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SELECTOR[®] Money Management 2003 Third Quarter Review

The third quarter of 2003 saw all major equity markets continue to advance and provide investors with two consecutive quarters of market gains for the year. The third quarter is usually a difficult quarter, even in bull markets. In fact, the S&P 500 had not enjoyed a winning third quarter since 1997. The focus of the third quarter is always on the month of September. September started strong, but succumbed to selling pressure in the last two weeks, with the NASDAQ Composite and the S&P 500 ending down 1.2% for the month. The last four years, however, during the month of September the S&P 500 had averaged losses of 6.9%, and the NASDAQ had average losses of 10%. More importantly, in the third quarter the S&P 500 gained 2% and the NASDAQ gained 9%.

The best performing sector in the third quarter was technology, with the average technology fund up over 10%, according to Morningstar. The second best performing sector was small cap growth with average gains of 9%. Mid cap growth funds averaged 5% gains in the third quarter, and finally the average large cap growth fund was 3% higher. For the second quarter in a row we are seeing the manager-driven funds outperform the index funds, which is typical in a Bull Market. It is also typical to see the small cap and mid cap sectors outperforming the large cap sector in the early phases of a cyclical Bull Market.

The third quarter was a roller coaster for bond markets. July was one of the worst months in history but bonds rebounded in August to break even for the quarter. According to Lipper, the best performing bond sector for the quarter and for the year continued to be the high yield bonds, up over 2% for the quarter and up over 17% for the year. By contrast, the Lehman Brothers Credit Index was flat in the third quarter and the 10-year Treasury bond lost 1.87% for the quarter to yield 3.93%. The Federal Reserve Board in September restated their desire to keep interest rates low as they continue to predict economic recovery without inflation.

The ultimate scorecard of the economy is corporate earnings, which are rebounding. Economists are projecting that the economy will grow at the rate of 4.5% in the third quarter, after growing 2.4% in the second quarter. The number of companies upwardly revising their guidance for third quarter earnings announcements has grown about 20% from the same period last year. According to a Thomson Financial poll, S&P 500 corporate earnings are forecasted to increase an average of 16% in the third quarter, and 22% in the fourth quarter, over last year's results.

In September, allocations to equities were increased and allocations to bonds were decreased for all SELECTOR[®] styles. The emphasis for equities continues to be with small cap and mid cap sectors, along with technology. The emphasis for bonds continues to rest with the high yield sector that has been performing so well all year. The long-term trend remains positive and our young Bull Market is very healthy. We have had good progress year-to-date, and the stage is set for what historically is the best quarter of the year for stocks.

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