



Investment Watch

3rd Quarter, 2001

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"BLACK TUESDAY"

We just ended the **worst month** of the **worst quarter** of the stock-market since the last quarter of 1987 — "Black Monday". It wasn't a Monday this time, it was a Tuesday - a "Black Tuesday" on September 11th that the real tragedy, not in dollar terms, but in the loss of the innocence of our Freedom and loss of our fellow citizens.

We all feel the financial pain due to the drop in our investments. At the same time, it seems irrelevant to be discussing investments when all of us are grieving over the personal losses of our country. But somehow I feel that for the foreseeable future, the US economy will be linked with the war on terrorism. Inseparably joined - sharing the same fate. We've just begun this war on terrorism, but "Black Tuesday" did not mark the beginning of our losing fight with the economy, the market meltdown nor the losses in our assets. It had started a many, many months before. Let's look back to the time before the terrorist attack.

Since April, 1999 the markets and the economy have been battered and bruised. The

past 18 months feel like those historic heavy weight fights between Ali and Frazier. The second quarter was a pretty good round. We thought the April market rebound may signal an end to the fight followed by a rebound in the economy. But, as soon as we

thought the worst was over, we walk right



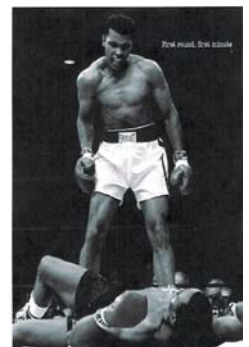
into that *stinging left jab*, again. How did Frazier feel? No one had ever seen that constant circling footwork, those lightning fast left-right combinations, and then the flurry of punches following the famed "Ali Shuffle".

The pummeling has lasted an eternity - bad news followed by worse news. Poor corporate earnings and the surprising increase in unemployment in August (from 4.5% to 4.8%!) triggered forecasters to postpone and downsize the projected economic recovery. Ali felt in control after knocking down Frazier with that hard right hand, but then realized Frazier would not only get up, but also continue his relentless, punishing body attack. The ups-and-downs, ebb-and-flow of these epic battles were exhausting and frustrating.

Back in August, we asked ourselves, *what round is the stock market in?* Will Greenspan's Fed rate easing take hold and end the fight by knockout or are we in a battle which will last a full 15 rounds?

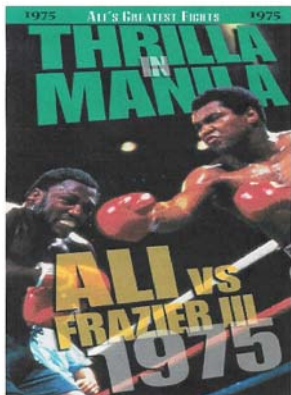
Historically, bear markets have lasted between 3 to 70 months and average 21 months. We're about 18 months into this bear market. Therefore, we haven't quite passed the mid-point, which would put us into about the 7th round.

Greenspan, trying to end it early, has aggressively cut the Fed rates beginning in January and again in March, April, May, June and August. Fed rate easings are not one-punch Sonny Liston knockouts, but rather they take six months to work their way through the economy. This means, we should



"Black Tuesday" (cont'd)

have already seen the effects of the January easing and the March through August easings should be showing up soon. Some pundits believe Greenspan's attempts to stimulate the economy were too slow and too weak, but if he has any power left in his punches, we'll be glad, once again, that he is in our corner.



Based on these historic measures, it looked like the markets were in the later rounds of that ultimate brawl dubbed the "Thrilla in Manila", which will result in two consecutive negative years

that haven't been seen since 1973-74. With the world economy nearing recession, we couldn't imagine it getting any worse.

And then it happened September 11th — "Black Tuesday". It was a left followed by a short, straight right hand that came out of nowhere and landed squarely on our jaw. Our whole being was shaken. Our whole country was brought to it's knees. We were dazed as the referee began his knockout count, everything stopped. The planes quit flying, the airports and the stock market closed, it felt like we were down for the count.

The subtraction of two weeks in September will take its toll on our economy, which will most likely push us into a recession this year. But just like Ali, we have a lot of good people in our corner — Bush and Congress with a bi-partisan push for a substantial tax cut. Greenspan pumping billions into the banking system and slashing rates further.



Most experts believe you need capitulation and contagion to signal the bottom of the market. This means that people have given up on the markets. Did this occur in the days following the terrorist attack? No one knows

for sure. The S&P is still trading at 26 times earnings which is much higher than the historic bottoms of 16-17 and has gained back half of the loss it took immediately after September 11th.

What "Black Tuesday" changed was the near term outlook. The intermediate and long-term economic outlooks for the United States are still bright—low inflation, substantial cash on the sidelines, favorable fed policies designed to stimulate the economy and the unity of all Americans behind bi-partisan leadership.

However, even with all this solid framework, we need a spark. A spark to ignite renewed economic growth. Although the aftermath of September 11th punctuated the downturn. It was not the cause. The U.S. markets merely



grieved along with its people. The spark for the rebound may now indeed be tied to the war on terrorism.

Implausibly, many financial gurus are now talking about faith - faith in the greatness of America, faith in our freedoms, faith in our financial system, faith in our ability to overcome inhumanity. Maybe faith is the link and the spark. The will of the American people and of the world will win this war on terrorism.

However, trying to predict the duration and emotional swings of this war is just as impossible as predicting when the economy will rebound and the direction of the stock market. *They are inexplicably linked.* Just like the strength of our economy will flourish, the will and unity of the American people will prevail over inhumanity.

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