

2nd Quarter 2007 Market Review

The DJIA led all major indices through the 2nd quarter, returning 8.8%, while the NASDAQ and S&P500 gained 8.2% and 7.0%, respectively. Both the Dow and the S&P ended the quarter within shouting distance of their respective record highs, though the Nasdaq is only half way back to its dot.com peak above 5,000. (Please refer to the performance illustration for comprehensive YTD returns.)

Despite its impressive advance, the market was not without risk as it was spooked by the near-collapse of a pair of hedge funds run by investment firm Bear Stearns. These funds, whose underlying investments were in derivatives of sub-prime mortgages, narrowly averted failure only due to an infusion of billions in cash from their sponsor.

Among the various style categories, growth built upon its 1st quarter strength by outperforming value at all capitalization levels during the 2nd quarter. Mid-Cap Growth (12.3% YTD) was the hottest capitalization sector, out-dueling both its large and small cap cousins. Small-Cap Value was the laggard, though it still posted a very respectable 7.0% mid-year gain.

Energy led all market sectors during the 2nd quarter, gaining 14.3%, as commodity gas and oil prices hovered near recent highs due to refining difficulties in the U.S., oil field attacks in Nigeria, and greater demand for gasoline during the summer driving season. Utilities, a top performing sector until recently, slid 1.1% in the quarter, underperforming all other sectors, as investors demanded higher yields due to rising interest rates. Financials, still reeling from their mortgage market losses, trailed all sectors, with a six-month setback of -2.0%.

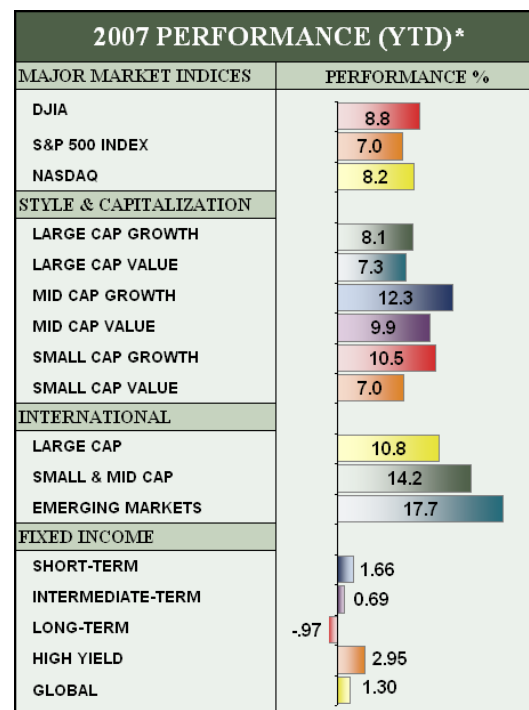
Emerging markets shrugged off worries from the previous quarter, climbing 17.7% to end the 1st half. Strong returns were contributed by Latin America (representing strength from countries with abundant natural resources) and solid performance in Asia. International small and mid caps continued to perform well, outpacing

international large caps while posting a 14.2% return for the quarter.

On the bond side, the Federal Reserve stood pat at 5.25% as they balanced inflationary fears against a possible housing sector driven economic slowdown. Market interest rates were forced higher by increases in overseas rates and an unanticipated exit from the dollar as foreign governments diversified their reserve holdings out of U.S. Treasuries and into non-dollar currencies.

The resulting upward shift in longer-term interest rates “renormalized” the yield curve (where short-term rates are lower than longer-term ones) while also causing a 1% mid-year loss on longer maturity securities due to principal erosion. Shorter duration bonds were largely unaffected, gaining 1.66%. As a possible harbinger of events to come, investors expressed their mounting concerns over credit quality as reflected in their “flight to quality” and the expansion of the spread between Treasuries and high yield bonds by over 50 basis points.

Tim Hai



Source Data: Morningstar, Inc. (Investment category performance)
*Year-to-date as of 6/30/2007