Stamper Capital & Investments, Inc.

The Wealth Preserver

www.risk-adjusted.com

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Fair Value on the DOW: 5,000 Biggest Bond Manager Agrees With Us

5,000 DOW - Biggest Bond Manager agrees with us, 3,000 negative DOW points later

"**Stocks Stink and will continue to do so until they're priced appropriately, probably around DOW 5,000, S&P 650, or NASDAQ God knows where.**" That's what **Bill Gross**, manager of the world's largest bond fund and routinely touted as the Peter Lynch (the best known manager of stock mutual funds) of the Bond Market, says in the September 2002 issue of his Investment Outlook published on the www.pimco.com website.

We will get to his analysis later in the article – first to explain our original forecasts (and toot our horn a bit).

We at Stamper Capital & Investments, first alluded to that opinion over 3000 negative DOW points ago (and something like 70% points ago higher on the NASDAQ) on our website (www.risk-adjusted.com) in our May 11, 1999 Best Opportunities section (under the Market Opinion tab): "Forgotten Asset Class (Muni's) Offer Best Relative Upside/Downside Characteristics Since 1987 Tops." In that article, we used investment analysis methodology, similar to what is now used by Bill Gross and his numerous sources (who are credited in his recent article on his website), to agree with our earlier conclusion. Basically, we graphed the S&P dividend yield divided by the yield of the U.S. Government Long bond. We demonstrated that "U.S. Treasuries were cheaper than stocks even just before the 1987 stock crash." We also demonstrated that "Muni's [were] as attractive to U.S. Treasuries as they get" and "The Clincher: Muni's represent[ed] an exceptional value versus their primary alternative: Stocks." We updated that study on our website on September 27, 2001 and demonstrated that it turned out that "[stocks] were their most expensive at the end of 1999 (about eight months after our initial study)," and that "Our original contention from April 1999, which [had] already paid off, still [held]."

In the January 2001 MONTHLY MISER (since renamed THE WEALTH PRESERVER), we much more explicitly explained the stock markets gross overvaluation in our article: "Money Magazine Predicts Dow Jones Plunge [by] 4,527 to 9,145 Points!" In this article, using data from the January 2001 issue of MONEY, "A Matter of Expecta-

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Bill Gross, King of Bonds, VS. Peter Lynch, King of Stocks

In his recent Investment Outlook Bill Gross asked, **How could earnings growth (0.6% annually over the last 100 years) be such a "pathetically small factor" of long term growth of the stock market?** Quoting from Mr. Gross' article: "As Peter Lynch said in a recent CNBC interview when asked about the future of the stock market, 'Well, since WWII corporate profits have grown about 8 or 9 percent a year….I don't see why that won't be different the next 50 years,' implying that stock prices would do the same or more." In response, Mr. Gross cites Peter Bernstein's August 2002 research piece entitled "The Trouble with Earnings" in pointing out:

> "At least 50% of the earnings growth over the past 40 years has been earnings of the 'mystical' kind – pro forma, operating, phonied up – those "earnings" didn't flow through to dividends."

In addition, Mr. Gross points out that:

> "A goodly portion of Lynch's 8-9% - and the faster portion it turns out – has come from newly created companies that are not even listed and available for purchase by outside investors."

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tions," by Jason Zweig, we looked at then current dividends and net profit multiples in relation to historically average market multiples and multiples at the 1973-1974 stock market bottom to determine **average values of the DOW at 3,110 based on dividends, 6,173 based on net profits and bear-market-bottom DOW levels of 1,555 based on dividends, and 3,086 based on net profits**. We summarized these findings on our website in our January 2001 Market Commentary (and a few more times since then).

Back to Bill Gross' recently published data and opinions.

Some gutsy quotes by Mr. Gross from his article are:

"…[Stock] earnings have been phonied up for years…"

"…the [stock] market still sells at high multiples of phony earnings."

"…[the general public] has been hoodwinked into believing corporations should hold onto [dividends] so that they can convert them into capital gains and save you taxes."

"Companies have been diluting your equity via stock options…."

"Then they pick you off by trading on insider information…."

"**Come on stockholders of America, are you naïve, stupid, masochistic, or better yet, in this for the 'long run?'"**

I believe these early statements are basically to get readers interested into the more mundane financial analysis (the part that is most interesting to us and uses a slightly different (but highly related) method that validates the methods we have used).

The crux of his argument and his methodology is that:

In order for the stock market to put forth superior returns (primarily in relation to bonds), **the most significant factor is "their beginning valuation** and that right now valuation remains poor. DOW 5,000 is more reasonable." In his words: "Stocks historically return more than almost all other alternative investments but **only when priced right when the race begins.** If you start from day one with P/E's too high or importantly, dividends too low, you will not obtain equity returns in excess of bonds." Thus, this is where his methodology is essentially the same as ours – relating current and historic multiples of earnings and dividends. In addition, the research he cites has some very important insights:

The 100 year average annual return in excess of inflation for stocks is only 6.7% (funny, academics used to say 10% to 11% then 8% to 9%)

The primary components of this 100 year historical 6.7% annual return are:

1) a beginning dividend yield of 4.2% (compared to only 1.7% currently)

2) rising valuations (P/E's going up) – these tripled from 100 years ago to now

3) "real earnings growth" or "real dividend growth" of only 0.6% points.

With reference to those insights he points out that:

1) **In order to get that "high" 6.7% real return, you have to start out at a low valuation point – a dividend yield of 4.2% just as the average investor did in 1900 – thus, dividends do really matter!!**

2) Real earnings and real dividends grew hardly at all - at 0.6% points per year. (**My comment - This knowledge goes completely against what the majority of financial professionals and consultants have been saying and completely opposite of what the financial media has published over the past ten years – its really unbelievable that the majority of financial professionals are lacking in such important knowledge.**)

Thus, he concludes:

1) **90% of the markets 100 year real return came from factors other than earnings growth** – "most of its came from the initial dividend yield."

2) **"The primary element in**

About Stamper Capital & Investments, Inc.

Stamper Capital & Investments, Inc. specializes in fixed-income portfolio management strategies and implementation tailored to each client's specifications. In order to help our clients meet their long-term investment goals while maintaining their chosen life-style, we focus on maximizing risk-adjusted performance, that is, we seek to obtain the most return per amount of risk our clients choose to take. The majority of our fixed income portfolios are invested in municipal bonds, but we also offer strategies for taxable municipal bonds, corporate bonds, mortgage-backed securities, high yield corporate (junk) bonds and convertible bonds. You could say we like bonds! In addition to private account management, Stamper Capital & Investments, Inc. manages The Evergreen High Income Municipal Bond Fund. In the 16 years our Portfolio Manager, Clark Stamper, has been managing accounts in the fixed income markets, he has come to believe that maximizing investor risk-adjusted performance is the most professional and prudent investment approach that can be implemented – and it works, as you can see from our top performance in the table on the back page of this newsletter. Call us today at 888-206-6295 for your free consultation to learn how municipal bonds can dramatically decrease your overall portfolio risk. We would love to teach you how our strategies will help secure your wealth for your future, or check out our website at www.risk-adjusted.com.

determining how a stock market is priced - whether it is cheap or expensive – is its yield." (Basically the method we at Stamper Capital have been using – and not just for stocks - our "Real Estate – Overvalued?" article in 4th quarter of 2001 THE WEALTH PRESERVER, essentially used the same analysis. **Incidentally, we believe Real Estate is headed for a NASDAQ style crash from its post - 1999 grossly overvalued levels).**
3) **"The [stock] market needs to yield close to 3.5% before it approaches fair value, and that means DOW 5,000.**

Bill Gross's DOW 5,000 forecast for fair value is similar our forecast of 6,173 based on net profits and 3,110 based on dividends at average multiples. Both studies used yield as the ultimate basis for their conclusions. **We want to emphasize that we believe the stock market will drop below fair value as it almost always does at a market bottom** – thus, we also projected market-bottom levels of 3,086 based on profits and 1,555 based on dividends at bear-market-bottom multiples.

No Accompanying Depression?

Here is where we and Bill Gross of PIMCO differ. In his most recent Investment Outlook for September 2002 on www.pimco.com, Bill Gross makes the case for a fairly valued Dow Jones Industrial Average of 5,000, or 41% lower that the 8,600 it stands at today. While we agree that 5,000 is about right for fair value, we expect an even lower level at the major bear market bottom coming up.

However, a possibly larger difference from our opinion is that **Mr. Gross indicates that "…[his] primary thesis is not that the U.S. economy is headed for a depression or that the economic sky is falling…"** Given his forecast for a 41% drop in the DOW (from today's 8,600) to be at fair value, we ask ourselves **just how large a drop in economic wealth does he think has to happen to cause a depression?** Remember the drop is really from the top at 11,722 in January 2000 – the drop from that level to DOW 5000 is 57%. **Our best answer is to look at what has been happening in Japan**, the economy that was going to own the world back in the 1980's and has now been in depression for over ten years with a new Nikkei low last week.

Japan's Nikkei Stock Index peaked in December 1989 at 38,915. By the September 1990 it was down 52% to 20,228. From that level the Nikkei had its second largest bear market rally – 35% to 27,400 in March 1991. Sadly the index has subsequently gyrated with a downward bear bias to a new low of 9,075 last week – thus, a 77% drop, so far and over ten years of depression.

In what is turning out to be an eerie repeat of Japan's experience, the S&P dropped 48% from its top at 1,527 in March 2000 to 797 this past July. Importantly, that index has already had two large bear market rallies - one of 24% from the low July 2002 to the rebound high of 962.70 on August 22, 2002 and an earlier 28% rebound from the July 2001 bottom to a rebound high in December 2001.

The numbers for the NASDAQ are worse than the S&P with a drop, so far, of 76% - one percentage point short of the Nikkei drop. The DOW has held up better but will probably catch up.

As far as U.S. investment forecasting goes, the equity downtrend is still intact and is continuing with lower highs and lower lows. **As far as forecasting the economy, as long as the trend in the stock market is down, we believe we are heading for continued economic weakness and with such large wipeouts in wealth (and the accompanying misallocations these wipeouts represent), we believe depression is inevitable from this point.**

"Investment Kings" - continued from page 1...

In this regard, we at Stamper Capital would also like to point out:

> Executive stock option compensation has not been accounted for correctly as an expense but as a dilution of shares. If accounted for correctly (based on the Accounting Principle of Conservatism – which apparently most accountants forgot about) as an expense that is deducted from revenues, the result would have been lower earnings.

Thus, Mr. Gross believes "You are being Hoodwinked America."

Conflicted Interests - **In relation to these two investment Super Stars, I would like to point out potential conflicts of interest that both of them face as officers of some of the largest financial management companies in the world. Peter Lynch is Vice Chairman of Fidelity – his conflict is that Fidelity's major source of revenues is equity investment management. William Gross is the Chief Investment Officier of PIMCO which generates a large majority of its revenues from the management of bond portfolios.** The question is, who can you rely on for information and advice on these two sectors (stocks and bonds)?

Our Fund Performance

Stamper Capital & Investments, Inc. has managed the Evergreen High Income Municipal Bond Fund since June 1990. The $848 million fund has been repeatedly recognized by Morningstar as a top-performer among its class, with the highest ratings in the overall and three-year periods. Stamper Capital & Investments, Inc. is a Registered Investment Adviser that specializes in the municipal bond market and is dedicated to helping investors earn the maximum return per the amount of risk taken. **Check out our website at www.risk-adjusted.com to find out more about how our strategies can reduce your overall portfolio risk, while maintaining equity-sized returns!**

Short-Term Municipal Bond Fund Category, Morningstar Rankings

Period As of 9-6-02	E.H.I.M.B.F.* Rank	Number of Competitors	Category Average Total Return	E.H.I.M.B.F. Tax-Free Total Returns	Pre-Tax Equivalent Total Return	Morningstar Ratings[2] (5 stars possible)	Percentage Ranking
1 Year	**75**	97	4.71%	3.97%	6.47%		
3 Years	**17**	88	5.20%	5.86%	9.54%	★★★★★	Top 10%
5 Years	**34**	77	4.56%	4.68%	7.62%	★★★	Top 67.5%
10 Years**	**7**	24	4.74%	4.99%	8.13%	★★★★	Top 32.5%
Overall	**-**	-	-	-	-	★★★★★	Top 10%

*E.H.I.M.B.F. = Evergreen High Income Municipal Bond Fund, subadvised by Stamper Capital & Investments, Inc.
** Results from the B shares. A share estimate: 4.74 + .75 basis points = 5.74% or 9.35% pre-tax equivalent

The above chart summarizes the performance of our mutual fund client. We also offer Private Account Management with different strategies and greater opportunities to earn higher yields. **To give you an idea of the types of strategies available and the potentials offered through our Private Account Management, be sure to check out our website at: www.risk-adjusted.com.**

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Disclaimer: Prior Performance achievements are not necessarily an indication of future performance. In other words, past performance does not guarantee future results. There are many types of risks and returns, and the trade-offs among them can result in different positive or negative returns depending upon the subtleties of the specific credit and security characteristics.

1. The pre-tax equivalent total returns are figured based on the highest Federal income tax bracket of 38.6%, no state taxes were included in the calculation.

2. Morningstar's proprietary ratings reflect historical risk-adjusted performance within a narrow investment category. Morningstar calculates a Morningstar Rating based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a fund's monthly performance, including the effects of sales charges, loads and redemption fees, placing more emphasis on downward variations and rewarding consistent performance. The ratings are subject to change every month. Morningstar ratings are calculated from the fund's three-, five- and ten- year (or life of fund, which ever is shorter) average annual returns in excess of 90-day U.S. Treasury Bill returns (on a monthly basis) with appropriate fee and tax adjustments and a risk factor that reflects the fund performance below 90-day T-bill returns (on a monthly basis). The top 10% of the funds in each category receive the highest a rating of five stars. The next 22.5% receive four stars, the next 35% receive three stars, the next 22.5% receive two stars, and the final 10% receive one star. Each share class is counted as a fraction of one fund within this scale and rated separately, which may cause slight variations in the distribution percentages.