SELECTOR® Money Management
2011 Second Quarter Review

The final four trading days of June preserved the month, the second quarter, and the year for equities. While prices rested below the April highs, they did settle comfortably into a well-defined trading range. The second quarter's activity was dominated by a six-and-a-half week decline in equity markets that started on May 1st and didn't stop until it had literally erased all of the major markets' gains for the year. Then, in a surprisingly persistence Hail Mary run that included the first day of July, equity prices regained those gains and settled into the long Independence Day weekend.

The S&P 500 Index finished the second quarter with a gain of +6.02% for the year. This was after gaining +5.92% in the first quarter, then falling to within one-half of one percent of its 2010 close on June 16th before that final, dramatic week of June. So while the second quarter might have looked like a yawner from a distance, the live performance was pretty exciting. The S&P 400 Mid Cap Index finished the first half of 2011 up +8.56%, -0.80% lower than its first quarter close, and the Russell 2000 Small Cap Index was up +6.21%, -1.73% lower than its first quarter finish. Interestingly, equity market declines in the second quarter occurred in harmony with lower energy prices. The Dow Jones U.S. Oil & Gas Index fell -5.03% in the second quarter, holding gains of +11.55% YTD.

The strongest performances of the second quarter were in the health care sectors. The Dow Jones U.S. Health Care Index gained +8.50% in the second quarter, to finish the first half of 2011 up +21.18%. The Dow Jones U.S. Pharmaceuticals Index gained +11.08% in the second quarter, ending the first half +15.7%. European equities, as well as real estate equities, also were very steady during the second quarter. The S&P Europe 350 rose +2.37% in the second quarter, ending up +9.62% YTD, while the Dow Jones U.S. Real Estate Index gained +3.36% in the quarter, finishing up +10.08% YTD. The weakest performers of the second quarter included energy and natural resources sectors, financial services, and emerging markets equities.

Bond markets took full advantage of the equity markets' volatility in the second quarter. Treasury inflation protected securities, known as TIPS bonds, were very active, with the Barclays Capital U.S. TIPS index gaining +3.85% in the second quarter alone, and ending up +5.81% YTD. Municipal, U.S. government, corporate, and high yield bonds also gained ground in the second quarter. The S&P National Municipal Bond Index is up +4.79%, the iBoxx $ Liquid High Yield Index up +4.64%, the Barclays Capital U.S. 7-10 Year Treasury Bond Index up +3.58%, and the Barclays Capital U.S. Credit Bond Index up 3.41% YTD.

While the long-term trend remains intact, the intermediate-term has now clearly entered a trading range environment. Trading range markets have their own dynamics, and can provide investors with opportunities to fine tune their asset allocations with the old 'buy low/sell high' adage in mind. It requires patience as cash positions may fluctuate to higher-than-normal levels as these adjustments are being synchronized with market fluctuations. In a strongly trending marketplace, there is inherently greater risk in being uninvested. In trading range markets this risk is diminished. If we may use a NASCAR example, it is like making a pit stop during a yellow flag, when speeds are reduced and ones position in the race is less affected by time off the track.

We continue to like international equities and real estate securities. Our interest in small cap and energy related equities has been reduced, while the health care and utilities equities are definitely on our radar. Until there is further development of leadership in equities markets, there is more benefit to being diversified than concentrated in any particular capitalization weighting or sector. You may expect to see money market/cash allocations fluctuate during this trading range environment as we reposition portfolios. Our long-term **SELECTOR®** Aggressive Growth and Growth models are still to be 100% invested in equities. **SELECTOR®** Conservative Growth models are 80% equities/20% high yield bonds. **SELECTOR®** Balanced Growth models are 60% equities/40% bonds, and **SELECTOR®** Income & Growth models are 40% equities/60% bonds. **SELECTOR®** Income models remain 100% invested in bonds.

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