

Good News/Bad News

We are now halfway through another year and the stock market has barely budged, again. In 2005, at the halfway point, the S&P 500 had declined 1.7% on its way to a 3% gain for the year. This year the benchmark index has gained 1.8% at the end of the first half as we enter the summer slow period. The net gain for the last 18 months is a rather tepid 4.8%, not much considering the high level of volatility in the financial markets.

While many investors view this sideways movement of the stock market as bad news, we are inclined to look at the action in another light. If we step back and take a hard look at the many headwinds facing the market over the same timeframe, stocks have held up remarkably well. The federal funds rate in effect on January 1, 2005 was 2.25%; today it is 5.25% with the possibility of further increases. Crude oil has risen from the low forties to just over \$73 per barrel, and the world political situation has seen little improvement especially with the most recent uprising in Israel. The good news is that despite all of these problems, the stock market has not collapsed and indeed, has been able to make some forward progress.

One of the major investment themes at Abbot after the 2003 taxation change is dividends. According to Standard & Poor's, since the start of 2003 there have been 45 initiations of dividends, and 972 dividend increases in the S&P 500. We expect this trend to continue, and believe that technology companies, long known for not paying dividends, will begin to participate. Rising earnings within a flat market have brought price-to-earnings ratios down to below historical levels creating what we feel is an undervalued market and a lot of opportunity. Our value investment philosophy emphasizes quality combined with diversification. We will continue to position portfolios with these characteristics. We welcome your questions, comments and greatly appreciate any referrals you may send our way.

Scoreboard 1st Half 2006

Dow Jones: +4.04%
NASDAQ: -1.51%
S&P 500: +1.76%

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