ALLEN TRUST COMPANY

Monthly Newsletter

April 15, 2005

William A. Harris, CFA
Portfolio Manager

First Quarter Stock Market Review

I did a bit of a "double take" upon compiling the numbers for the First Quarter of this year… somehow the equities markets *felt* worse than this performance summary seems to indicate they actually were:

First Quarter, 2005	
Dow Jones Industrial Avg	-2.59%
S&P 500	-2.59%
Nasdaq Composite	-8.10%
10-Year Treasury	-1.23%
3-month Treasury	0.57%
Allen Trust Core Equities	-1.60%
Allen Trust Total Equities	-1.95%
Allen Trust Bonds	-0.54%

One of my duties as portfolio manager is, of course, *not* to let feelings (whether vague misgivings or unquantifiable enthusiasms) undermine my decision-making process. Even so, I can't help but feel the tenor of the markets, and when my sense of them doesn't jibe with summary statistics like you see above, I know it's time to start pulling the numbers apart.

So here goes… let's disaggregate the S&P 500's performance by industry sector:

S&P 500 Sector	First Qtr	Weight
Energy	17.07%	8.8%
Materials	1.27%	3.3%
Industrials	-2.04%	11.9%
Consumer Discretionary	-5.90%	11.5%
Consumer Staples	0.15%	10.3%
Health Care	-1.02%	13.0%
Financials	-6.96%	19.8%
Information Technology	-7.47%	15.1%
Telecommunications	-8.61%	3.1%
Utilities	4.44%	3.2%

What's remarkable here? Immediately evident is how soundly Energy (+17.1%) trounced the other sectors. The only other sector up significantly was Utilities, at +4.4%, and it comprises a mere 3.2% of the S&P 500. In contrast, relatively "big" sectors Consumer Discretionary, Financials, and Technology — which make up nearly half the index — dropped a combined 6.9%.

In short, the S&P did well only narrowly (i.e. in just two sectors) and shallowly (in just 12% of its market capitalization), while it did poorly both broadly (in five sectors) and deeply (in 58% of its market cap). So the numbers and the palpable negativity I felt over the last three months are reconciled in the details.

Allen Trust's **Core Equities** exhibited a similar lumpiness. While in the aggregate they edged out the Dow and S&P by 0.99%, this was due to just six out of 23 total positions performing positively. Most notable were **ConocoPhilips (+24.2%)** and **KB Homes (+12.5%)**, whose strength was nonetheless insufficient to make up for the likes of **Verizon (-12.4%)**, **Countrywide (-12.3%)**, and **Home Depot (-10.5%)**. Regarding these laggards, we keep buying Verizon and Home Depot for clients whom they suit, and we are holding steady on Countrywide.

While the quality of our investment *buy* decisions is manifest in how your portfolios grow over time, the quality of our *sell* decisions is not so plainly seen. It can help to revisit stocks deleted from the Core List to appraise their subsequent performance, which will represent either losses avoided (if the shares went down) or returns foregone (if they went up). On the first trading day of 2005, we removed **Bank of New York** from the Core and sold all positions. Thus far at least, that was a good move; BONY lost 12.9% for the quarter, while the money center banks we kept on the list — Citigroup and recent addition Wells Fargo — fell 6.7% and 3.8% respectively. So selling BONY in favor of holding Citi and Wells proved to be a *relatively* good decision.

But let me close with a saying perhaps too little heeded in portfolio management: "You can't eat relative returns." In other words, for a client looking at real losses — relatively smaller or not — a portfolio manager's celebration of having bested a benchmark is scant solace. Rest assured, we know that a loss is a loss.

Bill Harris