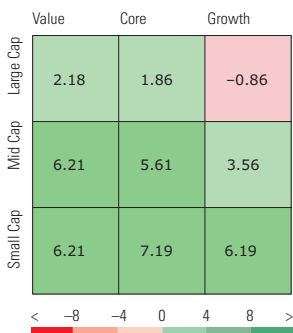


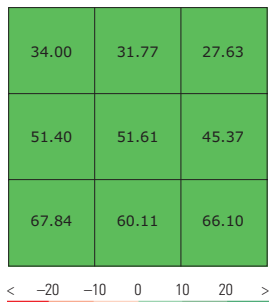
# Morningstar Market Commentary

First Quarter 2004

## Morningstar Market Barometer™



## 1st Quarter (% Return)



## 1-Year (% Return)

## Overview: Markets Take a Breather

As the first quarter of 2004 drew to a close, the U.S. stock market looked uncertain.

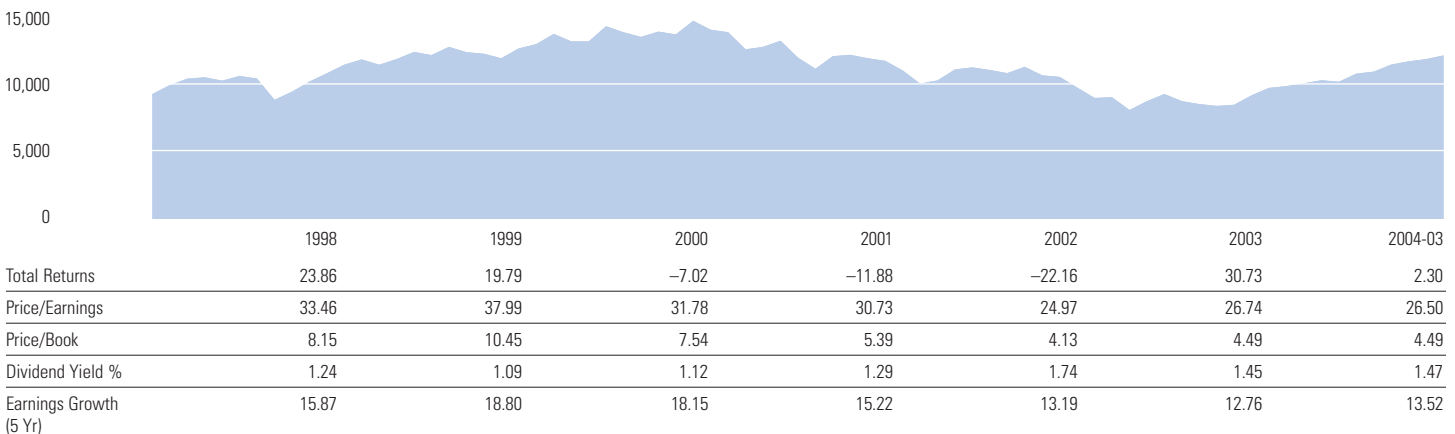
The so-called low-quality rally of 2003, which featured smaller-cap, technology, telecommunications, and Internet companies with dubious balance sheets doubling or tripling in value, lost some momentum toward the end of the first quarter of 2004. However, the long-awaited rotation into the shares of large, high-quality companies with proven records of earnings growth hasn't yet fully materialized.

Optimism fought anxiety during the period. Through March 31, 2004, the Morningstar US Market Index gained 2.3% as investors searched through a fog of conflicting data and news. The economy looked strong, but there remained doubts about the sustainability of its vigor, with anemic job growth a nagging concern. Corporate balance sheets and earnings looked better, but many stocks looked pricey. There were also mixed signals on the geopolitical front. A year after the start of the Iraq War, stability in the region is a distant dream and the specter of global terrorism continues to shake the financial markets.

Merger news, both good and bad, also influenced the broad market's performance. Bank One and J.P. Morgan Chase, which agreed to combine, were among the leading positive contributors to the Morningstar US Market Index's performance, as was AT&T Wireless, which sold itself to competitor Cingular for \$41 billion. Business-software firm Oracle proved to be one of the biggest drags on the broad market in the first quarter. Its stock fell more than 9% as the U.S. Department of Justice filed a lawsuit to block CEO Larry Ellison's bold and controversial bid to buy rival PeopleSoft.

Small cap stocks continued their long winning streak, as they outperformed large caps once again. The market's big gains of late and the lower-interest-rate environment seem to have whetted investors' appetite for risk, and some of the tiniest, most speculative stocks have logged enormous gains. The Morningstar Small Cap Index was up 6.5% for the quarter. Among investing styles, value stocks beat growth in the first quarter. The best performer among Morningstar's nine style indexes for the quarter was Small Core Index, which gained 7.1%. The Large Growth Index—which tracks the performance of fast growing large cap stocks—was the worst performer with a return of -0.86% for the same period.

## Morningstar U.S. Market Index (Growth of \$10,000)



## Surveying the Sectors

Largely helped by casinos and hotels, but also by retail stores and restaurants, the consumer-services sector had the best returns by a significant margin, gaining an average of 8.3% through March 31, 2004. Among larger firms, Station Casinos led its industry with a 45% gain, and Mandalay Resort Group advanced 29% for the quarter. The rally in the sector was broad, however, with McDonald's and a swath of department stores, including May, Federated, and Nordstrom, all posting double-digit gains in the first three months of the year.

Software was the worst sector by far, losing more than 4%. Antitrust woes sank Oracle and Microsoft. Other software vendors, such as SAP, Computer Associates, and Veritas, took a breather after posting exuberant advances in 2003.

Software titan Microsoft also struggled as it failed to settle antitrust complaints with European Commission regulators. Microsoft has suffered a drop in its unearned revenue in recent quarters, which could indicate that some large customers are balking at signing big long-term software deals.

The hardware sector, in which most wireless-gear makers reside, was a mixed bag during the quarter. The shares of several big semiconductor, computer, and network-equipment companies, such as Intel, Cisco, and Dell, gave back some of the ground they gained in 2003.

The picture in the health-care sector was similarly mixed. Large-cap drug stocks languished. Abbott Laboratories, Bristol-Myers Squibb, and Wyeth each posted double-digit losses as investors fretted about thin product pipelines, patent expirations, product approvals, and operational issues. Meanwhile, some smaller-cap biotech and specialty pharmaceutical stocks continued to flourish.

### Morningstar Sectors (% Return)

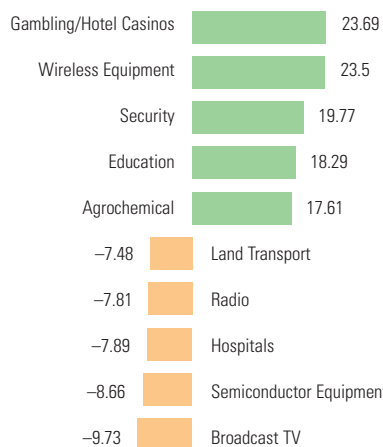
	Quarter	1 Year	3 Year		Quarter	1 Year	3 Year		Quarter	1 Year	3 Year
<b>Information</b>	<b>0.54</b>	<b>47.40</b>	<b>-3.26</b>	<b>Service</b>	<b>3.69</b>	<b>42.40</b>	<b>7.83</b>	<b>Manufacturing</b>	<b>2.50</b>	<b>44.70</b>	<b>8.17</b>
Software	-4.26	30.60	-0.45	Healthcare	0.43	26.40	3.31	Consumer Goods	4.43	38.50	9.03
Hardware	2.24	69.90	-1.95	Consumer Services	8.30	45.60	12.00	Industrial Materials	0.27	54.80	8.22
Media	-2.88	31.90	-3.80	Business Services	-0.48	41.50	12.60	Energy	2.08	41.40	8.51
Telecom	2.64	39.90	-5.93	Financial Services	4.79	51.90	8.76	Utilities	5.60	42.40	4.01

## Industry Performance

As some consumers felt their wallets a bit fatter and their confidence slightly higher, they increasingly sought leisure activities in late 2003 and early 2004. The gambling, hotel,

and casino industry was the best performer for the quarter, surging 23.7% through March 31, 2004.

### Top and Bottom 5 Industries 1st Quarter (% Return)



Wireless-equipment firms did nearly as well, gaining an average of 23.5%. Strong demand for wireless phones and increased business spending boosted the fortunes of wireless-infrastructure stocks both large and small. Brand-name handset manufacturers, such as Nokia and Motorola, and small speculative players, such as Sierra Wireless, a maker of modems for handheld computers and other devices, benefited.

Makers of semiconductor-manufacturing equipment ceded ground—losing 8.7% for the quarter. After posting stellar gains ranging from 50% to more than 100% in 2003, many of that industry's biggest constituents including Applied Materials, KLA-Tencor, ASML Holding, Novellus Systems, and Lam Research—backslid. Many of these companies' prospects remain strong, but they are notoriously volatile due to their cyclical nature.

## Value Outperforms Growth

A strong performance by several financial-services stocks helped value stocks beat growth stocks in the first quarter. And thanks to a broad rally among an eclectic mix of stocks in the small cap category, the Morningstar Small Cap Index pulled well ahead of its larger-cap counterparts. Here is a closer look at how each of the nine Morningstar style indexes fared during the quarter.

### Morningstar Large Growth Index: -0.86%

Retreating technology stocks, such as Microsoft, Intel, Cisco, Oracle, and Veritas, swamped advances by AT&T Wireless, Wal-Mart, and Qualcomm, making the Morningstar Large Growth Index, which lost almost 1%, the poorest performing benchmark of the quarter.

Also weighing on the large-growth index were media and entertainment stocks such as Viacom, Time Warner, and Liberty Media Corp. Such stocks posted decent gains

in 2003 as investors bet an improving economy and the 2004 presidential election would help strengthen the advertising market. After that runup, it wasn't surprising that these issues began the year with a pullback.

### Morningstar Mid Growth Index: +3.56%

The Morningstar Mid Growth Index advanced 3.6% through March 31, as selected health-care and hardware sector stocks, including biotech firm Biogen Idec and Juniper Networks, posted strong gains. Offsetting this, however, were semiconductor-equipment makers such as Novellus and software firms such as Siebel Systems, which both fell by double digits.

Biogen Idec rose more than 50% as it became clearer that the company's multiple sclerosis drug Antegren had a good chance of reaching the market. Meanwhile, investors excited by a stronger-than-expected rebound in demand for Juniper's products bid up its shares by nearly 40%.

On the other hand, Novellus fell with other chip-equipment stocks that gave back gains after a strong 2003, and Siebel dropped by 17% due to worries about software license sales.

### Morningstar Small Growth Index: +6.19%

The Morningstar Small Growth Index, the best performing diversified domestic-equity benchmark of 2003, held on to its momentum in the first quarter of 2004. The bogy started losing steam in the latter weeks of the period, but still posted a gain of more than 6% for the quarter.

Wireless-equipment maker Andrew Corp. bolstered the index, as did Internet firm Ask Jeeves, which advanced more than 95% for the quarter. Biotech stocks such as Protein Design Labs, Affymetrix, and Nektar Therapeutics also gained.

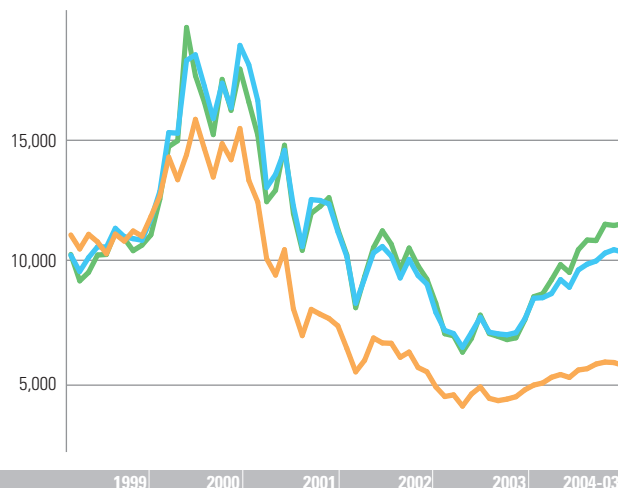
### Morningstar Large Core Index: +1.86%

A lot of pundits predicted investors would shift to so-called high-quality companies this year after gorging themselves on smaller, more speculative names in 2003. One look at the Morningstar Large Core Index, however, shows that the long-awaited rally in "high quality" stocks—those with solid track records of profitability, good prospects for continued growth, and firm balance sheets—didn't really get started in the first quarter.

A few blue chips did rise. Insurer AIG gained nearly 8% through March 31, due to successful acquisitions and improved growth prospects for its Asian business.

## Growth of \$10,000

- Morningstar Large Growth
- Morningstar Mid Growth
- Morningstar Small Growth



### Morningstar Large Growth

Total Returns %	42.59	-33.51	-29.07	-33.15	30.65	-0.86
Price/Earnings	53.00	46.06	50.85	32.83	39.24	38.35
Price/Book	17.27	11.77	7.38	6.05	6.06	6.15
Dividend Yield %	0.20	0.14	0.21	0.64	0.53	0.53
Earning Growth (5 Yr)	25.31	27.88	20.52	16.50	16.40	17.38

### Morningstar Mid Growth

Total Returns %	52.46	-11.10	-21.59	-32.54	40.02	3.56
Price/Earnings	46.11	42.90	39.87	33.78	35.47	35.73
Price/Book	12.51	8.38	6.41	4.64	5.63	5.57
Dividend Yield %	0.15	0.12	0.09	0.18	0.25	0.28
Earning Growth (5 Yr)	29.45	28.18	24.17	19.77	17.97	19.61

### Morningstar Small Growth

Total Returns %	46.80	-12.10	-12.92	-36.87	52.64	6.19
Price/Earnings	43.16	30.63	35.43	30.55	37.70	38.11
Price/Book	10.23	5.66	4.24	3.94	5.42	5.38
Dividend Yield %	0.06	0.04	0.06	0.11	0.13	0.15
Earning Growth (5 Yr)	28.65	30.60	25.66	21.75	21.78	22.39

Restaurant chain McDonald's also advanced about 15% as it shifted its focus from expansion to increasing sales at existing sites.

However, some of the best performing stocks in the index during the quarter, such as Lucent Technologies and Motorola, are more turnaround stories than high-quality companies. And lagging pharmaceutical stocks such as Abbott and Wyeth also dragged on the index. Cable television provider Comcast, whose shares dropped after its brazen attempt to buy Walt Disney, also proved detrimental.

### Morningstar Mid Core Index: +5.61%

Homebuilders helped fuel a nearly 6% gain in the Morningstar Mid Core Index. Historically low interest rates, strong demand and tight supply for new homes, and consolidation among mom-and-pop developers continued

to push stocks such as D.R. Horton, Lennar, and Pulte Homes higher. Oil and gas services stocks, such as B.J. Services and Smith International, also benefited as high oil and natural-gas prices improved the prospects for new exploration and drilling.

### Morningstar Small Core Index: +7.19%

A mixed bag of stocks helped propel the Morningstar Small Core Index to a more than 7% gain through March 31, making it the top-performing benchmark for the quarter. Insurer Fremont General, savings and loans Indymac Bancorp, and retailer American Eagle Outfitters made prominent contributions. In a sign of the times, InVision Technologies, a maker of an explosive-detection system used in airports, was one of the best performing stocks with a 48% gain.

### Morningstar Large Value Index: +2.18%

The Morningstar Large Value Index put up a respectable 2.2% gain for the quarter. Financial-services giants such as the merging J.P. Morgan Chase and Bank One, as well as Citigroup and Washington Mutual led the field. Securities firm Lehman Brothers, which is well-known for its bond business, rose as its efforts to build its equity business bore fruit. Major energy companies, such as ExxonMobil and ConocoPhillips, benefited from high oil prices.

### Morningstar Mid Value Index: +6.21%

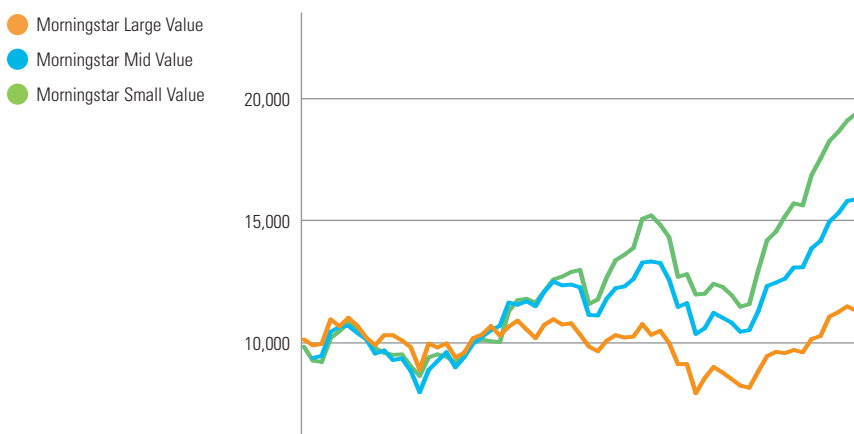
The Morningstar Mid Value Index was among the top-performing benchmarks of the quarter with a 6.2% gain through March 31. An eclectic mix of stocks served as the index's impetus.

Retailer J.C. Penney rose as it made progress in the fourth year of a five-year plan to overhaul its department-store operations. The retailer also said it would sell its Eckerd chain of drugstores. Simon Property Group, which controls nearly one third of the best malls in America, rose as low interest rates, tax cuts, and high levels of cash-out refinancing of home mortgages kept shopping centers busy.

### Morningstar Small Value Index: 6.21%

The Morningstar Small Value Index also was among the best performing benchmarks. Financial stocks such as health-care REITs Ventas and Healthcare Realty Trust were among the index's top performers, as were mining firms Stillwater Mining and Coeur d'Alene Mines. The miners benefited, respectively, from high prices for palladium and gold.

Growth of \$10,000



	1999	2000	2001	2002	2003	2004-03
<b>Morningstar Large Value</b>						
Total Returns %	0.57	5.66	-3.38	-15.05	26.26	2.18
Price/Earnings	23.30	21.50	22.83	21.33	18.38	18.14
Price/Book	5.20	4.75	3.33	2.38	3.08	3.04
Dividend Yield %	2.51	1.97	2.55	3.29	2.76	2.83
Earning Growth (5 Yr)	11.05	12.20	10.59	9.21	8.63	9.55
<b>Morningstar Mid Value</b>						
Total Returns %	-6.83	24.59	5.66	-10.00	35.93	6.21
Price/Earnings	18.68	16.79	17.95	18.21	18.25	19.16
Price/Book	2.08	2.68	1.99	1.67	2.19	2.29
Dividend Yield %	3.63	3.04	3.29	3.71	2.61	2.23
Earning Growth (5 Yr)	8.88	9.67	8.94	8.69	8.35	9.10
<b>Morningstar Small Value</b>						
Total Returns %	-5.19	18.65	18.58	-8.24	48.87	6.21
Price/Earnings	17.46	15.45	20.30	18.23	21.71	22.57
Price/Book	1.85	1.81	2.25	1.52	2.27	2.29
Dividend Yield %	3.46	3.64	3.22	3.72	2.32	2.83
Earning Growth (5 Yr)	10.50	9.87	9.60	8.67	8.60	9.09

## Active Managers Trail Benchmarks

One quarter won't settle the long-running debate over the merits of active versus passive investment management. The first three months of the 2004, however, went to the active managers, by a nose.

In six of the nine domestic style-box categories, the returns of the average mutual fund beat those of Morningstar's benchmarks through March 31. The winning indexes were Large Core, Mid Core and Mid Value, Small Value, Small Core and Small Growth.

Large-cap managers provided a very short-term rebuttal to the notion that passive management is tough to beat in efficient markets. The large-growth, large-blend, and large-value categories each topped their respective indexes by nearly a full percentage point. The disparity was most notable in the large-growth category, where the index lost nearly 1% for the quarter, while the average large-growth fund gained more than 1.4%.

Meanwhile, in less-efficient mid-caps and small caps, the indexes tended to outperform. Active managers added only a bit of value in the small-value and mid-cap growth categories. These results seem to uphold what is known as Dunn's law, developed by Oregon neurologist-turned portfolio-theorist William J. Bernstein and his colleague, Steve Dunn. The law posits that in the short term, when an asset class does well (as mid-caps and small caps did), its corresponding index does even better.

## Conclusion

At the end of the first quarter of 2004, the equity market appeared to be at a crossroads.

Stocks bounced around in the waning days of the period as concerns about terrorism, jobs, valuations, and company-specific issues swirled. Despite cooling off, though, stocks still looked expensive. Some outstanding investors, including Warren Buffett, First Eagle Global's Jean-Marie Eveillard, and the team running Clipper Fund, currently have significant cash holdings because they believe the U.S. market is pricey.

Here at Morningstar, just under 5% of the stocks covered by our stock analysts currently are undervalued enough to have 5 stars. As the end of the quarter neared, Morningstar's market valuation graph also indicated stocks were overvalued.

Given the environment, investors would do well to exercise caution going forward. In the first quarter, no one sector or industry dominated the performance of the Morningstar Indexes, and it paid to be selective. Expect more of the same in the future.

It also isn't too late for investors to rebalance their portfolios. With interest rates at historic lows and poised to increase, the decision isn't as simple as trimming stock exposure and adding to bond holdings. Nevertheless, it's probably a good idea to rein in bets on lower-quality small- and mid-cap growth equities, and reallocate money to issues with more attractive valuations further up the market cap and quality spectrum, and even overseas.

—Dan Culloton and Todd Trubey, Fund Analysts

	Value	Core	Growth
Large Cap	55.6 2.2	44.5 1.9	91.1 -0.9
Mid Cap	40.5 6.2	28.2 5.6	51.5 3.6
Small Cap	12.2 6.2	19.6 7.2	29.5 6.2

### Active vs. Passive, 2004

○ Percent of actively managed mutual funds outperforming their respective benchmark

● Index Returns (%) for 1st Quarter

Includes the oldest share class for all U.S. diversified mutual funds with at least one-year history. As of March 31, 2004, there were 2,347 eligible funds. Morningstar classifies funds into style categories based on the average style score (using the same 10-factor methodology as the underlying benchmarks) of all available portfolio holdings over three-year period.

### Value Fund Manager Darlings

	# Funds	3 Month	1 Year	3 Year
Citigroup	319	7.33	53.85	6.51
ExxonMobil	263	2.05	21.86	3.13
Altria Group	225	1.3	90.69	9.26
Bank of America	267	1.68	25.7	17.48
J.P. Morgan Chase & Co.	245	15.14	82.67	0.83
ChevronTexaco	236	2.45	40.25	3.08
Fannie Mae	182	-0.25	16.54	-0.35
Wells Fargo	219	-3.01	29.63	6.92
Verizon Communications	261	5.26	7.72	-5.83
Pfizer	233	-0.31	14.47	-3.61

### Growth Fund Manager Darlings

	# Funds	3 Month	1 Year	3 Year
Microsoft	404	-8.91	3.63	-2.72
Cisco Sys	427	-2.72	81.59	14.22
Pfizer	382	-0.31	14.47	-3.61
Intel	410	-15.01	67.69	1.43
General Elec	297	-0.84	22.75	-7.88
American Intl Group	270	7.75	44.78	-3.68
Dell	378	-1.06	23.11	9.38
Citigroup	305	7.33	53.85	6.51
Amgen	382	-5.89	1.04	-1.14
UnitedHealth Group	224	10.81	40.66	29.57

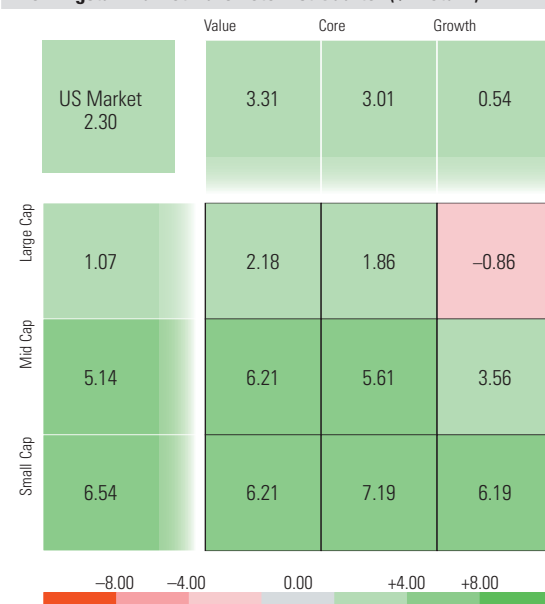
Value and Growth Fund Darlings represent the most widely held stocks held by value and growth fund managers. Rankings based on aggregate market value of stocks held. Data as of March 31, 2004.

# Morningstar Market Commentary

## Trailing Returns %

	Qtr	6-Month	1-Yr	3-Yr	5-Yr	10-Yr
Morningstar Indexes						
US Market	2.30	15.00	37.93	1.64	-0.28	11.24
.....						
Large Cap	1.07	12.92	32.39	-0.97	-3.25	11.04
Mid Cap	5.14	19.63	49.59	7.77	7.33	11.23
Small Cap	6.54	22.78	64.28	12.11	12.43	11.36
.....						
US Value	3.31	19.07	43.54	5.98	5.03	NA
US Core	3.01	14.93	37.47	2.07	2.30	NA
US Growth	0.54	11.33	33.71	-4.25	-8.83	NA
.....						
Large Value	2.18	17.83	39.00	3.50	2.56	NA
Large Core	1.86	12.34	31.77	-1.39	-0.72	NA
Large Growth	-0.86	9.16	27.63	-6.10	-12.16	NA
.....						
Mid Value	6.21	21.48	51.40	11.41	10.95	NA
Mid Core	5.61	21.23	51.61	11.90	9.73	NA
Mid Growth	3.56	15.78	45.37	-0.76	0.37	NA
.....						
Small Value	6.21	24.23	67.89	18.60	16.08	NA
Small Core	7.19	23.87	60.11	15.10	18.68	NA
Small Growth	6.19	20.41	66.10	3.17	3.66	NA

## Morningstar Market Barometer 1st Quarter (% Return)



## Morningstar Market Barometer Trailing 4 Quarters (% Return)

### 2nd Quarter 2003

18.16	15.05	12.05
18.61	16.95	19.71
25.85	19.99	25.51

### 3rd Quarter 2003

-0.16	1.95	4.35
5.07	6.94	4.88
7.38	7.73	9.90

### 4th Quarter 2003

15.32	10.29	10.10
14.38	14.79	11.80
16.96	15.57	13.40

### 1st Quarter 2004

2.18	1.86	-0.86
6.21	5.61	3.56
6.21	7.19	6.19

## Biggest Positive Influence on Morningstar US Market Index

	Style	Contribution %	3 Month	1 Year	3 Year
AT&T Wireless Services Inc.	■	0.18	70.34	129.05	-9.67
Wal-Mart Stores Inc.	■	0.17	12.76	18.17	7.87
Citigroup Inc.	■	0.16	7.33	51.97	4.98
PepsiCo Inc.	■	0.12	15.85	32.92	7.23
J.P. Morgan Chase & Co.	■	0.11	15.14	100.80	0.62
American Intl Group Inc.	■	0.11	7.75	45.88	-2.74
Bank One Corp.	■	0.10	20.57	56.25	17.91
Qualcomm Inc.	■	0.10	23.05	71.80	8.59
Motorola Inc.	■	0.09	26.00	104.76	6.87
Biogen Idec Inc.	■	0.08	51.50	70.67	2.47

## Biggest Negative Influence on Morningstar US Market Index

	Style	Contribution %	3 Month	1 Year	3 Year
Intel Corp.	■	-0.22	-15.01	58.77	-0.55
Microsoft Corp.	■	-0.19	-8.92	1.93	-2.33
Abbott Laboratories	■	-0.06	-11.28	20.89	-0.51
Viacom Inc. Cl B	■	-0.06	-11.51	0.65	-6.67
Bristol-Myers Squibb Co.	■	-0.06	-14.30	21.75	-20.13
Wyeth	■	-0.05	-11.00	9.20	-9.46
Time Warner Inc.	■	-0.04	-6.28	46.27	-25.47
Oracle Corp.	■	-0.04	-9.30	-2.01	-5.94
Comcast Corp. Cl A	■	-0.04	-12.29	1.72	-11.65
Amgen Inc.	■	-0.04	-5.89	2.45	-1.81

Biggest Influence on quarterly performance is calculated by multiplying stock returns for the quarter with their respective weight in the Index as of the start of the quarter.

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