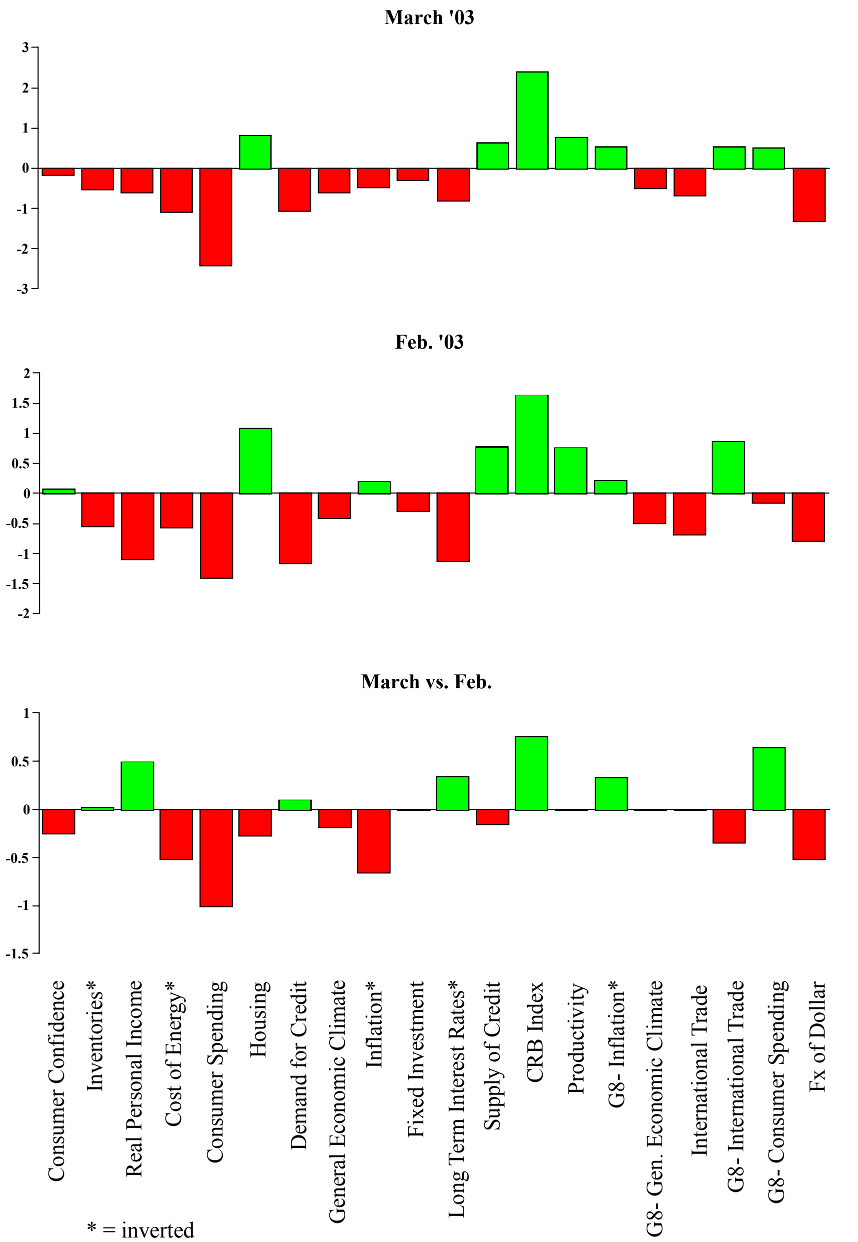
Downturn May Be Short Lived March 18, 2003

The following charts show fact based trends in ASC Economic factors as of March 2003 as compared to February 2003 and changes expressed in standard deviations around the norm, hereinafter referred to as “units”.



* = inverted

[-------------Domestic-------------][-International-]

ASC Factor indicators of future activity show that the economy weakened last month. Following are significant changes in trends last month expressed in standard deviations around the average rate of change or "units." Initial unemployment claims fell by .88 units. Real Income rose by .49 units. Cost of Energy rose by .51 units. Consumption fell by a unit. Inflation rose by .65 units. The CRB Index rose by .76 units. G8 Exports fell by .34 units. G8 Consumption rose by .64 units. The Foreign Value of the dollar fell by .51 units. The current ASC factor sum is 95.9, as compared to 97 last month. Last month there was significant weakness in consumption and a large loss of jobs. The shock of higher energy prices, high levels of indebtedness, war uncertainty and lack of job creation are taking their toll on the consumer.

The US economy has now experienced back to back declines in consumption and recent declines in consumer installment credit which generally only occur during recessionary conditions. Unfortunately, the slow down that we began discussing in Dec. '02 has apparently arrived. The question now is how long and how deep. Since there was some limited improvement in the ranking of economic sensitive groups, we appear to be getting close to the bottom. When the economy stabilizes at a depressed condition, poised to begin recovering again, some of the economic sensitive groups begin to perk up. In terms of changes, the 1.5% decline in consumption and the 310,000 loss in jobs may already be at a high water mark. Even though the second quarter is likely to remain weak, the rate of descent is likely to diminish. Unless there is a cascading effect which does not appear that likely, the third quarter should see some improvement over the second. So the next few quarters are projected to follow along the lines of the following: Q1 '03 through Q4 '03, 1.5 %, 1.5%, 2%, 3.5 %, respectively. Not exactly a robust outlook, but an improvement nonetheless. Of course, if cascading were to take place, then these projections would have to be modified.

The case for the lack of cascading is based upon precursor conditions. Cascading is the familiar progression of weakness in consumption leading to involuntary inventory accumulation and cutbacks in production creating job losses, lack of real income growth and a depressed consumer which restarts another cycle. This process has already happened to a certain extent. We have already had an inventory correction. We have already lost over two million jobs. We are now seeing the retreat of the consumer. Since goods production accounts for less than 20% of our economy, cutbacks by the autos are unlikely to have a significant rippling effect because the potential for further reductions has been limited by existing low inventory levels. With the uncertainty of terrorism, sniper shootings, war against Iraq, negative wealth effect, weakening US dollar, soaring energy costs and job losses, what else is likely to go wrong? Even if the war against Iraq goes badly, it should not last over a month. When the war begins, energy costs are likely to drop significantly giving the consumer immediate disposable income. Seeing US firepower in action should help restore Americans' self confidence.

This is not the first time that Fed Chairman Greenspan has been slow to recognize the need for stimulus. In November 1989, just before the recession of 1990, Fed minutes indicated "that there is no sign of a slowdown", and late in the year in 2000 when President-elect Bush was talking about a recession, Greenspan did not agree at first. To his credit, he quickly reversed course in early 2001. The quicker he realizes that a slow down is upon us and responds, the shorter this slow down will be. Now that the Japanese have been monetizing their debt at around $10 billion per month to get out of deflation and nothing has occurred, other Fed officials are likely to get comfortable with such a notion. The US's $6.5 trillion in outstanding debt represents a lot of potential stimulus. Remember it was only several years ago that Fed Chairman Greenspan was talking about the problem of a disappearing long bond market because of all the government surpluses. My, how quickly conditions can change!

Based on current fact based trends, defensive groups slipped in rank. The utilities stayed at the top at a rank of 1, up from 4 last month. Other defensive groups such as foods and consumer growth fell quite sharply from 5 and 10 respectively to 18 and 28. The ASC model has taken a significant step away from its prior defensive position. Accounting for part of the change in the decline of defensive groups and rise of energy and chemicals are inflation and the CRB Index. The recent large increases in the PPI are having an effect on ASC's Inflation factor. With the consensus having a deflationary mind set, large increases in the PPI, up 11.7% over three months, have been practically ignored. Since the ASC model is fact-based, it does not ignore any reported result, no matter what the consensus.

Investment Strategy

Equities:

Groups that are well positioned are electric utilities, pharmaceuticals, and weak dollar cyclicals such as capital goods, papers and chemicals. Over weights in S&P groups are advised in Basic Industries, Health Care, Capital Goods Technology and Utilities. Market weights are advised in Capital Goods, Communications Technology and Energy. Underweighted are Financials, Consumer Cyclicals and Consumer Staples. With slightly less defensive rankings this month, we upgraded Capital Goods Technology to an overweight and downgraded Financials and Consumer Staples to underweights.

Fixed Income:

With a whiff of a stabilizing economy and a little inflation, our posture on bonds is less positive. Over the intermediate to longer term, the yield on the long bond is likely to be heading higher. Regarding the issue of duration, on a scale of 1 to 10, with 10 representing a maximum position in shorter term debt and 1 representing a maximum position in Long Treasuries, we would rate the current environment as an 8, up from 6 last month, suggesting an average maturity of 3-4 years.

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