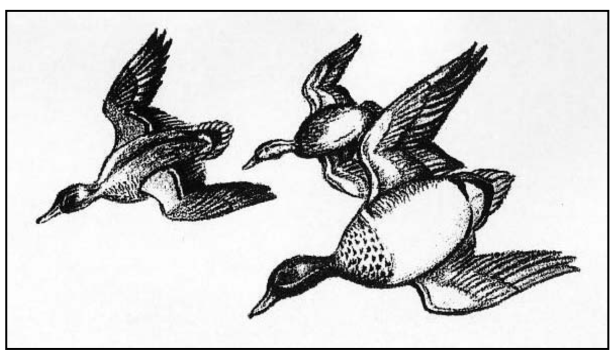
October 28, 2002

Dear PCM Client:

Each autumn we start our client letter with comments about the season, its beauty, and the transition to winter. This year summer gave up its fight early as there was a late September frost in some parts of Minnesota. Precious flowers and tomato plants were covered by their owners in an attempt to save them for a while, but the benefit of the frost was the reduction in the infuriating mosquito population, which grew out of proportion this year because of the above average rainfall. This summer Minnesota has been very wet, making it difficult for farmers to work in the fields, even now. While searching for his favorite banana squash at the farmers market recently, Perk found none; the reason given was that the fields were too wet to enter to get them. In fact, the summer of 2002 was the fourth wettest on record with 22 inches versus the 1987 record of 23.5 inches.

NO FALLING DUCKS TO WATCH OUT FOR

The duck hunting season opened early this year, at least that is how it seemed. It is scheduled for the weekend closest to October 1; this year it was September 28, which just seemed too early somehow. Early or not, we went, and the usual "suspects" showed up at the Hawick camp, which was described in detail in our October 2000 letter. Remember that paragraph was titled "Watch Out For Falling Ducks" because of the sign there. But somehow this year it just didn't come together the way it has in the past. For starters, none of the hunters arrived on Friday for a variety of reasons, and when they did get there Saturday morning everyone was late because of a road detour. It looked rainy and by the time we all got into the boats to move out into the slough to select our spot, and toss out the decoys, it had started to sprinkle. By noon, when the season officially opened it was raining pretty hard. Minutes passed with no ducks in sight.



Unusual. More minutes passed and no ducks in sight, and no shooting in the distance from other nearby lakes and potholes. Very unusual. More rain, harder. David "the Duker" Hyduke, Perk's companion in the boat said, "You know, ducks don't fly much in the rain." We agreed that was right, for they are not stupid-they just find a nice secluded spot to sit and rest. Sort of like people. When it's raining pretty hard we don't usually waddle around in it; we hole up in a house, a store or a movie theater. And so, after seeing one lone wood duck flying about, we decided to call it a short day, picked up our decoys and headed into the shack, turned on the gas heater and poured a glass of shooting sherry to

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warm up. Soon Dick Perkins and son, Richie, called it a day and so did Kit Dahl, but Dan Perkins and Alan Hoiseth stuck it out. After the sherry and lunch, with the rain still coming down, it looked like a very different first day hunt. Duker, who had hurt his back the day before lugging a briefcase through the San Diego airport, decided to go home to rest as did Kit Dahl who was leaving the next day for California. Perk, who was feeling uncomfortable because of falling and landing on his "tailbone" earlier in the week also decided to head out. So while most of the usual suspects got to see each other on Saturday, those who left missed seeing Tony Rocheford who arrived Saturday night and Harry "Dead Eye" Lindberg who was scheduled to come Sunday morning. Dick and Richie decided to leave and go to another hunting camp near Ortonville, and Tony, hearing there was no shooting, turned around and went back home. Harry Lindberg was called on the cell phone and told not to bother. So the opener 2002 was a total bust. No birds were shot, and there was no campfire for everyone to sit around and enjoy after the evening meal. And that left Dan Perkins there at the camp all alone. Dan is very dedicated and not easily frustrated. He went out alone the next morning and still didn't shoot a duck. Yes, a total bust. As we said, very unusual.

Driving home, Perk was thinking about all the years of hunting ducks, for Duker had said in the boat that this was his fiftieth season. How old is he anyway? And Perk, a late bloomer, started in 1960 when he lived in Rochester and Dick Spurzem took him to the Mississippi backwaters through Murphy's ditch. Ah, reminiscing is fun. Ducks are interesting creatures; they have very acute color vision compared to other animals. It is very important to them for courting purposes as males are very colorful to attract the females, while the females are very plain so as not to attract aerial predators when they are on the nest or caring for the very young. Nature has set this all up so that hunters like Perk, and all the others, can come back year after year to a supply of birds to shoot and eat, but obviously, not on some opening days.

A SUMMER OF DISCONTENT

Good riddance to the third quarter, and especially September. This has truly been a summer of discontent with uncertainty aplenty and we all are tired of it. Market watchers know that September is the worst month of the year, but most folks think October is the worst month because they remember the October "massacres" which have been seen in many Octobers, especially October 1987, which is indelibly imprinted in everyone's mind. Looking just at September, it was the fourth worst on record, in terms of the Dow Jones Industrial Average, which was down 12.37%; worse performances were in September 1931, September 1930, and September 1937, all during that terrible decade that followed the 1929 stock

WORST PERIODS FOR DJIA

Date	Month	Monthly	Quarterly	Semi-Annual
Sep-31	9	-30.70%	-35.69%	-43.97%
Sep-74	9	-10.42%	-24.24%	-28.20%
Sep-02	9	-12.37%	-17.87%	-27.03%
Sep-46	9	-8.88%	-16.15%	-13.63%
Sep-01	9	-11.08%	-15.76%	-10.44%
Sep-90	9	-6.19%	-14.86%	-9.41%
Sep-81	9	-3.57%	-12.99%	-15.33%
Sep-98	9	4.03%	-12.39%	-10.88%
Sep-66	9	-1.80%	-11.02%	-16.28%
Sep-75	9	-4.96%	-9.68%	3.35%
Sep-30	9	-14.77%	-9.46%	-28.38%
Sep-60	9	-7.33%	-9.44%	-5.92%
Sep-57	9	-5.80%	-9.34%	-3.90%
Sep-37	9	-12.85%	-8.68%	-17.06%
Sep-77	9	-1.67%	-7.55%	-7.83%
Sep-69	9	-2.82%	-6.88%	-13.08%
Sep-86	9	-6.89%	-6.61%	-2.80%
Sep-48	9	-1.87%	-5.91%	0.62%
Sep-99	9	-4.55%	-5.78%	5.63%
Sep-33	9	-8.01%	-3.98%	70.04%

Source: Hays Advisory Group

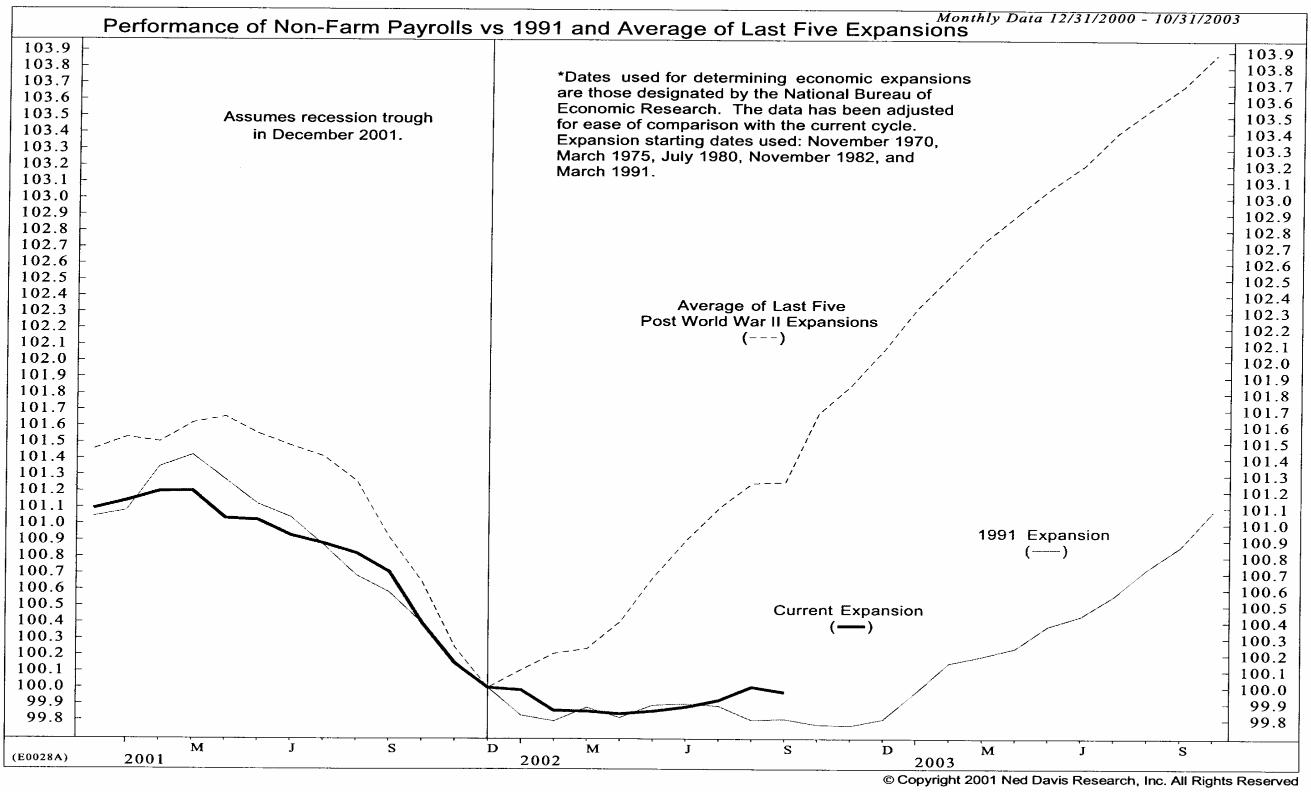
market peak. And the September quarter was the third worst, and the six months the fourth worst in terms of the Dow Jones. The S&P 500 turned in the thirteenth worst quarter on record, as shown in the next chart. It is not surprising that the S&P fared better than the Dow, since the S&P is a broader index of 500 stocks, and also it is weighted, while the Dow has only 30 stocks and is unweighted. So, all of the above is the bad news. The good news is that it is history and if we can get through October without a serious decline, we could be "out of the woods." The table below shows the performance of the S&P 500 in subsequent quarters since 1929 and, separately, since the end of World War II. The market recovered after these disastrous quarters and went higher in the nearby subsequent quarters.

WORST QUARTERS FOR S&P 500

Date	Rank	% Change	Subsequent Performance 1Q	2Q	3Q	4Q	8Q
12/31/1929	3	-28.88	17.20	-4.62	-13.33	-28.48	-62.14
06/30/1930	11	-18.62	-9.14	-25.02	-18.43	-27.52	-78.35
12/31/1930	14	-17.48	8.80	-3.32	-36.70	-47.07	-55.08
09/30/1931	2	-34.52	-16.37	-24.72	-54.38	-16.79	1.24
12/31/1931	16	-16.37	-9.98	-45.44	-0.49	-15.15	24.38
06/30/1932	1	-39.40	82.39	55.53	32.05	146.28	121.44
03/31/1933	17	-15.09	86.50	68.03	72.65	83.76	44.79
12/31/1937	5	-23.33	-19.43	9.57	16.02	25.21	18.39
03/31/1938	8	-19.43	36.00	44.00	55.41	29.18	44.12
03/31/1939	15	-16.88	-1.09	18.58	13.75	11.57	-9.29
06/30/1940	12	-18.53	6.81	6.01	-0.20	-1.30	-16.83
09/30/1946	10	-18.83	2.27	1.40	1.67	1.00	3.54
06/30/1962	7	-21.28	2.78	15.25	21.59	26.70	49.21
06/30/1970	9	-18.87	15.80	26.72	37.94	37.10	47.33
09/30/1974	4	-26.12	7.90	31.19	49.81	32.00	65.63
12/31/1987	6	-23.23	4.78	10.69	10.05	12.40	43.03
09/30/2002	13	-17.63	n/a	n/a	n/a	n/a	n/a
Total *							
Mean		**-22.30**	**13.45**	**11.49**	**11.71**	**16.81**	**15.09**
Median		**-19.15**	**5.80**	**10.13**	**11.90**	**11.99**	**21.39**
Standard deviation		**6.84**	**30.84**	**29.86**	**33.60**	**46.96**	**51.79**
Post WW II *							
Mean		**-21.67**	**6.71**	**17.05**	**24.21**	**21.84**	**41.75**
Median		**-21.28**	**4.78**	**15.25**	**21.59**	**26.70**	**47.33**
Standard deviation		**3.09**	**5.54**	**12.06**	**19.74**	**14.86**	**23.01**

* *Excludes 09/30/2002*
Note: All returns are price only.
Ned Davis Research, Inc.

Why has this past nine months, six months, three months, and one month been so miserable? We can think of lots of reasons besides the continuing comedown from the bubble. In our July letter we devoted several pages to the fraudulent activities at Adelphi, Enron, Tyco, WorldCom, and others. All of this continues in the news today as officers of these companies are now being indicted for criminal fraud. This damage to corporate reliability is exacerbated by the more recent indiscretions of Goldman Sachs and other firms who gave "hot issue" stocks to corporate executives in an effort to win their investment banking business. It never seems to end and continues to undermine confidence in the American capitalistic system. Even the revered Jack Welch is seen as part of the problem through his retirement "perks." And then, there is the sluggish economy and the ramifications of a possible double dip recession. The very interesting chart on page four shows the current expansion compared to the average of the last five post World War II expansions and the 1991 recovery. This current time has followed the 1991 scenario, which implies a flat economy and possibly a little bit of a dip until the end of the year before the recovery really gets going. And last, but certainly not least, is the debate over the war with Iraq. We all know the worst thing for the market is uncertainty and the debate in the United Nations and Congress has created plenty of it. No wonder the third quarter and September were so bad. But it follows that as these uncertainties are eliminated, the tenor of the market will change.



SEARCHING FOR THE BOTTOM

For many years we have been believers in the so called "presidential cycle," in which the market posts a bottom in the second year of the presidential term. Our July letter included a 35-year chart of the Dow which clearly showed those bottoms. This four-year cycle calls for a bottom in 2002, and this year is also the year of the 20-year cycle bottom, as in 1962 and 1982.

What happens after the bottom is what really matters, however, so just take a good look at the numbers. The first table on page five shows the percentage gain in the Dow Jones Industrial Average from the midterm low to the high the following year. The average gain going all the way back to 1914 has been 50%, with the lowest gain 14.5% in 1946. Pretty impressive. Looking at the same statistics for the S&P 500, but only since 1934, the number is nearly the same at about 51%. If the recent lows of 7178 and 769 for the Dow and the S&P 500 respectively represent the bottom, a 50% gain gets them back to 10,767 and 1153 sometime next year. And if only a 15% gain is achieved, they will reach 8255 and 905 respectively. But even if 50% sounds too high and 15% too low, something in the middle, say 33%, might be a more likely outcome, which would still get those averages up to 9547 and 1022.

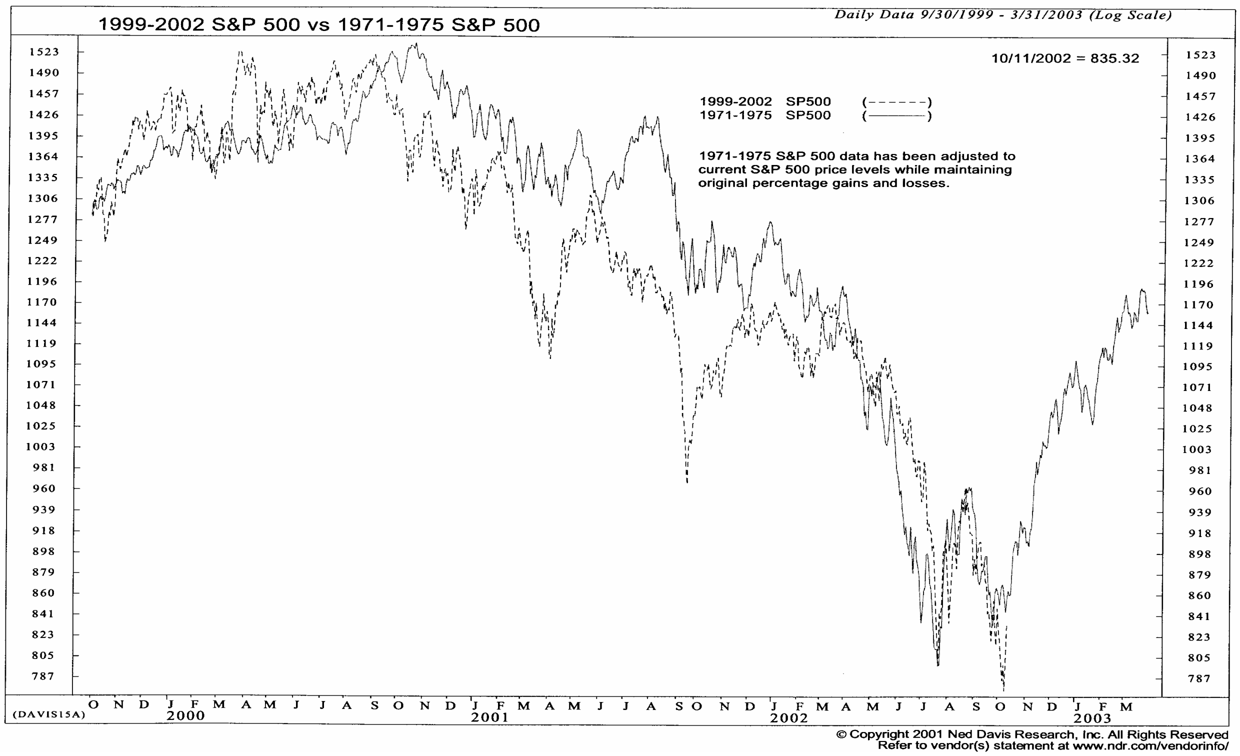
% GAIN IN DOW JONES INDUSTRIALS BETWEEN THE MIDTERM YEAR LOW AND THE HIGH IN THE FOLLOWING YEAR

Midterm Year Low		Pre-Election Year High		
Date of Low	Dow	Date of High	Dow	% Gain
Jul 30 1914	71.42	Dec 8 1915	134.00	87.6%
Jan 15 1918	73.38	Nov 3 1919	119.62	63.0
Jan 10 1922	78.59	Mar 20 1923	105.38	34.1
Mar 30 1926	135.20	Dec 31 1927	202.40	49.7
Dec 31 1930	157.51	Feb 24 1931	194.36	23.4
Jul 26 1934	85.51	Nov 19 1935	148.44	73.6
Mar 31 1938	98.95	Sep 12 1939	155.92	57.6
Apr 28 1942	92.92	Jul 14 1943	145.82	56.9
Oct 9 1946	163.12	Jul 24 1947	186.85	14.5
Jan 13 1950	196.81	Sep 13 1951	276.37	40.4
Jan 11 1954	279.87	Dec 30 1955	488.40	74.5
Feb 25 1958	436.89	Dec 31 1959	679.36	55.5
Jun 26 1962	535.74	Dec 18 1963	767.21	43.2
Oct 7 1966	744.32	Sep 25 1967	943.08	26.7
May 26 1970	631.16	Apr 28 1971	950.82	50.6
Dec 6 1974	577.60	Jul 16 1975	881.81	52.7
Feb 28 1978	742.12	Oct 5 1979	897.61	20.9
Aug 12 1982	776.92	Nov 29 1983	1287.20	65.7
Jan 22 1986	1502.29	Aug 25 1987	2722.42	81.2
Oct 11 1990	2365.10	Dec 31 1991	3168.84	34.0
Apr 4 1994	3593.35	Dec 13 1995	5216.47	45.2
Sep 10 1998	7539.07	Aug 25 1999	11326.04	50.2
			Average Gain	50%

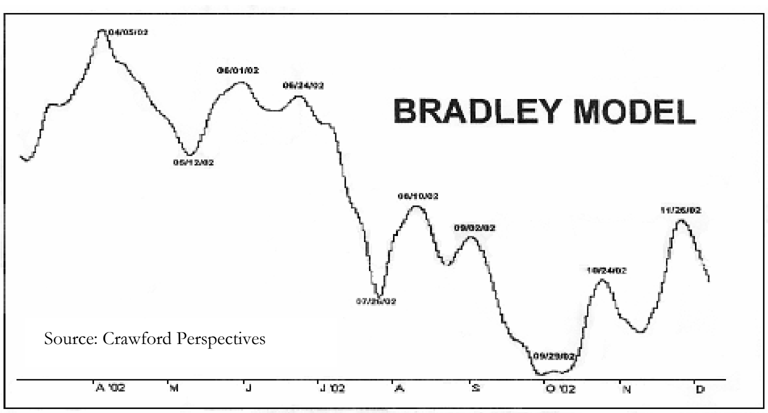
S&P 500 Index Performance from Mid-Term Election Year Lows to Following Year Highs since 1934

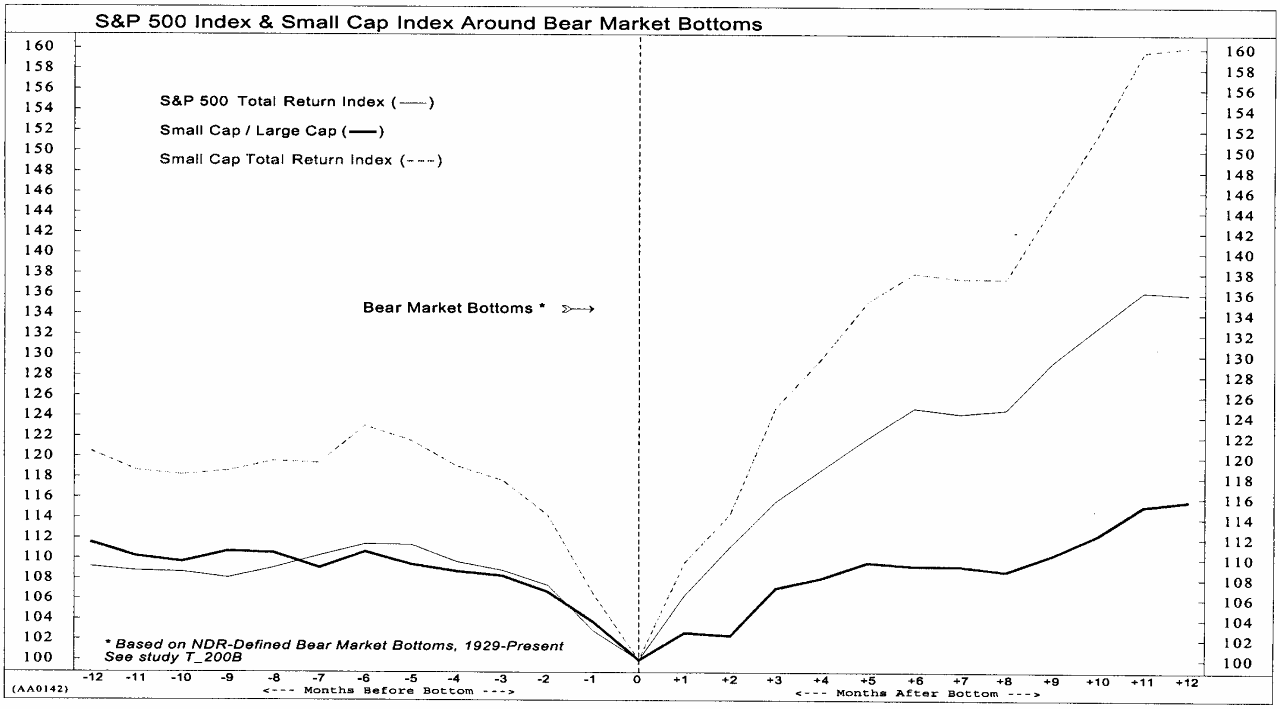
Low Date	S&P 500 Value	High Date	S&P 500 Value	Gain over Period
7/26/1934	8.36	11/19/1935	13.46	61.0%
3/31/1938	8.5	1/4/1939	13.23	55.6%
4/28/1942	7.47	7/14/1943	12.64	69.2%
10/9/1946	14.12	2/8/1947	16.2	14.7%
1/14/1950	16.65	10/15/1951	23.85	43.2%
1/11/1954	24.8	11/14/1955	46.41	87.1%
1/2/1958	40.33	8/3/1959	60.71	50.5%
6/26/1962	52.32	12/31/1963	75.02	43.4%
10/7/1966	73.2	9/25/1967	97.59	33.3%
5/26/1970	69.29	4/28/1971	104.77	51.2%
10/3/1974	62.28	7/15/1975	95.61	53.5%
3/6/1978	86.9	10/5/1979	111.27	28.0%
8/12/1982	102.42	10/10/1983	172.65	68.6%
1/22/1986	203.49	8/25/1987	336.77	65.5%
10/11/1990	295.46	12/31/1991	417.09	41.2%
4/4/1994	438.92	12/13/1995	621.69	41.6%
1/9/1998	927.69	12/31/1999	1469.25	58.4%
				Average gain: 50.9%

In recent letters we have said many times that the 1995-2000 period reminded us of 1966-1972, the era of the Nifty Fifty, a term used to describe the one-decision growth stocks of that time—American Home Products, Avon Products, General Electric, Johnson & Johnson, McDonald's, Medtronic, Merck, Pfizer and many, many more. Those were companies that had grown consistently at rates of 12% to 20% or more per annum, and which could confidently be expected to do so in the future, and so, they were called one-decision stocks, companies you could buy, put away, and never look at again. In 1966, American Home Products was selling at a 20 P/E, and McDonald's at a 15 P/E and by the end of 1972, six years later, their P/E ratios were 36 and 60 respectively. Why, when their earnings per share growth rate had not changed, should their P/E ratios rise so dramatically? A bull market, that's why, good old price earnings multiple expansion, which is what a bull market is all about. So when the market collapsed off that high P/E top into the 1974 bottom with the Dow Jones dropping 40%, the Nifty Fifty stocks which were selling at those hefty P/E ratios declined broadly, and continued to decline for many years in the future even though for most of them their earnings continued to grow. And finally, at their 1980 lows the P/E ratios of American Home Products and McDonalds were 10 and 8 respectively, even lower than they were at the beginning of the run in 1966. All of this is why the 1995-2000 period and top reminded us of that period. Stocks such as Oracle, Sun Micro Systems, Microsoft, GE and many others, began to break away from their traditional P/E ratios in 1995 and advanced in price to where their P/E ratios were at the same relative place as the Nifty Fifty were in 1972. And so once again, history has repeated itself, as it always does. Indeed, the market similarity between the 1999-2002 and 1971-1975 periods has become almost eerie, as the chart reproduced on page six shows. If history continues to repeat itself, this chart could be a good forecast of what is to come between now and 2003. For as you can see, the current market has followed that 1971-75 market almost perfectly.



From time to time, we have printed the Bradley Model, a forecasting tool developed in 1948 by David Bradley, detailed in a pamphlet titled "Stock Market Predictions," which describes the methodology for creating a model of stock market possibilities using harmonic angles between two-planet pairs. Over time, the Bradley Model has precisely pinpointed highs and lows, but also has missed the mark sometimes. Shown here is the Bradley Model for most of 2002, which was “right on” with the market, especially the July 26 bottom which was only a few days off the mark. It called for a lower low at the end of September, specifically September 26, and again missed it only by a day or two. It is then looking for a rise into October-November with an interim correction in between. It would be nice if that were to happen, but we can’t be sure because of the fact that of the last ten bear markets, five have ended in October, specifically 1957, 1960, 1966, 1987 and 1990. And so while October is nearly over, many things can happen in just a few days.





Year	Large U.S. Stocks	Small U.S. Stocks
1972	**18.91**	4.43
1973	**-14.82**	-30.90
1974	-26.57	**-19.95**
1975	37.23	**52.82**
1976	23.60	**57.38**
1977	-7.49	**25.38**
1978	6.36	**23.46**
1979	18.24	**43.46**
1980	32.17	**39.88**
1981	-5.11	**13.88**
1982	21.44	**28.01**
1983	22.45	**39.67**
1984	**6.11**	-6.67
1985	**31.60**	24.66
1986	**18.57**	6.85
1987	**5.14**	-9.30
1988	16.32	**22.87**
1989	**31.33**	10.18
1990	**-3.25**	-21.56
1991	30.40	**44.63**
1992	7.59	**23.35**
1993	10.04	**20.98**
1994	1.24	**3.11**
1995	**37.45**	34.46
1996	**22.84**	17.62
1997	**33.31**	22.78
1998	**28.54**	-7.31
1999	21.02	**29.79**
2000	-9.08	**-3.59**
2001	-11.87	**2.49**

Best performance year in bold
Source: Ned Davis Research, Inc.

We think the preceding charts and commentary are quite conclusive as to expected market performance from here into 2003. But we don't buy the "market," nor do most investors, unless you own an index fund. The question becomes, then, what to buy? Based on both personal and historical performance, it is clear that small-cap stocks will do best as we come out of this bottom. The chart above shows the S&P 500 total return and small-cap total return (Russell 2000 Growth) coming out of bear market bottoms. The difference is very clear, and in fact, quite astounding. Small-caps today are very oversold, with many selling below cash and at low valuations relative to earnings and/or potential earnings.

But let's go back to that 1971-1975 period which we discussed earlier. When the carnage was over in 1974 and the market began to recover, it was not the Nifty Fifty leaders that came back. We have already said that didn't happen until the rise out of the 1982 bottom. What did happen is that small-caps took over and turned in performance numbers for the next nine years that were better than large-cap stocks. The same will be true this time. Don't even consider owning the 1996-2000 leaders as they will underperform just as the 1968-1972 leaders underperformed after that 1971-1972 top. They didn't deliver until years later coming out of the 1982 bottom. The only guide we have to the future is the past and we think what has happened in the past as detailed in these paragraphs is a pretty decent blueprint for the future.

THE FLOATING CONDOMINUIM

A recent *New York Times* article described The World, a seagoing floating condominium, with 110 apartments ranging in size from two bedrooms to six bedrooms and in price from $2 million to $7 million each. Yes, each, plus several hundred thousand dollars a year in maintenance fees. Not to mention that the apartments are on a 50-year leasehold and thus are a depreciating, not an appreciating, asset. This 43,000 ton, 644-foot long ship, with 12 decks will visit 140 ports in 40 countries in its first year, the start of perpetual circumnavigation of the globe. In fact, a home away from home, away from home.

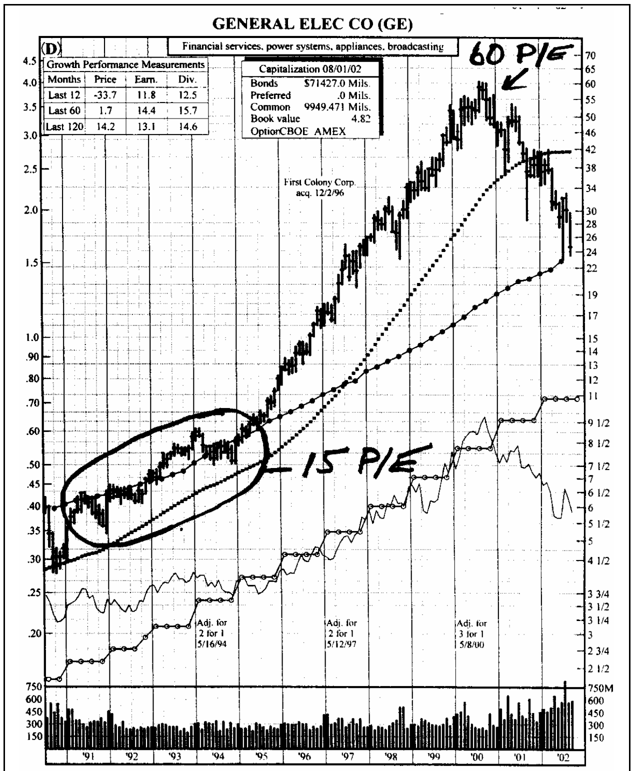
Well, reading this reminded Perk of Bob and Ginny Keeley, his friends of many years, who have literally been cruising the oceans for many years now. In a recent letter Bob said they had spent over 700 nights (two years!) on Holland America ships, and that number will cross 800 in 2003. His letters to Perk come in between cruises on ships such as the Rotterdam VI, the Maasdam, the Prinsendam, and the Vollendam, to mention a few. His letters say they love to cruise, and that it is a wonderful way to see the world. They unpack, and pack up again only once in several weeks or more as their “hotel” travels at night while they sleep. But Bob says “No” to the floating condo. They want to go where they want to go, and when they want to go, and not where the captain of some large condominium decides.

But let’s back up a few years. Who is Bob Keeley (aka SHM #2), and how does Perk know him? Here is the story. When Perk was an assistant portfolio manager at the American National Bank & Trust Company on LaSalle Street in Chicago in 1957, Bob was selling bonds at First Boston Corporation, and they became friends and fishing buddies. Perk left the bank for a job at the Mayo Clinic Endowment Fund in 1959, but they continued their friendship, including a fishing trip or two. Then Bob moved to the New York office of First Boston, but Perk visited him on trips that he took to New York, and he occasionally went to Bob and Ginny’s home in Ridgewood, New Jersey. Bob, after coming out of the army in 1945, went to Ripon College in Wisconsin, courtesy of the U.S. Government, and then on to Wharton, and then to First Boston. At First Boston (New York) he worked his way up to Financial Vice President. But then, somehow, Perk lost track of Bob. Perk took fewer trips to New York, as most of his traveling was to Europe. He recalls that a Christmas card was returned, and so it was obvious that Bob and Ginny had moved. Years later, in August of 1991, a handwritten letter arrived and although the writer did not say who he was until well into the letter Perk knew Bob’s penmanship right away, because it was always perfect. Bob had found Perk because of the Barron’s article titled “Happy Hunting Grounds” published in August 1991. Bob’s correspondence revealed that he had retired from First Boston at age 50, which was probably in 1975 or 1976. When he left First Boston he went to Fordham Law School, “just because I always wanted to” he said, but then didn’t pursue a second career in the legal profession, instead retiring again at age 56. Today Bob and Ginny live in Sarasota, Florida, and have a “get away” spot in North Carolina. The Keeleys are a wonderful and interesting couple. Ginny is an artist, and a good one, but Bob says they long ago ran out of room to hang her paintings.

Bob is intuitive when it comes to investing: he has three investment principals—(1) The Rule of 72, (2) The Law of Motion, and (3) Keeley's Kaveats. As for the rule of 72, it is well known that dividing 72 by a growth rate number will tell you the number of years it will take to double your money. For example, if you can compound at 12% your money will double in six years (72÷12). Rule two, the Law of Motion, says that a body in motion will continue in motion in that direction until some force turns it the other way. Rule three, Keeley's Kaveats says 1) don't buy turnarounds (the Law of Motion), 2) the majority is always wrong (contrary opinion), and 3) time is your friend (patience). Bob has been a very successful investor following these rules, otherwise how could he take 64-day cruises; Perk has trouble missing his quotes for one day. Perk remembers when he was on a cruise and he couldn't wait to get off at a port of call to get a Wall Street Journal or a New York Times, which were always at least a day or two old. Perk thinks Bob Keeley has the right answer. His rules are simple and by following them Bob has done well despite the long cruises.

THE JACK WELCH LEGACY

Before his retirement in September 2001, Jack Welch, President of General Electric for 20 years, was "King of the Hill." He had been given credit for the enormous success of GE, and had written a very popular book, *Jack-Straight from the Gut.* Now, however, in recent months, Jack has gotten himself into a messy divorce, an SEC investigation concerning his retirement "perks" and a possible tax issue because of them. How did all of this start? An affair, actually, started it all. Suzy Welaufer, a Harvard Business Review editor, interviewed Welch for an article, or for a series of them, but the interview time gave way to an intimate relationship, ultimately resulting in her resignation from the magazine and the resultant publicity in a divorce proceeding filed by Jane Welch, his wife of many years. Jack had been doing just fine, relishing his retirement and the publicity which his book had generated; after all, he had grown GE from a market cap of $15 billion in 1981 to $400 billion at the time of his retirement in September 2001. That in itself is somewhat of a myth because the GE cap of $600 billion at its top in the fall of 2000 was the result of a bull market putting an outrageous P/E multiple of 50 times on the company's estimated earnings per share. If the stock had sold in 2000 at the P/E of 15 which it was accorded from 1985 to 1995 (an appropriate valuation for a company growing at 12%) it would have been $190 billion. The fact is that from 1965 to 1981 when Welch became president, GE had grown its earnings at nearly 12% per annum. And from 1981, when Jack came on board, to 2001 when he retired, they grew at 12%. We have read many articles about his management style, and to be sure, he was a powerful manager and had to be to run a company as large and diverse as GE. And that is really the compliment that should be paid him, namely the achievement of managing continued growth at 12%, a difficult task for a large company getting larger. A 25-year chart of GE was shown in our July 2001 letter, but at this time we are producing only a 12-year chart, because it still tells the story of the P/E expansion. During the period 1986 to 1995, GE sold at an average of 15 times earnings. Then beginning at the end of 1995 when the bull market started in earnest, GE left its old P/E ratio behind and moved up to the point where at the top in 2000 it was selling at a P/E of about 50 times its estimated earnings for that year and nearly 60 times the previous year's earnings. The stock built a top, which is very discernable, and since reaching that high of 60, has declined to its present price in the mid 20s. In our opinion, GE is now more fairly valued since it is selling at approximately 15 times this year's estimated earnings. Recently, GE has risen on the back of a 25% earnings gain for the September quarter. However, if you eliminate gains from asset sales, pension income and tax settlements, GE's earnings were up only about 7%. So what you see is not always how it is.



Source: Securities Research Company

But back to Jack and Jane, and their travails. Jack, you see, during his tenure at GE was paid handsomely. His salary in his last year was $16 million, and he had the use of GE jets, apartments, etc. But his affair was his undoing, and when Jane filed for divorce she blew his cover, for many of Jack's retirement perks had not been disclosed by GE. Some are shown below.

<u>JACK'S GE PERKS</u>

Jack Welch, the former chief executive of GE, is receiving a multitude of benefits paid for by the company, according to papers filed by his wife in their divorce case. Here is a sample of what she says the company pays for:

HOUSEHOLD EXPENSES Most expenses at their palatial apartment in the Trump International Hotel and Tower on Central Park West at Columbus Circle in New York, including condominium fees, property taxes, furnishings, food, wine, flowers, cook and wait staff, housekeeper, laundry and dry cleaning, utilities, newspaper and magazine subscriptions, and postage.

TRAVEL Boeing 737 business jets, helicopter, limousine service, rental cars and security personnel when traveling abroad.

ENTERTAIMENT Metropolitan Opera (box seats, Grand Tier level); Yankee Stadium box seats (behind dugout); Red Sox skybox; Knicks seats (floor level); fees at golf clubs including Augusta National, Pine Valley (N.J.) and Blind Brook (Purchase, N.Y.); U.S. Open (court side), French Open and Wimbledon seats; V.I.P. tickets to Olympic events and V.I.P. tickets to NBC entertainment, news and sports events.

Source: *New York Times*

<u>SOME OF JANE WELCH'S EXPENSES</u>

Financial manager	$7,500
Office rent	1,000
Internet/fax/telephone	430
Books/CDs	160
Clothing	7,500
Cell phones	2,500
Dry cleaning/laundry	120
Dining out	2,500
Opera, theater, movies	1,000
Gifts	3,100
Gratuities	300
Groceries	1,200
Personal trainer	900
Hairdresser	650
Jewelry	10,360
Lessons	1,080
Petty cash	5,000
Car and driver	4,000
Travel	20,000
Wine	8,260

But poor Jane was getting only $35,000 per month in expense money during the pendency of their divorce, while estimating a need for several times that amount per month. So now Jack has agreed to pay GE the estimated cost of his perks since leaving in September 2001, and to reimburse GE $2.5 million per year in the future for his retirement perks as long as he lives. It is unfortunate that all of this has resulted in an SEC investigation regarding proper disclosure to shareholders and likely an IRS investigation concerning payment of taxes on the benefits. But almost worse, however, is the humiliation of being put in the same category as Kozlowski, the former Tyco chief, who also had many corporate perks, but has been indicted for fraud.

RACOONS LOVE GRAPES TOO

The content of this paragraph has been inspired by a situation in which Perk's sister, Mary Ann, finds herself at this time of the year. Raccoons are found in every part of North America except for the higher elevations of the Rocky Mountains and parts of the desert in the Southwest. In the northland, such as Minnesota or Massachusetts, they are much more common now than they were 40 or 50 years ago, and therefore, they are one of the few animals that have benefited from urban sprawl. Visibly they are unmistakable, with their black mask and bushy ring tail. They have short ears and a long white snout and they sort of waddle when they walk. They use trees for dens, but can be found in an underground den occasionally. The adult raccoons are solitary things, except when the mother has her young. The babies stay with the mother for nearly a year. The mother gives birth to three to six young raccoons near the end of May, and then leads the young away from the den in July and August. And this is when most raccoons end up flattened on the highway. They spend most of the summer sleeping during the day and searching for food at night. We are told they find a new place to sleep each night, and the goal is to build layers of fat that will allow them a winter's sleep. Raccoons are true omnivores, which means they will eat both plants and animals. It is not uncommon for raccoons to eat bird eggs, baby birds, fish, acorns, berries, green leaves, and grapes. Yes, grapes. Perk's sister, Mary Ann, lives in Concord, Massachusetts, which is famous not only for Walden's Pond and Henry David Thoreau, but for the Concord grape. Mary Ann has an overhanging structure on which her grapes grow, and it is a covering for her outdoor patio. At this time of the year, Mary Ann reports that the raccoons of Concord gather at her home for a grape party many nights and, of

course, keep her awake. She thinks they need to go to the "insomnia clinic," per the cartoon. When the grapes ferment they get especially noisy as they get a little "tipsy!"

Fortunately, our friends send us lots of e-mails that provide ammunition for our quarterly letters; the addendum consists of the best of the recent ones. We hope you enjoy them.

Finally, we always put a cartoon at the end of the letter and the two that have been selected this month are for the benefit of our banker friends.

Sincerely,

Richard W. Perkins, C.F.A.
President
Senior Portfolio Manager

Daniel S. Perkins, C.F.A.
Vice President
Portfolio Manager

Richard C. Perkins, C.F.A.
Vice President
Portfolio Manager

RWP:DSP:RCP/jah

"Yes, you're charged a fee for minimum balance, teller service and ATM use--that's why we consider you a valued customer."

ACTUAL SIGNS WITNESSED BY SOMEONE, SOMEWHERE, AT SOMETIME...

On a septic tank truck: "We're #1 in the #2 business."

At a Gynecologist's office: "Dr. Jones, at your cervix.”

On a Proctologist's office door: "To expedite your visit please back in."

On a plumber's truck: "We repair what your husband fixed."

At a pizza shop: "7 days without pizza makes one weak."

At a tire shop in Milwaukee: "Invite us to your next blowout."

On a Plastic Surgeon's office door: "Can we pick your nose?"

At a towing company: "We don't charge an arm and a leg. We want tows."

On an electrician's truck: "Let us remove your shorts."

In a nonsmoking area: "If we see smoke, we will assume you are on fire and take appropriate action."

On a maternity room door: "Push. Push. Push."

At an Optometrist's office: "If you don't see what you're looking for, you've come to the right place."

On a taxidermist's window: "We really know our stuff."

On a plumber's truck: "Don't sleep with a drip. Call your plumber."

In a Podiatrist's office: "Time wounds all heels."

On a fence: "Salesmen welcome! Dog food is expensive."

At a car dealership: "The best way to get back on your feet - miss a car payment."

Outside a muffler shop: "No appointment necessary. We hear you coming."

In a Veterinarian's waiting room: "Be back in 5 minutes. Sit! Stay!"

At the electric company: "We would be delighted if you send in your payment. However, if you don't, you will be."

In a restaurant window: "Don't stand there and be hungry. Come on in and get fed up."

In the front yard of a funeral home: "Drive carefully. We'll wait."

At a propane filling station: "Tank heaven for little grills."

On a garbage truck: "Satisfaction guaranteed or double your trash back.”

And don't forget the sign at a Chicago radiator shop: "Best place in town to take a leak.”

ACTUAL SENTENCES FOUND IN PATIENTS' HOSPITAL CHARTS

She has no rigors or shaking chills, but her husband states she was very hot in bed last night.

Patient has chest pain if she lies on her left side for over a year.

On the second day the knee was better, and on the third day it disappeared.

The patient is tearful and crying constantly. She also appears to be depressed.

The patient has been depressed since she began seeing me in 1993.

Discharge status: Alive, but without my permission.

Healthy appearing decrepit 69-year-old-male, mentally alert but forgetful.

The patient has no previous history of suicides.

Patient has left white blood cells at another hospital.

Patient's medical history has been remarkably insignificant with only a 40 pound weight gain in the past three days.

Between you and me, we ought to be able to get this lady pregnant.

Since she can't get pregnant with her husband, I thought you might like to work her up.

She is numb from her toes down.

While in ER, she was examined, X-rated, and sent home.

The skin was moist and dry.

Occasional, constant, infrequent headaches.

Patient was alert and unresponsive.

She stated that she had been constipated for most of her life, until she got a divorce.

The lab test indicated abnormal lover function.

The patient was to have a bowel resection. However, he took a job as a stockbroker instead.

Skin: somewhat pale but present.

The pelvic exam will be done later on the floor.

Patient was seen in consultation by Dr. Blank, who felt we should sit on the abdomen, and I agree.

Patient has two teenage children, but no other abnormalities.