

# **SELECTOR<sup>®</sup> Money Management**

## **2004 Second Quarter Review**

**The second quarter of 2004 confirmed our caution of three months ago.** Volatility remained high for all equity indices. Early in the second quarter prices, rose into the upper levels of the trading range that has now contained prices since January. What followed was an excruciating decline over the next six weeks that took equities right to the bottom of the range. Several major indices were bruised by this decline, and the support at the bottom of the trading range was severely tested. Cooler heads finally began to buy at those depressed levels, and in just two weeks major market indices were comfortably back into the upper tier of the trading range. At quarter's end, equity prices closed in that upper level of the two-tier trading range.

**Equity markets have essentially been traveling within this broad trading range for the entire year-to-date.** While a considerable amount of territory has been covered, not much progress has been made for all of the back-tracking and doubling back. The S&P 500, the Russell 1000 and 2000 and the NASDAQ Composite are all up just over two percent for the year, gaining about one percent in the second quarter to match their gains of the first quarter. This sounds more like the type of returns one would expect from a bond investment, but that is another story entirely.

**The biggest jump in the financial markets during the second quarter was in the 30-year Treasury bond interest rate.** Interest rates had been falling for the past four years, and deserved a great share of credit for our strengthening economy. As the economy continued to grow stronger this year the Federal Reserve Board held rates low. In the second quarter the Fed indicated that it was time for short term rates to rise, and that precipitated a decline in bond prices. Remember, when interest rates rise, bond prices decline. They don't decline as severely as equities, but they do move. The total return for bonds is the interest rate yield, plus or minus the price movement. Year-to-date, the high yield bonds continue to be the best performing bond sector, with a total return just over one percent. Short and intermediate term bonds closed about flat at mid-year, and long-term bonds closed down about one percent after being up four percent after the first quarter.

**The net result for SELECTOR<sup>®</sup> managed portfolios is that equities gained a little ground, and bonds lost some ground but were very effective in managing the high volatility of the equities.** In other words, everything worked like it was supposed to work, even if things seem pretty boring at this juncture. Looking ahead, the Fed has transformed the interest rate rumors to fact, (and it didn't hurt all that bad,) corporate earnings have been better than forecast, and we remain in a Bull Market cycle for equities. The Presidential Election and a lively international environment should provide plenty of electricity for journalists and short-term investors. And we long-term investors remain diligent and opportunistic.

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