

Value View

april 5

2004

A STRAIGHTFORWARD INVESTMENT REPORT FEATURING VALUE AND GROWTH-ORIENTED STOCK-PICKS, FINANCIAL NEWS, MONEY TIPS AND INSIGHTS FOR INVESTORS.



China

A Closer Look

key to the future centers on China's currency and their banking system. Trade with the US, while important,

IT'S NO LONGER NEWS THAT CHINA IS BECOMING A MAJOR player on the world economic scene. Yet, as we've noted in past editions, investing in China is fraught with uncertainty, due to a still-unfree political situation, and insecure property rights. Despite our current lack of interest in Chinese stocks, China's renaissance clearly has implications for investor decisions worldwide, simply due to its market's enormous size.

Recently, China's newfound economic strength has become fodder for political electioneering, and talk of protectionism is once again rearing its ugly head. Candidates are falling over each other to see who can blame the Chinese more effectively than their opponents. Of course, our readers recognize such ranting as nothing more than political gamesmanship. Nonetheless, all efforts to "save jobs" at the expense of free trade can only be dangerous to the US economy. Looking back in history, identical rhetoric led to trade barriers, and the Great Depression.

For the moment, the greater issue may be what the future holds for China, and what impact that may have globally. The

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Nextel is a leading American provider of integrated cellular phone/walkie-talkie/pager/data communications. The company, which recently reported sizeable increase in 4th quarter profits, has seen its unique brand of wireless devices growing in popularity, and has been experiencing strong positive cash-flow trends. This has helped the company to reduce interest expense as well, further increasing profits. Nextel announced plans to increase capital spending on new antennas in coming quarters, and conservatively projected reduced subscriber growth, but is still projecting earnings in the \$2 range for the coming year. Marketing plans that include a strong presence at NASCAR events have proven particularly effective in growing their customer base, and effective coverage has helped the company's retention rate. Nextel's ability to keep its customers sets it apart from some competitors and provides an opportunity to gain market share. These factors provide us some confidence in Nextel's future. Even with somewhat lower growth, the company will still be tearing up the market. Nextel is a top pick for this era.

The gambling known as business
looks with austere disfavor upon the business known as gambling.
~ Ambrose Bierce ~

A dinner lubricates business.
~ Lord William Stowell ~

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... are companies on the cutting edge of the world's new architecture. Each enjoys a strong position in their changing field. They could be the blue chips of the future but are relatively unproven, and operate in fast-paced industries. The risk is greater, but returns can be outstanding. While they tend to be most appropriate for risk-oriented investors, conservative investors may want to hold a small position of some of these potential world-beaters as well.

First Data Corp. announced the availability of its DataSign™ products; which protect businesses and consumers from identity theft and fraud. DataSign™ products use a digital signing microchip that can be used in payment kiosks, cellular phones and other devices to verify users' identities.

Just days after reporting record third-quarter earnings, **Biomet** announced the successful completion of its move to acquire Merck's 50% interest in the Biomet-Merck Joint Venture for a purchase price of \$300 million. Biomet designs and manufactures products used primarily by musculoskeletal medical specialists including operating room supplies, spinal implants, and bone cements. Biomet attributes its strong earnings to an increase in sales and the company's aggressive push toward the spinal market.

A federal court upheld **Pfizer's** exclusivity for Diflucan until July 29th. This will prevent Indian drug-maker Ranbaxy Laboratories Ltd. from distributing a generic version of the drug until then. Pfizer announced that the FDA has approved Caduet, a new medication containing both of the company's Lipitor and Norvasc. Caduet will be used to simultaneously treat high cholesterol and high blood pressure. Pfizer is counting on this new pill, among several other drugs, which will maintain the company's strong earnings growth. Pfizer has also announced that it will discontinue development of the experimental antibiotic known as DK-507k, used to treat respiratory-tract and other infections.

In a move to better compete with rivals, **SBC Communications** has teamed up with EchoStar to offer satellite television to local telephone customers. SBC will receive and handle orders, customer billing, and installation scheduling. EchoStar will perform the actual installation in homes. The company plans to sell about 650,000 telephone lines in rural Michigan and Texas; which could bring the company about \$1.5 billion. In other news, Cingular Wireless, a joint venture between SBC Communications and BellSouth Corp., agreed to purchase AT&T Wireless Services Inc. for approximately \$41 billion.

Johnson & Johnson released a new adhesive bandage, BAND-AID: KIZU POWER PAD,

into the Japanese market. The company also announced an agreement to purchase Merck's 50 percent interest in the European non-prescription pharmaceuticals joint venture, Johnson & Johnson MSD Europe, for an undisclosed amount.

Tetra-Tech was awarded new contracts for various services including part of a \$200 million U.S. Air Force contract, a U.S. Navy CLEAN II contract, and a Port of San Diego Homeland Security contract. The leading provider of consulting, engineering, and technical services announced that it would buy Advanced Management Technology, which provides systems engineering and information management services to federal customers.

U.S. bond insurer, **MBIA**, reported a sharp increase in fourth-quarter earnings. The earnings boost was attributed to its international operations and record municipal bond sales. The company also increased its quarterly dividend to \$0.24 from \$0.20, showing managements' confidence in future performance.

Merck announced that Mexico has approved a new cholesterol drug, co-developed with Schering-Plough. The new drug is expected to be the best "bad cholesterol" blocking product on the market and should boost revenues for Merck. Merck was also

awarded an extra six months exclusivity for Vioxx.

Unilever PLC announced the sale of its Mexican food oils brands to a Mexican subsidiary of Associated British Foods PLC, for \$110 million. The brands included Capullo bottled canola oil, Mazola edible oil and Inca white fat. In 2003, these products had combined sales of \$124 million in Mexico.

Heinz reported an increase in third-quarter earnings. Analysts believe that the weak dollar drove the company's sales growth in Europe and Asia. Heinz also introduced several low-carbohydrate food products in the midst of the Atkins diet craze, which likely contributed to the earnings increase.

Home Depot reported an increase in fourth-quarter profits. The company made heavy investments in self-checkout counters, new merchandise, and other store upgrades to help reverse the previous year's decline in sales and hopes to regain some of the market share that was lost to Lowe's.

Microsoft was fined a record \$613 million by the European Union in one of numerous anti-trust suits involving the company's popular Windows program. However, the lawsuit is expected to be appealed and will likely have no immediate effect on Microsoft.

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Stock	Symbol	Price	Earnings	P/E	Gr. Est.	Recommendation
America Movil	AMX	\$38.65	\$2.11	18.3	20%	Buy Aggressively
CheckPoint Sftwre	CHKP	\$22.75	\$0.52	43.8	30%	Harvest
ChoicePoint Inc	CPS	\$38.03	\$1.22	31.2	20%	Harvest
Compudyne	CDCY	\$11.24	\$0.56	20.1	18%	Hold Loosely
Cytec	CYTC	\$22.25	\$0.65	34.2	35%	Hold Loosely
Engin'r'd Sup't Syst	EASI	\$48.81	\$2.61	18.7	18%	Buy
Intuit	INTU	\$44.63	\$2.09	21.4	20%	Hold
JAKKS Pacific	JAKK	\$14.99	\$1.66	9.0	15%	Buy
L-3 Comm.	LLL	\$59.48	\$2.35	25.3	25%	Hold Tightly
LeapFrog	LF	\$19.35	\$1.18	16.4	22%	Buy Aggressively
Nautilus Group	NLS	\$15.75	\$1.24	12.7	15%	Hold Loosely
NexTel	NXTL	\$24.66	\$1.41	17.5	25%	Buy Aggressively
Nvidia	NVDA	\$26.40	\$0.36	73.3	30%	Harvest
Priceline.com	PCLN	\$26.50	\$0.46	57.6	30%	Nibble
1-800-Flowers	FLWS	\$9.55	\$0.26	36.7	30%	Buy

GLOSSARY OF TERMS

Buy Aggressively	This rating designates the best buys at the best prices. It does not indicate momentum.
Buy	Also a good buy, but not as exciting or certain as the above.
Speculative Buy	Stocks with great potential, that may not be great values. These certainly involve higher risk.
Nibble	This rating suggests buying a little at a time as prices become more favorable.
Hold Tightly	An attractive stock which is probably too high to buy but does not warrant selling.
Hold Loosely	Stock approaching excessive valuation that may be traded out selectively for better buys.
Harvest	This is a sell rating for quality stocks which seem to be inflated in price. This does not suggest any impending problems. These stocks may be held by those who cannot afford to take profits, but the risk of holding is greater. Selling a portion of such shares is a good strategy.
Inconclusive	This terms is used when news creates uncertainty, or action appears to be negative, even if news has not yet appeared. Most people prefer not to hold stocks in periods of uncertainty and this rating is similar to a clear sell rating. We make this distinction because such undertainty can create outstanding valuations. We do not want to create the impression that we know something we do not.
Sell	The clear sell rating is reserved for stocks that have struck bad times and should be unloaded by all investors.



... features stocks that appear to be below their reasonable valuations, based on their expected future growth. Unlike many stock-pickers who seem to divide stocks into "growth" or "value" picks, we believe the growth outlook is one of the prime factors for determining value. These stocks may not always show immediate results, but should provide outstanding returns in the long-run.

Barnes & Noble continues to grow. Same-store sales are flying high, and earnings are also rising. In addition, sales at the company's dotcom subsidiary have also risen, and losses in that venture are being managed, as the company prepares to combine the two entities. The company also offered conservative estimates of next year's earnings between \$2.20 and \$2.27, slightly below analysts' expectations. Nonetheless, we still find the shares attractive, as all present news is positive.

Bio-Rad Labs, the leading producer of mad cow disease tests, has been selected by Canada's leading beef producing province, Alberta, as the exclusive provider of tests for their beef industry. Additionally, the tests received USDA approval here in the U.S. Bio-Rad's tests are highly desirable since they provide results within hours, unlike other methods. The company also continues to seek diverse products to add to its line of research diagnostics and research products, most recently acquiring Texas-based Hematronix, Inc., a developer of blood-testing quality control and reagent products. Earnings and sales continue to rise, and shares remain attractive.

After rising as high as \$12, **Atlantic Coast Airlines** has fallen back to \$7, providing a rare buying opportunity. The company is dealing with uncertainty about its ability to replace a commuter deal with bankrupt United Airlines. ACAI still has 33 planes in service with Delta Connection, but United made up a larger portion of its business, and that deal is ending with no reconciliation in sight. Atlantic Coast has plans to use its planes for an upstart low-fare commuter flight service with a hub in Washington, D.C. While any start-up is risky, the low-fare model has proven to be the most profitable approach to air travel. ACAI has historically been profitable, and we believe the company will find its way to continued profitability. We also like the fact that the shares sell significantly below its book value of close to \$8, providing a safety net of sorts.

ITLA Capital, parent of Imperial Capital Bank, is our latest pick in small banking. We've found significant success among these undervalued institutions, and continue to seek new opportunities as prices rise among the previous picks. ITLA is a niche market lender, primarily serving income real estate investors and also providing financing for movies, franchising, tax refund loans and small business lines. The company has recently been expanding its traditional banking arm, taking deposits in a variety of ways. Earnings are growing regularly, and ITLA attributes growth to positive improvements in most of the divisions. We rate the stock a strong buy. Meanwhile, among other small banks, **NetBank** and **Interest Bancshares** remain most attractive.

Also in the financial sector, **Countrywide Financial** is continuing to emphasize non-mortgage businesses. Management recognizes that growth in the future will come in other quadrants, and are repositioning toward traditional banking and bond

sales, in an effort to diversify. Enormous profit growth in mortgages over the past few years have given the company a lot of flexibility to adapt today, and we expect good results. The company recently announced their 2nd 3-for-2 split in 6 months.

National City Corp. will acquire Provident Financial Group, which owns 65 branches in the Cincinnati area in an all-stock deal. National City is still nicely priced, and we'd continue to buy.

Bancolumbia reported solidly higher earnings, as the bank improved efficiency and their mix of business. With earnings growth, the shares become even more undervalued than they had been, and become an increasingly good bargain for those interested in overseas investments.

Converium Holdings has proposed a dividend increase in the foreseeable future, and appears to have a successful focus on earnings growth in a cyclical industry. These shares are very attractive at current prices.

Conexant has completed the acquisition of GlobespanVirata. The combined company should remain profitable, and may allow the company to reduce costs. In addition, Conexant's penchant for decoupling unnecessary segments may cause the company to sell off parts of the old Globespan that may not fit. Either way, we think these tech shares are a value, and are buying.

Ariba continues to expand its Spend Management software system, adding new innovations to the popular expense management technologies. Shares have fallen in price recently, and this may be an ideal buying range.

Sea Containers reported increased revenues, while reported earnings fell. The company also announced a plan to purchase seven container ships at favorable prices in Australia and New Zealand, which will serve those markets and Asia. The company

also believes that the entry of the Baltic states into the European community will increase ferry traffic on its Silja line, and they plan to open new routes in the region linking Russia, Estonia, and Germany. The company also has plans for further acquisitions. We believe the company is significantly undervalued, and recommend these shares for all value-focused investors.

BT Group, the old British Telecom, has growing revenues from a fast-expanding broadband business, while the traditional phone business lags. The sizeable dividend will make investors happy while they await results. Overall, earnings per share, without currency adjustment, rose 7%.

We still find homebuilder **Beazer Homes** attractive, despite continued fears of a drop in new home sales. Thus far, the projected drop has not materialized, and we don't believe small rises in interest rates will significantly impact sales. We don't see sizeable rate increases until after November; the early stages of rising interest rates may actually see an increase in home sales, as buyers scramble to get in before they are priced out of the market. Thus, homebuilders are safe for the remainder of the year, and those in the Sunbelt, like Beazer, will probably achieve successes through the winter and early spring of 2005. Beazer is the most attractively priced of the builders, and thus earns our recommendation.

Nokia sees sales of picture phones skyrocketing and demand for cell phones generally growing rapidly. Schwab researchers downgraded the stock, fearing that new models may not be as cool as those of competitors, but we don't see the problem. Nokia is the market leader, and as such, will attract the mainstream buyers, who may not be seeking the sleekest phone. The company approved a sizeable share buyback, suggesting they have high expectations.

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Stock	Symbol	Price	Earnings	P/E	Gr. Est.	Yld.	Recommendation
Ariba	ARBA	\$2.83	\$0.05	56.6	35%	0.0%	Speculative Buy
Atlantic Coast Air.	ACAI	\$7.19	\$1.82	4.0	N/A	0.0%	Speculative Buy
Bancolumbia, SA	CIB	\$7.56	\$0.80	9.4	10%	2.4%	Speculative Buy
Barnes & Noble	BKS	\$32.60	\$1.94	16.8	14%	0.0%	Buy Aggressively
Beazer Homes	BZH	\$105.91	\$13.44	7.9	12%	0.4%	Buy Aggressively
Bio-Rad Labs	BIO	\$56.37	\$3.36	16.8	16%	0.0%	Buy Aggressively
BT Group	BTY	\$33.39	\$5.48	6.1	12%	3.3%	Buy Aggressively
Conexant Systems	CNXT	\$6.13	\$0.04	153.3	22%	0.0%	Speculative Buy
Constellation Brands	STZ	\$32.10	\$2.37	13.5	15%	0.0%	Buy
Converium Hldgs.	CHR	\$24.57	\$4.60	5.3	12%	0.0%	Buy Aggressively
Countrywide Fin.	CFC	\$95.90	\$12.47	7.7	16%	0.9%	Buy Aggressively
Intervest Bancshares	IBCA	\$18.00	\$1.53	11.8	14%	0.0%	Buy
ITLA Capital	ITLA	\$49.23	\$4.55	10.8	10%	0.0%	Buy
National City Corp	NCC	\$35.58	\$3.30	10.8	10%	3.6%	Buy Aggressively
NetBank	NTBK	\$12.21	\$1.13	10.8	14%	0.0%	Speculative Buy
Nokia	NOK	\$20.28	\$0.97	20.9	16%	1.5%	Buy
Sea Containers A	SCR.A	\$20.60	\$2.43	8.5	12%	0.2%	Buy Aggressively
Tele. de Mexico	TMX	\$34.91	\$3.30	10.6	13%	3.2%	Buy

... is a list of legitimate "blue chips" that we follow monthly. These stocks can generally be held for the long term without great concern for market changes. We rate them buy/sell for valuation only. While it may sometimes pay to move from an overvalued member of this list to a bargain-priced choice, most of these stocks can be held even when they are overvalued without significant long-term risk.

Compudyne Corp., an industry leader in sophisticated security products, reported an increase in fourth quarter earnings compared to last year. The company announced that it received a total of \$13.8 million in various contracts and awards in February. More recently, Compudyne Corp. was awarded a \$2.3 million U.S. Embassy contract for blast-resistant windows and doors.

America Movil posted significantly higher fourth-quarter earnings compared to one year ago, driven by recent acquisitions as its customer base rose to 43.7 million subscribers. The company also paid \$268 million for the use of rival Unefon's network capacity to keep up with increased demand for wireless voice and Internet services.

Engineered Support Systems was awarded several new contracts including a \$7.5 million U.S. Military agreement, an \$18 million Iraq support contract, and a \$13.6 million Army order. A \$6.8 million contract with the U.S. Army will provide equipment such as Warlock Green Jammers, which block radio frequencies that detonate remote-controlled bombs to Iraq.

Leading provider of identification and credential verification services, **ChoicePoint Inc.**, announced the purchase of iMapData, an information and analytics company, for an undisclosed amount. IMapData creates multicolor maps and reports that simplify complex business, economic, and geographic information. ChoicePoint also recently unveiled a new Mortgage Fraud Alert System that allows companies to contribute information into the system and then use the shared data to take action in suspected fraud cases.

Intuit reported a considerable increase in second-quarter earnings compared to one year ago. The developer and producer of tax preparation software also saw a ten percent increase in sales of its Turbo Tax product compared with the previous year. Intuit is now focusing on retail stores and the internet for software sales instead of directly selling to consumers.

JAKKS Pacific, a popular toy maker, reported a large increase in fourth-quarter earnings. The company also signed a licensing deal with Marvel Enterprises Inc. to make a version of its own TV Games device featuring Spider-Man character games. JAKKS' TV Games is a hand-held device that incorporates the games, controller, and processing functions into a single unit.

L-3 Communications, a leader in security and defense products and services, was awarded several new contracts for various duties. These include a \$3.6 million Air Force contract, a four-year Navy contract that could total \$63.6 million, a \$26 million agreement with the Israeli Airport Authority, and a \$12 million deal with the U.S. Army

Despite higher revenues, computer chip designer, **Nvidia**, posted lower fourth-quarter earnings compared to one year ago due to higher costs. Nvidia recently released a new software development kit for

3D artists and programmers. This new kit delivers a comprehensive development environment for optimized advanced shader effects in conjunction with Microsoft's DirectX® Shader Model 3.0. Nvidia also announced that it has teamed up with HI Corporation, the world leader in 3D software and games for mobile devices, to facilitate the advancement of interactive 3D games on mobile communication devices.

LeapFrog, a popular maker of children's educational toys, announced a considerable increase in fourth-quarter earnings. The company attributes these strong earnings to the popularity of its Leapster and Little Touch learning toys. However, shares of LeapFrog tumbled after the company announced that it would likely fall short of analysts' first-quarter predicted earnings.

Fitness equipment maker, **Nautilus**, announced that it would double warranties on Bowflex exercise machines to ten years. This move is intended to boost consumer confidence after the company was

forced to recall 420,000 Bowflex machines due to injury-causing defects earlier this year. Nautilus reported a substantial decrease in fourth-quarter earnings due to lower sales of its exercise machines.

Cytec, a maker of cervical cancer screening tests, announced it would purchase Novacept Inc., a producer of medical devices intended to treat excessive menstrual bleeding. The deal is intended to expand Cytec's line of women's health treatments and will cost the company \$325 million in cash.

NexTel reported a huge decrease in fourth-quarter earnings, but a substantial increase in revenue. The company states that this is due to a gain from the sale of an international unit that NexTel reported last year.

Priceline.com posted increased fourth-quarter earnings and reversed an earnings loss due to increases in travel bookings and decreases in operating expenses.

Stock	Symbol	Price	Earnings	P/E	Gr. Est.	Yld.	Recommendation
Biomet	BMET	\$38.36	\$1.28	30.0	18%	0.3%	Hold Loosely
ConAgra	CAG	\$26.94	\$1.63	16.5	12%	3.7%	Buy
Equifax	EFX	\$25.82	\$1.20	21.5	15%	0.3%	Buy
Fair, Isaac & Co.	FIC	\$36.08	\$1.62	22.3	20%	0.1%	Buy
FedEx	FDX	\$75.16	\$2.89	26.0	16%	0.0%	Hold Loosely
First Data Corp.	FDC	\$42.16	\$1.94	21.7	14%	0.2%	Hold Tightly
General Electric	GE	\$30.52	\$1.66	18.4	14%	2.5%	Buy
Heinz	HNZ	\$37.29	\$2.15	17.3	12%	4.3%	Nibble
Home Depot	HD	\$37.36	\$1.87	20.0	12%	0.6%	Nibble
Johnson & Johnson	JNJ	\$50.72	\$2.47	20.5	14%	1.9%	Hold
MBIA	MBI	\$62.70	\$5.52	11.4	14%	1.1%	Buy Aggressively
Merck	MRK	\$44.19	\$3.08	14.3	15%	3.3%	Buy
Microsoft	MSFT	\$24.93	\$0.88	28.3	20%	0.0%	Hold
Pfizer	PFE	\$35.05	\$1.56	22.5	15%	1.7%	Nibble
Radian	RDN	\$42.60	\$3.88	11.0	13%	0.2%	Inconclusive
Reuters	RTRSY	\$42.75	\$(0.24)	N/A	20%	2.1%	Harvest
Safeway	SWY	\$20.58	\$(0.08)	N/A	14%	0.0%	Sell
SBC Communic.	SBC	\$24.54	\$1.97	12.5	12%	4.4%	Nibble
SouthTrust Bank	SOTR	\$33.17	\$1.93	17.2	12%	2.5%	Hold Loosely
Tetra-Tech	TTEK	\$21.46	\$1.16	18.5	22%	0.0%	Hold Tightly
UniLever PLC	UL	\$40.30	\$2.56	15.7	11%	2.6%	Nibble

In the business world,
the rearview mirror is always clearer
than the windshield.
~ Warren Buffett ~

Margin Benefits are Marginal at Best

Margin is one of those things that novices find puzzling about the stock market, but the concept is really quite simple. Still, with understanding the basics of using margin accounts, determining the wisdom of using margin can be quite a conundrum.

A margin account is a traditional investment account with margin privileges. This means your broker has set up what amounts to a line of credit secured by the stocks and bonds in your account. Often this margin credit line is used to buy more stocks in the same account. But the account can also be borrowed against to buy real estate, make other kinds of investments, or simply to pay personal bills. The simple requirement is that enough assets must be kept in the account to maintain a certain value as collateral for the loan.

This is where trouble comes in. It's easy enough to maintain that collateral level when all is well, but when the economy becomes difficult and you are strapped for cash, this is also often the time when the market may drop. When the market drops temporarily, your equity value may fall, but the value of your debt doesn't change; you may encounter a "margin call" when you can least afford it.

A margin call is similar to any other loan being called in. You must pay up immediately. If you don't have the cash, your stocks and bonds are sold automatically to pay your debts. This compounds your problem: you end up selling your stocks when they are down, usually the worst possible time. Remember, the idea is to buy when prices are down and sell when they are up. So, in addition to all the other problems, margin loans can force you to make poor investment moves. In times of market crashes, a heavily margined account might be completely lost when the market drops only a fractional amount.

This leads to the idea of leverage, which is what margin accounts represent. Anytime you borrow to invest, you leverage your investment, or buying more than you can afford for a fractional down payment. Since one is buying stocks with borrowed money, or borrowing against stocks already owned, this is the result. Buying a home with a mortgage is a very similar process, but since the bank doesn't typically call your loan if home prices dip temporarily, many of the problems listed above do not arise. Still, a 95% mortgage is a highly leveraged deal, and it is very easy to lose your entire investment with even a small change in real estate prices. Even a typical 80% mortgage can wipe out the entire investment in a poor market.

Despite the many risks associated with margin or other forms of leverage, there definitely are advantages. Certainly, we've emphasized the opportunity to lose money faster, but you can also make money faster using these tools. If half of your equity comes from margin, you can gain money twice as fast. As stocks go up, your profits are compounded, because you own twice as many shares as you could normally afford. Thusly, when the market drops, you lose twice as fast.

Also, some people benefit simply by having a margin credit line available, without making use of it at all, or by only using it for short-term turnover. If used judiciously by a disciplined investor, there is virtually no risk in having access to a margin account. It is the use of the debt obligations that carry the costs. Imagine having a credit card that is never used, but the credit line is available in case of major emergencies.

In the end, leverage simply means that your gains or losses will be multiplied. Each investor must consider for him/herself the acceptable level of risk. However, we firmly believe that there are other risks, which carry better payoffs than simple use of leverage. While it is good for most investors to have access to margin, it may not be wise to use it often. In addition to interest costs, the added risks may end up causing more harm than good.

Bureaucracy defends the status quo long past the time when the quo has lost its status.

~ Laurence J. Peter ~

China, from page 1

is truly a secondary issue. So far, every story in the press involving China's economy seems to focus on trade issues, business growth, and cheap labor. Those are interesting. But an issue that is getting little or no press dwarfs them.

China has two overwhelmingly significant flaws in its economic structure that must converge in the relatively near future to cause a devastating collapse. When that happens, politicians and reporters who have focused on trade issues will look silly at best. Only recently have we begun to see unfocused stories about China's economic bubble. They cite skyrocketing real estate prices, and over-investment in specific industries such as automotive or aluminum, but they miss the bigger picture. Blame is cast upon Chinese peoples' penchant for gambling, as though it is the citizens who have brought this upon themselves. As usual, we know to look to the government for most of the fault.

China's financial system is a relic from the past: a dinosaur from the days before competition entered the economy. The nation's financial system primarily comprises four government-owned banks, which may be privatized in the near future. Thus far, these institutions have been shielded from competition and guaranteed by the government. Those who remember the savings & loan fiasco here know that thrusting such incompetent institutions into a competitive world is disastrous.

Long overdue for reform and utterly unprepared for the pressures of competition, the problem with China's financial system doesn't end there. China's economy has grown impressively over the past decade but much of that growth has resulted from tricks played by the government related to its currency and exchange rates. Over the past decade, the Chinese government has carefully "managed" exchange rates in such a way to devalue its own currency. This has made Chinese goods unnaturally cheaper for foreign currency holders, simultaneously impoverishing segments of the Chinese population. To accomplish this valuation, China has had to hold vast sums of dollars, yen, and other currencies, instead of exchanging them for yuan. This leaves other countries holding their yuan, and causes their value to fall. The falling yuan makes Chinese trade goods more attractive to the rest of the world, but the citizens suffer in the short-term, due to their weak currency.

We hear that the "new" administration in China (which is directly related to the "old" administration) has an interest in seeking a more responsible balance of payments and reducing inflation, but we find this unimpressive. Until actions follow the talk, there is little evidence that any real change will develop.

The combination of currency disruption and a weak banking system is a recipe for near-sure collapse. This leads us to recommend against the rush to Chinese stocks. However, the bigger question is

what impact this collapse will have on the world economy. It is difficult to determine how devastating the repercussions would be, but suffice to say, it won't be good. We'd imagine that stable economies will hold up best, but the very size of China's economy would likely affect everyone. On the other hand, due to the nation's relative isolation, it is possible that problems will be somewhat muted. The greatest threat would normally be a trade disruption. We might see some price increases in Chinese-produced goods, but the impact on the U.S. economy or those of other developed economies would not seem to be incredibly susceptible.

The greater fear may be that when China runs into trouble, it will start spending all those dollars they've been holding. The result may be further pushes toward inflation in the US, an outcome we've already predicted. In these days of rabid spending, and increasing debt, an inflation rate that pushes interest rates higher cannot be good. These concerns are not immediate, but a long-term investment plan requires some foresight.

Despite our concerns about the longer term, we are still quite confident that the economy, and hence the market, will perform relatively well through the elections in November. As a result, we strongly recommend making the best of it, as the longer-term outlook is uncertain. Perhaps when November comes, we will have a clearer view of the future, but for now, investing for the present is all that can be done.

The Synergy Effect

Have you ever considered that everything you want in life comes from someone else? The greatest minds in any field are keenly aware of the value of working with and involving others in life plans, business, work and personal commitments. We often have the notion that we operate in a vacuum, and that we are solely responsible for everything that happens in our lives. It is true that you are solely responsible for the thoughts you think and the things to which you choose to be committed. But when you reflect on all of your accomplishments, it becomes evident that many people play various roles in your achievements and pursuits. Since others are almost always involved at some level in our lives, a good question to ponder is how to effectively involve others more meaningfully.

Synergy, according to Webster's Dictionary is the "cooperative action of discrete agencies such that the total effect is greater than the sum of the effects taken independently." Note that a single horse can pull several thousand pounds. Two horses of equal size can pull nearly 4 times that. One community volunteer, who learned late in life the value of working with others, commented upon receiving a presidential award: "I thought about how you can't do anything by yourself, but with

other people you can change things." What a simple yet profound truth! One key area to focus upon is the manner in which they seek others to be enrolled in what is important to them. The first step, of course, is to realize the value of others. Next, we need to select the right people to work with us, to flesh out what we desire to create. Potential helpers are everywhere. Another important task for effective people is to clearly communicate the project or goal at hand. The help that is needed will lift any project into the stratosphere. This is similar to the "mastermind group" as outlined in Napoleon Hill's best-seller, Think and Grow Rich. In the chapter about the mastermind group, Hill expounds on the importance of aligning others in word, deed and advisement on any project. Hill further declares that a separate and distinct mind is created in the assembly of such a group and that the power derived from it is profound indeed.

Carefully look for more effective ways of communication. Not only is this enriching, the lives of others will also be enriched in countless ways. The real call here is to take on an attribute of leadership to draw others in. Synergy is a dynamic form of leverage. Avoid using it, and end up working four times as hard for half the results. Use it and watch the results expand exponentially!

Many persons have a wrong idea of what constitutes true happiness.
 It is not attained through self-gratification
 but through fidelity to a worthy purpose.
 ~Helen Keller~

Dynamics, from page 3

Safeway Inc. reported a significant fourth quarter loss. Safeway claims to have earned \$0.66 per share, \$0.02 above analysts' estimates. Much of these results stem from the recent Southern California strike, which the company estimates has cost \$0.23 per share. The company also took charges of \$0.88 per share after taking its Chicago-based Dominick's chain off the selling market. Safeway took additional charges of \$1.01 per share to cover impairment costs related to Randall's, its struggling, Texas-based chain. Moreover, the company has recently hired a new Chief Financial Officer. Certain pension funds have begun efforts to oust company management and directors because of accusations of personal gain from company relationships. Management's claims make us uncomfortable and we feel that the results are unclear, at best. As a result, we feel that most investors should avoid these shares until the dust settles. This will be our last report on Safeway for now.

SouthTrust, announced that it would purchase FloridaFirst Bancorp Inc. for \$146.1 million to help SouthTrust's expansion into central Florida.

ConAgra reported an increase in third-quarter earnings. The company attributes this growth to strong sales from its Armour, Banquet, and Chef Boyardee brands.

Fair, Isaac & Co., a maker of financial analytical software, announced a 3-for-2 stock split in the form of a 50 percent stock dividend.

FedEx reported a substantial increase in third-quarter earnings, citing growth in international priority shipments and savings from job cuts. More recently, the company announced that it intends to issue \$1.6 billion in grade 'BBB' debt to finance growth.



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