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FINANCIAL MARKET OVERVIEW

The U.S. stock market is finally showing signs that it may be coming back to "normal times" after a brutal two years, the September 11th terrorists attacks, and the Enron Corp. bankruptcy disaster earlier this year. Top quality stocks are leading the way with the Dow Jones Industrial Average ending up 3.8% during the first quarter, 2002. The Standard & Poor's 500 (index of the largest 500 U.S. stocks) ended the quarter flat – down less than 1% and the NASDAQ Composite Index of smaller growth and tech stocks ended the quarter down 5.4%. We are not out of the woods yet. Several companies are still reporting flat or declining earnings and these surprise announcements often adversely impact the stock market on any given day. The fears of a gradual recession are fading and oddly, the most recent concern is the potential adverse impact of a gradual increase in interest rates.

Alan Greenspan lowered bank borrowing rates 11 times in 2001. Interest rates were lowered to combat a potential recession following the correction in large-company growth stocks – mainly tech stocks. The September 11th terrorist attacks brought another round of aggressive interest rate cuts in an effort to calm the global financial markets. From an economic perspective, the aggressive rate reductions were not justified. Now, we share the concern that rates will likely be moved back up to where they were prior to the terrorists attacks. In fact, interest rates have already begun to move back up. Initially, interest rate increases are viewed negatively by both stock and bond investors. The price (or value) of bonds and bond mutual funds has already moved downward. In the first quarter 2002, intermediate and long-term bonds and bond mutual fund prices have declined by 2% to 3%. This decline in principal value completely offsets the interest income received on the bonds. Below are sample returns of specific categories of stocks and broad market indexes for the **first quarter 2002:**

Return	Category
+ 3.8%	*Dow Jones Industrial Average*
- 0.6%	*Standard & Poor's 500 Index*
+ 1.0%	*Wilshire 5000 (broad market)*
- 5.8%	*NASDAQ (dominated by tech)*
- 2.9%	*Large-company growth*
+ 1.8%	*Large-company value*
- 3.8%	*Mid-size growth*
+ 6.3%	*Mid-size value*
- 2.6%	*Small-company growth*
+ 8.7%	*Small-company value*
+ 1.2%	*International*
- 7.9%	*Technology*
- 7.6%	*Health/Biotechnology*
+ 7.9%	*Real Estate*

Investment Strategy

Individual investors and professional investment advisors should have a sound basis and systematic process or methodology for their investment selection and portfolio management process. While this premise is simple, there are literally hundreds of different strategies and approaches to the investment selection process. Further, different approaches seem to work better than others do under varying economic circumstances. But very few strategies will be consistently successful beyond a short period of time.

In our opinion, the primary goal is to "stay in the game" and attain investment results that are better than 70% of all other investors with the *same target return objectives and similar risk tolerance*. A simple analogy can be found in sports. The best athletes focus on consistent performance over the entire season or

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match. They don't alter their game plans, take enormous risks, or alter their basic strategy because of short-term problems or unexpected events.

When applied to the wealth management process, investors should select and maintain a systematic investment management process or methodology that works best over a long-term evaluation period. Below are important characteristics of a successful long-term investment strategy:

1) Overall or total portfolio return is more important than the performance of individual securities.

2) Avoiding big losses in bear markets is more important than achieving extraordinary gains in bull markets. Investors must be willing to trade the opportunity to earn an exceptionally high short-term return in exchange for avoiding devastating losses that severely impact long-term investment results.

3) Infrequent trading improves investment results by minimizing income taxes and transaction costs (commissions). Each time a change is made to an investment portfolio, not only does the move have the potential to be incorrect, investors will also incur commission or transaction costs and a potential income tax liability. These costs can dramatically reduce investment performance.

In our opinion, the first step is to prepare a written *Investment Policy Statement*. This document requires an assessment of your rate of return objectives and willingness to accept the risk necessary to achieve the target return. In addition, your liquidity needs, income needs, income tax situation, time horizon and several other unique circumstances need to be considered before you even think about specific investment selection. It's the next step that I feel is the cornerstone of starting down the right path in formulating an investment strategy.

The Wisdom of Asset Allocation Verses Active Trading Strategies

Asset allocation is the foundation of a sensible long-term wealth-building plan. To be a successful investor over a long period of time, you *must* have a basis or starting point in the portfolio management process. To many, the starting point is deciding what stocks or other investments to purchase. However, investment selection is the *last step* in the process.

Asset allocation is simply the process of apportioning your total investment funds among categories of assets. Examples of common asset categories are: *cash equivalents, stocks, fixed income or bonds, real estate, etc.* Asset allocation affects both the risk and return of your total portfolio. For example, the larger the allocation of funds to stocks, the greater the risk and potential investment return.

Using an asset allocation model for your portfolio has the following benefits. The model serves as a blueprint for building an investment portfolio that matches your investment return objective without exceeding your risk tolerance. Simply stated, asset allocation creates boundaries and helps you maintain the desired exposure to different asset categories. More importantly, using the asset allocation model as a starting point or framework for making investment decisions forces you to include the three important characteristics identified above.

One, the focus of allocating your funds to various asset categories first before considering individual security selections places the emphasis on the total portfolio return, not the prospective performance of one or more individual investment selections. Two, spreading your funds over a variety of asset categories provides diversification. Diversification is the best the way to avoid large losses in bear markets. Three, while the asset allocation model allows enough flexibility to overweight certain asset classes that are expected to perform well, it also provides the discipline to maintain a minimum exposure in each asset category. This approach reduces the frequency and magnitude of making changes to your portfolio. Infrequent trading reduces commissions or transaction fees and reduces the frequency of paying income taxes on short-term gains.

Once the overall asset allocation decision has been made and the entire portfolio is divided into specific asset categories, the next step is deciding which SUBCATEGORIES to use within each broad asset class. For example, if an investor has decided that 65% percent of the total portfolio should be invested in stocks, which types of stocks should be included? It is

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important to note that we haven't yet arrived at the point in the process where individual stock or mutual funds are evaluated. The investor must decide how much of the 65% allocation to stocks should be invested in *growth* or *value stocks*, *large companies, midsize* or *small companies*, *international, global* or *U.S.* stocks.

Some investors and portfolio managers do not include this step in their portfolio management process. Their reasoning is that it doesn't matter whether the company is considered a growth stock or value stock or whether the company is large or small. If the company financials are strong and the product line or services are in high demand, then further classification is not necessary. This approach is referred to as "bottom-up", where the evaluation process begins at the company level without much regard to the overall economy, industry or the "big picture".

When analysts begin the evaluation process with an assessment of the overall economy and then determine what type of industries should perform well in that specific economic environment, the last step is identifying and evaluating which specific stocks or companies have the best competitive advantage within that industry. The latter method or process is referred to as a "top-down" approach. While both methods are acceptable and widely used in the security selection process, we prefer using the "top-down" approach before evaluating specific securities to purchase or sell.

While an evaluation of the overall economy is certainly a difficult and uncertain endeavor, we find the exercise is worth the effort. Certain subcategories perform better than others depending upon the economic environment. For example, during the late 1990's, *large-company growth stocks* (especially technology and internet-related companies) were very popular. The economy was strong and all companies found it necessary to update their computer hardware and information technology applications in preparation for the year 2000 (new millennium). The combination of a growing economy and very high demand sent stock prices of *large-company growth stocks* into the stratosphere.

The strategy of moving your funds into the "hot" stocks or into the best performing equity categories at the moment is referred to as an *active trading strategy*. Stock selections are based primarily on which stocks have the upward price momentum at the moment. This approach is very appealing and irresistible to most investors. It is also the approach that resulted in the most devastating loses to many investor portfolios when the market correction hit in March 2000. While using an asset allocation model would not have prevented losses in the *large-company stock* category during the year 2000, it did prevent investors from over-exposing their portfolio to this single asset subcategory. Chasing the "hot stocks", individual securities or mutual funds within the best-performing subcategory, is a losing proposition over a long-term evaluation period. The rotation of the hot stocks or best performing subcategory to the top of the performance chart is frequent and nearly impossible to predict. One year, large-company growth stocks are the best performing asset category followed by small-company value stocks in the following year. In support of this statement and assessment, we offer the charts on the following two pages.

The first chart simply ranks the performance of six different stock subcategories and one bond category from best to worst over the previous 18 years. The columns indicate the calendar years from 1984 to 2001 and the rows indicate performance with the best performing category in the top row and the worst performing category in the bottom row. For example, in the first year 1984, the *Bond* category performed best followed by *Large Value* stocks and so on. The worst-performing category was *Small Growth* stocks.

Several observations can be made. As the chart clearly illustrates, a strategy of trying to predict the best performing investment category for any year will have little success because top performing categories do not always repeat. Furthermore, the top performing category in one year often ranks among the bottom performers in subsequent years. Since no one can guess next year's top performing category, it makes sound investment sense to diversify your money into more than one investment category. This is exactly what asset allocation models do.

The first chart also illustrates which asset categories are the most volatile and unpredictable. The *International* stock category is the most volatile. Very rarely does this category fall into the middle section of relative performance. During most of the eighteen-year period, *International* stocks either perform very

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Ranking of Investment Categories from Best to Worst Over the Last 18 Years

Performance	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
BEST	Bond	Intern'l	Intern'l	Intern'l	Small Value	Large Growth	Bond	Small Growth	Small Value	Intern'l	Intern'l	Large Growth	Large Growth	Large Growth	Large Growth	Small Growth	Small Value	Small Value
	Large Value	Large Growth	Large Value	Large Growth	Intern'l	Mid Cap	Large Growth	Small Value	Mid Cap	Small Value	Large Growth	Large Value	Large Value	Small Value	Intern'l	Large Growth	Bond	Bond
	Intern'l	Mid Cap	Mid Cap	Large Value	Large Value	Large Value	Large Value	Mid Cap	Large Value	Large Value	Large Value	Mid Cap	Small Value	Large Value	Large Value	Intern'l	Mid Cap	Mid Cap
	Large Growth	Small Value	Bond	Bond	Small Growth	Small Growth	Mid Cap	Large Growth	Small Growth	Mid Cap	Small Value	Small Growth	Mid Cap	Mid Cap	Mid Cap	Mid Cap	Large Value	Small Growth
	Small Value	Small Growth	Large Growth	Mid Cap	Mid Cap	Bond	Small Growth	Large Value	Bond	Small Growth	Mid Cap	Small Value	Small Growth	Small Growth	Bond	Large Value	Intern'l	Large Value
	Mid Cap	Large Value	Small Value	Small Value	Large Growth	Small Value	Small Value	Bond	Large Growth	Bond	Small Growth	Bond	Intern'l	Bond	Small Growth	Bond	Large Growth	Large Growth
WORST	Small Growth	Bond	Small Growth	Small Growth	Bond	Intern'l	Intern'l	Intern'l	Intern'l	Large Growth	Bond	Intern'l	Bond	Intern'l	Small Value	Small Value	Small Growth	Intern'l

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Performance	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
BEST	Bond	Intern'l	Intern'l	Intern'l	Small Value	Large Growth	Bond	Small Growth	Small Value	Intern'l	Intern'l	Large Growth	Large Growth	Large Growth	Large Growth	Small Growth	Small Value	Small Value
	Large Value	Large Growth	Large Value	Large Growth	Intern'l	Mid Cap	Large Growth	Small Value	Mid Cap	Small Value	Large Growth	Large Value	Large Value	Small Value	Intern'l	Large Growth	Bond	Bond
	Intern'l	Mid Cap	Mid Cap	Large Value	Large Value	Large Value	Large Value	Mid Cap	Large Value	Large Value	Large Value	Mid Cap	Small Value	Large Value	Large Value	Intern'l	Mid Cap	Mid Cap
	Large Growth	Small Value	Bond	Bond	Small Growth	Small Growth	Mid Cap	Large Growth	Small Growth	Mid Cap	Small Value	Small Growth	Mid Cap	Mid Cap	Mid Cap	Mid Cap	Large Value	Small Growth
	Small Value	Small Growth	Large Growth	Mid Cap	Mid Cap	Bond	Small Growth	Large Value	Bond	Small Growth	Mid Cap	Small Value	Small Growth	Small Growth	Bond	Large Value	Intern'l	Large Value
	Mid Cap	Large Value	Small Value	Small Value	Large Growth	Small Value	Small Value	Bond	Large Growth	Bond	Small Growth	Bond	Intern'l	Bond	Small Growth	Bond	Large Growth	Large Growth
WORST	Small Growth	Bond	Small Growth	Small Growth	Bond	Intern'l	Intern'l	Intern'l	Intern'l	Large Growth	Bond	Intern'l	Bond	Intern'l	Small Value	Small Value	Small Growth	Intern'l

Ranking of Investment Categories from Best to Worst Over the Last 18 Years

Performance	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
BEST	Bond	Intern'l	Intern'l	Intern'l	Small Value	Large Growth	Bond	Small Growth	Small Value	Intern'l	Intern'l	Large Growth	Large Growth	Large Growth	Large Growth	Small Growth	Small Value	Small Value
	Large Value	Large Growth	Large Value	Large Growth	Intern'l	Mid Cap	Large Growth	Small Value	Mid Cap	Small Value	Large Growth	Large Value	Large Value	Small Value	Intern'l	Large Growth	Bond	Bond
	Intern'l	Mid Cap	Mid Cap	Large Value	Large Value	Large Value	Large Value	Mid Cap	Large Value	Large Value	Large Value	Mid Cap	Small Value	Large Value	Large Value	Intern'l	Mid Cap	Mid Cap
	Large Growth	Small Value	Bond	Bond	Small Growth	Small Growth	Mid Cap	Large Growth	Small Growth	Mid Cap	Small Value	Small Growth	Mid Cap	Mid Cap	Mid Cap	Mid Cap	Large Value	Small Growth
	Small Value	Small Growth	Large Growth	Mid Cap	Mid Cap	Bond	Small Growth	Large Value	Bond	Small Growth	Mid Cap	Small Value	Small Growth	Small Growth	Bond	Large Value	Intern'l	Large Value
	Mid Cap	Large Value	Small Value	Small Value	Large Growth	Small Value	Small Value	Bond	Large Growth	Bond	Small Growth	Bond	Intern'l	Bond	Small Growth	Bond	Large Growth	Large Growth
WORST	Small Growth	Bond	Small Growth	Small Growth	Bond	Intern'l	Intern'l	Intern'l	Intern'l	Large Growth	Bond	Intern'l	Bond	Intern'l	Small Value	Small Value	Small Growth	Intern'l

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well or very poorly. During the eighteen-year period, the *International* stock category performed best in 5 of those years and second best twice. On the other hand, the *International* stock category also ranked last seven times during this period.

The *Large Growth* stock category is also relatively volatile. The second chart isolates only the *Large Growth* category over the past eighteen years.

This is the category where many of the "hot stocks" with great growth stories are categorized. As you can see, this category is somewhat unpredictable. From 1984 through 1993, growth stock performance was very volatile – fifty percent of the time landing in the top 50% of relative performance and an equal number of times in the bottom half of performance. The period 1994 – 1999 was unprecedented and unusual. This was the time period where the technology and large-company stocks performed well – so well that the superior performance turned into a bubble that burst in 2000-2001. The category fell straight to the bottom.

The third and final chart illustrates the two asset categories that we favor over both the long and short-term time horizons. *Large-Company Value* stocks and *Mid-Cap* stocks have a consistent record of above-average and relatively predictable performance records. While neither category has performed as the absolute best over the past 18 years, they also have not recorded the worst performance either. The most important point to remember is that the average return in these two stock categories is still a very acceptable return for long-term wealth accumulation.

In summary, the asset allocation strategy gives you a starting point for assessing risk and return, provides a blueprint for selecting asset categories, creates boundaries, promotes diversification and infrequent trading and best of all, is one of the best long-term investment management strategies. We use asset allocation models for all of our clients because it provides a disciplined basis or framework for creating and maintaining a diversified portfolio.

You may have noticed that we have systematically reduced your exposure to *large-company growth* stocks and *international* stocks over the past three years. We have increased your exposure to *mid- cap* stocks, *small-company value* stocks and *large-company value* stocks. At this point in time, we expect to continue favoring these categories. Interestingly, international emerging stock mutual funds have begun to perform quite well this year after experiencing a four-year decline. We expect to begin shifting part of client funds into this category, however, this change is reserved for only above-average risk clients. We hope this discussion is helpful in understanding the purpose and benefits of using asset allocation as a starting point in the investment management process.

Bristol Myers Squibb Stock - Update

What's going on with Bristol Myers Squibb stock? In March, the company announced the FDA would not review its cancer drug, Erbitux, in which Bristol Myers Squibb had invested heavily with its partner ImClone. Bristol Myers wrote off $735 million of its $1.2 billion investment in ImClone. The stock price actually increased during the following 60 days. The rift raised eyebrows in that Bristol Myers Squibb was taking a hard-line position with its partner. Then, in late March, researchers announced that a promising new heart medication drug, Vanlev, was not more effective than a generic version of the same drug already on the market. The stock price immediately dropped from the mid-forties to the mid-thirties. Analysts had already expected that sales of Vanlev would begin in late 2002. Now, the company is set to begin FDA trials all over again. Since the expected revenue will not occur, the stock price was cut.

Disagreements and setbacks in FDA trials are a normal business occurrence for all drug companies. We did not view the latest setback as a reason to sell, especially since the stock price had already moved down in a matter of minutes.

In the first week of April, Bristol Myers Squibb announced it expected lower revenue and earnings as a result of the changes discussed above. Again, the stock price opened for trading over 20% below where the stock price closed the day before. Now, analysts believe a takeover by the giant Swiss drugmaker, Novartis, is a possibility.

We believe reactions to the news and the immediate stock price decline is an overreaction. We would only consider selling when the price recovers to its fair market valuation of $45 to $48 per share.