



## Schorpp Capital Management, P.C.

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#### 2nd Quarter Market Results

- > S & P Energy +4.99%
- > 10Yr Treasury -11.02%
- > Gold Futures -0.76%
- > S & P 500 +1.10%
- > DJIA -2.25%
- > Hang Sang +4.97%
- > Russell 2000 +4.58%
- > Nasdaq Comp. +2.58%

### The Federal Reserve, Alan Greenspan and the effect they have on your assets

As investors we often hear about the efforts of the Federal Reserve (the Fed) and especially its Chairman, Alan Greenspan. I want to take this time to inform our clients about the activities of the Fed, what its function is, and how it effects all of us.

The Fed holds eight regularly scheduled meetings per year. At these meetings they review economic conditions, determine monetary policy and assess risks to long-term economic growth. The rates we always hear about on the news are called the Federal Funds rate and the discount rate. The discount rate or primary credit rate is generally set at 1% above the Federal Funds target. This discount rate is the rate that banks can borrow from

the Fed usually on an overnight basis.

The Fed has stated that its main mission is to fight inflation. It does this by tightening (raising interest rates) or loosening (lowering interest rates) credit. In times of robust economic growth the Fed is likely to raise interest rates to slow growth and the possibility of inflation. During times of economic weakness the Fed will lower rates to stimulate the economy. When the economy is weak the possibility of inflation is also weak therefore the Fed can usually lower rates without creating inflation fears.

So, what does all of this mean to us. When the Fed raises rates it decreases the value of fixed

income investments. For example, let's say the Fed has raised rates over the course of a year 1.5%. At the beginning of the year the Discount rate was 3% and at the end of the year the Discount rate was at 4.5%. I have a bond in my portfolio with a return of 3.5%. By the end of the year rates had rose above the return I was getting on my bond and made it less attractive to other investors. I would see this decrease in value of the bond on my Schwab statement under market value. In a cycle where the Fed is lowering rates the fixed income investment I am holding becomes more valuable due to the fact that I am receiving a fixed return in an environment where interest rates are falling.

### 2nd Quarter Market Highlights and Lowlights

The 2nd quarter gave us a mixed return as far as equities were concerned. The NASDAQ and S & P 500 were both up and the narrowly based Dow Jones 30 was in the red. As we look at the equity markets they seem to be driven by the price of crude oil at the moment. Right now we are at peak summer driving season and the market is acting fairly well. Look for the price of crude

to fall into the low \$50 range as we approach the end of the summer. This should provide a nice run for stocks in the second half of the year.

Greenspan continues to raise short term rates. Up till now the longer term rates have remained stable. We see an increase of at least a half a point in the return of the 10 year bond by December.

Real Estate is hot, Right? If you were to look at home prices in the Philadelphia region and compare them to the performance of the S & P 500 since 1980 you will find that while home prices are up three fold the S & P is up a whopping twelve times. A pretty amazing fact given all the talk about real estate lately.

### Tip of the Quarter

Invest for the long term. Investing in any asset class is an exercise in patience and planning. Assets often have valuation swings from one quarter to the next. As an investor it is important to have a plan, execute the plan and have the temperament to stay the course even though every one around you is panicking. The smart money is always buying when everybody else is selling.