Market Review and Outlook—April 11, 2005

With the strong finish in the last quarter of 2004 the bullish investor would have expected the momentum to carry over to the first quarter of 2005. No such luck. US stocks fell 3% while non-US stocks and bond funds fell slightly.

Two factors stunted equity return growth. Oil prices increased, receded, and then increased again to record levels by the end of the quarter. The Fed continued its money tightening policy by raising rates through March. Inflation concerns were the justification for the seventh increase in short term rates in a year. With no end in sight to higher oil demand from China and India, higher oil prices in the US will likely continue to weigh down domestic stocks growth.

The largest casualties were science and tech funds (-9%), and telecom, health, and real estate (down 6 to 7%). Growth funds fell over 4% and small caps fell over 3%. There were a few bright spots during the quarter, however. Natural resource funds, with their allocation of oil industry stocks, leapt 13%. Utility funds (+3%) benefited from the increased demand for energy as the economy continued to expand, and from their energy holdings.

International stock funds faired better than their US peers. Latin American funds led the way (+2%), while Emerging Market and European funds posted 1% gains in the first quarter. However, the category was dragged down by Japan funds, which declined 2%.

Bonds and bond funds suffered from the Fed rate hikes, as bond prices dropped and fund values shrank. High yield municipal funds were the one bright fixed income segment with a 1% increase in value for the quarter. A recovery late in the quarter for the dollar versus foreign currencies (especially the Euro) stymied last year's interest in global bonds; they were down almost 2%. High yield taxable bonds fell 1.6%.

Best Approach

As always, we believe in the value of setting targets and regular rebalancing. At this point we see more opportunities for growth in non-US stocks than in US stocks. We continue to favor emerging markets and international small cap funds. We also continue to recommend that investors keep their bonds shorter term, and utilize inflation-linked and floating rate bonds where practical. We expect the energy sector of the economy to continue to grow. The following figures come from the April 10th issue of Barron's and from Morningstar.

Category	1st Q '05	Past Year	3-Yr Avg	5-Yr Avg	10-Yr Avg
Money Market—Taxable	+0.39%	+1.02%	+0.84%	+2.15%	+3.60%
Intermediate Term Bond	-0.61%	+0.82%	+5.44%	+6.39%	+6.34%
Intermediate Muni Bond	-0.90%	+0.44%	+4.25%	+4.95%	+4.82%
Large-Cap Core Stock	-2.42%	+4.00%	+0.65%	-4.46%	+8.87%
Mid-Cap Core	-1.16%	+9.48%	+7.17%	+3.36%	+12.13%
Small-Cap Core	-3.27%	+7.92%	+8.57%	+7.26%	+11.53%
International Stock	-0.36%	+12.61%	+9.52%	-2.24%	+6.59%
Real Estate	-6.68%	+10.08%	+17.89%	+19.30%	+14.80%
Natural Resources	+12.52%	+37.93%	+17.13%	+14.46%	+14.39%
Science/Technology	-8.81%	-5.32%	-2.26%	-20.49%	+7.90%
Multi-Cap Growth	-4.44%	+2.96%	+1.73%	-10.32%	+9.40%
Multi-Cap Value	-0.81%	+9.98%	+5.74%	+5.24%	+10.92%
Balanced	-1.38%	+4.28%	+3.85%	+1.29%	+8.21%