sargen, CIO of Fort Washington Investment Advisors on the outlook of the economy.

Los Angeles Times, September 23, 2006, “Investors Rush Into Bonds on Dim Outlook” — Quotes by Nick Sargen, CIO of Fort Washington Investment Advisors on the economic outlook of stock and bonds.

CNBC’s “SquawkBox”, September 21, 2006, Nick Sargen, CIO of Fort Washington Investment Advisors, appeared on the program.

Consuelo Mack WealthTrack, September 16, 2006, Nick Sargen, CIO of Fort Washington Investment Advisors, appeared on the program.

Bloomberg Television’s “After The Bell”, September 8, 2006, Nick Sargen, CIO of Fort Washington Investment Advisors, appeared on the program. Nick discussed his views on what happened in the market during the week and what to expect in the near future.

PR Newswire, September 6, 2006, “Touchstone Investments Launches Diversified Small Cap Growth Fund; Fort Washington Investment Advisors Named Sub-Advisor” — Quotes by Maribeth Rahe, President & CEO of Fort Washington Investment Advisors, Inc.

Cincinnati Business Courier, August 21, 2006, “Investor Profile” — Rick Jandrain, Managing Director and Senior Portfolio Manager at Fort Washington Investment Advisors was interviewed and featured in the Investor Profile.

Pensions and Investments, August 21, 2006, “SPECIAL REPORT: TOP-PERFORMING MANAGERS” — Fort Washington Investment Advisors’ High Yield Commingled Fund was named one of the five top-performing commingled fund managers for five years ended June 30, 2006.

Bloomberg Television’s The Bloomberg Report, August 7, 2006, Nick Sargen, CIO of Fort Washington Investment Advisors, appeared on the program. The topic of discussion was how current events are impacting the financial markets.

USA Today, August 3, 2006 “Dividend paying stocks pull ahead” — Quotes by Nick Sargen, CIO of Fort Washington Investment Advisors.

International Herald Tribune (Paris), July 31, 2006, “Petrodollars alter outlook for U.S. debt” — Quotes by Nick Sargen, CIO of Fort Washington Investment Advisors.

Bloomberg Television’s After The Bell, July 14, 2006, Nick Sargen, CIO of Fort Washington Investment Advisors, appeared on the program.