

SELECTOR[®] Money Management

2005 Year End Review

The Bull Market in U.S. equities continued for a third year, with the Standard & Poors 500 Index (S&P 500) and the NASDAQ at their highest levels since June of 2001. For the year, the S&P 500 finished with a gain of +4.91%, while the NASDAQ closed +1.37%. The Dow Jones Industrial Average (DJIA) closed down 1.72% in 2005, largely due to General Motors, which declined by 51%. Single digit returns were the rule for the U.S. major market indexes, with double digit returns common in overseas major market indexes. The MSCI EAFE Index finished +13.54% and the MSCI Emerging Market Index +30.31%. Domestically the best performances came from natural resources and oil & gas sectors, with the Goldman Sachs Natural Resources Index +36.48% and the Dow Jones Oil & Gas Index +34.46% in 2005.

Oil prices and Federal Reserve interest rates hikes provided most of the headlines, and most of the negative pressure on financial markets during 2005. Oil prices and gasoline prices increased to their highest nominal levels, while the Federal Reserve raised the discount rate and the federal funds rates eight times in 2005. Additional negative pressure was provided mid-year from Hurricane Katrina, the most destructive hurricane ever to hit the U.S. in a season which saw the most hurricanes in history. These negative pressures were effectively countered, however, by continuing strength of the housing market, strong corporate earnings, low inflation rates, decreasing unemployment numbers. Growth in the U.S. economy as measured by the Gross Domestic Product (GDP) topped 4% in the third quarter, and has been at 3% or better for 13 straight quarters, the longest streak since the mid 1980's.

Rising short-term interest rates and above-average economic growth are usually thorny for bond returns, but fixed-income funds defied conventional thinking with respectable returns for the year. The Lehman Brothers U.S. Aggregate Bond Index closed +2.43% in 2005, including interest. A healthy appetite for intermediate and long-term bonds kept prices strong and yields down, despite the short-term increases from the Federal Reserve. At year's end, the yield on the two-year Treasury Note was 4.408%, slightly higher than that of the ten-year Treasury Note at 4.393%. All eyes are now on the Federal Reserve to determine when they stop their string of 13 consecutive interest rate increases.

Financial markets' fundamental strengths continue to outweigh their weaknesses and SELECTOR[®] allocations remain fully invested according to the respective styles, as we enter 2006. SELECTOR[®] Aggressive Growth and SELECTOR[®] Growth allocations are 100% invested in equities. SELECTOR[®] Conservative Growth portfolios are 80% equities/20% bonds. SELECTOR[®] Balanced Growth is 60% equities/40% bonds, and SELECTOR[®] Income & Growth is 40% equities/60% bonds. These allocations are a reflection of our positive fundamental and technical environment and outlook.

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