INVESTMENT GUIDE

Published Monthly by

American Investment Services, Inc.

Vol. XXII, No. 11 | Great Barrington, Massachusetts 01230 | November 30, 2000

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It Pays to Start Early

Most individuals do not begin to think about accumulating, or are unable to set aside, funds for retirement until they reach their late 40s or 50s. Starting much sooner can be astonishingly rewarding.

In the instances of an IRA, which has a $2,000 limit on annual contributions, the annual earnings an account receiving $2,000 annually eventually will become larger than $2,000. Once that happens, the account of someone who starts contributing early enough will always be larger than that of someone who waits until middle age to start saving for retirement. This will be so even if the "early bird" discontinues contributions completely. Compounding over long periods is what gives systematic savings plans their greatest potential.

Consider, for example, an individual who contributes $2,000 per year to an IRA beginning at age 21. If the contributions continue at that rate and the account consistently earns 11.3% (which is slightly less than the total return on the S&P 500 index since 1926 as calculated by Ibbotson Associates, Inc.), the account's value will reach roughly $3 million when the individual turns 65. The most mind-boggling aspect of this astonishing number is that *half* of the $3 million would reflect the compounded earnings on just the first 6 annual $2,000 contributions (totaling $12,000). The other $1.5 million would reflect the compounded earnings on the 39 annual contributions (totaling $78,000) made between ages 27 and 65. The foregoing calculation assumes away several uncertainties (such as earning a consistent 11.3% return — by no means assured over periods as short as 6 years, or even over the next 45 years), but it does indicate the extraordinary advantage of "starting early."

However, it usually is very difficult for 21-year-olds to set aside funds in this manner (it often is difficult for 45-year-olds). This suggests an important opportunity and consideration for those who are making annual gifts (for estate planning purposes or other reasons) to children, grandchildren, and other potential heirs. Such donors might suggest, or even insist as a condition of their gift, that the recipients place as much as possible in tax-deferred pension accounts.

To be eligible to contribute to an IRA, the recipient of the gift must have earned income at least equal to the IRA contribution (up to the $2,000 maximum). If the recipient's current taxable income and marginal tax rate is low, a Roth IRA (for which there is no current deduction for the contribution, but no tax due on eventual withdrawals) would appear to be more attractive than a regular IRA.

Finally, it cannot be stressed too strongly that only relatively secure income-producing investments should be placed in tax-deferred pension accounts (*i.e.*, one should resist the temptation to use such accounts for "flyers" on high risk investments, in hopes of realizing large untaxed capital gains). It is the ability to compound free of taxes the income earned within such accounts that gives them their potential and power over the long term. If the value of the holdings decrease to zero, no amount of compounding will make them grow.

Subscription: $49 per year. American Investment Services, Inc. is wholly owned by the American Institute for Economic Research.

THE JOY OF GIVING

As the holidays approach, investors have the opportunity to make gifts that can provide substantial benefits for both recipients and donors. The federal tax code provides investors with ample opportunity, through the judicious use of gifts, to reduce their taxable estates as part of a comprehensive estate plan. It also provides investors who have substantial unrealized capital gains a way to reinvest their assets for income, while avoiding the potential tax liability that accompanies such gains, and benefits charities.

Although there have been no significant changes in tax legislation affecting the rules pertaining to gift-giving this year (and the election results suggest that there is little hope for significant changes in the next few years), prudent investors should review their current situations in the light of the basic principles discussed below.

Estate Planning Primer

Federal estate taxes begin at a marginal rate of 18% initially and climb to a marginal rate as high as 55%. However, every American is entitled to a Unified Credit ($220,550 in 2000 and 2001) against federal Estate and Gift Taxes. This means that no tax will be due on estates of up to the exclusion amount ($675,000 in 2000 and 2001), and it also means that the effective marginal rates on the first dollar over the exclusion amount is now 37%. The exclusion amount will be gradually increased until it reaches $1,000,000 per individual in 2007. Proper titling of assets and trust arrangements can enable married couples to pass on up to twice the exclusion amount to their heirs.

The credit is referred to as a "unified" credit because federal gift and estate taxation are integrated into one unified tax system. For example, suppose you give $25,000 to your son or daughter this year. The first $10,000 of your $25,000 gift is tax-free, but you will be required to file a gift tax return on the excess $15,000 ($5,000 if your spouse consents to the gift). No tax will be due on such returns until the total over your lifetime exceeds the exclusion amount ($675,000 at present). For the purposes of calculating the tax, the total of your taxable gifts will be included in your estate, but any previously paid taxes will be credited against any final estate tax due.

Taxable estates include all property left to anyone other than a spouse or a charity. Few, if any, assets escape this final count. Bank accounts, securities, pension and retirement plan assets, IRAs, possibly even insurance proceeds, are included, as are taxable gifts made during one's lifetime. Add to these the equity in your home(s) and your estate can quickly climb into taxable range. And this can creep up on investors who do not now think of themselves as wealthy enough to face estate taxes. For example, a 45-year old with $250,000 in assets could find his estate to be in excess of $1 million, and therefore subject to future estate taxes, by the time he turned 75, if his assets appreciated at a 5% annual rate of return on the assets.

Contemplating one's demise is seldom at the top of one's "to do list," and estate planning is easily postponed. However, if you have delayed estate planning as some dreaded chore, there is no time like the present to sit down with your attorney and give yourself the best gift of all: peace of mind. Even investors with existing estate plans should review their plans with their attorney to make any necessary revisions in order to take full advantage of the latest changes, and in the light of their current financial situation.

Trust Techniques

Assets left to your spouse will not be taxed: the "marital deduction" can reduce or eliminate estate taxes on assets left to one's spouse. However, the unified credit of the first to die can be "wasted" if all of one's assets pass to a surviving spouse under the marital deduction, because assets transferred under the marital deduction will eventually enter the estate of the surviving spouse.

Substantial estates can therefore enter the highest marginal estate tax brackets upon the second death. Many investors have therefore created "unified credit equivalent bypass trusts" for children or others. Typically, when the first spouse dies, these trusts are fully funded with assets valued at the credit equivalent, thereby shielding $675,000 (currently) in that estate, and those assets, if the trust is properly structured, ultimately escape estate taxation on the death of the second spouse as well. The income from assets left in such trusts is often payable to the surviving spouse. Those with holdings that are currently well below the exclusion amount should seriously consider incorporating such trust arrangements in their will anyway. Assets can appreciate and savings accumulate before you next get around to reviewing your will.

In short, everyone with significant assets should have a will (and perhaps living trust documents, which can simplify the administration of an estate) prepared by a competent attorney, as a first step toward minimizing federal estate taxes. (Even where taxes are not a consideration, a will can greatly simplify, reduce the costs of, and accelerate the disposition of a decedent's property.)

Married persons with significant assets should give first consideration to retitling of assets and/or the trust arrangement described to ensure that no assets will be taxed unless both spouses' estates receive all of their unified credit, as well as other means of reducing or eliminating estate taxes.

Estate planning would be incomplete

We have reviewed the terms of the merger proposal recently sent to shareholders of **J.P. Morgan & Co. Inc.** and **The Chase Manhattan Corp**. We recommend that shareholders of J.P. Morgan approve the proposed merger that will create a worldwide, diversified financial services organization that together will be a formidable competitor in the rapidly expanding financial services sector. Each common shareholder of J.P. Morgan will receive 3.7 shares of the common stock of The Chase Manhattan Corp.

The Securities and Exchange Commission has approved the merger of **Newmont Mining Corp** and **Battle Mountain Gold Co**. Each common share of Battle Mountain Gold will be exchanged for 0.105 shares of Newmont Mining common stock. At the completion of the merger, Battle Mountain's 2.3 million shares of convertible preferred stock will become Newmont Mining convertible, preferred stock and Newmont will assume approximately $199 million in Battle Mountain's long-term debt. A special meeting of Battle Mountain shareholders of record on December 1, 2000, is scheduled for January 5, 2001. Proxy material is expected to be mailed to Battle Mountain shareholders during the first week of December 2000. We recommend that Battle Mountain and Battle Mountain Canada shareholders approve this merger.

without consideration of various gift provisions that allow donors to bestow gifts upon loved ones while reducing their own tax burden.

'Tis Better to Give

The simplest way to reduce estate taxes is to give assets away. In addition to estate tax savings, gifts during your lifetime enable you to assess the benefits and use of those gifts while you still are living.

Current tax law permits you to give up to $10,000 each year without incurring estate or gift taxes. Through this so-called "annual exclusion" a husband and wife together can give twice as much—$20,000 annually—to an individual. For example, a married couple with three children and six grandchildren could make tax-free gifts of up to $180,000 each year to their children and grandchildren. In this example, nontaxable gifts could remove more than $540,000 from the couple's taxable estate in just 3 years.

The $10,000 exclusion will now be indexed to inflation under the new law, but changes will come in $1,000 increments, so several years could pass before the limit actually rises.

These annual exclusion gifts produce valuable estate tax savings limited only by the number of heirs, the life expectancy of donors, and, of course, the assets available. We do not recommend extensive gifts where they would affect what you have available for your living expenses, or for modest estates unlikely to be subject to estate taxes.

Tuition (and, in some instances, medical expenses) paid on behalf of children and grandchildren are not considered taxable gifts. This exclusion is not limited in amount and is independent of the annual exclusion. However, payments must be made directly to the provider of the services to qualify for the exemption, and are strictly limited to tuition (i.e., payments of room and board expenses could be taxable). Many states have recently enacted qualified college savings plans that allow earnings to grow tax-deferred, and take full advantage of federal gift tax provisions.

In addition, parents with adjusted gross incomes below $95,000 ($150,000 for couples) can now contribute an aggregate nondeductible total of $500 each year to an Educational IRA that can grow and be withdrawn tax-free to pay for tuition and related costs until the child reaches age 30. Other donors can also contribute a portion of the $500.

The tax code includes the Uniform Gifts to Minors Act (UGMA), which allows gifts to minors that qualify for the annual exclusion, while permitting parent-donors to serve as custodian of the gift. Another option is a section 2503(c) trust, which also allows annual exclusion gifts. Taxable investment income can be "shifted" from donors in a high marginal tax bracket to the trust as long as it accumulates on behalf of a minor beneficiary. Both devices have additional features and drawbacks; three of AIER's publications address these plans in detail: *The Estate Plan Book 2000* (148 pages, $10), *How to Make Tax-Saving Gifts* (43 pages, $3), and *How to Produce Savings in the Administration of an Estate* (36 pages, $3).

In instances where funds are ample and estates will fall into the highest estate tax brackets, it might be advisable to make taxable gifts, i.e., gifts over and above the annual exclusion. The effective gift tax rate is often significantly lower than the marginal estate tax rate that would apply if the assets were left in the estate, especially if the income from the property and its future appreciation eventually add to the taxable estate. Giving the property away now at today's values, and filing a gift tax return (no tax will actually have to be paid until the total value of such taxable gifts in your lifetime exceeds the estate exemption) could therefore serve to reduce the total taxes paid. Since the IRS is allowed retroactively to revalue past taxable gifts in calculating the estate tax, investors should maintain accurate estate and gift tax records. Such gifts should also undergo a rigorous examination by an accountant.

Cash is King

The type of asset given can also have tax consequences. The recipient's cost "basis" for income tax purposes is the donor's cost at the time it is given. In contrast, an heir's "basis" for property received from an estate is its fair market value at the time of death. Thus, it is usually preferable not to use highly appreciated property for any gifts if the recipient will be subject to capital gains taxes. Otherwise when the recipient eventually sells the property he will owe gains taxes based on the donor's original cost. It is best to give cash or recently acquired assets.

There is little reason to make gifts that are subject to indebtedness or that have fallen in value. If the property is subject

MINI TENDERS: BIG RIP OFF

"Mini tender offers" differ dramatically from usual tender offers, which are made for more than 5% of a company's securities at a price higher than that offered on a major stock exchange. "Mini tender offers" are for less than 5% of a company's securities and are regulated under far less stringent SEC rules than tenders for more than 5% of a company's securities, which can be either common stock or fixed income securities that are usually convertible into common stock.

"Mini tender" offers increasingly have been used to catch investors off guard. Over the past two years, offers have been were made to holders of Agnico-Eagle Mines and Homestake Mining, along with more than 200 companies *at offering prices below the prevailing market prices* Apparently many investors surrender their securities without investigating these offers, unaware that the offers are made below market. Usually the offering period of a "mini tender" offer is short, prompting many unwary investors to accept these offers without doing their homework. Unlike the SEC rules guiding tender offers of 5% or more, investors cannot withdraw their tendered shares before the expiration date. Moreover, these deals are typically one-sided; if a mini-tender offer is accepted by an unwary investor and the share price does not remain above the tender offer price, the shares will be returned to the investor. If the share price rises, however, the bidder will be in a position to sell the shares and make a quick profit.

Recently a "mini tender offer" was made by TRC Capital Corp on November 3, 2000, to purchase up to 15 million, or approximately 4%, of Barrick Gold's common shares, at a price of CDN $20 per share. Barrick Gold is a company long recommended in the ***INVESTMENT GUIDE*** and owned by many of our subscribers and investment management clients. Barrick announced on November 16, 2000, that This offering price was actually about 1%-2% below Barrick's listed price on the Toronto and New York Stock Exchanges. **American Investment Services, Inc recommends that investors refuse these "mini tender" offers, and we specifically recommend that investors ignore this offer for Barrick Gold.**

CHARITABLE REMAINDER PROGRAMS AT AIER

Our parent, the American Institute for Economic Research, maintains pooled Reserve Life Income funds (RLIs) and accepts and manages Charitable Remainder Unitrusts (CRUs). These may be of interest to readers, not only because they serve to support the work of AIER, but also because, unlike many charities, AIER does not place restrictions of its own on the naming of income beneficiaries. Of course, the statutory requirement that the beneficiaries be living at the time of the donation applies. AIS serves as the investment advisor to AIER's charitable remainder funds, which are invested to reflect AIER's findings concerning long-term monetary and economic trends. For more information contact:

Mr. Edward Welker, Vice President
American Institute for Economic Research, Box 1000, Great Barrington, MA 01230
Telephone (413) 528-1216, FAX (413) 528-0103

to indebtedness, the donor will incur a taxable gain to the extent that the indebtedness exceeds his cost. If the fair market value of the gift is below the donor's cost, neither the donor nor the recipient can recognize a capital loss.

Benefits of Benevolence

While appreciated assets should be avoided as gifts to other taxpayers, they are well suited for gifts to charities. As is well known, charitable gifts are deductible from income taxes, and legacies to charities are not taxed in estates. Less understood is the benefit derived from the fact that charitable gifts of appreciated property are not subject to capital gains taxes: in most instances, taxpayers will receive a deduction for the full fair market value of assets donated to charity.

Such gifts need not be substantial. If a taxpayer in the 31% bracket donates 10 shares of stock worth $30 per share that had been purchased for $15 per share, his or her taxable income would be reduced by $300, yielding a tax savings of $93. If instead the taxpayer sold the stock and donated the proceeds, the $93 tax savings from the donation would remain, but there would be a taxable capital gain of $150, on which $30 in taxes would be due, based on the 20% maximum rate applicable to long term gains.

Charitable deductions for appreciated property donated to a public charity are generally limited to 30% of adjusted gross income (in contrast to the 50% allowed for cash contributions), but any excess may be carried forward to future tax returns. Documentation of charitable gifts is critical; charitable gifts of $250 or more may be deducted only if the donor has written substantiation from the charity.

"Split Interest" Donations

The IRS goes one step further, in effect allowing investor-donors to "have their cake and eat it" by simultaneously avoiding gains taxes via donations of appreciated property, while retaining the right to receive the income from the donated property. The income stream can last for the donor's lifetime and/or the lifetimes of other named beneficiaries. Such "split interest" donations may be accomplished via charitable remainder trusts, in which the appreciated property can be sold by the charity without incurring a gains tax. The principal eventually goes to the charity. We recommend two main types of trusts: pooled income funds and Charitable Remainder Unitrusts (CRUs).

Pooled income funds are maintained by the charity, much in the manner of a mutual fund. The donor is assigned a number of units, according to the value of the donated assets. The income received by the fund (dividends, interest, etc.) is pooled, and distributed among the income beneficiaries according to the number of units so assigned. When no further income distributions are due because the last income beneficiary named by the donor has died, the value of the units is "severed" from the fund and become available for the charity's use.

CRUs function similarly, except that the funds are held in a separate account and not "pooled" with other donations. The trustee of a CRU need not be the charity itself, but it is required that the donor stipulate a fixed percentage of the annually determined value of the fund be distributed annually to income beneficiaries. The donor may stipulate that distributions are to be of "income only." This can include a further stipulation that any shortfall of actual income received by the funds from the fixed percentage be "carried forward," and be made available for distribution in subsequent years in which the actual income is in excess of the fixed percentage.

Gifts for the Giver

Under these plans the charity will not receive the severed funds until some future date. The present value of an asset to be received at a future date is less than the value of assets that can be used immediately. Thus, donors, while enjoying the benefit of income from the full value of the donated asset, do not receive the full value as a deduction against income. The value of the deduction that can be claimed is determined by (1) the fair market value of the gift, (2) the expected lifetimes of the named income beneficiaries, and (3) the expected rate of return on the fund. For pooled income funds, the estimated rate of return is based on past experience of the fund; for CRUs it is based on the fixed percentage to be distributed (which may not be less than 5%).

If there are additional income beneficiaries living at the time of the donor's death, the values of pooled income funds and CRUs will be included in the donor's taxable estate. However, the estate will receive a charitable deduction for the estimated value of the charity's remainder interest at the time. If there are no additional income beneficiaries, because none were named to begin with, because the named beneficiaries predeceased the donor, or because the donor revoked their income interest by will, the estate will receive a deduction for the full value of the funds going to the charity.

It is important for donors to retain the right to revoke by will the income interests of named beneficiaries. The present values of irrevocable income interests in a charitable remainder that vest upon the donor's death are taxable gifts. Furthermore, as future interest gifts, these would not be eligible for the gift tax exclusion. The donor can only exclude gifts that are immediately available to the recipient.

Pooled income funds and CRUs may be viewed as a means of obtaining administration of funds for the benefit of heirs. As such, their main difference (aside from the cost and quality of management) from an ordinary trust fund would be that the principal would eventually go to a charity instead of, say, great-grandchildren that are not yet born. However, the major benefit of these "split-interest" arrangements is that they allow the transfer of appreciated assets for reinvestment with no reduction in the amount that can be reinvested to produce spendable income for the donor and his heirs.

The unique features of pooled income funds and CRUs remain very attractive, especially in the light of the phenomenal 18-year bull market. So-called "growth" stocks have performed exceptionally well, and have generated significant potential capital gains tax liabilities in the process. In many instances, the best performing stocks of the past 20 years or so, pay little or nothing in dividends at present. Someone who is retiring or about to retire might wish to reinvest for income but does not want to have the amount available for reinvestment reduced by taxes due. If the highly appreciated stock is donated to a charitable trust or pooled income funds, the full proceeds of its sale may be reinvested and income paid to the donor, who will also receive a charitable deduction in the year the gift is made.

Such gifts could provide additional tax savings. Many investors don't realize that the effective marginal tax rate on capital gains can exceed the statutory capital gains tax limit of 20%. At higher levels of taxable income, an increase in capital gains can phase out exemptions and deductions, subjecting to taxation income that was previously protected.

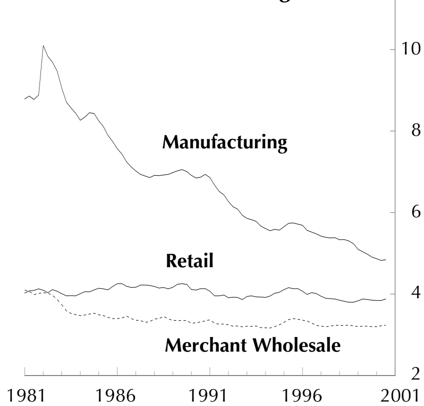
HAS THE INVENTORY CYCLE BEEN REPEALED?

It is canonical in New Economy thinking that the improved management of intermediate goods and wholesale and retail stocks enabled by the advent of computerized inventory accounts has moderated the inventory shocks that punctuated business cycles in earlier times. The virtually instantaneous flow of information between retailers, distributors, and producers, it is said, today has permanently changed the environment in which goods come to market.

There is ostensibly good warrant for such views. As the top curve in Chart 1 shows, manufacturing inventories (expressed as a percentage of GDP) have dropped very sharply since the 1981-82 recession—from about ten percent of GDP to under five percent. Similarly, merchant wholesale inventories (e.g., jobbers, industrial distributors, exporters, and importers) have decreased from about four percent of GDP to under three percent. In the aggregate these changes are favorable developments—and would seem to imply that inventory shocks, in the manufacturing sector at least, can be expected to be less severe and of shorter duration than in the recessions that antedated "just in time delivery" inventory practices.

Perhaps most notable, however, is how little (in terms of the overall economy) inventory stocks have changed in the retail sector—which has undertaken the most visible innovations over the past three decades and which remains the ultimate target of investment in the "New Economy." As shown in the middle curve of Chart 1, as a percent of GDP retail inventories have remained virtually unchanged over the past two decades. For all the brouhaha that has accompanied the age of the shopping mall and most recently "e-tailing," there is scarce evidence that retail inventory concerns today are any less worrisome than they were several decades ago.

Chart 1
Inventories as a Percentage of GDP

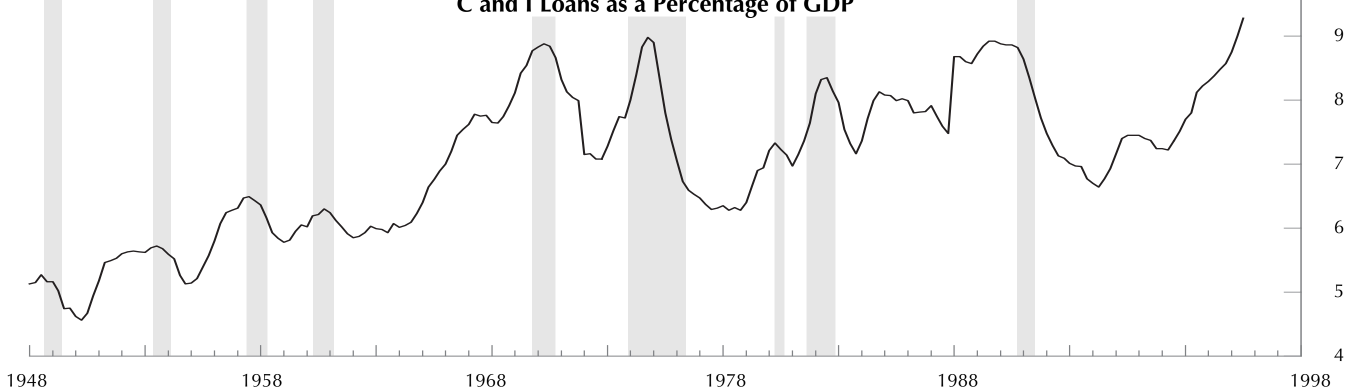


This is not to say that in other respects there has not been a genuine revolution in retailing. Those with memory of the leading department stores of the 1950s, 1960s or 1970s—often elegantly appointed, overstaffed, and bulging with slow-moving inventory—know that the way most people shop has changed greatly since then—and may say they lament the decline of civility in the environment of today's malls and discount stores. But it was mainly the consumers themselves—who decided to place price above other considerations—who supported the retailing innovations of recent years. If they genuinely valued the service provided by sales personnel and the ambience of surroundings dripping with high-priced goods, both Walmart and upscale catalog shopping (to cite extremes) presumably would have died early deaths.

The point is that this revolution in retailing apparently has not necessarily implied reduced inventory demands for shopkeepers. In earlier times the few department stores that serviced a given locale may have maintained huge inventories of relatively high-priced goods. Today the hundreds of mall outlets and the like that dot most communities bulge with inventories of low-priced goods (if one can term a $150 pair of sneakers low-priced). Indeed, that retail inventories as a percent of GDP have remained largely unchanged even while, as noted below, the service sector component of GDP has grown markedly, implies that inventory stocks actually have increased in relation to total output of the retail economy.

Over the long term, it is the growth of service sector output as a proportion of GDP that could prove to be one of the largest influences in moderating the inventory cycle. Services have been increasing as a percent of GDP since the 1950s,

Chart 2
C and I Loans as a Percentage of GDP



and during the 1980s accelerated sharply. Today service-sector output accounts proportionally for roughly twice as much of total GDP, almost 40 percent, as it did in 1950. By definition, services are largely exempt from inventory concerns and in general display less cyclicality than the goods-producing sector.

As a consequence, one might presume some moderation of inventory cycles and relatively muted business cycles. The difficulty is that—even during the mild 1990-91 "white collar" recession—there simply was no evidence to support the notion that the inventory cycle had disappeared. On the contrary, conventional measures suggest that it remains extraordinarily robust, and could be an important factor in future recessions.

We Doubt It

For example, one of the clearest graphical representations of the inventory cycle is portrayed in Chart 2, which shows Commercial and Industrial loans as a percentage of GDP. C&I loans usually mature in 90 days or less and historically have provided the basis for short-term inventory finance. As shown in the chart, in terms of GDP such lending has peaked at contractionary turning points in the business cycle throughout the postwar era.

The current situation does seem notable, but not in the ways that would support the notion that the inventory cycle has been repealed. Not only has the cycle remained undiminished across the "digital divide," but it actually appears to have become more pronounced. As a percentage of GDP, short-term inventory finance now stands at a historic high.

Given the aggregate decrease in total inventories as a percentage of GDP (the sum of the three curves in Chart 1), this

ALTERNATIVE HIGH-YIELD DOW INVESTMENT STRATEGY

We are convinced that long-term common stock investors will receive superior returns if they consistently purchase (and hold) higher-yielding Dow stocks from a listing such as that on the opposite page. Selecting from such lists is not a "cut and dried" process, however. Individual circumstances and a variety of ad hoc decisions will perforce determine the timing of purchases and sales.

In our monthly listings, a given issue may retain a ★ or a ☆ for months, even years at a time. As a result, investment (and reinvestment of sales proceeds) in particular stocks will vary with each individual investor. This means that, while it would be possible to calculate total returns (dividends and capital gains) for a specific investor, it is not possible to compute such returns on our recommendations *per se*.

Our parent has exhaustively researched many possible High-Yield Dow approaches, "backtesting" various possible selections from the DJIA ranked by yield for various holding periods. For the 35 years ended in December 1998, it was found that the best combination of total return and risk (volatility) was obtained by purchasing the 4 highest yielding issues and holding them for 18 months. (For a thorough discussion of the strategy for investing in the highest-yielding stocks in the DJIA, please read AIER's booklet, "How to Invest Wisely, with Toward an Optimal Stock Selection Strategy," 139 pp. $9.)

In our model described below, which is distinct from the table on the opposite page, about one-eighteenth of the portfolio is devoted to the 4 issues eligible each month. (We say "about" because various adjustments and rebalancings are needed to ensure that both the composition of the model portfolio and its returns are independent of when it is presumed to have been initiated.) Eligible issues include the 4 highest-yielding Dow issues that are neither General Motors nor Philip Morris. A HYD strategy derives much of its effectiveness because it "forces" the investor to purchase sound companies when they are out of favor and sell them when they return to relative popularity. We exclude GM because its erratic dividend history has usually rendered its relative yield ineffective as a means of signaling timely purchases, especially when it has ranked no. 4 or higher on the list. We have chosen to exclude Philip Morris also, because, in present circumstances, it seem unlikely that there will be sufficient "good news" for it to be sold out of the model portfolio, whatever its ups and downs, unless it is specifically excluded. The hypothetical trades used to compute the composition of the model (as well as the returns on the model and the full list of 30 Dow stocks) are based on mid-month closing prices, plus or minus $0.125 per share.

This month, the strategy sold some Chevron, which is no longer in the Dow, and some Minnesota Mining and J.P. Morgan to buy Caterpillar, A.T.& T., and Dupont. These transactions assume the investor has been following the model for at least 18 months. Investors following the model for less than 18 months would be buying all 4 eligible stocks, using one-eighteenth of their total portfolio each month. Investors can also accumulate portfolios that approximate the model in less than 18 months, by "jumping in" and duplicating the model immediately. However, only investors with sizable portfolios should attempt to track the exact percentages month to month: To avoid excessive transaction costs, investors should adjust their holdings toward the percentages below only when commissions are less than 1% of the value of a trade. By making such adjustments from time to time, investors should achieve results roughly equal to the future performance of the model.

*Our **HYD Investment Management Program** provides professional and disciplined application of this alternative strategy for individual accounts. For accounts of $100,000 or more, the fees and expenses of AIS discretionary portfolio management programs are comparable to those of most mutual funds. Contact us for information on this and our other discretionary investment management services.*

As of November 15, 2000					*——Percent of Portfolio*——*	
	Rank	*Yield*	*Price*	*Status*	*Value*	*No. Shares‡‡*
Philip Morris	1	5.93%	35.7500	*-0-	-0-	
A.T.&T.	2	4.28%	20.5625	Buying	3.7	9.3
Caterpillar	3	3.71%	36.6875	Buying	17.4	25.1
Eastman Kodak	2	3.69%	47.7500	Holding**	17.3	19.1
General Motors	5	3.46%	57.8125	*	-0-	-0-
Dupont	6	3.22%	43.4375	Buying	8.4	10.2
Int'l Paper	7	2.78%	36.0000	Holding	10.8	10.1
Morgan, J.P.	8	2.66%	150.6250	Selling	24.0	8.4
Minn.Mng.& Mfg.	9	2.43%	95.3750	Selling	10.6	5.8
Exxon Mobil	10	1.95%	90.3750			
Proctor & Gamble	11	1.91%	73.3750			
SBC Communications	12	1.76%	57.3125	Holding	1.9	1.7
Chevron	-	3.10%	83.9375	Selling	6.4	4.0
Goodyear Tire	-	6.63%	18.1000	Holding	0.5	1.5
Sears, Roebuck	-	2.92%	31.4600	Holding	2.9	4.8
					100.0	100.0

Change in Portfolio Value‡

	1 mo.	*1 yr.*	*5 yrs.*	*10 yrs.*	*15 yrs.*	*From 12/63*	*Std. Dev.*
Alt. Strategy	10.2%	-6.1%	18.0%	20.2%	19.2%	16.5%	18.7
Dow	4.7%	0.9%	18.6%	17.9%	17.3%	11.3%	16.9

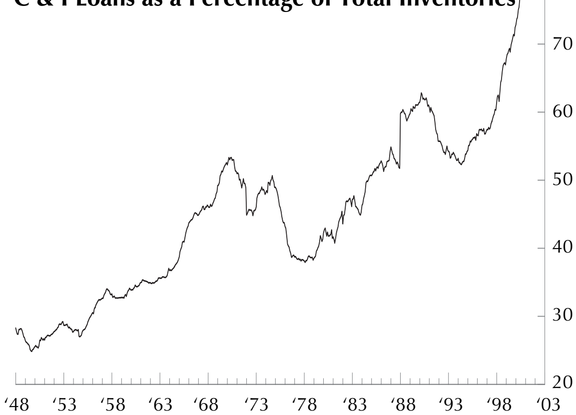
* The strategy excludes Philip Morris and General Motors. ** Indicated purchases approximately offset by sales of shares purchased 18 months ago. ‡ Assuming all purchases and sales at mid-month prices (+/– $0.125 per share commissions) reinvestment of all dividends and interest, and no taxes. The 5, 10 and 15-year total returns are annualized as are the total returns and the standard deviations of those returns since December 1963. ‡‡ Because the percentage of each issue in the portfolio by value reflects the prices shown in the table, we are also showing the number of *shares* of each stock as a percentage of the total number of shares in the entire portfolio.

Note: These calculations are based on hypothetical trades following very exacting stock selection strategies. They do not reflect returns on actual investments or previous recommendations of AIS. Past performance may iffer from future results.

circumstance might seem puzzling. As shown in Chart 3, however, in recent years (i.e., those coinciding with the advent of the "new economy") the proportion of inventory financed by short-term borrowing instead of with equity or long-term debt has skyrocketed. At this time, it is difficult to know precisely what this increase indicates. It might be in some part an effect of the buy-backs of corporate stock that accompanied the historic bull market of 1982-99. It could reflect an extraordinary optimism among corporate controllers and treasurers who expected returns from other funds larger than the costs of short-term finance. Or it could mean that the lending practices for C&I loans, and the uses made of such funds (how about another party for prospective venture capitalists?) have changed. Probably some combination of these as well as other factors is involved.

Chart 3

C & I Loans as a Percentage of Total Inventories



But whatever the reasons, the decision to finance inventory overwhelmingly through short-term debt (now almost 10 percent of GDP and 80 percent of the value of all inventory) would seem to imply greater inventory-related risk exposure to business than ever. In this circumstance, it is the lenders who will call the tune—and if the banks get scared, watch out. And they have every reason to be scared. As a percent of GDP, *the only other times C&I loans even approached current levels, the economy was headed for or already in recession.* The Federal Reserve's most recent quarterly survey of business lending shows that more than a fifth of all C&I loans now are either in the "acceptable," "special mention," or "classified" troubled loan categories. And Bank of America's recently announced charge-offs could scarcely have been good news to the banking community. In response, lenders already reportedly are tightening their C&I loan requirements.

The economy still could be headed for a soft landing, but the current interest-rate and inventory-cycle data are not reassuring. It may pay to hold off a bit on those big-ticket purchases—the closeout sales may be coming.

— *Adapted from A.I.E.R.'s* Research Reports*, 11/27/2000.*

THE DOW JONES INDUSTRIALS RANKED BY YIELD

	Ticker Symbol	Months On/(Off) Top 10	Market Prices 11/15/00	Market Prices 10/13/00	Market Prices 11/15/99	12-Month High	12-Month Low	Latest Dividend Amount	Latest Dividend Record Date	Latest Dividend Paid	Indicated Annual Dividend	Indicated Yield† (%)
Philip Morris	MO	93	**$35.75**	31.00	25.38	38.63 *H*	18.69	0.530	12/15/00	1/10/01	2.120	5.93
AT&T	T	6	**$20.56**	24.63	46.00	61.00	20.06 *L*	0.220	9/29/00	11/01/00	0.880	4.28
★ Caterpillar	CAT	19	**$36.69**	31.69	55.56	57.06	29.00	0.340	10/20/00	11/20/00	1.360	3.71
★ Eastman Kodak	EK	26	**$47.75**	38.94	65.75	67.81	35.31 *L*	0.440	12/01/00	1/02/01	1.760	3.69
★ General Motors ‡	GM	58	**$57.81**	57.69	72.31	94.63	54.50 *L*	0.500	11/16/00	12/09/00	2.000	3.46
☆ DuPont	DD	13/(31)	**$43.44**	40.56	62.13	74.00	38.19	0.350	11/15/00	12/14/00	1.400	3.22
★ International Paper	IP	12	**$36.00**	27.44	55.69	60.00	26.31 *L*	0.250	11/24/00	12/15/00	1.000	2.78
★ J. P. Morgan	JPM	85	**$150.63**	143.13	138.38	187.63	104.88	1.000	9/25/00	10/13/00	4.000	2.66
★ Minn. Min. & Mfg.	MMM	73	**$95.38**	91.00	97.44	103.81	78.19	0.580	11/24/00	12/12/00	2.320	2.43
☆ Exxon Mobil	XOM	1/(6)	**$90.38**	90.50	78.00	95.44	69.88	0.440	11/13/00	12/11/00	1.760	1.95
Procter & Gamble	PG		**$73.38**	72.63	106.56	118.38	52.75	0.350	10/20/00	11/15/00	1.400	1.91
☆ SBC Comm.	SBC	(2)	**$57.31**	50.13	50.94	59.00 *H*	34.81	0.254	10/10/00	11/01/00	1.010	1.76
Alcoa (s)	AA		**$29.25**	25.81	31.97	43.63	23.13 *L*	0.125	11/03/00	11/25/00	0.500	1.71
Merck	MRK		**$91.63**	76.19	75.19	92.75 *H*	52.00	0.340	12/08/00	1/02/01	1.360	1.48
Honeywell Intl.	HON		**$51.63**	34.63	60.94	64.00	32.13	0.188	11/20/00	12/08/00	0.750	1.45
Johnson & Johnson	JNJ		**$95.00**	95.81	103.50	106.88	66.13	0.320	11/21/00	12/12/00	1.280	1.35
United Tech.	UTX		**$67.06**	69.69	54.50	72.94	46.50	0.225	11/17/00	12/10/00	0.900	1.34
Citigroup * (s)	C		**$50.19**	49.81	55.88	59.13	35.34	0.140	11/06/00	11/22/00	0.560	1.12
Coca-Cola	KO		**$61.31**	57.19	58.25	69.00	42.88	0.170	12/01/00	12/15/00	0.680	1.11
General Electric (s)	GE		**$52.50**	57.00	45.17	60.50	41.65	0.137	10/03/00	10/25/00	0.550	1.05
Hewlett-Packard (s)	HWP		**$35.31**	45.31	37.32	68.09	29.36 *L*	0.080	12/20/00	1/10/01	0.320	0.91
Boeing	BA		**$63.56**	58.75	40.13	67.88 *H*	32.00	0.140	11/10/00	12/01/00	0.560	0.88
McDonald's	MCD		**$33.31**	28.88	46.88	48.00	26.38	0.215	11/15/00	12/01/00	0.220	0.66
Walt Disney	DIS		**$31.81**	39.75	25.88	43.88	25.50	0.210	11/16/99	12/17/99	0.210	0.66
American Express (s)	AXP		**$57.69**	53.94	52.42	63.00	39.83	0.080	1/05/01	2/09/01	0.320	0.55
IBM	IBM		**$99.38**	109.06	94.06	134.94	86.94 *L*	0.130	11/10/00	12/09/00	0.520	0.52
Wal-Mart Stores	WMT		**$49.00**	45.00	61.00	70.25	41.44	0.060	12/22/00	1/08/01	0.240	0.49
Home Depot, Inc.(s)	HD		**$39.63**	36.31	52.50	70.00	34.69	0.040	8/31/00	9/14/00	0.160	0.40
Intel Corp. (s)	INTC		**$41.50**	40.38	37.03	75.81	35.00	0.020	11/07/00	12/01/00	0.080	0.19
Microsoft Corp.	MSFT		**$70.06**	53.75	87.00	119.94	48.44 *L*	0.000	-	-	0.000	0.00
☆ Chevron	CHV	(13)	**$83.94**	84.25	91.38	96.94	69.94	0.650	11/17/00	12/11/00	2.600	3.10
☆ Goodyear	GT	(13)	**$18.10**	15.90	37.13	39.25	15.60	0.300	11/16/00	12/15/00	1.200	6.63
Sears, Roebuck	S	(13)	**$31.46**	31.94	30.00	43.50	25.25	0.230	11/30/00	1/02/01	0.920	2.92

★ BUY. ☆ HOLD. † Based on indicated dividends and market price as of 11/15/00. *H* New 52-week high. *L* New 52-week low. (s) All data adjusted for splits. • Excludes extras. * Travelers Group merged with Citibank as of 10/8/98 to form Citigroup. ‡ Spinoff of 0.69893 shares of Delphi Automotive per share of GM on 5/29/99.

Note: The count in months for the Top 10 issues indicates how long they have ranked among the Top 10. Issues are recommended for purchase (★) after having been among the Top 10 for 12 or more consecutive months, but this period can be changed if conditions warrant. Issues recommended for retention (☆) had qualified for purchase, but subsequently ranked no. 11 or lower and the monthly count (in parentheses) indicates how long ago they left the Top 10. If an issue became a ☆, but subsequently returned to the Top 10, both monthly counts are shown.

RECENT MARKET STATISTICS

Precious Metals & Commodity Prices

	11/15/00	Mo. Earlier	Yr. Earlier
Gold, London p.m. fixing	**264.60**	273.25	290.90
Silver, London Spot Price	**4.66**	4.88	5.07
Copper, COMEX Spot Price	**0.83**	0.89	0.78
Crude Oil, W. Texas Int. Spot	**35.58**	34.98	25.13
Dow Jones Spot Index	**111.02**	113.92	117.12
Dow Jones-AIG Futures Index	**110.94**	110.61	91.29
CRB-Bridge Futures Index	**226.83**	230.85	206.66

Interest Rates (%)

U.S. Treasury bills -	91 day	**6.35**	6.17	5.25
	182 day	**6.34**	6.19	5.42
	52 week	**6.14**	6.31	5.48
U.S. Treasury bonds -	15 year	**5.93**	6.02	6.28
Corporates:				
High Quality -	10+ year	**7.61**	7.66	7.28
Medium Quality -	10+ year	**8.25**	8.25	7.74
Federal Reserve Discount Rate		**6.00**	6.00	5.00
New York Prime Rate		**9.50**	9.50	8.50
Euro Rates	3 month	**5.17**	5.07	3.49
Government bonds -	10 year	**5.18**	5.11	5.06
Swiss Rates -	3 month	**3.50**	3.54	2.29
Government bonds -	10 year	**3.81**	3.73	na

Exchange Rates

British Pound	**$1.424000**	1.448100	1.622500
Canadian Dollar	**$0.644200**	0.661800	0.682000
Euro	**$0.856700**	0.851900	1.033600
Japanese Yen	**$0.009186**	0.009246	0.009445
South African Rand	**$0.130100**	0.132800	0.162600
Swiss Franc	**$0.560900**	0.563400	0.644200

Securities Markets

	11/15/00	Mo. Earlier	Yr. Earlier
S & P 500 Stock Composite	**1,389.81**	1,374.17	1,394.39
Dow Jones Industrial Average	**10,707.60**	10,192.18	10,760.75
Dow Jones Transportation Average	**2,841.01**	2,430.18	3,064.60
Dow Jones Utilities Average	**388.20**	388.75	298.13
Dow Jones Bond Average	**95.60**	95.96	99.50
Nasdaq Composite	**3,165.49**	3,316.77	3,219.54
Financial Times Gold Mines Index	**571.59**	645.53	973.47
FT African Gold Mines	**624.53**	804.27	1,176.89
FT Australasian Gold Mines	**711.28**	757.64	1,196.01
FT North American Gold Mines	**531.92**	574.67	872.33

Coin Prices

	11/15/00	Mo. Earlier	Yr. Earlier	Premium
American Eagle (1.00)	**$271.65**	277.35	299.20	2.66
Austrian 100-Corona (0.9803)	**$258.93**	264.33	283.93	-0.18
British Sovereign (0.2354)	**$65.75**	67.15	71.85	5.56
Canadian Maple Leaf (1.00)	**$271.90**	277.60	298.20	2.76
Mexican 50-Peso (1.2057)	**$319.70**	326.40	350.50	0.21
Mexican Ounce (1.00)	**$265.00**	270.50	290.50	0.15
S. African Krugerrand (1.00)	**$269.75**	275.35	295.55	1.95
U.S. Double Eagle-$20 (0.9675)				
St. Gaudens (MS-60)	**$345.00**	345.00	422.50	34.77
Liberty (Type I-AU)	**$675.00**	675.00	675.00	163.67
Liberty (Type II-AU)	**$435.00**	435.00	470.00	69.92
Liberty (Type III-AU)	**$312.50**	307.50	385.00	22.07
U.S. Silver Coins ($1,000 face value)				
90% Silver (715 oz.)	**$3,900.00**	3,900.00	4,350.00	17.05
40% Silver (292 oz.)	**$1,537.50**	1,562.50	1,600.00	12.99
Silver Dollars	**$5,700.00**	5,750.00	6,825.00	58.11

Note: Premium reflects percentage difference between coin price and value of metal in a coin, with gold at $264.60 per ounce and silver at $4.66 per ounce. The weight in troy ounces of the precious metal in coins is indicated in parentheses.

Selected Mutual Funds

	Ticker Symbol	11/15/00	Month Earlier	Year Earlier	— 52-Week — High	Low	Distributions Latest 12 Months Income	Capital Gains	Yield (%)
★ Duff & Phelps Utilities Income[1]	DNP	**$10.25**	9.63	9.63	10.31	8.25	0.7800	0.0000	7.61
★ T Rowe Price European Stock	PRESX	**$21.58**	20.69	23.25	25.32	20.15	0.1400	1.9000	0.65
★ Vanguard European Stk Index	VEURX	**$25.76**	24.82	26.82	29.85	24.16	0.5000	0.2000	1.94
☆ Vanguard REIT Index	VGSIX	**$10.94**	10.92	9.99	11.98	9.38	0.8000	0.0000	7.31
★ Vanguard Growth Index	VIGRX	**$34.78**	35.24	36.94	42.38	33.55	0.1580	0.9050	0.45
★ Fidelity Target Timeline 2003	FTARX	**$9.14**	9.15	9.26	9.26	8.88	0.6511	0.0000	7.12
★ USAA Short Term Bond	USSBX	**$9.59**	9.60	9.71	9.74	9.53	0.6459	0.0003	6.74
★ Vanguard Short Term Corp	VFSTX	**$10.54**	10.56	10.60	10.60	10.33	0.6998	0.0000	6.64

North American and Diversified Mining Companies

	Ticker Symbol	11/15/00	Month Earlier	Year Earlier	— 52-Week — High	Low	Indicated Annual Net Dividends	Payment Schedule	Yield (%)
Agnico-Eagle†	AEM	**$5.13**	5.56	7.44	8.13	4.88	0.020	Annual	0.39
★ Barrick Gold Corp.†	ABX	**$13.31**	13.94	18.19	20.00	12.31	0.220	Semiannual	1.65
Battle Mountain Gold	BMG	**$1.31**	1.56	2.81	3.00	1.25	0.000	-	0.00
Freeport-McMoran C&G, Cl.A	FCXA	**$6.88**	7.88	15.75	18.75	6.81	0.000	-	0.00
★ Homestake Mining	HM	**$3.69**	4.50	8.88	9.19	3.56	0.050	Semiannual	1.36
★ Newmont Mining	NEM	**$13.50**	14.81	23.00	28.38	12.75	0.120	Quarterly	0.89
★ Placer Dome†	PDG	**$7.75**	8.25	12.63	12.88	7.25	0.100	Semiannual	1.29
★ Rio Tinto PLC‡	RTP	**$61.56**	56.81	71.75	97.25	55.13	2.300	Semiannual	3.74

South African Mining Companies, Finance Houses and Investment Trusts

	Ticker Symbol	11/15/00	Month Earlier	Year Earlier	— 52-Week — High	Low	ADR Net Dividends• and Ex-Dividend Dates				Yield (%)
ASA Ltd.	ASA	**$14.44**	15.06	20.25	20.88	14.06	-	-	-	0.600°	4.16
Anglo American PLC[2]	AAUK	**$55.23**	51.44	53.00	71.00	36.75	4/05/00	1.060	9/20/00	0.580	2.97
★ Anglogold Ltd.[3]	AU	**$13.31**	17.44	28.63	28.69	13.25	2/23/00	0.834	8/09/00	0.511	10.31
Avgold Ltd.	AVGLY	**$3.32**	3.40	6.84	7.50	3.11	No Dividends Declared				
De Beers Consolidated Mines	DBRSY	**$29.19**	26.94	26.13	31.75	18.19	3/29/00	0.675	9/13/00	0.345	3.49
Gencor Ltd.	GNCRY	**$4.03**	3.22	3.71	4.68	2.27	3/29/00	0.041	9/13/00	0.164	5.24
★ Gold Fields Ltd.[4]	GOLD	**$2.72**	3.06	4.25	5.69	2.56	9/15/99	0.045	2/16/00	0.026	2.60

★ Buy. ☆ Hold. (s) All data adjusted for splits. † Dividend shown is after 15% Canadian tax withholding. ‡ Dividend shown is after 15% U.K. tax withholding on a portion of the total. na Not applicable. • Paid or announced last 12 months. ° Total dividend paid in latest 12 months. [1] Closed-end fund—traded on the NYSE. Dividends paid monthly. [2] Anglo American Gold Inv. Co. merger in Anglo American plc. [3] Formerly Vaal Reefs plus interests in Free State, Western Deep, Ergo, Elandsrand and others. 2 ADRs = 1 ordinary share. [4] Gold Fields Ltd. and Driefontonein Consolidated merged to form Gold Fields, Ltd. e Estimated.