Market Review and Outlook—June 8, 2006

March and April were going so well; the S&P 500 rose over 2.5%. In May the US stock markets began to fall and by the end of the month they had given back all of March and April's gains. This was partially due to concern that the Federal Reserve Bank has not finished raising overnight interest rates, disappointing stock investors. The new Fed Chairman, Ben Bernanke, just this month made clear that he is committed to keeping inflation in check, and will not shrink from raising rates as long as it takes to cool the US economy. While bond investors like to know that the Fed will keep inflation from spiraling upwards, they don't like rising rates, and bonds continued to lose money this year.

Other factors weighing on US and foreign markets include continued global instability (tensions over Iran's nuclear energy/weapon programs hit the headlines), and oil prices which seemed to hover around $70 a barrel without any intention of returning to the $50 and below level we had grown accustomed to for twenty years. Investors also have begun to take profits earned during the rebound of the past three years, and when the stock markets began to slip, these sales accelerated, causing the markets to fall further. When investors get jittery, they tend to sell growth and technology first (value-investors as a group are more patient, or slow-to-react, depending on whom you ask), and the results below reflect that, as growth and technology stock funds lost the most money in the past three months..

In the past three months, US stocks are fairly flat, while foreign stocks are up about 3%. One– and three-year trailing annual returns for stocks are uniformly strong. Keep in mind that 5/31/2003 was close to the bottom of the bear market, and comparisons are destined to look wonderful.

Bond returns have been very weak this year, and their one– and three-year results are also anemic. This merely reinforces the **critical role of bonds in a well-diversified portfolio**. While stocks in a portfolio are enjoying a three year rebound, we have no problem if bonds are flat. What is important is that bonds hold up when stocks are falling; **they delivered during the bear market** earlier this decade. The table on the right shows how bonds have helped smooth the ride for investors during bear (losing) and bull (gaining) markets this decade.

Annualized Returns	Bonds	Large US	Mid US	Small US	Foreign
Bear (9/00 to 2/03)	+9%	-18%	-10%	-7%	-22%
Bull (3/03 to 4/06)	+3%	+17%	+24%	+28%	+28%

Category	3 Months	Past Year	3-Yr Avg	5-Yr Avg	10-Yr Avg
Money Market—Taxable	+0.97%	+3.26%	+1.67%	+1.69%	+3.40%
Intermediate Term Bond	-1.16%	-0.43%	+1.79%	+4.51%	+5.62%
Intermediate Muni Bond	-0.24%	+1.07%	+1.90%	+4.10%	+4.80%
Large-Cap Core Stock	-0.46%	+9.68%	+11.44%	+1.81%	+7.37%
Mid-Cap Core	-0.03%	+14.93%	+17.06%	+7.97%	+10.57%
Small-Cap Core	-0.02%	+18.32%	+19.99%	+10.32%	+10.86%
International Stock	+3.28%	+28.86%	+22.89%	+7.39%	+6.46%
Real Estate	-1.09%	+19.03%	+24.82%	+19.39%	+14.97%
Natural Resources	+8.18%	+41.42%	+33.45%	+16.41%	+14.24%
Science/Technology	-5.65%	+9.77%	+11.19%	-4.53%	+5.67%
Multi-Cap Growth	-2.55%	+13.52%	+13.78%	+2.19%	+6.61%
Multi-Cap Value	+0.80%	+13.86%	+9.05%	+8.33%	+10.46%
Balanced	-0.32%	+6.66%	+8.31%	+3.49%	+6.82%