WHAT RECOVERY?

The economic recovery is now over two years old and, yet, we continually hear that "jobs are scarce". The fact is, they are.

We experienced 3 consecutive quarters of negative economic growth in 2001, but since then the economy has grown every quarter. It grew at an annualized rate in excess of 7% in the most recent quarter and yet the "jobs are scarce" phenomenon persists.

Fortunately, the 2001 recession was fairly shallow and short lived. It was short lived, in part, because consumers spent thru the recession of 2001. Our economic growth since then has been sluggish. Why the slow growth? When will it begin to accelerate? What impact will economic change have on our bond market and interest rates?

The unemployment rate that peaked at close to 6.5%, has declined slowly and still hovers at around 6%. The fact is that most companies have been slow to add new workers even as the economy has improved.

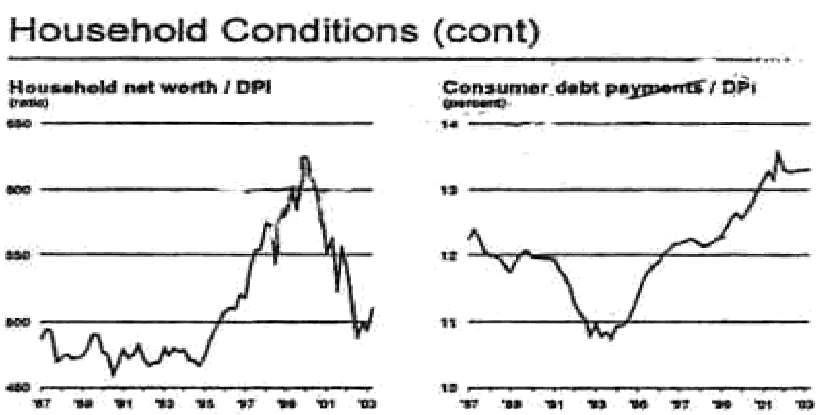
Business inventories remain low after reaching a 5-year high in mid 2001. Most companies remain "lean and mean" unwilling to stock a surplus of goods. The result, of course, translates into underutilized factories and under or unemployed workers. This explains why our unemployment rate continues to hover around 6%.

Growth in business spending last year was positive, but moderate. In the first quarter of this year, business spending was negative.

Manufacturing output declined steadily in late 2000/2001. That trend reversed itself this past year, but the current level of our manufacturing index remains far below its peak in early 2000. This fact contributes to a slower growth cycle.

"BORROWING DULLS THE EDGE OF HUSBANDRY"

The chart below also helps to explain why our economy has grown slowly since 2001:



The graph on the left depicts household net worth; the graph on the right measures consumer debt levels. Household net worth peaked in late 2000/early 2001 fueled primarily by increased stock values much of which existed in "unspendable" retirement accounts. Consumer debt levels INCREASED in 2000 at the same time household net worth was increasing. One would think the trend would have been the exact opposite. It was not. Consumers felt wealthier (and they were) so they borrowed against that newly created wealth and bought things. As the stock market declined in value over the next 3 years, wealth levels declined and the debt, for the most part, has remained. Consumers who now feel poorer (and they are) have significant debt to repay and, as a result, are not spending money as they have in the recent past. Debt levels are down from the peak, but remain historically high. This phenomenon has helped contribute to our slow growth over the past year.

HERE'S THE GOOD NEWS

The good news is that the sources for economic stimulus are all in place:

-low interest rates
-federal tax cuts
-a better performing stock market
-strong productivity growth
-dollar exchange rate depreciation

WHAT'S NEXT-WHAT TO DO?

We are not economists, but our market experience and instincts coupled with the economic analysis we share with you here lead us to conclude this:

There is no doubt in our minds that a strong foundation for economic growth is present. Inflationary pressures should remain contained in the short term.

Values in the bond market persist. Do not keep an abundance of cash in money markets. Remain vigilant in following your investor profile. If you would like help in developing one, please call us.

Review your portfolio for value added trading opportunities. This is an easy way to extract extra value in a low yielding environment. As always, stagger your bond maturities in the part of the yield curve where value exists. This strategy is time tested and helps insulate your portfolio from rising and declining interest rates.

We hope this is helpful.

Sincerely,

Ronald P. Bernardi
December, 2003

P.S. PLEASE CONTACT US TO LEARN MORE ABOUT OUR NEW INTERACTIVE ONLINE PORTFOLIO REVIEW SERVICE.