

**COMMENTS: INDEX RESULTS, period ending August 30, 2002**

	<u>YEAR</u>	<u>YEAR</u>	<u>YEAR</u>	<u>YTD</u>	<u>CURRENT</u>
<u>STOCKS</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>MONTH</u>
S&P 500	19.6%	(10.1)%	(13.0)%	(20.2)%	5.5%
S&P 500 Growth	28.8%	(22.2)%	(13.0)%	(20.4)%	5.3%
S&P 500 Value	12.6%	6.1%	(12.0)%	(18.7)%	6.1%
Dow Jones	25.2%	(6.2)%	(7.1)%	(13.5)%	4.0%
NASDAQ Comp.	85.6%	(39.3)%	(21.0)%	(32.5)%	2.8%
Ext/MidCap US	25.0%	2.6%	(4.8)%	(15.0)%	4.7%
Small Cap US	19.6%	(4.2)%	1.0%	(19.0)%	1.7%
Intl, EAFE	25.3%	(15.2)%	(22.6)%	(11.0)%	2.7%

**BONDS, Interm.**

Taxable	(0.8)%	11.3%	8.3%	5.0%	1.6%
Tax-Exempt	(2.9)%	9.2%	5.0%	6.3%	0.6%

	<u>1999</u>				<u>2000</u>				<u>2001</u>			
	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>
<b>S&amp;P 500</b>	4.1	7.6	(7.7)	15.6	2.0	(3.0)	(1.3)	(7.8)	(12.1)	4.8	(13.8)	8.1
<b>NASDAQ COMP</b>	14.6	10.0	0.0	61.0	12.4	(14.8)	(7.2)	(29.6)	(25.5)	12.9	(26.7)	18.3
<b>BONDS: Interm. Taxable</b>	0.0	(0.5)	0.4	(0.7)	2.4	1.5	3.1	4.3	3.2	0.8	4.3	0.0

	<u>2002</u>			
	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>
<b>S&amp;P 500</b>	0.0	(13.8)		
<b>NASDAQ COMP</b>	(5.5)	(19.5)		
<b>BONDS: Interm. Taxable</b>	0.0	2.8		

**AUGUST 2002 COMMENTS**

**Balis Lewittes & Coleman, Inc. is moving September 13, 2002.**  
**Please make note of our new address for all correspondence:**  
**909 Third Avenue – 30<sup>th</sup> Floor**  
**NY, NY 10022**  
**All phone numbers will remain the same.**

During the five-week period of July 29<sup>th</sup> through August 30<sup>th</sup> 2002, STOCK PRICES were highly volatile, both up and down. By the end of this August period, stock prices were higher for the first period since March. Since stock prices were essentially flat during the first quarter of 2002, following substantial gains in the fourth quarter of 2001, the declines from April through July were both extensive and surprising, reaching 26% for the S&P 500, 18% for the Dow Industrials, and 35% for the NASDAQ Composite. The August gains reduced the year to date declines to 20% for the S&P 500, 13.5% for the Dow, and 32.5% for the NASDAQ (see page 1 for these and other related figures). (Note also that the results for this five-week period are different from the calendar month of August, as they include the last three days of July. Our time periods coincide with the last Friday of each month, which is the closing date for your Bear Stearns statements.)

Measured from the 2000 highs, the Bear Market of 2000-02 has delivered declines comparable to those of the 1973-74 period, but not yet approaching those of the 1929-32 period. (Our July 22<sup>nd</sup> Special Comments details the results for these periods.) The figures below set out both the extent of the 2\_-year decline, and the longer-term context of the 1995-99 Bull Market gains, with returns from 1995 through the July 2002 lows (see also figures on page 7).

	<u>S&amp;P 500</u>	<u>DOW</u>	<u>NASDAQ</u>
1st Qtr 2000 High	1,527	11,723	5,048
Year End 2000	1,320 (13)%	10,785 (8)%	2,470 (51)%
April 2001 Low	1,103 (28)%	9,390 (20)%	1,684 (67)%
Sept 2001 Low	965 (37)%	8,235 (30)%	1,425 (72)%
Year End 2001	1,148 (25)%	10,020 (17)%	1,950 (61)%
July 2002 Low	798 (48)%	7,702 (34)%	1,206 (76)%

**Context: Prior Five Year Gains in Bull Market of 1995 - 1999:**

End 1994	459	3,834	752
End 1999	<u>1,470</u>	<u>11,500</u>	<u>4,070</u>
Gain	1,011	7,666	3,318
Avg. Annual % Gain, '95-'99	26.2%	24.6%	40.2%
Avg. Annual % Gain, '95-7/02 Low	7.4%	9.5%	6.3%

### Dealing with the Bear Market

During early August, I (referring to Vic) attended a program hosted by a well-known investment advisory firm, which provides investment management and research but does not engage in investment banking or other activities that create conflicts with its investment advice. My primary reason for attending was to determine how this firm's advice compared to ours during this current, and most difficult, phase of the Bear Market. While our Monthly Comments cite a number of well-respected authorities writing in either the Wall Street Journal or New York Times, we think it is also important to know what others working directly with individual clients are advising. The following points (1) and (2) summarize the key information presented. You will find these points very familiar, as our advice, and the content of our Monthly Comments, closely parallels the advice of this firm.

- (1) Make a Plan and Stick with it. This refers to an asset allocation based on your particular circumstances, designed to meet your reasonable, long-term financial objectives without taking more risk than is needed. The Plan is designed not to be changed in the midst of a period of declining stock prices.
  - (a) In evaluating the degree of risk you need to take, likely investment returns should be aligned with your needs. Given the current low interest rates on bonds, annual pretax returns of 4-5% are reasonable expectations. For investors who have no, or insufficient, additional sources of earnings over and above their investment portfolios, the key question is, how long is your capital going to last if all, or most of it, is earning 4-5% pretax annually? While stocks obviously can decline in price, and are a risky asset class, they also have a long-term record of annual pretax returns approximating 10% (1926-2001). Therefore, some appropriate allocation to stocks is called for if your spending needs cannot be met by the returns from bonds. And those spending needs involve accounting for future inflation and lengthening life expectancies.
  - (b) Recent stock price declines, while substantial, are not a reason to sell stocks. If anything, lower stock prices create opportunity to buy stocks. This strategy is part of an approach referred to as rebalancing, which involves adding to the declining asset class (in this period, stocks) to restore the allocation to stocks and bonds previously determined to be appropriate for your situation. The advice to rebalance, or not, is specific to each client.
  - (c) Individual investors need to avoid the "rear view mirror" approach to investing, i.e. buying after stock prices rise and selling after they decline. This approach leads to buying high and selling low, just the opposite of what should be done.
  - (d) Investors should not try to time the market.
  - (e) All of this advice is premised on the history of favorable long-term returns of stocks compared to alternative liquid investments, and on the corresponding view that stock prices recover after declines.

- (f) Finally, the firm referred to the July 2002 declines as a “Four Standard Deviation event.” As relates to the stock market, Standard Deviation (SD) is the statistical measure of the range of stock prices. One SD covers the range of prices that occur 2/3 of the time; two SD is the range for 95% of time; and three SD is the range for 99%. Since there is no fourth SD, this is another way of saying that July's declines should be considered highly, highly unusual.
- (2) Diversify Your Portfolio. This includes your allocation to bonds, which is out of the stock market completely, as well as diversification within the stock market.
- (a) Diversification within the stock market (all of which has been discussed regularly in our Monthly Comments) relates to:
- (i) Size of companies: Largecap, Midcap, Smallcap
  - (ii) Style: Growth or Value
  - (iii) Geography: International in addition to U.S.
- (b) The benefits of diversification come from asset classes and categories within asset classes that have a low degree of correlation; that is, prices of the assets tend to move in different directions, or not as much in the same direction, in a given time frame. Owning a large number of securities whose prices are highly correlated does not provide diversification.

### Is There a Recovery In Our Near Future?

As you know, we avoid any short-term predictions on the direction of stock prices, but rather rely on the long-term history of stock price gains as the basis for our advice regarding allocations to the stock market. However, since the near-term is always on everyone's mind, some observations on this question are appropriate.

Even though the declines of the last 2\_ years have certainly made stock prices cheaper, there are many who argue that stock prices are still too high relative to current and projected earnings. The weakness in earnings relates directly to an overall economy that has little if any growth at the moment, and to certain key sectors that are still contracting. While the media furor casting doubt on reported earnings has subsided for the moment, the earnings credibility issue adds to investor uncertainty.

The hope is that economic activity is cyclical, and that slow growth and no growth periods typically are followed by higher growth rates, leading to improved profits and higher stock prices. Therefore, the strength of the economy is the key issue, and the timing of the economic recovery is the key to the timing of improved stock prices. This conclusion presupposes no additional international political crises, and no major additional earnings credibility problems.

### The Difficulty of Picking Individual Stocks

As many of you know, we present our "Informed Investing" Seminar at various times and places during the year. In updating the Seminar for Fall 2002, the following chart --which sets out the P/E (Price/Earnings Ratio) and Total Market Value of fifteen of the largest U.S. companies for the five years 12/31/1997 through 12/31/2001, and to 8/30/02-- is of particular interest.

Value in \$ Billions	1997		1998		1999		2000		2001		8/30/02	
	P/E	VAL	P/E	VAL	P/E	VAL	P/E	VAL	P/E	VAL	P/E	VAL
<b>General Electric</b>	30	240	38	339	48	507	37	475	28	400	20	300
<b>Microsoft</b>	40	155	57	346	73	602	24	230	61	357	35	265
<b>Exxon Mobil</b>	18	150	28	177	35	196	19	305	18	263	23	237
<b>Citigroup</b>	n/a	□100	n/a	□160	20	187	19	255	18	258	10	171
<b>Walmart</b>	n/a	□100	42	183	55	308	37	240	38	253	32	235
<b>Pfizer</b>	n/a	□100	85	162	n/a	□180	78	290	33	248	25	205
<b>Intel</b>	16	115	35	197	40	275	20	200	165	208	56	110
<b>AIG Insurance</b>	n/a	□100	n/a	□160	n/a	□180	41	225	38	207	28	163
<b>IBM</b>	17	104	28	170	26	194	n/a	□200	28	205	26	128
<b>Cisco</b>	n/a	□100	n/a	□160	146	366	93	275	neg.	131	55	101
<b>Merck</b>	28	127	33	174	n/a	□180	32	215	19	130	16	111
<b>Coca Cola</b>	40	165	46	165	n/a	□180	n/a	□200	29	118	31	128
<b>Procter &amp; Gamble</b>	30	107	n/a	□160	n/a	□180	n/a	□200	38	102	29	115
<b>Philip Morris</b>	17	110	n/a	□160	n/a	□180	n/a	□200	12	97	11	105
<b>Lucent</b>	n/a	□100	n/a	□160	69	235	n/a	□200	neg.	17	neg.	6
<b>S&amp;P 500: T = \$ Trillions</b>	20	7.6T	25	9.6T	28	11.3T	24	10.3T	25	9.2T	20	7.3T

To fully understand the chart, you need to note the following:

- (1) P/E is the relationship of the price of the stock (per share) to its earnings (per share). P/E ratios are discussed regularly in these Monthly Comments. For the figures in the chart, the P/E reflects the period-ending stock price and the most recent four quarters of actual published earnings per share for each relevant period. The accounting issues that have come to the forefront in 2002, and have cast doubts on reported earnings, did not create any changes in the earnings figures used in the chart.
- (2) Market Value is determined by multiplying the price per share by the total number of shares outstanding.
- (3) Making the List: For 1997, the nine largest U.S. companies all had market values in excess of \$100 billion; by 1998, the nine largest (not necessarily the same nine) had market values in excess of \$160 billion; by 1999, the nine largest had market values in excess of \$180 billion; and in 2000, an expanded list of the ten largest companies had market values in excess of \$200 billion. The 2001 list of fifteen traces the fate of each company that at one time or another from 1997 to 2000 grew large enough to make that year's cutoff.

The chart is instructive on a number of points:

- (1) In a lesson now clearly understood, the prices of even the largest and most successful of companies can decline significantly.
  - (i) GE declined 20% from its 1999 close to the end of 2001, and 40% as of 8/30/02. Note that it is still up 25% from its 1997 value, which is approximately a 5% annualized gain.
  - (ii) Microsoft declined by over 60% from its 1999 close to its 2000 close, but has recovered from its lows. The stock is up 70% from its 1997 close to 8/30/02, which is approximately a 12% annualized gain.
  - (iii) Citigroup, which had done well in the down years of 2000 and 2001, has declined 33% from its 2001 close to 8/30/02.
  - (iv) Merck declined 40% from 2000 to 2001 and has continued its decline. As of 8/30/02, it is down over 48% from 2000.
  - (v) Cisco, from 1999-2001, declined by over 60% and has continued its decline. As of 8/30/02, it is down 72% from 1999.
  - (vi) Lucent, once a Wall Street darling, has all but disappeared, down more than 95% from its 1999 high.
- (2) Does it appear possible to pick, in advance of the occurrence, those stocks whose prices have held their value, as compared to those stocks that have not held up well? Notice that Merck, Coca Cola, P&G, Philip Morris, and Lucent have all had negative investment returns from 1997 through 2001 (without even including 2002). And of the ten winners from 1997 through 2001, only Citigroup and IBM grew in each of the five years, and each of these stocks has had a significant 2002 decline (33% and 40% respectively from their 2001 closing prices). The other eight companies all reached price levels during the five-year period that exceeded their 2001 closing price, some by extreme amounts (Microsoft, 40%; Intel, 25%; Cisco, 60%).
  - (a) In the investment world, all the active stock pickers, whether individuals or professional mutual fund or other institutional managers, are engaged in just such an effort, believing they can pick stocks that will do better than the broad market averages (i.e., the indexes). They may succeed for a time, but over the long term, it is extremely difficult to identify ongoing outperformers.
- (3) All of these companies are large, and well-known, and covered by many professional analysts. Nonetheless, many of the stock prices show major volatility. Stocks are bought on the way up and sold on the way down, with individuals and professional managers most often running with the herd. If the largest companies are subject to these kinds of price swings, do you want to try and pick the future outperformers?

	<u>S&amp;P 500</u>		<u>Dow</u>		<u>NASDAQ</u>	
<b><u>I. Figures From Period Starting 2001 (% Figures Are Declines From 1/01/01)</u></b>						
Start of 2001	1,320		10,785		2,470	
Sept. 21, 2001 <u>Low</u>	965	(26.9)%	8,235	(23.7)%	1,425	(42.3)%
End of 2001	1,148	(13.0)%	10,020	(7.1)%	1,950	(21.0)%
July 2002 <u>Low</u>	798	(39.5)%	7,702	(28.5)%	1,206	(51.0)%
August 30, 2002	916	(30.6)%	8,663	(19.7)%	1,315	(46.8)%

<b><u>II. Figures From Period Starting 2000 (% Figures Are Declines From 1/01/00)</u></b>						
Start of 2000	1,470		11,500		4,070	
End of 2000	1,320	(10.1)%	10,785	(6.2)%	2,470	(39.3)%
End of 2001	1,148	(13.0)%	10,020	(7.1)%	1,950	(21.0)%
Two Years		(21.8)%		(12.8)%		(52.0)%
August 30, 2002	916	(37.7)%	8,663	(24.7)%	1,315	(67.7)%

<b><u>III. Figures From Period Starting 1995 (% Figures Are Gains From 1/01/95)</u></b>						
Start of 1995	459		3,834		752	
End of 1999	1,470		11,500		4,070	
End of 2001	<u>1,148</u>		<u>10,020</u>		<u>1,950</u>	
5 Yr Gain; Annualized %	1,011;	26.2%	7,666;	24.6%	3,318;	40.2%
7 Yr Gain; Annualized %	689;	14.0%	6,186;	14.7%	1,198;	14.6%
August 30, 2002	<u>916</u>		<u>8,663</u>		<u>1,315</u>	
7yr&8mo Gain; Annual. %	457	9.4%	4,829	11.2%	563	7.5%