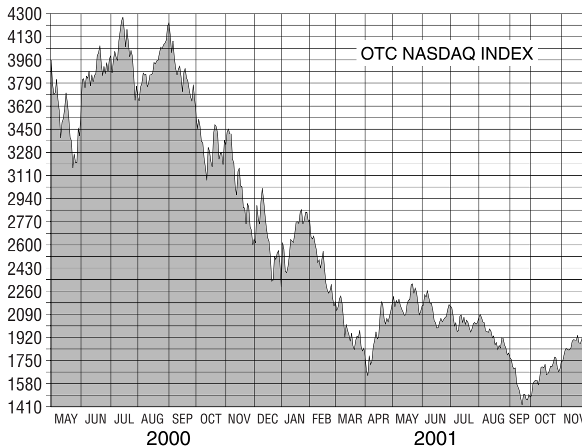
InvesTech® Research
Market Analyst

Vol01 Iss16 — Technical and Monetary Investment Analysis — NOV 30, 2001



4 Weeks Ending November 23, 2001

	HIGH	LOW	LAST
Financial			
Discount Rate	2.00%	1.50%	1.50%
Federal Funds	2.65%	1.93%	1.93%
10yr T-Bonds	5.04%	4.22	5.04%
Stock Market			
DJIA	9976.46	9075.14	9959.71
DJTA	2534.90	2195.26	2534.90
DJUA	300.24	286.47	289.14
NASDAQ	1934.42	1667.41	1903.20
Silver	4.29	4.07	4.07
Gold	282.00	274.10	274.50

A HUMBLE "TOLD YOU SO!"
[and another "whoops" for economists]

On our front page last March we wrote:

> "Do Wall Street analysts really believe the high tech crash is over, or that the Nasdaq will soon be back above 3,000? Do investors really buy the notion that a buy-&-hold strategy will always bail them out? Do they really trust Greenspan's reassurances that the economy is not going into recession? Well if so, then we have news for them… it isn't, it won't, it doesn't, and the economy **is already in** a recession. Over the past 3 months, Consumer Sentiment (University of Michigan) has taken its second sharpest plunge in 48 years. *The only other instance was in a recession.* This week, it was reported that Consumer Confidence (Conference Board) fell another whopping 9 points – making its 3-month drop the 6th largest on record. *In all 5 other instances, the economy was already in a recession.* And today, the NAPM (Purchasing Managers') report registered its second monthly reading below 45 – a level hit on only 5 occasions in the past 33 years. *Again, all 5 were in recessions!*"
>
> ***InvesTech Market Analyst** – March 2, 2001*

> **Panel: U.S. Recession Began in March**
>
> It's official. The National Bureau of Economic Research announced Monday that the United States entered a recession in March, the month in which the longest expansion in U.S. history celebrated its 10th anniversary.
>
> ***The New York Times** – November 26, 2001*

OK, the NBER didn't backdate the starting point as much as we expected [only to the first quarter instead of the tail-end of last year], but at least we weren't caught flat-footed like Fed officials who were insisting the economy wasn't in recession – even after it started:

Fed's Parry Says U.S. Economy Isn't in Recession
Robert Parry, President
Federal Reserve Bank of San Francisco
***Bloomberg News** – April 5, 2001*

U.S. not in recession, Fed must be vigilant–Moskow
Michael Moskow, President
Federal Reserve Bank of Chicago
***Reuters** – April 4, 2001*

Fed's McTeer Says U.S. Economy Not in Recession
Robert McTeer, President
Federal Reserve Bank of Dallas
***Reuters** – April 4, 2001*

Within this issue we tackle another hotly debated topic: *When is a bear market **not** a bear any more?* Traditional Wall Street might argue that once the major stock indexes have rallied 20% or more from their lows, then a new bull market is in control. But as you'll see, the historical question is not that simple. Also inside, we update the bullish (and not-so-bullish) evidence that more Wall Street profits lie ahead, and the U.S. economy may be poised for an upturn sooner than economic pundits think. That's good news for astute investors who survived the bubble with their portfolios intact… but bad news for the Federal Reserve, who might find itself backpedaling on the latest interest rate cuts.

EDITOR: JAMES B. STACK
2472 Birch Glen ♦ Whitefish, MT 59937 ♦ 406 / 862-7777
http://www.investech.com
COPYRIGHT 2001 INVESTECH

Let's put this recent bear market in perspective. Assuming the final lows were hit on September 21st…

- With a -36.8% loss in the S&P 500 Index, this bear was surprisingly close to the "average" sized bear market of the past 70 years (-32.6%). Yet it was the 2nd largest bear market of the past 60 years.
- At 18 months of age, this bear lasted slightly longer than the "average" bear market of the past 70 years (17 months). And no bear market since 1938 has lasted longer than 21 months.
- The loss of wealth, of course, has been greater than any bear market in history. From the broad market's peak on March 24th of last year, through the recent September 21st low, over $5.85 ***trillion*** in paper value was wiped out. *That's more than the entire U.S. stock market was worth just six years ago.*
- Exactly 2/3's of that $5.85 trillion loss came in Nasdaq traded issues. And over $1 trillion came in just 318 telecom stocks listed on the Nasdaq exchange.

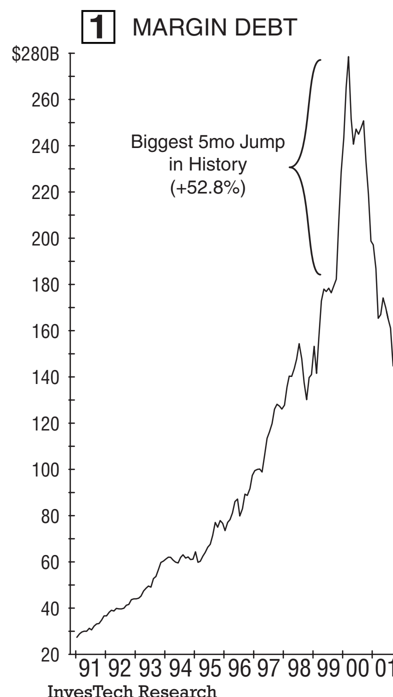
Rather sobering when you stop to think about it. These losses are real. They're not just numbers. And investors are feeling real pain out there. The only ones not feeling devastated are those trying to fool themselves (i.e., *"It's not a loss if I don't sell the stock."*), and those fortunate enough to survive the bubble intact (knock on wood).

All the Excesses are Not Resolved

We won't pull any punches. The lofty valuations still make us nervous. That's particularly true of the big cap blue chips and the earningless technology sector. No one can argue that stocks –in general– are on the bargain counter. At least they can't argue that without ignoring long-term history.

We're also bothered by the degree of investor confidence out there. Surveys do not show the doom-and-gloom investor pessimism we'd like to see near a market bottom. But rather than call it confidence, we'd prefer the label of "complacency" – and we might even be a tad off target there. It might best be called "resignation" as discouraged investors accept the fact that their bubble has popped and the U.S. is in recession.

Another excess we're not yet comfortable with is the level of margin debt, or money borrowed to buy stocks on margin. Yes, it has contracted with the bear market. But at $145 billion [1], it's only back to the levels of 1997. Hardly a depressed or "sold-out" condition.



Meanwhile, another debate topic has moved to the forefront on Wall Street: *When is a bear market <u>not</u> a bear any more?* Traditional Wall Street would argue that once the major stock indexes have rallied 20% or more from their lows, then a new bull market is in control. Indeed, such a viewpoint has proven indisputable for over 50 years. And by such a definition, the DJIA and Nasdaq Index all qualified for new bull market status in these eight weeks since their September 21st lows. Not quite so for the S&P 500 Index (+19.8%) or the broad-based Wilshire 5000 Index (+19.9%).

However, there's a historical problem in simply slapping a "bull market" label on a new 20% rise in the DJIA. To understand this dilemma, one must step back more than half a century…

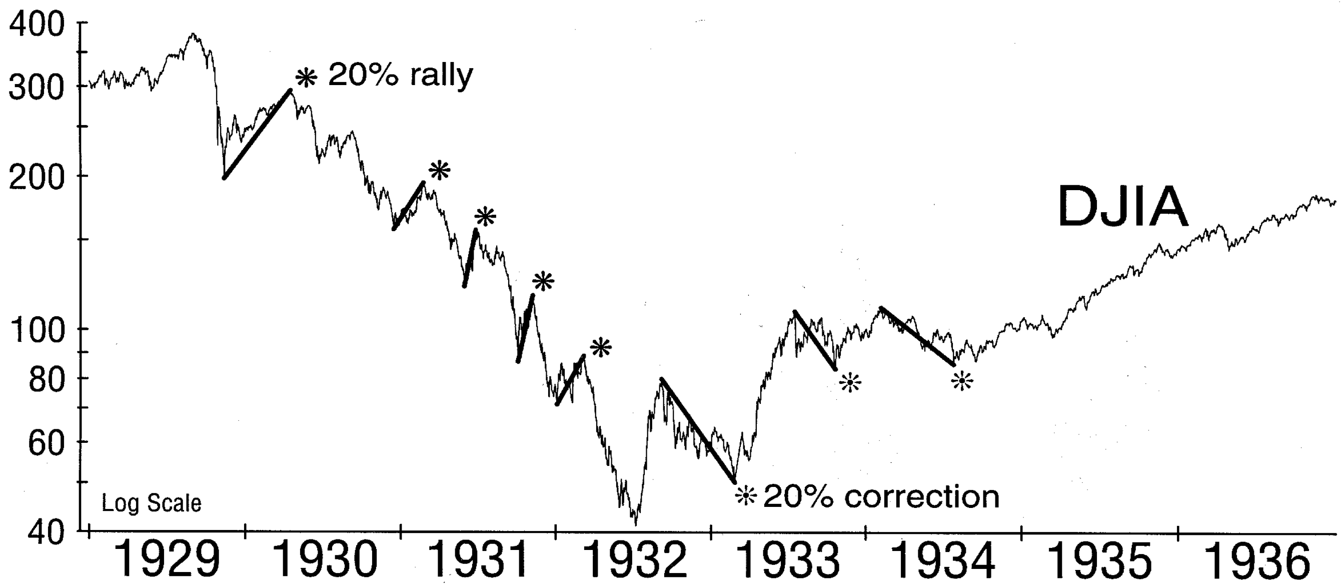
Since the early 1940s, treating a 20% loss as a bear market, and each subsequent 20% gain as a new bull market, has worked quite well. There is little disagreement among analysts, in 20/20 hindsight, about when bear and bull markets started and ended. But the same is not true about the 14-year period between 1929 and 1942 (see graph [2] at top of page 3).

Notice in the 2½ years between the 1929 Crash and 1932 bottom, that there were five separate rallies of 20% or more. These could hardly be called new bull markets in the full scheme of things. They were rallies… sucker rallies… that pulled unsuspecting investors back into the midst of the biggest bear market in Wall Street history.

Also notice the dilemma in the bull market following that 1932 low. Should 1932-1936 be labeled as one bull market (which is a visually appealing alternative)? Or should it be labeled as 4 separate bull markets – since there were -20% declines in late 1932, 1933, and 1934? It becomes a real quandary for market historians, even with the advantage of 20/20 hindsight. *Imagine what it must have felt like at the time!*

Which, of course, brings us to today. Does this 20% rally off the September 21st low officially qualify as the start of a new bull market? That's a very good question which we hesitate to answer. One reason for our reluctance is that we know so much about market history (shown here). Another is that we don't want to give subscribers a false sense of long-term security. Let us summarize our position this way…

1) We do believe important lows are in place for most indexes, except perhaps the tech-laden Nasdaq.
2) We do view this as a viable profit opportunity that will likely extend well into next year, based on favorable monetary and technical evidence.
3) In all probability, it is a new bull market. However, it will be a selective bull with some sectors and many individual stocks still headed for more washout in the year ahead.
4) There are warning flags that "bear" watching – including a possibility that the Federal Reserve may lose control, just as the Central Bank of Japan did after their bubble burst in 1989.
5) The semantics of "bull" versus "bear" isn't as important as allocating your portfolio and gradually updating it based on the level of risk.



Economic, Monetary, and Technical Update

As shown in our previous issue, most of the blocks for a "best buy" profit opportunity have dropped into place. Not the least of these is the widespread recession headlines… which, more often than not, actually causes the sell-off into the final bear market lows. That may have been the case on September 21st.

Also, as we have shown in recent issues, even if the market did hit bottom in September, you should expect fundamental news about the economy and earnings to deteriorate for many months to come. That is the norm, not the exception, in a recession and new bull market. While the media this week focused on the 5th consecutive drop in Consumer Confidence…

Rally Fades as Consumer Gloom Rules

***Reuters** – 11/27/01*

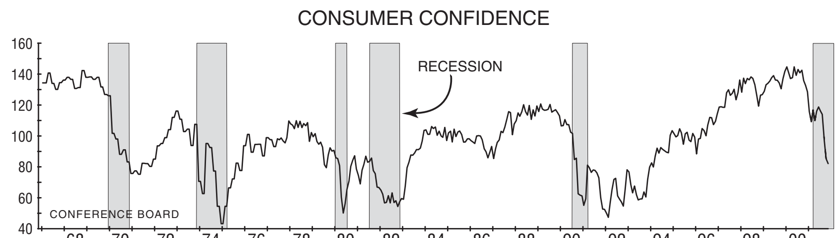
Consumer Confidence Hits 7 1/2 Year Low

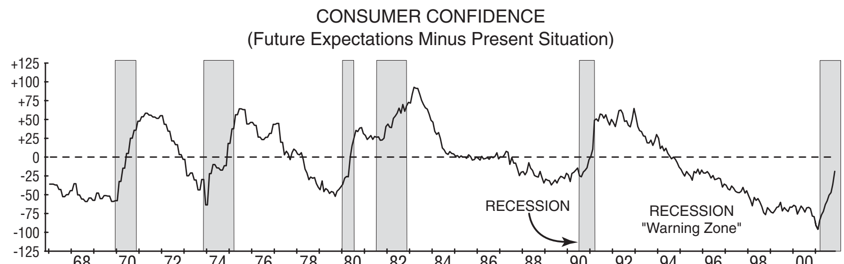
***Washington Post** – 11/27/01*

…we see compelling evidence that the stock market is anticipating an economic bottom in the first half of 2002. More importantly, it reinforces our belief that the Federal Reserve has not lost control, and the U.S. economy is not heading for a Japan-style debacle.

Underlying the headlines was the fact that all of the drop in Consumer Confidence came in how consumers view the "present situation." Meanwhile, the "future expectations" component of that gauge unexpectedly rose – after testing its previous bottom hit back in February. What this means is that consumers are actually more optimistic –looking out six months– than they were back in the first quarter of this year.

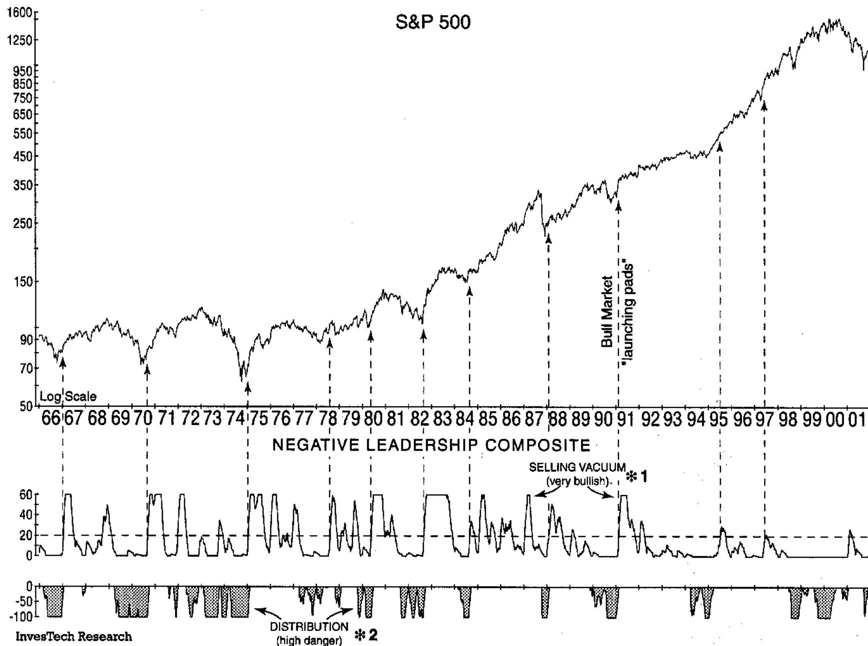
What you need to know as an investor is: *This difference or spread (Future expectations minus Present situation) has commonly led the path out of recession.* One caveat – this is our interpretation, and not necessarily the Conference Board's. But to us, one picture is worth a thousand words:

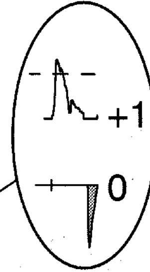




The media, as we said, is mesmerized by the top picture. We, instead, are focusing on the bottom. KEY QUESTION: *When has that bottom graph turned upward (like this) without forecasting the end of recession in the next 6 months?*

There are also important shifts underway on the technical side of the market. And we hit the highlights on these couple pages…



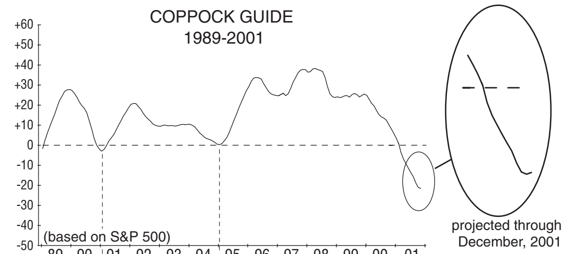


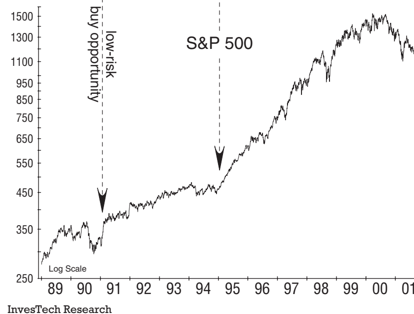
Bear market leadership is ending. Our Negative Leadership Composite reveals that bear market "DISTRIBUTION" [*2 shaded region] has ended. More importantly, we may soon see a bullish "SELLING VACUUM" appear in the top half of this index. The +1 reading triggered on the Friday after Thanksgiving, and may be partially due to the shortened trading session. Consequently, we're waiting for further upturn before putting a "✔" next to this bull market confirmation.

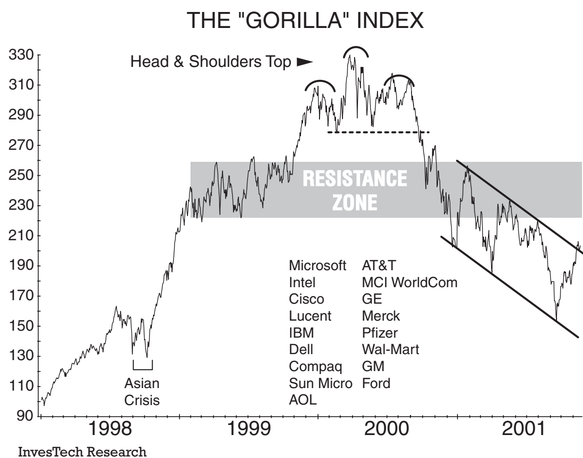
✻1 SELLING VACUUM [-BULLISH-]: This confirms the absence of negative or downside leadership. It is normally a very bullish signal since a stock market without any downside leadership is destined to move much higher.

✻2 DISTRIBUTION [-BEARISH-]: This signals that investors are anxious to sell stocks regardless of whether their position is at a loss, or the stock market is tumbling to new lows. It carries bearish implications as it suggests investors will use any rallies to get out of the market.

Our Coppock Guide is now on course to turn bullish in December. A turn upward from below "0" would be the last remaining block of our "Best Buy" conditions to drop into place. Without a significant sell-off on severe weakness, it will automatically occur. And this gauge has ultimately confirmed every major profit opportunity of the past 80+ years [see our previous issue for complete details].

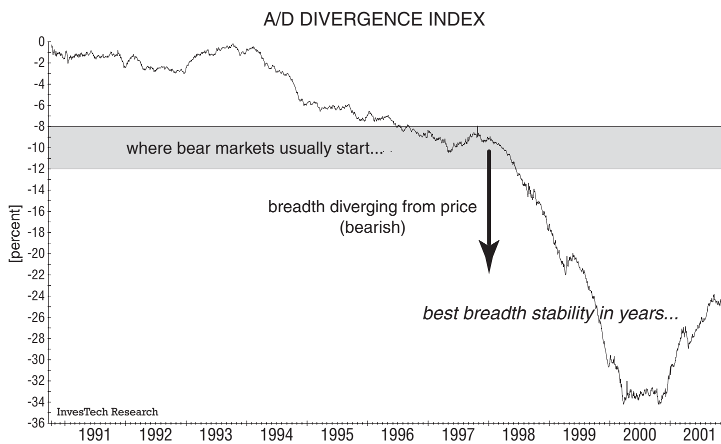


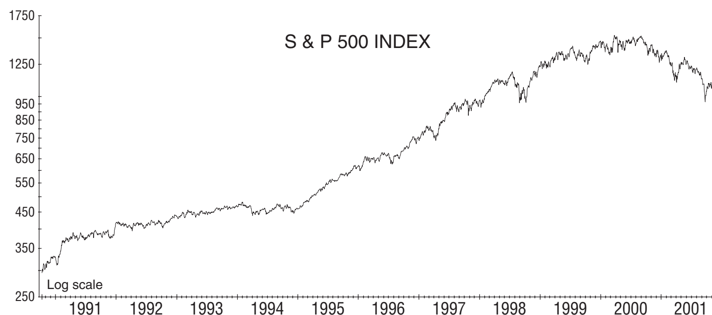




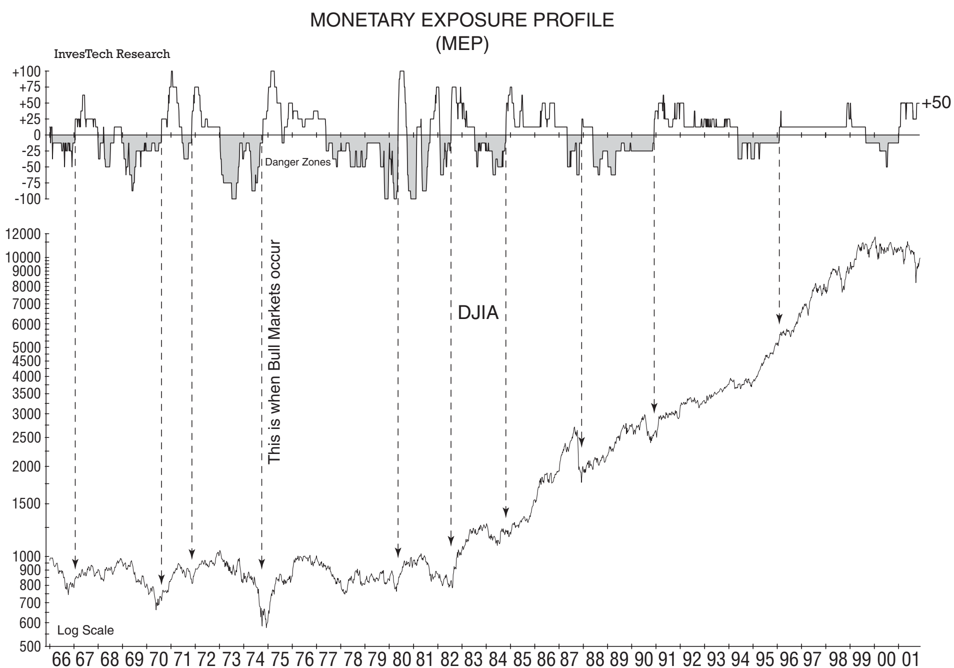
✻ These 17 stocks represent the behemoths in the major market indexes. Composed of only 3% of the 500 stocks in the S&P 500 Index (25% by capitalization weight), they accounted for almost 60% of the S&P 500 Index's rally from the October 1998 lows to the March 2000 peak.

Even the crashed momentum stocks are showing signs of strength. Our Gorilla Index has rallied back to challenge the upper trendline of its down-channel. With any stability, this index could move sideways to break out of its bearish pattern of the past year and a half. That could prove important over coming months in breaking the bear market psychology.





Breadth continues to show stability and broadening participation. Our A/D Divergence Index has been rising in bullish fashion. Some will argue that such breadth gauges are distorted by the number of interest rate-sensitive issues on the NYSE, or by the decimalization of exchange trading (changing to cents from 1/8's). Even so… as long as this A/D Divergence is not heading south in bearish divergence, we'll give breadth our bullish benefit of doubt.



Monetary Policy is still on track with the Fed's most aggressive easing in 88-years. Our MEP remains at a bullish +50, and regardless of whether Greenspan cuts rates again in December, we see no chance of a bearish shift in policy until the middle of next year or later.

STRATEGY & LAST MINUTE THOUGHTS

We're certainly not 100% confident that the September 21st bottom was **the final** bottom. But headlines of the past four weeks have lamented about falling CEO confidence, tumbling industrial production, falling consumer spending, a $30 billion outflow from equity funds, and the largest drop in U.S. economic output since 1991. Yet stocks have continued their steady upward climb.

Think of it this way… if the market can shake off such gloomy news and actually rise over the past month, then there must be some technical strength behind it. Our key indicators confirm so. And while bears warn that there's too much euphoria and optimism, we raised an eyebrow to yesterday's report that Nasdaq short interest (shares sold short in expectation of falling prices) had reached record levels:

> **Short Interest in Nasdaq Stocks Hits Record Amid Climb in Tech Sector**
> ***WSJ** – 11/28/01*

That suggests a lot of healthy skepticism, since bull markets traditionally climb a "wall of worry." It may also indicate a surprising amount of "forced" buying that could be triggered as we enter the seasonally strong period between early December and late January.

Bottomline… count us as conservatively, cautiously, watchfully bullish. And we'll remain so until the balance of evidence warrants otherwise.

THE 24TH ANNUAL FLORIDA MONEY SHOW ✦ FEBRUARY 20-23, 2002

Make plans now to attend the **24th Annual Florida Money Show**, **February 20-23, 2002** at the Gaylord Palms™ Resort in Orlando, Florida. This unique one-stop educational resource is an excellent opportunity to get your questions answered about today's uncertain economy. Whether you are developing your investment skills and knowledge, or you are an experienced investor who wants to advance to a higher level of investment sophistication, you won't want to miss The 2002 Florida Money Show.

***Brand New Format*:** Editor James Stack, along with four other renowned journalists and financial advisors, will join Master of Ceremonies Paul Kangas at the Money Show's first-ever Opening Ceremonies. Mr. Stack's keynote presentation, "What History Tells Us About Bubbles, Bear Markets, Recessions… and What Lies Ahead," promises to put the current markets into objective historical perspective and transform fear and uncertainty into confidence and profit.

Best of all, admission is absolutely FREE with your subscription renewal to InvesTech. Call today toll-free **1-800-955-8500** to reserve your tickets to this exciting investment event!

Accessing www.investech.com

Our Internet Service Provider recently upgraded their server, and until your ISP refreshes their cache servers to reflect this upgrade, you may temporarily experience difficulties accessing our web site. During this interim period, you may have better results using the numeric address **http://208.141.130.220**, rather than the standard text Internet address http://www.investech.com. We apologize for any inconvenience.

STOCK NEWS

THE INVESTECH MODEL STOCK PORTFOLIO is 62% invested with 8% in Scudder Japan (SJPNX), 5% in Franco-Nevada (FN.TO), 4% in Xerox (XRX), and 3% in each of the following: Phillips Petroleum (P), ConAgra Foods (CAG), Genuine Parts Co. (GPC), Xcel Energy (XEL) and Engelhard Corp. (EC). In addition, 15% is allocated to each of the following value mutual funds – Heartland Value (HRTVX) and Strong Multi Cap Value Fund (SMTVX). The 4% position in Stillwater Mining (SWC) was sold on 11/21/01, as recommended on the 11/20/01 Financial Hotline.

Of Interest: Newmont Mining has made a bid to acquire Franco-Nevada Mining (FN.TO) and Normandy Mining. The offer has been approved by the boards of directors of all three companies, but must be approved by shareholders. Franco-Nevada shareholders would receive 0.8 shares of Newmont Mining if the transaction is realized. The acquisition of Franco-Nevada and Normandy by Newmont would create the world's largest gold producer.

Phillips Petroleum (P) and Conoco have agreed to a merger that would result in one of the world's largest energy companies. The new company would be called ConocoPhillips and Phillips Petroleum shareholders would receive one share of the new company's stock for each share of Phillips Petroleum owned.

VALUE MODEL PORTFOLIO

CURRENT ADVICE	COMPANY	SYMBOL	EXCH	52 - WEEK Hi	52 - WEEK Low	INIT. RECOMMENDED Date	INIT. RECOMMENDED Price	RECENT PRICE	P/E	YIELD
HOLD[1]	**SCUDDER JAPAN FUND** Invests in Japanese securities and corp. debt. Holds about 60% of assets in small- and mid-cap stocks.	SJPNX	——	12.00	6.87	5/12/99	@ 7.77	7.36	29	0.0%
BUY/HOLD[3]	**FRANCO-NEVADA MINING CORP.** Canadian co. receives royalties from gold/natural resource properties, oil and gas. Company has $700+M working capital, no long-term debt.	FN-T	tse	25.10	14.60[a]	3/30/98	@ 33.00	22.76	28	1.3%
SOLD[2]	**STILLWATER MINING COMPANY** Only major source of palladium and platinum outside of South Africa and Russia. Planned expansion will triple current production.	SWC	amex	Sold 11/21/01 per 11/20/01 Hotline recommendation						
HOLD[2]	**XEROX CORP.** Develops, manufactures, markets, services and finances document processing equipment.	XRX	nyse	11.35	3.75	10/16/00	@ 7.75	8.20	N/A	0.0%
BUY/HOLD[4]	**PHILLIPS PETROLEUM** Integrated oil and petrochemicals company. Planned merger with Tosco will result in the 2nd largest refiner and 3rd largest marketer in the U.S.	P	nyse	68.00	50.00	1/31/01	@ 58.50	54.10	6	2.7%
HOLD[4]	**CONAGRA FOODS** Second largest food processor in U.S. Products include brands like Hunt's, Bumble Bee, Butterball, Peter Pan, and Swiss Miss.	CAG	nyse	26.19	17.50	1/31/01	@ 23.62	23.08	17	4.1%
HOLD[4]	**GENUINE PARTS COMPANY** National distributor of automotive replacement parts and accessory items. Owns 62 NAPA distribution centers.	GPC	nyse	35.24	19.00	1/31/01	@ 25.19	34.40	16	3.3%
BUY/HOLD[4]	**XCEL ENERGY** Supplies electricity and natural gas in 12 mid-western and western states. Formed by merger of Northern States Power and New Century Energies.	XEL	nyse	31.85	24.19	1/31/01	@ 25.66	28.23	12	5.3%
BUY/HOLD[4]	**ENGELHARD CORP.** Leading manufacturer of specialty chemicals, pigments, and catalysts for petroleum and environmental protection industries.	EC	nyse	29.20	17.63	1/31/01	@ 22.75	27.87	22	1.4%
BUY/HOLD[5]	**HEARTLAND VALUE FUND** Invests primarily in undervalued small stocks with market capitalizations less than $750 million.	HRTVX	——	40.35	30.95	1/31/01	@ 34.09	38.09	17	0.0%
HOLD[5]	**STRONG MULTI CAP VALUE FUND** Focuses on companies believed to have strong financial positions and low stock-market valuations relative to their intrinsic investment values.	SMTVX	——	57.37	42.74	1/31/01	@ 54.69	49.45	24	0.0%

[1] 8% position
[2] 4% position
[3] 5% position
[4] 3% position
[5] 15% position
[a] All figures in Canadian dollars

NEXT ISSUE: December 21, 2001

***InvesTech's Financial Hotline** is updated at 2:00PM (EST) on Saturday and 9:30PM on Tuesday.*

PERSONAL PERSPECTIVE

How Widespread is the Washout Waterfall?

It's difficult to measure the overall psychological impact when investors are left "holding the bag" on failed companies. And I'm not just talking about the crashed dot-coms – although they were at the core of the Wall Street frenzy near its peak. Unfortunately, many insiders knew they were fleecing the public as we warned in November of 1999 by publishing this text from the prospectus of Internet IPO Garden.com:

> "You should carefully consider the following risk factors and all other information contained in this prospectus before purchasing our common stock… We have a history of significant losses and we expect to incur substantial net losses in the future… As of June 30, 1999, we have incurred cumulative net losses of $26.8 million… We anticipate our losses will increase significantly from current levels… We do not have sufficient cash to indefinitely sustain these operating losses… We have been unable to fund our operations with the cash generated from our business… We believe it is likely that, in the future, fluctuations in our quarterly operating results will cause our results to fall below the expectations of securities analysts and investors, which could cause the price of our common stock to drop… As a result, investors in our common stock may not be able to resell their shares at or above the initial public offering price… We may in the future be the target of litigation… The broad discretion we have in the use of proceeds of this offering increases the risk that we may not use them effectively."

Now defunct, you can't say Garden.com underwriters didn't warn investors! It seems to say: *"We're blithering idiots… we're doing everything wrong, and will likely do so in the future… but give us your money."* So why weren't investors more cautious? Because in a mania, emotions rule and logic takes a vacation.

Yet one can't help but worry about the lasting effect on investor psychology. As I said, these devastating losses (where virtually <u>all</u> the investment disappears) were not limited to fly-by-night dot-coms. Just 318 telecom firms on the Nasdaq lost $1 trillion or 85% in value. Popular names of "can't-lose" stocks like Lucent and Cisco Systems have wiped out portfolios of investors over-allocated to the technology sector.

Such horror stories are the major reason this will not be a "V-shaped" market bottom. Now that we've had the initial bounce off the September 21st lows, expect a more labored advance as burned investors use every opportunity to lighten up on, or sell off, these issues. This is one reason (other than valuation) that we're not anxious to step into the technology sector anytime soon. And there are other sectors we'd be careful about venturing into merely because their prices appear depressed…

FLIGHT RAGE…

Forget about the highways of California. The flyways over the U.S. are the next boiling pot of frustration and consumer backlash. Having made three flights since the September 11th terrorist attacks, we've had the advantage of watching security measures tighten notch by notch. As with any government intercession in a crisis, we fear an overreaction… and no one knows how to do that better than the U.S. Government.

Not to downplay the importance of airport security, but we already see it being carried to extreme. Boarding in Kalispell, Montana now requires driving through an armed security checkpoint, showing your ID a minimum of 3 times, and in most cases a personal "wand search" –even after passing through the usual metal detector. While changing planes in Salt Lake City, my name was called at the check-in counter (along with a number of others) as the winning recipient of another random "wand search" and detailed dump search of all carry-on baggage. Our plane was subsequently 45 minutes late taking off.

At our next connection, we had to change concourses, which required another security check. Having pulled the unskilled and untrained off the x-ray scanning machines, these personnel now check boarding passes <u>prior</u> to the security screening. We were <u>un</u>fortunate enough to get one who didn't know how

(Continued on page 8…)

to read our ticket and didn't understand that "CO" stood for Continental Airlines. Yet we finally convinced him we were on the right concourse and indeed departing on a flight which would leave in 10 minutes. Arriving at the gate, we found the door had been closed early (again due to security measures) and could not be reopened. We missed the flight, *but believe it or not, the plane was held at the gate long enough for our checked baggage to be put on board without us!*

Now if one is on vacation, and travels infrequently, such hassles seem an acceptable trade-off for 100% security. But let's face it – security is far from 100% when considering checked baggage is not hand-searched, and may not even be on the same plane as the owner (case-in-point!). To business travelers, who are the cream of the airline profits, these repeated searches and resulting delays are more than inconveniences – they're time and money. On top of the current recession, this could spell bigger trouble for the airlines. It's not the fear or terrorists that endanger the airline industry, it's the hassles and delays. Consequently, we do not consider the airline stocks cheap, even at current levels.

THE NBER – WHO ARE THESE MASKED MEN?

As we predicted, the National Bureau of Economic Research finally came out and announced a recession, but backdated the starting point to 8 months ago. That is how the official "recession system" works. A recession is never forecast in advance by any poll of economists. And it's always recognized 6 to 12 months after the start by the NBER – a distinguished group of academic economists with perfect 20/20 hindsight. There are actually six economists as members of the NBER from such notable institutions as Stanford and Harvard.

They do not base their announcements on the simplistic view that it requires two consecutive quarters of negative GDP to create a recession, but instead examine unemployment, industrial production, income, and sales trends. Frankly, we're a little miffed they didn't predate the start several months earlier. To try to say the economy "peaked" and the recession began in March is a tad farfetched in light of the consumer confidence, purchasing managers', and unemployment data. But the NBER, we suppose, had good reason for selecting that month. After all, it did establish the length of the previous expansion (since the 1990-91 recession) at exactly 10 years – a new record.

So when will the NBER announce the end of the recession? Chances are it could be long after much of this bull market's profits have already been made. The last recession formally ended in March of 1991, however, the NBER didn't set that official ending date until December 1992 – a full 1 year and 9 months after the fact.

At that, we'll close this issue with a humorous, yet surprising, investment insight sent in by one *InvesTech* subscriber:

> *"If you bought $1000 worth of Nortel stock a little over a year ago, it would be worth $60. If you bought $1000 worth of Budweiser (the beer, not the stock) one year ago, drank the beer, and traded in the cans for the nickel deposits, you would have $79."*

And... you would have had a great time doing it!

James B Stack

The INVESTECH MARKET ANALYST and MUTUAL FUND ADVISOR are published 17 times per year and include access to the twice-weekly InvesTech Financial Hotline. Pursuant to the provisions of Rule 206(4)-1 of the Investment Advisors Act of 1940, we advise all readers to recognize that they should not assume that recommendations made in the future will be profitable or will equal the performance of past recommendations. The contents of this letter have been compiled from original and published sources believed to be reliable, but are not guaranteed as to accuracy or completeness. James B. Stack is also President of Stack Financial Management (SFM), a registered investment advisor, and a separate company from InvesTech Research. Clients of SFM and individuals associated with InvesTech Research may have positions in and may from time to time make purchases or sales of securities mentioned herein.

SUBSCRIPTION RATES (U.S. dollars):
InvesTech Market Analyst $190/yr
InvesTech Mutual Fund Advisor $190/yr
BOTH COMPLETE SERVICES $295/yr
(Foreign add $2.00/mo)

A Holiday Gift Idea... give Investech to a friend, relative or associate. They'll appreciate you all year long.

YOUR GIFT WILL INCLUDE:
- Both the *InvesTech Market Analyst and Mutual Fund Advisor*
- InvesTech's Profit Guide, Hotline & Subscriber Web Access
- InvesTech's *Updated* 80yr American Economy Wall Chart

Gift Subscriptions Available:
7 mos for $99 or 1 yr for $175
To order call: **1-800-955-8500** (24 hrs/7 days)

As our way of saying "thanks," we'll add *two extra issues* to your subscription for *each* gift you order!

InvesTech® Research

MUTUAL FUND ADVISOR

VOL 01 ISS 16 Professional Asset Allocation NOV 30, 2001

Shifting to a "Growth-Value" Strategy

Headlines this week announced formal recognition that the U.S. has been in a recession since last March. The National Bureau of Economic Research, the final authority on such matters, has now made it official… *and it's about time!* What does that mean for investors? In previous issues we've pointed out that stock market bottoms almost always occur within a month or two of formal recession recognition. That dramatically increases the chance that September saw the final market lows. While economic recovery will probably not kick in until the first half of 2002, the stock market generally leads the economy by at least six months. So putting lousy earnings and dour economic forecasts in proper perspective, we feel a buying opportunity is nearly in place. All we want to see is stronger confirmation from our Negative Leadership Composite as outlined in the current issue of the *InvesTech Market Analyst*.

Adding Investments

Clearly a sour economy will still take its toll in terms of defaults and bankruptcies, so it's important to step carefully. The question on everyone's mind is "what sectors do well coming out of a recession?" Conveniently, Ned Davis Research (NDR) recently addressed this with a study of the last three recessions, looking at which sectors typically performed the best as the economy started to rebound. We've included part of their findings in the table at right.

Listed in this table are the *average* gains of each sector during the two months prior to, and the six months following, the end of three recessions – in 1980, 1982 and 1991. Although individual recessions differ in some respects, there are definite patterns. According to NDR, the initial leaders in the final months of a recession have been Housing, Technology, Leisure/Entertainment, Retail, and Health Care. While 6 months into an economic expansion Aerospace/Defense and Transportation typically join the top ranks. In 1991, however, the Banking/Loans sector was the 6-month post-recession leader with an 18.9% gain, while Technology –an early winner, with a 20.7% gain prior to the recession end– dropped to the bottom of the list with a -5.5% loss.

NDR SECTOR LEADERSHIP
2 Months Prior & 6 Months Post-Recession End
(Average of Economic Recessions Ending: 07/31/1980, 11/30/1982, 03/31/1991)

NDR Sector	% Gain 2 mo. prior to recession end	NDR Sector	% Gain 6 mo. post-recession end
Housing	27.5%	Aerospace/Defense	21.4%
Technology	24.8	Transportation	18.2
Leisure/Entertainment	24.7	Retail	17.0
Retail	23.2	Broadcast/Media	15.7
Health Care	22.4	Technology	14.8
Non-Bank Financial	19.9	Health Care	14.4
Transportation	18.3	Foreign Stocks	13.6
Conglomerates	17.8	Industrial Materials	13.2
Broadcast/Media	17.7	Banking/Loans	13.1
Automotive	17.4	Housing	13.1
Foreign Stocks	17.2	Leisure/Entertainment	12.5
Capital Goods	17.0	Energy	12.4
Banking/Loans	16.6	Non-Bank Financial	11.2
Precious Metals	16.1	Conglomerates	11.1
Aerospace/Defense	14.3	Automotive	10.5
Foods	14.0	Capital Goods	10.4
Industrial Materials	13.6	Precious Metals	9.8
Energy	9.4	Foods	7.0
Utilities	6.7	Utilities	4.2
Mean =	**17.8%**	**Mean =**	**12.8%**

Ned Davis Research

So far in the current market, leadership is following the same pattern, with a few exceptions. Healthcare has lagged the market since September, while Industrial Materials (including Engelhard in our model portfolio) has outperformed. Here are some points to remember in today's recession… The battered Technology group has rebounded since September, but many of these stocks are overvalued and there's still a lot of washout ahead for companies in this sector. Also, popped bubbles do not easily re-inflate. And Housing, where projects are often

COPYRIGHT 2001 INVESTECH

planned at the height of an economic boom, has yet to feel the effects of a slowdown. Also, segments of the Transportation and Leisure/Entertainment sectors could still be vulnerable to terrorist fears.

With these factors in mind, we'll use this issue to review our selection criteria and to present some of the top stocks and mutual funds under consideration for our model portfolios.

Growth-oriented Value Stocks

As bullish evidence mounts, we intend to start shifting away from our defensive hedge focus in favor of a growth-oriented approach. Of course, it's still important to base stock selection on good value criteria. We want companies with solid track records, positive earnings and sound financial statements to avoid surprises like Lucent Technologies or the current basket case – Enron Corp. Therefore, our criteria is similar to that outlined in past issues, with some revisions:

Stock Selection Criteria

- P/E ratio less than or equal to industry average.
- Stable revenue and earnings growth over last four quarters, with strong 3rd quarter for retail stocks.
- Dividend yield consistent with or above historic norm (in income accounts).
- Consistent dividend growth history (if dividends paid).
- "B" or better Financial Strength.
- Low long-term debt as percent of capital and good debt coverage.
- Strong growth characteristics (leader in industry or niche market).

We want to look at stocks with strong growth potential for revenues and we'll consider higher P/E ratios... remember, earnings (especially for cyclical stocks) probably won't recover until next year. As long as the company's valuation is below the industry average and the mean P/E of the S&P 500 (currently 31), it's worth considering. Cyclical companies should also improve, but those specializing in high-end discretionary items like housing and cars could remain vulnerable. The best picks are consumable products or services. We're still avoiding much of the technology sector –due to competition and excess capacity– but if you're considering tech, stay with software and services. These are some of the top stocks on our list:

Retail

One of the immediate and primary beneficiaries of any improvement in the economy should be the retail sector – particularly companies that market smaller ticket items like clothing…

Ross Stores (ROST) – operates a chain of 453 retail apparel stores in 22 states. Sells brand name clothing and accessories below department store prices.

- P/E ratio of 15 is far below the industry average of 24.
- 12-month revenue/earnings growth = +11%/+3%.
- Q3 sales were up 15% from one year ago.
- "A" Financial Strength – debt is only 9% of capital.
- Ross plans to have 35 to 40 new stores open by the end of January, entering new markets in Georgia and the Carolinas. The company is increasing non-apparel offerings to about 18% of revenues.

TJX Companies, Inc. (TJX) – the world's largest off-price (value-priced) soft goods retailer. Store chains include T.J. Maxx and Marshalls.

- P/E ratio of 20 is below the industry average of 24.
- 12-month revenue/earnings growth = +10%/+2%.
- Q3 sales increased 11% over last year.
- "A" Financial Strength.
- TJX Companies sells about three times the volume of its nearest competitor. The company plans to increase the number of stores it opens each year, adding about 12% to its base annually.

Radioshack Corporation (RSH) – Leading retailer of consumer electronics with over 7,000 stores.

- P/E ratio of 19 is far less than the industry average of 37.
- 12-month revenue/earnings growth = +5%/-9%.
- Q3 revenue fell -5% compared to last year, but 2002 revenues should jump by 10-12% in an economic recovery.
- "A" Financial Strength.
- Electronics sales could rebound with an improving economy. Radioshack also plans to improve margins next year by reducing computer inventory and switching to a build-to-order model.

Transportation

In the aftermath of the World Trade Center event, one area in the transportation sector we'd avoid is the airline industry. Among the remaining industries, companies that are efficient and expanding should see significant improvement when the economy starts to recover. The following company meets both criteria. Although this is a Canadian Railway (traded on the NYSE), its system stretches the width of Canada and south through the mid-western U.S. to the Gulf of Mexico…

Canadian National Railway Company (CNI) – operates Canada's largest railroad system.

- P/E ratio of 14 is much lower than the industry average of 22.
- 12-month revenue/earnings growth = +2%/+7%.
- "B" Financial Strength.
- The company delivers 93% of shipments on time allowing it to cut costs and personnel. Expansion includes the recently completed acquisition of Wisconsin Central Transportation.

Health Care

Many stocks in the health care sector, and particularly the drug industry are overvalued by historic comparison. Although aging demographics and rapid growth favor this sector, we'd stay with market leaders or stocks that are selling below their historic P/E ratios. Of the following, Elan Corp. and Mentor Corp. are slightly higher risk growth companies, with valuations less than their 10-year median P/E's. Pfizer, Inc., on the other hand, is richly valued, but it's a market leader with a broad portfolio of drugs and prolific research and development. We would consider this stock a core holding.

Mentor Corp. (MNTR) – develops and markets products for aesthetic, urological and general surgery. Also produces clinical and consumer health items.

- P/E ratio of 19 is less than the 10-year median of 22.
- 12-month revenue/earnings growth = +15%/+22%.
- Q3 revenue increased 22% over last year.
- "B+" Financial Strength.
- No long-term debt.
- Solid cash flow and no debt should allow the company to make acquisitions. Also an improving economy will improve sales of products used in discretionary (aesthetic) surgery.

Elan Corp. (ELN) – researches, develops and sells drug delivery systems and pharmaceutical products, primarily for neurological disorders.

- P/E ratio of 24 is well below the 10-year median of 29.
- 12-month revenue/earnings growth = +27%/+23%.
- Q3 revenue increased 24% over last year.
- "B++" Financial Strength.
- Elan is a world leader in drug delivery technology and has a rich pipeline of drugs in development for a variety of applications, including Parkinson's disease and Alzheimer's.

Pfizer, Inc. (PFE) – one of the world's top pharmaceutical companies. Major products include Viagra and Lipitor.

- P/E ratio of 35 is below the industry average of 39.
- 12-month revenue/earnings growth = +9%/+24%.
- Q3 revenue increased 10% over last year.
- "A++" Financial Strength.
- Debt is only 12% of capital.
- Pfizer will save $1.4 billion in costs this year from its merger with Warner-Lambert and expects savings of $1.6 billion next year. The company has 29 new drugs in mid- to late-stage development.

Conglomerates

Although not typically a top performing sector in a recovery, this growth company stands out and warrants a closer look…

Tyco International, Ltd. (TYC) – manufactures a broad range of products, including fire protection & security, electronic components, underwater cables and medical supplies.

- P/E ratio of 21 is well below the industry average of 37.
- 12-month revenue/earnings growth = +25%/+28%.
- Sales have tripled in the last 3 years and Q3 revenue +29%.
- "A" Financial strength.
- Tyco is expanding through acquisitions – the latest being CIT Group, the largest independent commercial finance company.

Banking and Loans

While not always among the top performers in a recovery, the banking sector led the 1991 recovery with a 6-month gain of 18.9%. These stocks can provide both capital appreciation potential and a stable dividend… and the recent pullback in stock price makes them more attractive:

Washington Federal, Inc. (WFSL) – a smaller mid-cap stock, this Seattle-based Savings and Loan holding company has 111 branches in 6 Western states.

- P/E ratio of 14 is below the industry average of 16.
- 12-month revenue/earnings growth = +8%/+8%.
- "A+" Financial Strength.
- Dividend yield is 3.9%, with increases in 15 of the last 16 years.
- Company has also issued a 10% stock dividend in 7 of the last 9 years.

Washington Mutual, Inc. (WM) – largest Savings and Loan in the U.S. with over 2000 offices in 42 states.

- P/E ratio is 10, below the industry average of 16.
- 12-month revenue/earnings growth = +14%/+39%.
- "A" Financial Strength.
- Dividend yield is 2.9%, with increases in 15 of the last 16 years.
- Washington Mutual has announced or completed 4 acquisitions this year. The latest (Dime Bancorp) will give Washington Mutual access to the New York market.

Charter One Financial, Inc. (CF) – One of the 30 largest bank holding companies in the U.S.

- P/E ratio is 13, less than the industry average of 16.
- 12-month revenue/earnings growth = +8%/+12%.
- "A" Financial Strength.
- Dividend yield is 2.8%, with 10+ years of consecutive increases.
- Charter One is shifting from residential to higher yielding consumer and commercial loans. The company is also expanding branches to 436 through acquisitions.

Growth Mutual Funds

We want to retain our focus on small-cap funds in the portfolio. However, it's important to look at other growth funds for future additions. Our mutual fund selection criteria is basically the same, with only a few changes:

Mutual Fund Selection Criteria

- P/E ratio less than major market indexes (S&P=31).
- Net assets greater than $200M.
- Expense ratio less than category average (1.4).
- Portfolio turnover less than 75%.
- Less than 20% in technology.
- Manager tenure greater than 8 years.

It's fine to consider a broader range of median market caps for new growth fund additions. And, although we don't like technology right now, there are some opportunities in the sector, so we've relaxed our recommended exposure limitations a little. With the pullback in earnings, average P/E ratios will increase, but should still be less than major market averages. We also expect this economic recovery to resolve into a slow growth environment, similar to 1992-1994. The reason is twofold:

- This is a global recession.
- The severe psychological damage from the popping of the technology bubble will take time to repair.

So look for funds that performed well during those three challenging years and are still directed by the same fund manager. That's why we've added "Manager Tenure" to the list of selection criteria.

The top growth mutual funds under consideration are listed in the table below, with our preference being the two T. Rowe Price funds.

Growth-Value Mutual Funds

Fund Name	Symbol	Prospectus Objective	Min. Init. Purchase ($)	Expense Ratio	Net Assets ($MM)	P/E Ratio	Manager Tenure	Turnover Ratio	% Tech
T. Rowe Price Small-Cap Stock	OTCFX	Small Company	2,500	0.94	2487	22.9	9	33	12.7
T. Rowe Price Mid-Cap Growth	RPMGX	Growth	2,500	0.86	5468	29.4	9	54	19.6
Sound Shore Fund	SSHFX	Growth	10,000	0.98	996	23.5	16	41	3.2
Gabelli Asset Fund	GABAX	Growth	1,000	0.77	1720	23.4	15	48	3.3
FAM Value Fund	FAMVX	Small Company	2,000	1.26	430	19.7	8	10	8.1

Data: Morningstar

Strategy

As we prepare to increase our recommended equity allocation, now is the time to research new additions for your portfolio… focusing more on growth and less on defensive hedges. One should consider weeding out any positions that fail to respond with strong market rallies, or where the recession's impact has created undue risk. These weak stocks could easily suffer further losses or take a long time to recover – that's why we decided to step out of Stillwater Mining. We may also selectively sell other stocks or reduce our bond fund position, if the money can be put to better use in growth-value stocks or funds like those discussed in this issue. With increasing signs that this market has seen its final bottom, be sure to monitor the *InvesTech Financial Hotline* for any additions or changes to our model portfolio.

MODEL PORTFOLIO: The InvesTech model mutual fund portfolio remains 79% invested with 21% held in short-term Treasuries or a money market fund. Percentage allocations and specific investment vehicles are listed below. We are prepared to increase the model portfolio allocation of "growth-value" stocks as bullish evidence mounts. Recommended securities will include growth stocks/mutual funds that still compare favorably from a valuation standpoint. Monitor the InvesTech Financial Hotline or web site at www.investech.com for important strategy updates.

PERCENT	FUND	SYMBOL	52-WEEK Hi	52-WEEK Low	INIT. RECOMMENDED Date	INIT. RECOMMENDED Price	CURRENT PRICE	ALTERNATE FUNDS
21%	T-BILLS	----------						MONEY MARKET FUND
20%	VANGUARD L-T CORP BOND	VWESX	9.21	7.67	12/6/00	7.88	8.75	See funds below
15%	HEARTLAND VALUE FUND	HRTVX	40.35	30.95	1/31/01	34.09	38.09	OAKMARK FUND I
15%	STRONG MULTI CAP VALUE	SMTVX	57.37	42.74	1/31/01	54.69	49.45	OAKMARK FUND I
8%	SCUDDER JAPAN FUND	SJPNX	12.00	6.87	5/12/99	7.77	7.36	See funds below
4%	AMER. CENT. GLOBAL GOLD	BGEIX	5.44	3.58	3/30/98	6.72	4.85	See funds below
3%	PHILLIPS PETROLEUM	P	68.00	50.00	1/31/01	58.50	54.10	
3%	CONAGRA FOODS	CAG	26.19	17.50	1/31/01	23.62	23.08	
3%	GENUINE PARTS CO.	GPC	35.24	19.00	1/31/01	25.19	34.40	
3%	XCEL ENERGY	XEL	31.85	24.19	1/31/01	25.66	28.23	
3%	ENGELHARD CORP.	EC	29.20	17.63	1/31/01	22.75	27.87	
2%	FRANCO-NEVADA MINING	FN-T	25.10	14.60	9/29/99	30.30	22.76	* All figures in Canadian dollars

THE TOP-RATED FUNDS

CURRENT ADVICE	FUND	SYMBOL	RISK	CURRENT PERF[1] 6wk	CURRENT PERF[1] YTD	PAST PERF[1] 2000	PAST PERF[1] 1999	PAST PERF[1] 5yr annl	SIZE[2]	YIELD	RECENT[3] PRICE	NTF[4]
GROWTH FUNDS												
+	FAM VALUE FUND	FAMVX	High	+ 2.7%	+10%	+19%	- 5%	+ 14%	430M	0.9%	35.87	F,S,W
+	GABELLI ASSET FUND	GABAX	High	+ 4.8%	- 3%	- 2%	+28%	+ 14%	1720M	0.9%	32.90	F,S,W
+	SOUND SHORE FUND	SSHFX	High	+ 3.3%	- 2%	+20%	0%	+ 11%	996M	0.5%	32.86	F,S,W
+	T. ROWE PRICE MID-CAP GROWTH	RPMGX	High	+ 7.8%	- 6%	+ 7%	+24%	+ 13%	5468M	0.0%	37.57	
+	T. ROWE PRICE SMALL CAP STOCK	OTCFX	High	+ 6.6%	0%	+16%	+15%	+ 11%	2487M	0.6%	23.86	
VALUE FUNDS												
++	HEARTLAND VALUE FUND	HRTVX	High	+ 8.4%	+20%	+ 2%	+25%	+ 11%	907M	0.0%	38.09	F,S,W
++	OAKMARK FUND I	OAKMX	High	+ 5.1%	+16%	+12%	- 10%	+ 10%	2090M	1.2%	34.46	F,S,W
+	STRONG MULTI CAP VALUE FUND	SMTVX	High	+ 3.8%	- 3%	+ 4%	- 16%	+ 1%	312M	0.0%	49.45	F,S,W
BOND INCOME FUNDS												
INTERMEDIATE-TERM												
+	AMER. CENT. TREAS INV	CPTNX	Med	- 2.1%	+ 6%	+13%	- 2%	+ 7%	441M	3.9%	10.79	F,S,W
+	DODGE & COX INCOME	DODIX	Med	- 0.2%	+10%	+11%	- 1%	+ 8%	1227M	5.1%	12.33	
+	STRONG GOVT. SECURITIES	STVSX	Low	- 0.8%	+ 8%	+11%	- 1%	+ 7%	1691M	4.9%	10.95	F,S,W
LONG-TERM												
0	AMER.CENT. TARGET MATUR. 2025	BTTRX	High	- 2.7%	0%	+33%	- 21%	+ 10%	327M	6.0%	32.66	F,S,W
0	VANGUARD LONG-TM CORP BOND	VWESX	High	0.0%	+ 9%	+12%	- 7%	+ 7%	3776M	6.4%	8.75	
0	VANGUARD LONG-TM U.S. TREAS	VUSTX	High	- 1.8%	+ 5%	+20%	- 9%	+ 8%	1414M	5.3%	10.90	
GOLD FUNDS												
++	AMER. CENT. GLOBAL GOLD FUND	BGEIX	High	- 5.3%	+23%	- 24%	- 3%	- 15%	189M	1.1%	4.85	S,W
++	FIDELITY SELECT GOLD	FSAGX	High	- 0.2%	+15%	- 18%	+ 8%	- 11%	263M	0.7%	13.72	
++	VANGUARD PRECIOUS METALS	VGPMX	High	+ 0.1%	+10%	- 7%	+27%	- 6%	346M	3.4%	8.20	
INTERNATIONAL FUNDS – JAPAN												
0	FIDELITY JAPAN	FJPNX	High	+ 2.8%	- 26%	- 36%	+147%	+ 2%	322M	0.0%	10.11	
0	FIDELITY JAPAN SMALL COMPANIES	FJSCX	High	+ 3.0%	- 13%	- 50%	+237%	+ 3%	339M	0.0%	6.95	
+	SCUDDER JAPAN FUND	SJPNX	High	+ 1.0%	- 26%	- 27%	+120%	+ 3%	361M	0.0%	7.36	F,S,W

++ Very Favorable
+ Favorable
0 Neutral
– Unfavorable

1 % Return with dividends & capital gains reinvested
2 Net assets in millions of dollars
3 Price – Net asset value/share (NAV)

4 No Transaction Fee (NTF)
F – Fidelity NTF
S – Schwab OneSource
W – Waterhouse NTF

Data Sources: Morningstar Principia Plus
Investors FastTrack

The INVESTECH MARKET ANALYST and MUTUAL FUND ADVISOR are published 17 times per year and include access to the twice-weekly InvesTech Financial Hotline. Pursuant to the provisions of Rule 206(4)-1 of the Investment Advisors Act of 1940, we advise all readers to recognize that they should not assume that recommendations made in the future will be profitable or will equal the performance of past recommendations. The contents of this letter have been compiled from original and published sources believed to be reliable, but are not guaranteed as to accuracy or completeness. James B. Stack is also President of Stack Financial Management (SFM), a registered investment advisor, and a separate company from InvesTech Research. Clients of SFM and individuals associated with InvesTech Research may have positions in and may from time to time make purchases or sales of securities mentioned herein.

SUBSCRIPTION RATES (U.S. dollars):
InvesTech Market Analyst $190/yr
InvesTech Mutual Fund Advisor $190/yr
BOTH COMPLETE SERVICES $295/yr
(Foreign add $2.00/mo)