

Market Data & Commentary:

Source: Vestek & Frank Russell

Index	Month	Quarter	2001YTD
S&P 500	-2.4%	5.9%	-6.7%
Dow Jones Industrials	-3.7%	6.7%	-1.9%
NASDAQ	2.4%	17.4%	-12.6%
S&P/BARRA Value	-3.3%	4.4%	-2.5%
S&P/BARRA Growth	-1.3%	7.8%	-11.0%
S&P 500 Equal-Weighted	-1.6%	8.6%	3.8%
S&P 400 Midcap	-0.4%	13.2%	1.0%
Russell 2000	3.5%	14.3%	6.9%

SECTORS:	2001Q2	2001YTD
Basic Materials	7.6%	6.0%
Consumer Cyclical	11.8%	16.9%
Consumer Non-Cycl	5.1%	4.1%
Consumer Svcs	13.1%	13.8%
Commercial Svcs	19.6%	5.1%
Energy	-6.8%	-10.5%
Financial	10.9%	6.8%
Health Care	19.4%	3.1%
Industries	13.2%	10.5%
Technology	21.3%	-0.2%
Telecomm	7.5%	-4.8%
Transportation	4.0%	1.1%
Utilities	-0.2%	-5.6%

The U.S. stock markets staged a turnaround from the first quarter with all of the major indices finishing the second quarter firmly in positive territory. After leading the market down for the past few quarters, the tech-heavy NASDAQ staged a dramatic turnaround from its first quarter performance, up 17.4%, while the Dow Jones Industrial and S&P 500 were able to post solid performance of 6.7% and 5.9%, respectively. Some familiar patterns drove the markets:

- The quarter began strongly, driven by the Federal Reserve's surprise interest rate cut in April. The Fed continued its attempt to prime the economic pump with subsequent interest rate cuts of 50 bps in May and 25 bps in June. Offsetting the monetary easing was the constant flow of negative Q2 earnings news out of corporate America.
- After three quarters of out-performance, value investing handed over the performance baton to growth. In the large-cap. arena, the S&P/BARRA Growth index out-performed its value counterpart, returning 7.8% vs. 4.4% for the S&P/BARRA Value index. This trend was also evident in the mid-cap. and small-cap. arena where the growth indices returned 15.6% and 14.4%, respectively vs. 11.4% and 12.9% for the value indices.
- Large-cap. stocks continued to under-perform during the quarter, although not by as large a margin as in the first quarter. The equal weighted S&P 500 index out-performed the cap-weighted version by 276 bps in the second quarter. This brings the 12-month out-performance to a whopping 2,860 bps. The equal weighted index now leads the cap-weighted index over the 1, 2, 3, 4, 5 and 10 year time periods ended 6/30/01.
- Despite the dramatic turnaround in performance during the second quarter, for the 12 months ended 6/30/01, the NASDAQ and S&P 500 indices are still down -45.5% and -14.9%, respectively. For the same period, the Dow Jones is up 2.5%, driven primarily by exposure to more of the "old economy" stocks.

At the sector level, it was a case of Q1's dogs becoming Q2's darlings, led by the Technology sector (up 21.3%). Consumer Cyclical, up 11.8%, was one of only two sectors that registered consecutive positive quarterly results as investors continue to be attracted to companies that are more likely to be the early beneficiaries of an economic pick-up. Lower oil prices, due in part, to higher than expected stockpiles in the U.S. and the resumption of exports by IRAQ, was one of the primary drivers behind the weakness in the energy sector, down 6.8%.

Given the volatility that we have seen during the past two quarters, it is clear that investors are struggling to gain near-term visibility regarding the direction of the economy and individual corporate performance, in our opinion. Given this environment, and what we believe will be a slowdown in action by the Fed, we would expect to see continued short-term volatility, driven, in part, by the latest news headlines. In this type of environment, we expect that good or bad news on the economic and corporate front will be increasingly viewed as exactly that and not as a backdrop to the interest rate discussion.

Model Attribution: *Second Quarter, 2001*

Quint	Opt E/I	Earnings	Insider	DDM	Cashflow	Technical	Size
5 (high)	9.6%	8.3%	9.3%	15.9%	14.2%	6.6%	4.3%
4	7.6%	13.5%	11.2%	12.6%	11.8%	7.0%	9.6%
3	14.8%	11.5%	12.5%	12.9%	8.9%	6.6%	11.1%
2	12.6%	14.8%	11.1%	7.8%	11.5%	7.0%	14.0%
1 (low)	11.9%	9.9%	11.1%	7.8%	17.1%	11.2%	15.3%
Spread	-2.4%	-1.6%	-1.8%	8.1%	-2.9%	-4.6%	-11.0%

Note: "Spread" is the difference between the returns of the high (5) and low (1) quintiles by each model/measure.

The Shenandoah models do not confirm the growth bias evident in the market this quarter. Unlike the first quarter, in which the spreads in most models exhibited a positive monotonic pattern, second quarter quintile spreads appear more random. The level of inter-quintile spread was also well down from the first quarter. Interestingly, no model reported a negative quintile performance for the quarter. We believe these characteristics are consistent with the positive performance reversal exhibited by the technology sector and the overall positive bias of the equity market in the quarter. In this market environment, it is more likely that all ships will be lifted by the rising tide, in our opinion.

- The DDM was the only one of our primary models which added value during the quarter, as exhibited by the +8.1% spread between the best and worst returns.
- Excluding the DDM Model, all of the models exhibited negative performance. We believe that these were primarily driven by the performance reversal ("rubbish rally") that occurred in the technology sector during the quarter.
- In general, companies with weak earnings, lacking insider support and not attractively valued on a cash flow basis outperformed their mirror opposite. More specifically:
- The Earnings and Insider Trading models, which are two of the primary drivers of our process, under-performed by -1.6% and -1.8%, respectively. In both cases, the middle three quintiles outperformed the best and worst quintiles.
- Not surprisingly, the OPT E/I model, which combines our Earnings and Insider Trading models, also under-performed, -2.4%.
- Price momentum (our Technical model) reversed course from the first quarter with beaten down technology stocks leading the way up.
- Size continued to be a huge factor in determining performance this quarter. The smallest stocks out-performed the largest by 11.0% for the quarter.

Year to date model performance is mixed. Our value models, Cash Flow and DDM have been the best performers, +38.3% and +33.4%, respectively. Size has been the worst performing model, -27.2%, closely followed by Earnings, which has under-performed by -19.6%. One of the primary factors impacting the year to date performance of our models has been the volatility of the technology sector.

Model Attribution: *Year-to-date, 2001*

Quint	Opt E/I	Earnings	Insider	DDM	Cashflow	Technical	Size
5 (high)	3.5%	-4.2%	7.4%	25.3%	28.2%	1.1%	-9.2%
4	-1.5%	6.2%	8.4%	13.7%	16.8%	0.1%	2.0%
3	8.4%	5.0%	8.5%	8.3%	4.2%	1.7%	1.4%
2	5.2%	9.6%	2.0%	-0.8%	-1.7%	2.5%	10.3%
1 (low)	6.8%	15.4%	-5.0%	-8.2%	-10.1%	3.8%	17.9%
Spread	-3.4%	-19.6%	12.4%	33.4%	38.3%	-2.7%	-27.2%