Investment Watch

2nd Quarter, 2003

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"REBUILDING"

I've been so used to writing about *gloom & doom,* that the recent good investment news has given me writers block. Could switch to singing? "Happy days are here again, The skies above are clear again", but I **never** could carry a tune. And some of the experts say the market is already over-bought and will correct! So the skies may not be clear for long. After the downpour of negative returns during the last three years (*when it rains, it pours),* this quarter's dramatic rebound makes me feel warm like that bright and sunny day in February.

The volatility of the markets seems to confirm the law of gravity *whatever goes up, must come down*. We don't have any control over the markets. But, now that we're feeling a little better, let's set aside time to review the basic **truisms** that we should cling to *through thick and thin*. America's rebuilding. **Let's rebuild our 401k!**

Pay yourself first. We build wealth by saving. True now, true always. If you stopped or reduced your savings due to the market meltdown and because you felt that you didn't want *to throw good money after bad*, reverse course and start rebuilding. Your return is affected by the total money in your account not by your contributions. Stopping your contributions has very little affect on investment performance. All savings is "good money" - pay yourself first by contributing to your Plan.

Tax-deferred savings is "better money". Okay, not *exactly* a truism but kinda catchy. How can some money be better, you ask? Because tax-deferred money can build faster, not only due to the initial tax savings that gives you more to invest, but also due to the tax sheltered compounding of the investment earnings as they grow. This two-fold advantage can produce such dramatic results that Albert Einstein referred to this compounding effect as *the eighth wonder of the world.*

A penny saved is a penny earned. The ancient Scottish proverb tells us that the money we save is like earning it all over again. Ben Franklin got it right when he said, *"If you would be wealthy, think of saving as well as getting."* Hence, take direction from Ben and the old Scots before you're able to spend it, put the pennies away for your future.

Don't rob Peter to pay Paul. After you've saved, don't withdraw your money. Withdrawals destroy the tax advantages of your savings, result in income taxes and may be subject to additional tax penalties. Moreover, the last three years have proven Frank K. Houston's platitude, *"to acquire wealth is not easy, yet to keep it is even more difficult."* You've worked hard to build your savings, now give it time to work for you!

The early bird catches the worm. *A stitch in time... Time is money. There's no time like the present* to begin your retirement savings. Starting early gives you the financial

"REBUILDING"
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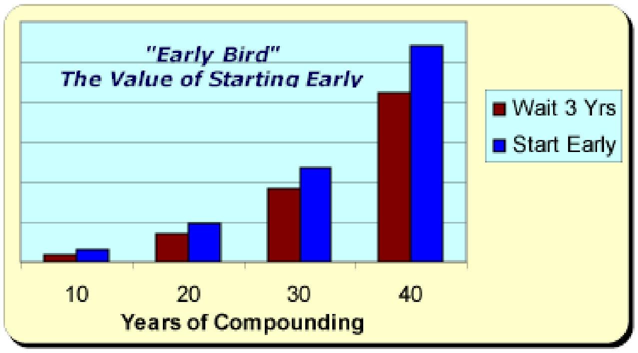
advantage of tax deferral for a longer period of ***time***. The compounding effect is more dramatic than you can imagine. The graph below



speaks louder than words to show you the dramatic difference of waiting just three years. Start early to build your retirement nest egg.

Okay, we get the message! We'll save *for that rainy day*. But are there any **truisms** about investing that can give me solace now that my 401k looks more like a 201k?

Dollar cost average. Studies show that you can't guess when to get in or out of the markets. Dollar cost averaging *takes the guesswork out* of investing by using the time-tested approach of regular periodic savings. The idea here is that the same dollar amount invested periodically will buy more shares when the price is down, but less when the market is up. Dollar cost averaging *takes the guesswork out* of when to invest by **averaging** the cost of your periodic purchases.

If you can't stand the heat, get out of the kitchen. The first step is to determine your **personal risk tolerance -** how much heat we can stand and not lose sleep? Back when the markets just went up & up, we were cool. Our risk tolerance wasn't tested. But now that the heat was turned up by one of the most severe market crashes, each of us has lost sleep to varying degrees and we understand our own risk tolerance a little bit better. That brings us to the second step in investing.

You're… **In it for the long run.** After you've determined your personal risk tolerance, the second step is to consider your investment **time horizon**, that is, how long you will be investing. This is a retirement plan. Your time horizon should extend until your retirement or even well into your retirement years. The longer you invest, the smoother the ride gets. Time smoothes out risk. So, the longer your time horizon the more risk you can take.

However, no matter what level of risk you choose to shoulder… **Don't put all of your eggs in one basket.** **Diversification** reduces your risk by spreading your savings among different asset classes. The two major "baskets" are stocks and bonds. Historically, stocks have **twice the yield** as bonds, but have **three times the risk**. Your choice between stocks and bonds is the most important determinant in the performance of your retirement plan investments.

After you make this main diversification choice, **bonds** are further diversified based on their maturity or duration. A money market fund has a very short duration and very little risk while a longer term bond fund has a long duration and more risk. **Stocks** can be diversified among many different asset classes with varying degrees of risk. Listed from least to most risk they are—Large Companies, Mid-sized, Small, International and Emerging Markets. The end result is your personal asset allocation of your investment portfolio.

Rebalance. Will Rogers said, "even if you're on the right track, you'll get run over if you just sit there." Therefore, after you decide on a certain asset mix, there's one last discipline you must learn. When your account gets out of kilter because one asset class does better than your others, you must rebalance to your original asset allocation. Rebalancing requires you to sell the "winners" and buy the "losers". Because we want to do the opposite, **rebalancing** is a difficult discipline to follow, but sound investing requires it.

A fool and his money are soon parted. No *get rich quick* schemes here. Remember, we are not gamblers nor speculators. We are long-term, disciplined investors. **Rebuild** with these time-tested **truisms** handed down through the ages!

Keith Kowalczyk 6/30/03