Review for the 2nd Quarter 2007 and Future Outlook

Blue Skies Followed by Scattered Clouds

The Dow Jones Industrial Average started the 2nd quarter with an eight session winning streak, the longest in four years. Many investors believed in the 'Goldilocks' scenario – an economy not too hot, not too cold, thinking that the Federal Reserve would achieve what economists call a soft landing. In fact, April was the best performing month since December 2003, with the Dow Jones Industrials rising 5.7%. However the positive mood was eventually under scrutiny as most markets experienced a 'June swoon.'

Equity Markets Cruise to Big Gains

Despite the June sell off, it was still a terrific quarter as most major stock markets performed better than expected. The Dow Jones Industrial Average was up 8.5%, the S&P 500 was up 7.5% and the NASDAQ Composite was up 5.8%. Better than expected earnings reports, increased activity in corporate mergers and acquisitions and a stable interest rate environment all contributed to the gains.

Many foreign equity markets performed better than their U.S. counterparts. In the face of June nervousness, The Dow Jones World Emerging Markets Index jumped 15% in the 2nd quarter, compared to a 4.2% rise in the 1st quarter. Global expansion continues to be driven by healthy economies and strong expansion. However, rising interest rates and pricey valuations threaten to slow further gains.

Interest Rate Worries Rain on the Parade

In early June, bond prices dropped causing a rise in rates. This was motivated by a number of factors including inflation fears, continued weakness in real estate and housing with emphasis on the riskier subprime sector. Because other borrowing costs are tied to Treasury yields, the rise also pushed up mortgage rates.

On June 6th, the European Central Bank raised a key rate to 4% from 3.75%, followed by the Bank of England raising its benchmark rate by one-quarter point. By the end of June, the yield on the 10-year Treasury remained above the psychological 5% level, at 5.034%, high enough to inflame worries about inflation.

Drilling for Profits in Energy

The energy sector benefited from the 16% rise in oil prices this year. While prices are below their record high of $77 a barrel last year, crude prices ended the 2nd quarter at $70.68. This was a windfall for energy stocks but a burden for consumers due to higher gas prices fueling inflation worries and contributing to higher treasury yields.

Corporate 'Wedding Bells'

The sun was shining brightly on mergers and acquisitions giving a lift to stock prices. Companies around the world signed merger deals worth $1.65 trillion aided by the growth of private equity buyout funds and high corporate cash levels. According to Thompson Financial, this was the biggest three month total, beating out the 1st quarter of 2000. Initial public offerings – or IPO's also saw increased demand as many companies brought new shares to the market.

Our Outlook

Looking ahead, the mood for the next few months will initially be set by the quality of corporate earnings, key economic reports and interest rates. Despite the unrest in the bond markets, we see this as an opportunity for fixed income investors to buy at lower prices and lock in higher yields.

In our portfolios with foreign equity exposure we continue to stay diversified globally and we will not overweight in 'hot spots' like China. Chasing the latest trends can be tempting but we believe in taking a longer term approach and never overweight based on past performance.

While it has been four years since the Dow Jones Industrials fell as much as 10% from a high point, an unusually long time without a correction, we feel that U.S. stock prices are still reasonably priced. One reason is that measured against corporate profits, stocks in the S&P 500 trade at about 17 times earnings, only slightly above their traditional level of 16.

Having a Financial Plan

Do you have a good understanding of your overall financial picture? Have you defined your financial goals for the next year, 5 years, 10 years or more?

With half of 2007 behind us, now is the perfect opportunity to check in on personal financial goals, set new goals or adjust existing goals. Although you can almost guarantee that a set plan will change over time, a solid financial picture can aid you in making educated and productive financial decisions.

The first step is to brainstorm by asking yourself about your financial goals and needs. Have you identified your goals and the steps to address these goals? For example, do you save enough each year to secure your retirement? Is your life insurance coverage adequate?

Next, evaluate where you are in comparison to where you want to be. Remember to be flexible and realistic; it often takes small steps over time to reach your goals. Although planning can be overwhelming, taking the extra steps now will make for a more solid financial future. Jennifer Simes, our CERTIFIED FINANCIAL PLANNER™ practitioner, can offer assistance in helping you conquer the financial planning process.

Please let us know how we can help you coordinate and reach your goals and we would be happy to schedule a complementary consultation.

Did You Know?

Did you know that we can create customized reports of your managed investment account? We can illustrate your portfolio with color charts, graphs, sector breakdowns and much more - at no additional cost. Please let us know if you would like to receive these reports.

We look forward to continue serving your investment management and financial planning needs. Please let us know if you have any questions – or to schedule a review call us at 508-791-7126 or 800-25-SHERR (800-257-4377).