

# MONEYLETTER.com<sup>®</sup>

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## Can Small Caps Continue?

by Walter S. Frank, Chief Investment Officer

You know what we mean. Small-cap funds, especially of the value variety, have been the only place to be over the last eighteen months. The performance of the small-cap funds has been outstanding, while the large-cap funds that make up the popular averages have languished in loss-land.

Naturally, when a broad group of stocks advances contrary to the "market" the question ultimately gets raised about how long this contrary outperformance will last? Small-cap specialists can come up with historical averages about small-cap outperformance as an economic upswing sets in. These are all well and good. But, as we have all learned by now, historical analogies can only take us so far. (How many times have we been told over the past two years, as the market went down and then up, that the Dow chart today looks eerily like the Dow in '29-'30. So what?) We come away from the evidence with little more than the fact that the small cap upswing will last for awhile. How long it will last is another matter. With that in mind, our answer to the small cap question is that, yes, the small cap rally can continue, but for how much longer, we just don't know.

What we do know, or at least common sense and market history tell us, is that the small cap outperformance will not last forever. In fact, what the long-term evidence (over 70 years) shows is that periods of outperformance by small caps are followed by periods of underperformance, and vice-versa. The important thing right now is to be aware of this phenomenon.

In the '90s we basically had a period of underperformance by small caps while the large-cap tech bubble swelled. Commenting on this, Ron Baron of the Baron family of funds quipped that small caps have underperformed since 1983 (when he started his first fund). This is an exaggeration, but it is true that the long-term trend did favor large-caps from '82-'90, and again from '94-'99. The bubble, remember, was a large-cap phenomenon in general. Only as the bubble burst did small caps come to the fore.

We should look at what has been happening these past two years as another phase of the cycle when the market swings from large caps to small caps. This rhythmic movement appears to be part of the natural life of the market. It can be seen as an example of the "reversion to the mean". By that we mean when one capitalization size pulls ahead of the other, the better performance finally ends as valuations diverge widely, and the second, now cheaper valued, group becomes the performance leader as it plays catch-up to the former market leader.

### Timely reversal

To paraphrase the old saw about market tops, nobody rings a bell to tell us when the capitalization pendulum is about to swing to the opposite direction. Yet we do have some hints about the timing of small-cap outperformance. Prof. Marc Reinganum of Southern Methodist University has studied the size effect in market returns. One of his findings, presented in an article in the Journal of Portfolio Management (Summer 1999), is that over a period as short as five years, the evidence shows that there are "reversals in the differential returns between small-cap and large-cap stocks." It doesn't make any difference whether one takes the smallest-cap stocks or mid-cap stocks. There is a time for large, and a time for non-large. The evidence for this reversal is equally strong right throughout the market when it is divided between the largest caps and any other cap segment of the market.

So five years is the longest period of outperformance by small caps we can reasonably expect, based on the evidence.

Another bite at the same apple comes from the T. Rowe Price New Horizons Fund. The fund is one of the oldest small-cap funds in existence. Using the fund's history since 1960, and marking periods of better or worse performance relative to the S&P 500, the fund's manager finds that the "New Horizons Fund's performance cycles typically last approximately 5 years." However, "recent performance cycles have been more compressed." The fund underperformed the S&P 500 by a significant amount from 5/96-3/99 (the bubble), but then outperformed, though by a lesser amount, from 3/99-12/01. Both periods were 2.8 years.

What the two results tell us is that the small-cap relative outperformance should last about 3-5 years. After looking at some charts in the small cap universe, we would date the beginning of the current small-cap upswing at about the beginning of last year. This means the small-cap thrust has lasted for about 1 1/2 years. We are led the conclusion that at the worst we have about another year of small-cap outperformance ahead of us. We may have more, but we are cognizant that things happen more swiftly in the market nowadays.

(continued on page 2)

### Market Trends

	Trailing 12-Mo Trend	Forward 6-Mo Estimate
Economy	Flat	Higher
Interest Rates	Lower	Flat/Higher
Dollar	Flat	Lower
Inflation	Lower	Flat
Dow	Higher	Higher
NASDAQ	Flat	Higher
Europe	Lower	Higher
Japan (Nikkei)	Lower	Higher
Hong Kong (Hang Seng)	Lower	Higher

(continued from page 1)

### The fund system

In the end, it is our fund selection system that will be the most useful indicator signaling that the small-cap era is ending. What we will see is large cap funds moving into buy territory and small caps falling back. So far we have not seen that pattern developing. When we do, we will not hesitate to follow the system's promptings.

## How Bad Are Profits?

If you read the numbers on operating profits churned out by the services, profits are woeful. As the final numbers for last quarter come in, overall profits are reported by Standard & Poor's to have dropped by 2% from a year ago. "That's the sixth straight quarter of falling profits," says Business Week (May 20, 2002). If you look a little deeper, it turns out the news is better than that. If you leave out coal, oil and gas companies, profits actually rose 9% from a year ago. The reason for the energy profit decline is that energy prices are still below last year's levels.

After the adjustment for energy, profits do not look so bad. Of course, with the broad averages down for the year, and the Nasdaq and S&P 500 challenging their February lows (remember Enron), Wall Street is in no mood to hear anything positive about profits. Gloom and skepticism are the order of the day.

### Positive profits surprise

Yes, you read it right. Despite Wall Street's hand-wringing there is positive news about profits. We borrowed this section's heading from a piece written by James Glassman, a senior economist at J.P. Morgan Chase. His point is that if we take a broader view of profits than that presented by the S&P 500 operating profits, we find that profits rose last year rather than fell as reported by the S&P 500.

This broader view of profits is presented by the Commerce Department's Bureau of Economic Analysis. What the Bureau reports, writes Glassman, is "that profits from current production of all corporations actually rose 5.7% over the four quarters of 2001. After-tax profits have returned to the impressive levels reached prior to the 2000 economic slowdown."

The important thing to remember is that the Commerce Department's profits numbers are of the entire corporate universe, both public and private. The S&P 500 is only a sample of the public portion of that universe, with some overrepresentation of some sectors. Also the government statisticians remove a few distortions in reported profits due to inventories, stock options and depreciation.

The bottom line is that after-tax profits, as calculated by the government, reached "an annual rate of \$628 billion in the fourth quarter—the highest figure ever recorded."

What does this mean for the market? Directly, not much. Wall Street is focused on S&P profits and P/Es derived from those profits. Wall Street generally couldn't care less about the Commerce profit numbers.

But indirectly we think these numbers are very encouraging. What they show is that the profit crunch has been concentrated in the large-cap firms. The crunch was not economy-wide. It implies that there was nothing systemic about the fall in profits we saw in the S&P 500 last year. It also implies that as the economy picks up we should see profits respond throughout the economy including the large caps.

We have maintained that we should see a market moving increase in profits as the economy improves over the rest of this year. The government figures for last year do not guarantee that outcome, but they certainly point in the right direction. \$

\* \* \*

Here are the alternatives for our "closed" portfolio funds:

- For Neuberger Berman Genesis substitute ICM/Isabelle Small Cap Value, T. Rowe Price Small-Cap Value, or Ariel Fund.
- For Fidelity Low-Priced Stock Fund substitute Fidelity Contrafund.

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## Perking Up

One of the worries that have been plaguing Wall Street is that the economy would slow down sharply after the booming 5.8% growth of the first quarter. The prime example of the slowdown for the recovery skeptics was the March retail sales number which showed only a trivial increase in sales for that month. Aha, said the skeptics, this shows that the consumer is tapped out and the all-important consumer will drag the economy down. And that will be the end of the recovery.

Let's leave aside that there was something suspicious about the weakness in the March numbers. Let's just consider that the idea of building a thesis about the economic outlook based on one month's numbers is naïve, at best. Well, the April sales number has arrived and the consumer weakness is a thing of the past (for the moment, at least). According to the preliminary numbers, retail sales rose sharply in April.

Aside from retail sales, the other economic numbers that have been coming out—the employment report and the Supply Managers' reports—all point to a recovering economy. True, the pace of recovery has slowed from the blistering pace of the first quarter, but that is normal. We weren't going to grow at 6% for the rest of this year.

True enough, the jury is still out on whether business investment will come through later this year. And this concern keeps the Wall Street bears in business. But if the economy continues on the pace it is now setting, and we believe it will, investment will follow. We expect to see a fairly robust economy for the rest of this year.

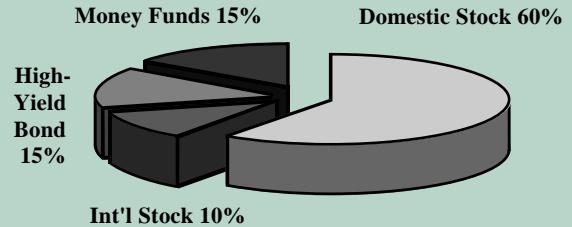
### Portfolio changes

The Hotline of April 30 contained our decision to transfer "hard" closed funds out of our portfolios and replace them with funds that are open to new investors. This new portfolio policy applied to Wasatch Core Growth in all three *MONEYLETTER* all-family portfolios and Wasatch Small Cap Value in the *MONEYLETTER* Venturesome and Conservative portfolios.

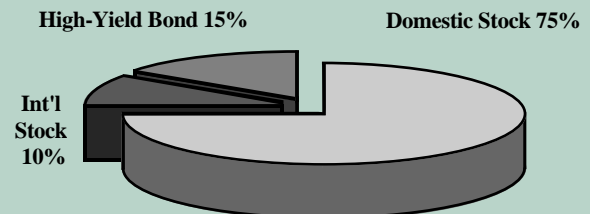
Here are the changes as of Wednesday, May 1. **Venturesome:** Switched 474 shares of Core Growth @ \$39.17 per share into 1,071 shares of Baron Small Cap Growth @ \$17.34 per share. Switched 4,011 shares of Wasatch Small Cap Value @ \$4.80 per share into 1,893 shares of Royce Opportunity @ \$10.17 per share. **Moderate:** Switched 501 shares of Core Growth into 1,131 shares of Baron Small Cap Growth. **Conservative:** Switched 419 shares of Core Growth into 946 shares of Baron Small Cap Growth. Switched 3,547 shares of Wasatch Small Cap Value into 1,647 shares of Royce Opportunity.

The same Hotline also advised the sale of Vanguard European Stock Index in the Vanguard Conservative Portfolio. The fund was to be switched into Vanguard International Growth. Here are the details. **Vanguard Conservative:** Sold 429 shares of Vanguard European Index @ \$20.17 per share. Purchased 568 shares of Vanguard International Growth @ \$15.22 per share. \$

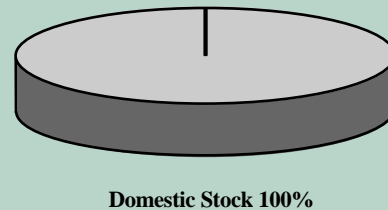
### CONSERVATIVE



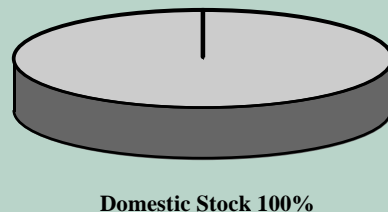
### MODERATE



### VENTURESOME



### SIGNAL



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## Domestic Stock Funds

RANK	5/10 2002	1Mo Ago	6Mo Ago	Ticker Symbol	FUND NAME (Max. Load)	Fund Type	Conservative Moderate Venturesome			TOTAL RETURN			PRICE	RISK		NTF/ wtf
							B	B	B	1 mo.	6 mo.	12 mo.	PER SHARE	Std. Dev.	Beta	
1	1	-	CGMFX	CGM Focus	SCVal	*	B	B	B	0.1%	40.7%	51.8%	\$25.91	55.1	0.02	
2	4	9	WMCVX	Wasatch Small Cap Value (closed)	SCVal	B	B	B	-3.3	28.6	26.5	4.68	27.5	0.71	FSW	
3	6	8	WGROX	Wasatch Core Growth+ (closed)	SCGro	B	B	B	-3.7	28.4	22.3	38.04	29.2	0.95	FSW	
4	9	85	IZZYX	ICM/Isabelle Small Cap Value	SCVal	B	B	B	-1.2	32.0	8.9	13.53	26.5	0.67	FSW	
5	13	17	PRSVX	T. Rowe Price Small-Cap Value	SCVal	B	B	B	1.2	24.0	23.8	25.81	16.4	0.44	fsw	
6	11	-	BSCFX	Baron Small Cap	SCGro	B	B	B	-0.9	28.5	14.5	16.91	28.0	1.07	FSW	
7	10	11	BERWX	Berwyn Fund	SCVal	B	B	B	-0.3	24.2	23.8	22.99	18.7	0.41	fsw	
8	8	22	VISVX	Vanguard Small-Cap Value Index	SCVal	B	B	B	-1.2	26.3	18.9	11.19	-	0.70	fsw	
9	15	46	EEQFX	Eclipse Small Cap Value	SCVal	B	B	B	1.4	24.7	16.4	13.78	18.6	0.75	sW	
10	2	-	OAKSX	Oakmark Small Cap	SCVal	B	B	B	-4.1	25.7	20.2	18.91	18.1	0.54	FSW	
11	7	48	RYPNX	Royce Opportunity+	SCVal	B	B	B	-1.2	25.3	14.8	9.94	27.3	0.77	fsw	
12	20	-	ARGFX	Ariel Fund	SCVal	(B)	(B)	(B)	0.4	20.6	22.4	41.65	18.9	0.40	FSW	
13	24	5	FLPSX	Fidelity Low Priced Stock (closed) (3%)	SCVal	B	B	B	0.5	19.6	23.8	29.95	16.6	0.57	fsw	
14	3	1	BPSCX	Boston Ptrns Smlcap Val (closed,1%<1yr)	SCVal	B	B	B	-2.8	20.7	22.9	18.97	-	0.52	FSW	
15	23	4	YACKX	Yacktman Fund	MC	B	B	B	0.4	19.0	21.8	11.98	18.2	0.55	FSW	
16	25	-	TRMCX	T. Rowe Price Mid Cap Value	MCVal	B	B	B	-0.9	20.2	19.6	17.97	15.9	0.60	fsw	
17	41	30	LLSCX	Longleaf Partners Smallcap (closed)	SCVal	H	H	H	0.6	21.8	13.3	24.60	17.0	0.45	fsw	
18	22	29	RYTRX	Royce Total Return	SCVal	B	B	B	-1.0	20.1	16.1	9.40	13.6	0.41	FSW	
19	18	26	PENN	Royce Penn Mutual+ (1%)	SCVal	B	B	B	-1.2	19.6	17.6	7.98	16.7	0.51	fsw	
20	12	19	RYLPX	Royce Low Priced Stock	SCVal	B	B	B	-1.9	20.1	17.3	12.28	24.8	0.69	FSW	
21	14	-	CRMSX	CRM Small Cap Value Inv	SCVal	B	B	B	-2.6	20.3	16.5	22.37	-	-	FSW	
22	29	43	RSPFX	RS Partners	SC	*	B	B	2.4	19.2	11.8	19.93	-	0.59	FSW	
23	19	217	NBFSX	Neuberger Berman Fasciano Inv	SCGro	B	B	B	-2.1	20.6	14.0	36.78	15.7	0.67	FSW	
24	16	14	HRTVX	Heartland Value	SCVal	B	B	B	-1.4	18.6	14.7	39.13	22.5	0.63	Fsw	
25	5	2	BUFSX	Buffalo Small Cap (closed)	SCGro	B	B	B	-4.3	17.5	21.2	20.41	-	0.69	FSW	
26	28	-	BGRFX	Baron Growth	SCGro	H	H	H	-1.0	18.3	14.1	31.88	25.4	1.06	FSW	
27	26	32	NBGNX	Neuberger Berman Genesis (closed)	SC	H	H	H	-1.0	17.7	14.0	22.14	19.6	0.62	FSW	
28	17	-	CRIMX	CRM Mid Cap Value Ins	MCVal	B	B	B	-3.0	18.6	14.6	19.40	-	-		
29	53	-	AVALX	Aegis Value Fund	SCVal	H	H	H	0.4	14.3	19.1	13.68	18.2	0.31	fw	
30	51	24	FDSCX	Fidelity Small Cap Ind. (1.5%r<90d)	SC	*	H	H	-0.3	13.2	20.9	17.16	22.8	0.83	fsw	
31	33	18	LSSCX	Loomis Sayles Small Cap Value	SC	B	B	B	-2.0	15.5	15.9	21.86	19.4	0.69	sW	
32	32	-	CAAPX	Ariel Appreciation	MCVal	B	B	B	-3.1	15.6	16.6	39.45	18.0	0.50	FSW	
33	-	-	SMCDX	Strong Mid Cap Disciplined	MCVal	H	H	H	-5.3	16.0	16.5	17.76	23.4	0.92	FSW	
34	21	16	MERDX	Meridian Fund	SCGro	H	H	H	-1.5	14.4	13.1	29.14	21.4	0.77	fsw	
35	48	21	FDVLX	Fidelity Value	MCVal	H	H	H	-1.6	15.7	10.2	55.59	22.8	0.64	Fsw	
36	38	45	LLPFX	Longleaf Partners	MCVal	H	H	H	-2.2	15.5	9.0	25.75	20.1	0.58	fsw	
37	30	37	OTCFX	T. Rowe Price Small Cap Stock Fund+	SC	H	H	H	-2.3	14.6	10.3	26.06	22.0	0.73	fsw	
38	27	-	BOGLX	Bogle Small Cap Growth (closed)	SCGro	H	H	H	-2.3	14.2	8.2	21.21	-	-		
39	61	23	VUSVX	Vontobel U.S. Value	LCVal	H	H	H	-1.9	11.5	13.4	21.40	22.0	0.44	FsW	
40	-	-	TASCX	Third Avenue Small-Cap Value	SCVal	H	H	H	-1.6	12.5	8.6	16.09	17.5	0.58	FSW	
41	44	20	BEMVX	Berger Mid Cap Value	MCVal	H	H	H	-2.7	13.0	8.7	17.38	23.3	0.80	FSW	
42	31	-	BPMCX	Boston Partners Mid Cap Value	MCVal	H	H	H	-4.4	13.5	9.7	11.56	18.3	0.76	FSW	
43	90	171	FFTYX	Fidelity Fifty+	LC	H	H	H	3.2	13.1	-1.0	18.46	28.2	0.87	Fsw	
44	35	52	MUHLX	Muhlenkamp Fund	MCVal	(H)	(H)	(H)	-3.2	15.6	2.3	56.03	26.4	0.91	FSW	
45	36	31	RYPRX	Royce Premier	SC	H	H	H	-3.6	11.7	10.8	10.85	18.7	0.62	fs	
46	45	72	VIMSX	Vanguard Mid-Cap Index+	MC	H	H	H	-3.1	12.7	4.1	12.20	26.2	1.02	fsw	
47	57	7	CFIMX	Clipper Fund	LCVal	H	H	H	-3.1	9.4	12.2	87.20	15.7	0.30	sw	
48	94	172	ACBGX	Bonnel Growth Fund	MCGro	H	H	H	-0.5	12.7	-0.2	14.52	43.9	1.10	fsw	
49	99	137	PRNEX	T. Rowe Price New Era	LC	H	H	H	0.3	12.2	-0.5	24.28	26.7	0.72	fsw	
50	47	78	PESPX	Dreyfus Mid Cap Index	MCGro	H	H	H	-3.2	12.5	3.5	21.85	25.8	1.02	FSW	
51	40	62	NAESX	Vanguard SmallCap Index+	SC	H	H	H	-3.6	13.1	2.5	20.08	26.7	0.87	fsw	
52	54	35	WPSRX	Westport Small Cap R	SCVal	H	H	H	-2.8	11.2	5.2	19.50	-	-	FSW	
53	39	6	TGVOX	TCW Galileo Value Opportunity	MCVal	H	H	H	-3.3	9.4	10.3	18.39	31.3	0.97		
54	-	-	TAVFX	Third Avenue Value	MCVal	H	H	H	-0.8	10.2	3.2	38.07	16.0	0.61	FSW	
55	75	28	PRWCX	T. Rowe Price Cap Appreciation	LCVal	H	H	H	-0.8	8.3	7.6	15.64	10.7	0.24	fsw	
56	34	117	LMASX	Legg Mason Special Investment Trust	MC	(H)	(H)	(H)	-4.3	15.4	-5.5	33.69	30.6	1.18	w	
57	65	98	SCHVX	Strong Multicap Value	MCVal	H	H	H	-0.9	11.6	-1.7	54.22	19.9	0.83	Fs	
58	60	120	DNLDX	Dreyfus New Leaders	MCGro	H	H	H	-1.6	11.8	-1.5	40.92	25.2	0.92	FSW	
59	66	70	BVALX	Babson Value	LCVal	S	S	S	-2.6	11.1	1.3	44.50	20.6	0.70	FSW	
60	43	125	BARAX	Baron Asset	MCGro	H	H	H	-4.9	13.7	-2.2	44.84	28.1	1.22	FSW	
61	50	10	WAAEX	Wasatch Small Cap Growth+ (closed)	SCGro	H	H	H	-3.1	7.0	11.6	31.42	37.8	1.15	FSW	
62	86	42	MQIFX	Mutual Qualified (1%) CIZ	MCVal	S	S	S	-0.9	9.0	2.9	17.10	16.9	0.61	sw	
63	73	15	OAKMX	Oakmark Fund	MCVal	S	S	S	-2.3	8.4	6.0	35.96	20.6	0.59	FSW	
64	49	162	JAVTX	Janus Venture (closed)	SCGro	S	S	S	-2.8	13.0	-5.9	42.76	58.6	1.63	FSW	
65	102	49	BEGRX	Mutual Beacon (1%) CIZ	MCVal	S	S	S	-0.3	8.0	1.5	13.54	15.9	0.58	sw	
66	72	3	OAKLX	Oakmark Select (closed)	MCVal	H	H	H	-2.9	6.2	9.1	27.54	26.2	0.83	FSW	
67	85	12	TWEIX	American Century Equity Income	MCVal	S	S	S	-2.5	5.9	8.9	7.18	15.1	0.44	FSW	
68	67	33	HOVLX	Homestead Value	MCVal	H	H	H	-2.5	8.2	3.2	26.33	18.1	0.59		

*Bold funds* are currently held in *MONEYLETTER* model portfolios.

*Advice:* B=Buy, H=Hold, S=Sell, (B), (H), (S)= advice new this issue, \*=not for this portfolio. +=Appropriate for Signal Investors.

*Std. Dev.:* monthly standard deviation based on two-year returns.

*Beta:* fund's correlation to the market (S&P 500 = 1.0). A fund with a beta greater than 1.0 is more volatile than the S&P 500.

*NTF/wtf:* NO TRANSACTION FEE/with transaction fee (F/f) for Fidelity, (S/s) for Schwab and (W/w) for TD Waterhouse.

# FUND SCORECARD & RECOMMENDATIONS

5

## Domestic Stock Funds (cont.)

RANK	5/10 2002	1Mo Ago	6Mo Ago	Ticker Symbol	FUND NAME (Max. Load)	Fund Type	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE PER SHARE	RISK		NTF/ wtf
										1 mo.	6 mo.	12 mo.		Std. Dev.	Beta	
69	74	27	DODGX	Dodge & Cox Stock	LCVal	*	S	S	-2.9	8.6	2.8	101.80	19.8	0.64	sw	
70	62	47	KAUFX	Federated Kaufmann Fund+ (0.2%)	MCGro	S	S	S	-2.7	7.6	4.4	4.26	33.5	0.86	FSW	
71	106	51	MUTHX	Mutual Shares (1%) CIZ	MCVal	S	S	S	-0.7	7.6	0.2	19.96	16.6	0.62	sw	
72	76	13	TWVLX	American Century Value	MCVal	S	S	S	-3.1	5.3	7.2	6.93	20.4	0.59	FSW	
73	71	34	HAVLX	Harbor Value	LCVal	S	S	S	-3.2	6.8	2.4	14.62	20.0	0.76	sw	
74	95	41	TWEBX	Tweedy, Browne American Value	MCVal	S	S	S	-1.8	6.3	0.9	23.82	15.2	0.51	fsw	
75	88	133	MFOCX	Marsico Focus	LCGro	S	S	S	-1.0	8.2	-5.3	14.21	31.5	1.12	FSW	
76	109	107	FCNTX	Fidelity Contrafund (3%)	LCGro	S	S	S	-1.4	6.4	-1.3	43.91	20.1	0.84	fsw	
77	37	39	SAFGX	Safeco Growth Opportunities+	SC	S	S	S	-5.4	7.5	1.7	24.67	26.0	1.12	fsw	
78	58	119	MPSCX	MSI Small Cap Value (closed)	SCVal	S	S	S	-4.4	9.0	-4.7	17.56	25.5	0.77	fsw	
79	117	36	SSHFX	Sound Shore	MCVal	S	S	S	-2.8	6.0	0.1	30.65	18.4	0.60	sW	
80	59	134	VEXMX	Vanguard Extended Market Index	MC	S	S	S	-3.5	8.4	-5.1	22.70	31.4	1.17	fsw	
81	77	74	GABAX	Gabelli Asset	MC	S	S	S	-3.6	7.6	-3.1	33.15	17.2	0.76	FSW	
82	68	181	SRFCX	Liberty-SteinRoe Capital Opportunities	MCGro	S	S	S	-3.2	10.4	-10.7	21.30	35.2	1.26	FSW	
83	112	106	SAOPX	Salomon Brothers Opportunity	LCVal	S	S	S	-1.8	6.1	-2.3	46.52	16.5	0.58	sw	
84	115	173	TWHIX	American Century Heritage	MCGro	S	S	S	-2.1	9.2	-9.9	11.06	32.1	0.98	FSW	
85	55	73	VEXPX	Vanguard Explorer+	SCGro	H	H	H	-4.8	7.7	-2.4	57.68	34.0	1.03	fsw	
86	107	44	PRFDX	T. Rowe Price Equity-Income	LCVal	S	S	S	-2.8	5.1	0.8	23.86	16.7	0.53	fsw	
87	46	118	LMOPX	Legg Mason Opportunity Trust	MC	H	H	H	-5.7	12.2	-12.9	9.88	-	-	-	
88	79	40	MPVLX	MSI Value Portfolio	MCVal	S	S	S	-5.2	6.8	-1.2	15.18	22.5	0.70	fsw	
89	92	139	MGRIX	Marsico Growth & Income	G&I	S	S	S	-1.9	7.0	-8.1	14.49	29.7	1.08	FSW	
90	64	79	RPMGX	T.Rowe Price Mid Cap Growth	MCGro	S	S	S	-3.8	5.5	-1.8	37.84	24.5	1.12	fsw	
91	52	-	THPGX	Thompson Plumb Growth	LC	S	S	S	-5.7	3.9	4.8	41.56	19.6	0.69	fsw	
92	56	50	PBSVX	PBHG Small Cap Value	SC	S	S	S	-5.4	6.5	-3.0	19.41	28.5	0.87	FSW	
93	96	157	SLSSX	Selected Special Shares	MCGro	S	S	S	-3.3	7.5	-9.4	10.57	23.9	1.04	sW	
94	69	84	STDIX	Strong Discovery+	MCGro	S	S	S	-3.5	5.1	-3.8	16.39	25.1	0.83	FSW	
95	81	67	FCV SX	Fidelity Convertible Securities	Convrt	S	S	S	-2.7	4.6	-5.0	18.94	27.4	0.89	Fsw	
96	98	178	FDFFX	Fidelity Independence (ret. only)	LCGro	S	S	S	-1.8	6.7	-13.5	16.23	42.4	1.24	Fsw	
97	80	90	STCSX	Strong Advisor Common Stock (closed)	MC	S	S	S	-4.7	5.1	-6.8	19.04	23.2	0.95	FSW	
105	119	59	FEQIX	Fidelity Equity-Income	LCVal	H	H	H	-4.5	2.1	-6.8	47.72	18.4	0.74	Fsw	
108	108	25	VWNDX	Vanguard Windsor	LCVal	H	H	H	-6.2	2.1	-5.9	14.76	23.3	0.86	fsw	
186	159	105	VHCOX	Vanguard Capital Opp (\$25,000)	MCGro	H	H	H	-8.4	-5.1	-19.9	20.51	38.1	1.06	fsw	

Dow Jones  
NASDAQ  
S&P 500

-4.3%  
-9.4  
-6.7

3.5%  
-12.5  
-5.8

-8.9  
-24.8  
-16.0

indexes do not  
include dividends

## International Stock Funds

1	10	2	OAKEX	Oakmark Intl Small Cap (closed)	Int'l	B	B	B	4.4%	30.9%	21.7%	\$13.43	25.6	-	FSW
2	5	3	MAPTX	Matthews Pacific Tiger	Pacific	*	B	B	5.5	32.6	11.4	9.93	47.1	-	FSW
3	1	4	FSEAX	Fidelity SE Asia (3%&1.5%r<90d)	Pacific	*	B	B	3.0	31.0	11.2	12.57	38.5	-	fsw
4	6	13	PRASX	T. Rowe Price New Asia	Pacific	*	B	B	2.5	28.0	4.9	6.86	33.6	-	fsw
5	2	8	FEMKX	Fidelity Emerg Mkts (3%&1.5%r<90d)	Int'l	*	B	B	0.3	27.0	9.6	8.73	32.9	-	fsw
6	3	-	OAKGX	Oakmark Global (2%r)	Global	B	B	B	-0.1	23.0	17.2	14.64	-	-	Fsw
7	13	5	OAKIX	Oakmark International	Int'l	B	B	B	1.7	24.1	8.5	16.42	24.3	-	FSW
8	9	10	SCOPX	Scudder Pacific Opportunity	Pacific	*	B	B	2.0	24.3	5.1	9.71	33.5	-	FSW
9	7	11	VEIEX	Vanguard Emerg Mkts Stock Index	Int'l	*	B	B	-0.1	23.2	6.9	9.20	32.3	-	fsw
10	4	12	MNEMX	Montgomery Emerg Mkts (closed)	Int'l	*	B	B	-1.0	23.9	5.2	9.49	31.6	-	FSW
11	29	-	ICHKX	Investec China & Hong Kong	Pacific	*	(B)	(B)	10.1	19.0	-12.4	12.65	39.2	-	FSW
12	14	-	FIVFX	Fidelity Aggressive Intl.	Intl	B	B	B	1.2	15.8	5.3	13.28	25.6	-	Fsw
13	16	14	PFIFX	Preferred International	Int'l	B	B	B	2.3	14.3	-0.4	12.40	17.4	-	w
14	17	16	HAINX	Harbor International	Int'l	H	H	H	2.1	12.6	0.5	32.03	17.8	-	sw
15	15	7	TBGVX	Tweedy, Browne Global Value	Global	H	H	H	-0.1	12.5	1.0	19.86	14.6	-	fsw
16	8	27	PRLAX	T. Rowe Price Latin America	LatinA	*	H	H	-7.8	15.6	-0.8	9.60	43.5	-	fsw
17	24	19	BJBIX	Julius Baer Intl. Equity A	Int'l	H	H	H	2.7	9.4	-1.7	22.46	28.8	-	FS
18	25	37	FPBFX	Fidelity Pacific Basin (3%&1.5%r<90d)	Pacific	*	H	H	3.3	11.4	-9.7	15.13	30.0	-	Fsw
19	12	15	SLAFX	Scudder Latin America	LatinA	*	H	H	-7.8	13.6	-1.0	20.46	37.7	-	FSW
20	22	24	FIGRX	Fidelity International G & I	Int'l	H	H	H	2.1	9.5	-5.8	19.99	22.0	-	Fsw
21	30	9	FDIVX	Fidelity Diversified International	Int'l	H	H	H	2.5	7.5	-2.2	20.03	20.4	-	Fsw
22	11	20	FLATX	Fidelity Latin Amer. (3%&1.5%r<90d)	LatinA	*	H	H	-9.3	12.6	-3.5	12.15	40.4	-	fs
23	23	1	LLINX	Longleaf Partners International	Int'l	H	H	H	-0.3	5.2	0.8	12.83	-	-	fsw
24	20	21	USIFX	USAA International	Int'l	H	H	H	0.8	7.2	-5.9	17.46	18.1	-	fw
25	28	23	ARTIX	Artisan International	Int'l	H	H	H	1.0	5.8	-5.2	18.84	32.6	-	FSW
26	26	58	WPJGX	CS Warburg Pincus Japan Growth	Japan	S	S	S	2.0	12.7	-30.0	5.50	52.7	-	FSW
27	32	28	VWIGX	Vanguard International Growth	Int'l	H	H	H	0.6	5.0	-12.7	15.02	17.6	-	fsw
28	44	48	VNEPX	Vontobel International Equity	Int'l	S	S	S	4.6	3.6	-15.5	13.31	21.1	-	Fsw
29	31	45	SGSCX	Scudder Global Discovery (closed)	Int'l	S	S	S	0.6	5.4	-14.2	23.30	34.4	-	FSW
30	38	30	CMISX	Columbia International Stock	Int'l	S	S	S	1.2	3.9	-11.3	12.19	22.2	-	fsw
31	21	6	FWWFX	Fidelity Worldwide	Global	H	H	H	-3.2	3.2	-5.4	14.41	18.5	-	Fsw
32	35	-	GIGRX	Gabelli Intl Growth	Intl	S	S	S	1.5	3.1	-12.6	14.24	21.0	-	FSW
33	36	39	TWGGX	American Century Global Growth	Global	S	S	S	0.2	4.1	-13.7	6.34	-	-	FSW
34	55	50	VPACX	Vanguard Pacific Stock Index	Pacific	*	S	S	3.1	3.4	-19.7	7.05	24.7	-	fsw
42	18	18	FIEUX	Fidelity Europe (3%&1%r<90d)	Europe	H	H	H	-4.3	2.5	-10.7	24.13	20.6	-	fsw

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## FUND SCORECARD &amp; RECOMMENDATIONS

## Specialty Funds

RANK	5/10 2002	1 Mo Ago	6 Mo Ago	Ticker Symbol	FUND NAME (Max. Load)	Fund Type	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE	RISK		NTF/ wtf
										1 mo.	6 mo.	12 mo.	PER SHARE	Std. Dev.	Beta	
1	1	-	USERX	United Services Gold Shares	Gold	*	*	*	19.3%	99.6%	91.2%	\$5.43	36.40	0.69	sw	
2	4	-	BGEIX	American Century Global Gold	Gold	*	*	*	19.8	69.0	81.0	8.60	45.30	0.69	FSW	
3	2	-	USAGX	USAA Precious Metals & Minerals	Gold	*	*	*	15.1	69.9	79.7	10.44	46.80	0.87	w	
4	3	-	FSAGX	Fidelity Sel Gold (3%)	Gold	*	*	*	11.9	63.1	67.4	22.17	49.20	0.89	fsw	
5	5	-	FGLDX	INVESCO Gold (3%)	Gold	*	*	*	18.1	60.5	60.5	2.68	39.20	0.72	FSW	
6	7	-	SCGDG	Scudder Gold	Gold	*	*	*	17.6	60.3	53.7	10.57	36.70	0.74	FSW	
7	6	-	VGPMX	Vanguard Sp Gold/Pr Metals (1%r)	Gold	*	*	*	10.1	46.0	46.9	11.59	43.10	0.87	fsw	
8	9	-	CGMRX	CGM Realty	RealEs	*	*	*	0.1	33.4	33.6	16.19	15.80	0.26	fsw	
9	10	-	STMDX	Stratton Monthly Dividend REIT	RealEs	*	*	*	-4.7	19.5	24.4	28.22	14.50	0.21	fsw	
10	12	-	VGSIX	Vanguard Special REIT Index	RealEs	*	*	*	-5.3	13.6	19.0	12.84	14.40	0.17	fsw	
11	14	-	FRESX	Fidelity Real Est Investment	RealEs	*	*	*	-4.6	12.8	17.0	19.38	15.10	0.21	Fsw	
12	20	-	FSTEX	INVESCO Energy	Energy	*	*	*	4.9	15.8	-6.5	19.82	46.20	0.90	FSW	
13	18	-	RSCOX	RS Contrarian	Altern	*	*	*	4.1	14.5	-3.8	10.87	23.50	0.72	FSW	
14	19	-	VGEXX	Vanguard Sp Energy (1%r)	Energy	*	*	*	1.6	13.6	2.2	27.86	32.00	0.70	fsw	
15	13	-	CSRSX	Cohen & Steers Realty Shares	RealEs	*	*	*	-5.9	12.5	15.3	46.80	16.20	0.25	FSW	
16	8	-	UMPIX	ProFunds Ultra Mid-Cap	Levrgrd	*	*	*	-7.0	20.4	-5.0	28.51	-	-	FSW	
17	11	-	POSCX	Potomac Small Cap Plus	Levrgrd	*	*	*	-4.6	14.2	-0.7	11.11	-	-	FSW	
18	30	-	FSENX	Fidelity Sel Energy (3%)	Energy	*	*	*	1.8	7.9	-6.9	24.83	33.40	0.78	fsw	
19	15	-	RYFIX	Rydex Financial Services	FinServ	*	*	*	-4.0	8.3	-2.2	10.04	28.80	1.05	fsw	
20	21	-	VGHCX	Vanguard Sp Health Care (1%r \$25k)	Health	*	*	*	-3.4	2.2	3.1	115.80	19.10	0.47	fsw	
21	16	-	FIDSX	Fidelity Sel Financial Serv (3%)	FinServ	*	*	*	-4.6	4.5	-2.6	101.70	27.40	0.94	fsw	
22	17	-	FSFSX	INVESCO Financial Serv	FinServ	*	*	*	-4.8	3.5	-4.4	27.14	26.90	0.93	FSW	
23	24	-	MERFX	Merger Fund	Altern	*	*	*	-0.6	-2.0	-2.6	14.57	5.42	0.13	FSW	
24	22	-	GATEX	Gateway Fund	Altern	*	*	*	-3.5	-0.2	-4.8	21.44	7.00	0.32	FSW	
25	32	-	RYEIX	Rydex Energy	Energy	*	*	*	-2.5	1.4	-12.2	10.72	27.50	0.64	fsw	
26	29	-	VGSUX	Vanguard Utilities Income	Utility	*	*	*	-4.8	-3.0	-18.2	11.51	14.30	0.26	fsw	
27	34	-	FSPHX	Fidelity Sel Health Care (3%)	Health	*	*	*	-4.6	-7.3	-8.1	112.50	20.00	0.40	fsw	
28	33	-	RYHIX	Rydex Health Care	Health	*	*	*	-6.0	-8.1	-9.5	10.43	19.60	0.41	fsw	
29	31	-	FHLIX	INVESCO Strategic Health Science	Health	*	*	*	-4.7	-9.8	-9.3	44.55	36.50	0.43	FSW	
30	23	-	RYNVX	Rydex Nova	Levrgrd	*	*	*	-9.9	-9.2	-24.8	22.51	29.60	1.49	fsw	
31	25	-	PSPLX	Potomac U.S. Plus	Levrgrd	*	*	*	-10.0	-10.1	-25.6	9.15	29.00	1.46	FSW	
32	36	-	FSTUX	INVESCO Utilities	Utility	*	*	*	-5.2	-14.3	-38.7	10.04	17.60	0.57	FSW	

## Bond Funds

RANK	5/10 2002	Ticker Symbol	FUND NAME (Max. Load)	Conservative	Moderate	Venturesome	TOTAL RETURN			PRICE	Standard Deviation	Sec 30-Day Yield	Average Maturity	Modified Duration <sup>1</sup>	NTF/ wtf
							1 mo.	6 mo.	12 mo.	PER SHARE					
<b>Short Term</b>															
1		VFSTX	Vanguard Short Term Corporate	*	*	*	0.6%	0.0%	4.9%	\$10.75	0.73	5.28%	2.7	2.3	fsw
2		SCSTX	Scudder Short Term Bond	*	*	*	0.2	-0.2	4.1	10.54	0.76	4.00	2.6	2.0	FSW
3		FSHBX	Fidelity Short Term Bond	*	*	*	0.2	-0.8	3.1	8.78	0.83	4.53	2.4	1.8	Fsw
<b>Intermediate Term</b>															
1		VBMFX	Vanguard Total Bond Market Index	*	*	*	0.8	-0.7	5.7	10.11	1.24	5.79	8.8	4.6	fsw
2		VFITX	Vanguard Fix-Inc Intrm. Treas.	*	*	*	1.5	-2.0	6.1	11.05	1.40	5.29	7.9	5.4	fsw
3		FBNDX	Fidelity Investment Grade	*	*	*	0.6	-1.6	4.3	7.33	1.40	4.95	6.5	4.8	Fsw
<b>High Yield ("Junk")</b>															
1		NTHSX	Northeast Investors Trust	*	B	*	1.6	12.8	4.1	7.87	7.34	8.49	5.9	-	fsw
2		VVEHX	Vanguard High Yield Corporate	B	B	*	0.8	4.1	1.3	6.27	1.52	8.46	6.7	4.5	FSW
3		BUFHX	Buffalo High-Yield	B	B	*	0.0	3.3	3.5	9.91	6.95	8.08	7.8	4.7	fsw
4		SPHIX	Fidelity High Income	B	B	*	0.0	4.9	-4.9	8.03	1.28	9.24	5.4	-	Fsw
5		CMHYX	Columbia High Yield	B	B	*	0.0	1.0	2.8	8.76	-	7.14	5.8	3.8	FSW
6		PRHYX	T. Rowe Price High Yield	B	B	*	0.3	1.1	-1.9	6.68	1.72	9.24	7.5	4.3	fsw
7		STHYX	Strong High Yield Bond(1%r)	*	B	*	-1.9	-1.4	-12.5	7.61	8.06	11.17	5.7	3.9	FSW
8		FHYPX	INVESCO High Yield	*	*	*	0.0	-3.6	-24.8	3.34	1.49	12.68	6.5	4.2	FSW
<b>Zero Coupon</b>															
		BTTRX	Benham 2025	*	*	*	2.8	-11.9	7.5	32.39	-	-	-	-	FSW
<b>Tax-Free Alternative</b>															
1		VWITX	Vanguard Muni Bond-Intermed	*	*	*	1.1	-0.1	4.4	13.43	1.37	3.97	6.1	4.7	fsw
2		FLTMX	Fidelity Spartan Intermed Muni	*	*	*	0.6	-1.6	3.0	9.95	1.50	3.86	7.9	5.3	Fsw
3		SRIMX	Liberty-SteinRoe Inter. Muni	*	*	*	1.1	-1.6	1.8	11.28	1.32	3.65	8.3	6.1	FSW
<b>International</b>															
1		BEGBX	American Century Intl Bond	*	*	*	3.4	-1.3	5.7	10.30	2.57	3.62	-	-	FSW
2		PYGFY	Payden Global Fixed Income	*	*	*	0.5	-2.2	3.9	9.82	3.34	3.83	8.0	5.7	fsw
3		RPIBX	T. Rowe Price Intl Bond	*	*	*	3.1	-3.6	1.7	7.99	2.29	3.33	9.0	6.3	fsw
<b>Strategic Income</b>															
1		FNMIX	Fidelity New Markets Income	*	*	*	-2.0	5.4	1.8	11.40	7.15	7.43	-	-	Fsw
2		RPSIX	T. Rowe Price Spectrum Income	*	*	*	0.4	-1.0	1.6	10.67	1.16	5.44	-	-	fsw
3		JAFIX	Janus Flexible Income	*	*	*	0.6	-3.5	1.4	9.18	1.42	5.49	8.2	5.4	FSW

<sup>1</sup>Modified Duration—Average time individual bonds within a fund are actually held.

## Fidelity Closes Low-Priced Stock for Six Months

Fidelity Investments announced on May 6th that it would be closing Fidelity Low-Priced Stock Fund (FLPSX) to new accounts for six months. Only existing shareholders as of the close of business on May 16th will be able to purchase the fund. Fidelity expects to reopen the fund in November.

The fund's assets more than doubled in the last 15 months, and its cash position had swelled to 19 percent at the end of March. By closing for six months, Fidelity believes Portfolio Manager Joel Tillinghast will have an opportunity to invest the cash in his best ideas and maintain his excellent performance. Tillinghast has been manager of the fund since its inception in 1989.

Fidelity Low-Priced Stock Fund has delivered excellent average annual total returns of 26.5%, 15.8%, and 17.0% over the one-, five, and 10-year periods ending March 31, 2002. The fund is currently rated a "Buy" at #13 in the *MONEYLETTER* rankings and is held in all three Fidelity-only portfolios. Since this is a "soft" close—meaning existing shareholders can still purchase shares—we will continue to hold the position.

For more information, contact Fidelity at (800) 544-8888.

### Comings and Goings

- Vanguard recently announced that they have dropped the 0.50% purchase fee on one of *MONEYLETTER*'s funds: **Vanguard Small-Cap Value Index** (VISVX). The fund is currently ranked #8 on our Fund Scorecard and is in all three Vanguard-only portfolios. Call Vanguard (800) 662-7447.
- **Oakmark International Small Cap** (OAKEX) closed to new investors as of last Friday, May 10th. The fund is ranked #1 this week among international stock funds. Call Oakmark (800) 625-6275.
- Berger Funds recently introduced the **Berger Small Cap Value Fund II** (BVSIX). Also, as of May 10th **Berger Select** (BESLX) and **Berger 100** (BEONX) are merging, with "100" surviving. Call (800) 333-1001.
- Ariel Capital Management recently offered a new large cap growth fund, **Ariel Premier Growth** (APGFX). The fund will be sub-advised by Lincoln Capital Management, a relationship that Ariel believes will add large-cap growth flavor to Ariel's value focus. Call Ariel (800) 292-7435.

### MANAGED ACCOUNTS

For information on the "*MONEYLETTER* Managed Account" Program<sup>1</sup>, call Principal Resource Inc. toll-free at (800) 707-2060. Ask about PRI's free, no-obligation portfolio review.

Minimum investment is \$100,000.

<sup>1</sup>As an independent Registered Investment Advisor, Principal Resource Inc. will exercise discretion with regard to asset allocation and fund selection and may make investment decisions for client accounts that differ from recommendations found in *MONEYLETTER*.

#### 100% U.S. TREASURY FUNDS

	7-Day	30-Day	1-Year
Vanguard Treasury MMF	1.60%	1.60%	2.77%
Fidelity Spartan US Treas MMF	1.51	1.50	2.66
Gabelli US Treasury MMF	1.50	1.51	2.60
T Rowe Price US Treasury MF	1.44	1.44	2.59
Amer Century Capital Presv Fund/Inv	1.41	1.45	2.58
CMA Treasury Fund	1.38	1.39	2.28
Prudential Govt Sec Tr/US Treas/CI A	1.31	1.32	2.36
Dreyfus 100% US Treas MMF	1.24	1.25	2.50
DBAB Cash Reserve Treasury	1.23	1.23	2.28
US Treasury MF of America	1.18	1.18	2.14

#### GENERAL PURPOSE TAXABLE FUNDS

	7-Day	30-Day	1-Year
PayPal Money Market Fund	1.93%	1.93%	-
Bunker Hill MMF	1.90	2.07	2.83%
Touchstone Money Market Fund	1.88	1.89	2.86
Vanguard Prime MMF/Retail	1.83	1.81	2.90
Dreyfus BASIC MMF	1.79	1.80	2.99
HSBC Investor MMF/CI Y	1.79	1.82	2.90
Transamerica Premier Cash Res/Inv	1.72	1.73	2.85
Fremont Money Market Fund	1.71	1.78	2.79
TIAA-CREF Money Market Fund	1.71	1.72	2.82
SSGa Money Market Fund/CI A	1.68	1.73	2.75

#### TAX-FREE GENERAL PURPOSE FUNDS

	7-Day	30-Day	1-Year
Vanguard Tax-Exempt MMF	1.62%	1.57%	2.05%
Strong Municipal MMF	1.46	1.44	2.14
Amer Century T-F MMF/Inv Class	1.43	1.35	1.79
USAA Tax Exempt MMF	1.40	1.34	1.88
Fidelity Municipal MMF	1.38	1.32	1.87
Dreyfus BASIC Muni MM Portfolio	1.36	1.32	1.83
T Rowe Price Summit Muni MMF	1.36	1.32	1.93
Wachovia T-F MMF/Invmt Shrs	1.32	1.27	1.57
Northern Municipal MMF	1.31	1.25	1.78
Scudder YieldWise Muni MF	1.31	1.28	2.11

#### TAX-FREE STATE-SPECIFIC FUNDS

	7-Day	30-Day	1-Year
Vanguard CA Tax-Exempt MMF	1.57%	1.51%	1.88%
Vanguard OH Tax-Exempt MMF	1.56	1.53	2.11
Vanguard NY Tax-Exempt MMF	1.50	1.45	1.92
Vanguard PA Tax-Exempt MMF	1.49	1.45	2.02
Vanguard NJ Tax-Exempt MMF	1.45	1.41	1.95
Amer Century CA T-F MMF/Inv Class	1.36	1.36	1.68
USAA Tax Exempt CA MMF	1.35	1.30	1.84
Fidelity OH Municipal MMF	1.34	1.29	1.84
Northern CA Municipal MMF	1.33	1.20	1.59
Fidelity FL Municipal MMF	1.28	1.28	1.79
Fidelity PA Municipal MMF	1.28	1.24	1.81

Taxable equivalent yield = yield / (1—total effective tax bracket).

Funds are ranked by 7-day yields; 7-day and 30-day yields are compound yields as of 5/7/02. Third column refers to 1-year total return. Criteria for inclusion include: top-yielding unrestricted retail funds only, with minimum initial investment <\$25,000 and assets >\$100 million.

### MONEYLETTER SIGNAL

#### iMoneyNet's Money Fund Report Averages (MFA) 7-day yield vs. The Signal

Date	Signal	MFA	Avg. Mat.
04/30/02	1.68%	1.37%	56 days
05/07/02	1.65%	1.34%	57 days

Signal Portfolio Status = 100% in Domestic Stock Funds

## Third Avenue Funds Concentrate on Value

Third Avenue Funds founder and veteran value investor Martin Whitman puts his own spin on value investing. He doesn't believe in diversification, a concept embraced by most fund managers. Indeed, he has termed that strategy as one that's for the lazy. He believes in employing stringent research to identify attractive companies, and then taking concentrated positions in the portfolios.

### Safe and cheap

Safe and cheap: That's the mantra chanted by Third Avenue managers, who embrace Whitman's philosophies. Safe investments are those companies that have strong financial positions, competitive products and services, strong management, and a business that is easily understandable. Management must be strongly shareholder oriented, and have a good track record. But why must the business be understandable? So that reliable benchmarks are available to assist in assessing the company and its value.

Cheap means real cheap, in this case. Whitman and his team are deep value investors—they aim to buy businesses when they are valued at half of their valuation as a private entity, or as a takeover candidate.

Meanwhile, where many fund managers place a great deal of emphasis on how a company is expected to perform—predicted future revenue and operating earnings—the Third Avenue team does not. They focus on the balance sheet as the best measure of a company's value, and assess the quality and quantity of business resources.

If Whitman's team cannot find stocks that meet their criteria, they do not hesitate to let cash build in the portfolio. Third Avenue Value's cash position was in the double digits last year, and currently is about 10%. Small-Cap Value's cash horde, meanwhile, is now a lush 25%.

Once they have bought that cheap, safe stock, Third Avenue managers are willing to wait, and wait, and wait for the expected appreciation. Portfolio turnover was a low 30% recently in Third Avenue Value (TAVFX) and only 18% in Third Avenue Small-Cap Value (TASCX). Looking at that another way, in Third Avenue Value, the average stock is held nearly seven years. But don't think the managers hold an investment unconditionally. Whitman and team will jettison a stock when there has been a fundamental change in the business or capital structure of the company. Should a stock's market value become overpriced relative to intrinsic value, it will be sold as well.

### Top Five Holdings and Industry Sectors (% of Assets)

Third Avenue Value (TAVFX)		
AVX Corp.	4.2%	Electronics 12.5%
Tejon Ranch	3.7	Real Estate 11.3
MBIA, Inc.	3.2	Japanese Blue Chips 9.0
Toyota Industries	3.1	Semiconductor Equip. Manuf. 8.9
Tokio Marine & Fire	2.7	Financial Insurance 4.8

Third Avenue Small-Cap Value (TASCX)		
MONY Group	3.1%	Natural Resources & Real Estate 14.5%
Credence Systems Corp.	3.0	Semiconductor Equip. Manuf. 9.9
Brascan Corp.	2.9	Electronics 7.5
Electro Scientific Inds.	2.8	Investment Cos. 6.6
The Phoenix Cos.	2.5	Life Insurance 6.3

As of March 31, 2002.

### Similarities and differences

The two funds mentioned above are both value funds, run in the same basic manner. But there are notable differences. Third Avenue Value, which dates to late 1990, has broader investment parameters. It is an all-capitalization fund—it can invest anywhere in the market capitalization spectrum. Recently, it has tilted to large-cap stocks. The fund can also invest overseas (Japanese blue chips are currently featured prominently in the portfolio). But its more interesting characteristic is its ability to invest in senior securities, such as preferred stocks and debt. Whitman, a specialist in bankruptcies, looks for high-yielding debt—at least 500 basis points above what comparable credits are yielding—with strong covenant protection. About 5%-15% of the portfolio's assets are often dedicated to distressed debt.

Third Avenue Small-Cap Value, dating to April 1997, is a more focused fund than its sibling, and is generally more concentrated. As its name suggests, this fund trolls only in the small-cap sector, defined as the market capitalization range of stocks in the Russell 2000 Index. Finally, it's a stock-only fund: no distressed debt here.

Third Avenue's deep discount value investing technique, combined with a concentrated portfolio approach, does not necessarily show stellar results year after year. However over the long haul, it has paid off. \$

*Third Avenue Funds*  
767 Third Avenue, Fifth Floor  
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Minimum investment: \$1,000/\$500 IRA

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