INVESTMENT GUIDE

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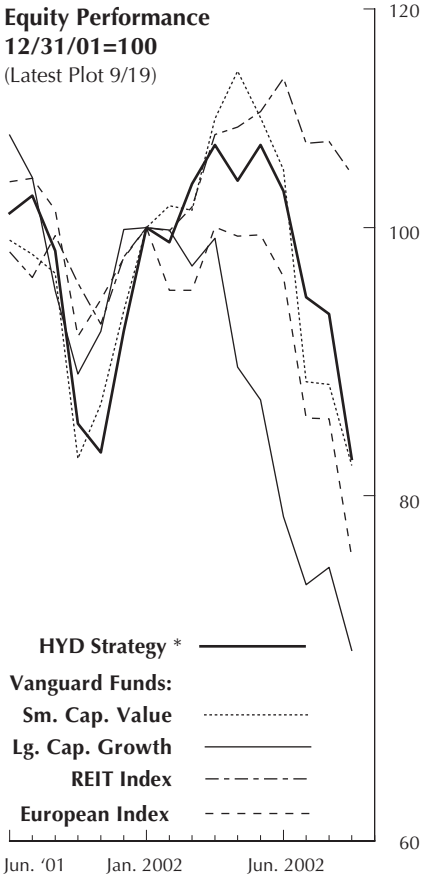

*** HYD is a hypothetical model based on back-tested results. See p. 70 for a full explanation.**

We offer two discretionary management services: Our Professional Asset Management (PAM) service covers all of our recommended assets and allows us to place trades in stocks, bonds, and mutual funds directly in our clients' accounts. (The accounts remain the property of our clients at all times—we are only authorized to trade on their behalf.) Our High-Yield Dow (HYD) service operates similarly, except it invests only in the highest-yielding Dow stocks, using the 4-for-18 model on a fully invested basis. Investors interested in these low-cost services should contact us at 413-528-1216 or Fax 413-528-0103.

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News of War

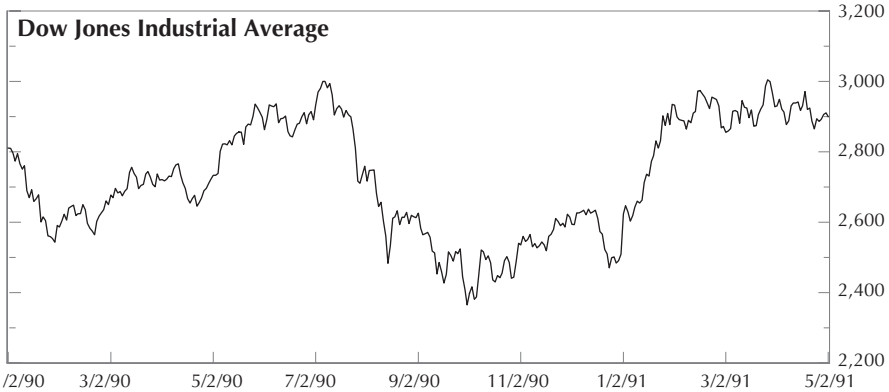
While politicians and pundits ponder the merits of war, investors too must consider its consequences. Dire warnings, from higher oil prices to the costs of protracted U.S. involvement, are everywhere. At bottom, however, the pertinent question is whether the probability of war and its impact are discounted in the markets.

Our investment approach is predicated on the notion that current prices reflect the information available to the public. Those counseling you to take action in anticipation of war and its outcome are in effect suggesting that you should place a bet on war-related news, which of course is currently unknown. If they happen to be right, they will no doubt trumpet their analytical "prowess." However, if they are wrong they will either return to the table to place another bet, or be replaced by another who claims to be smarter.

The chart below presents the weekly close for the Dow over the period encompassing the Gulf War. During the late summer in 1990, following Iraq's invasion of Kuwait, the market fell by over 20%, while oil prices skyrocketed. Iraq had taken Kuwait virtually unopposed, and appeared to be threatening the entire Middle East. The efficacy of U.S. troops in a desert environment was untested, and Iraq's reputedly formidable military was acknowledged to be capable of inflicting major casualties. But in very short order it became clear that Saddam's forces were no match for the U.N. coalition. By February 1991, oil prices subsided and capital markets had returned to their prewar levels.

Markets work, whether in oil, securities, or any other good or service. While there is no question that security prices overreact and underreact to information, these swings are offsetting and obvious only in retrospect. Though war now appears increasingly likely to some, we will not hazard a guess as to whether war will transpire or what its implications might be.

Rather than focus on external events, you should instead focus your efforts on exploiting the invaluable "insider" information you possess regarding your own goals and tolerance for risk. Diligent introspection will provide insights that will allow you to design and maintain a sound portfolio consistent with our recommended allocations.



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EXCHANGE-TRADED BOND FUNDS

Barclays Global Investors launched the first exchange-traded bond funds in the United States last July, pioneering one of the most interesting innovations for fixed-income investors in some time. These investment vehicles allow investors to capture broad segments of the bond market with a single trade and watch prices right along with stocks on an intra-day basis. The early success of the first four fixed-income exchange-traded funds (ETFs) with reported inflow of over $3 billion suggests that they could play a major role in the financial marketplace. Here we look a bit closer at the mechanics and various features of these assets.

The World of Exchange-traded Funds

Fixed income ETFs are only the most recent addition to the universe of ETFs. Those familiar with equity ETFs know that they are essentially index funds that trade on an exchange as if they were equities. First introduced in 1993 as unit investment trusts (a lower cost yet more rigid form of a mutual fund), they did not gain popularity for several years until a new structure came about that combined the best features of two traditional types of mutual funds: closed-end and open-end funds.

Closed-end funds, which have a rich history dating to the nineteenth century, have a net asset value (NAV) that reflects the underlying value of the securities in the portfolio. But shares of closed-end funds themselves trade on an exchange. This sounds very much like our description of ETFs, but once closed-end funds are brought to market, the number of shares outstanding remains fixed. That means that the price of a closed-end fund is determined by buyers and sellers of the fund's shares, so the price can vary significantly from NAV if market participants perceive the aggregate value of the assets to be more or less than their underlying value. However, outstanding ETF shares are not fixed; they have the ability to create new units and redeem units in-kind, which keeps the price in line with NAV. For example if an ETF's market price were to fall below its NAV, arbitrageurs could purchase the ETFs in the open market and sell the underlying shares for a gain. Market discipline thus forces the market price and NAV to converge.

Open-ended mutual funds are the structure most familiar to investors and are those you buy directly from a fund company or one of their authorized brokers. The open-end structure allows investors to pool money together to buy a diversified portfolio of securities that are either actively or passively managed to the characteristics of an index. When you put money into the fund, the portfolio manager buys more underlying securities (stock or bonds) and when you want your money back, the portfolio manager sells your share of underlying securities in order to cover your redemption (many managers maintain a small stash of cash on hand to cover the day-to-day flow of purchases and redemptions—this uninvested cash turns out to be a drag on performance in the long run). Because they can only be redeemed with the fund, and not sold on the open market, they always trade at net asset value (NAV).

This operational procedure makes an important yet subtle distinction between funds and their exchange-traded counterparts. Any turnover in a fund is potentially subject to capital-gains taxes that impact all holders, not just those that redeem. While fund managers may be sensitive to tax consequences of their day-to-day trading, they may have little control when investors all decide to head for the door at once. While ETFs are often structured as open-end mutual funds, they don't have this problem. When an investor wants to redeem, he merely sell his shares on the open market leaving other investors untouched. This keeps turnover to a minimum, aside from any rebalancing necessary to maintain the characteristics of the index.

This "best of both worlds" approach has proven successful over the last five years. ETFs appear to be another significant financial innovation largely attributable to enhanced information technology. Investors have long been drawn to the ease with which mutual funds allow them to diversify their holdings, but they can now do their investing in "real-time" instead of waiting for the *Wall Street Journal* to see what's happening. That may seem frivolous to a serious investor, but trading on an exchange comes along with other benefits, such as being able to trade using stop or limit orders, sell short, or trade on margin. In short, ETFs give investors greater control of their investing. According to the Investment Company Institute, an industry trade group, ETF assets have expanded from just over $2 billion in the beginning of 1997 to over $82 billion by the end of 2001. Demand for ETFs has resulted in a proliferation of new funds based on everything from the S&P 500 to very specific indices such as the Dow Jones US Financial Services Index or the MSCI Singapore index. Until now, the obvious gap in this array was the presence of any funds that capture the fixed-income market.

The Latest Innovation: Fixed-income ETFs

Very recently, with stocks dragging from the effects of an uncertain eco-

iShares Exchange-traded Bond Funds

Fund	*Ticker*	*Rating*	*Weighted Average Maturity*	*Effective Duration*	*Average Premium/ - Discount (%)*	*# Holdings Fund/Index*	*Expense Ratio (%)*	*Assets (000)*
Goldman Sachs								
$ InvesTop Corporate Bond	LQD	A2/A-	10.38 Yr	6.26	0.72	101/100	0.15	$1,597,783
Lehman 1-3 YR Treasury Bond	SHY	Aaa/AAA	1.63 Yr	1.54	- 0.06	9/30	0.15	$668,028
Lehman 7-10 YR Treasury Bond	IEF	Aaa/AAA	7.46 Yr	6.08	0.05	7/12	0.15	$739,946
Lehman 20+ YR Treasury Bond	TLT	Aaa/AAA	23.67 Yr	12.83	0.06	20/18	0.15	$728,387

Ratings are Moody's/S&P: based largely on the credit quality of the funds' underlying investments, but other factors such as management of a fund relative to its objective are also cited by the rating agencies. Ratings are subject to change. Duration measures a bond's sensitivity to interest rates and therefore its market risk. For example, a three-year duration portfolio will rise (fall) 3% if rates fall (rise) 1%. Premium/Discount is the log difference between the closing price of the fund and its NAV, expressed as a percentage. Data calculated daily from 7/26/02 to 9/10/02. *Source*: Barclays Global Investors, Bloomberg, author's calculation. All data as of 8/31/02, unless otherwise noted. Assets as of 9/10/02.

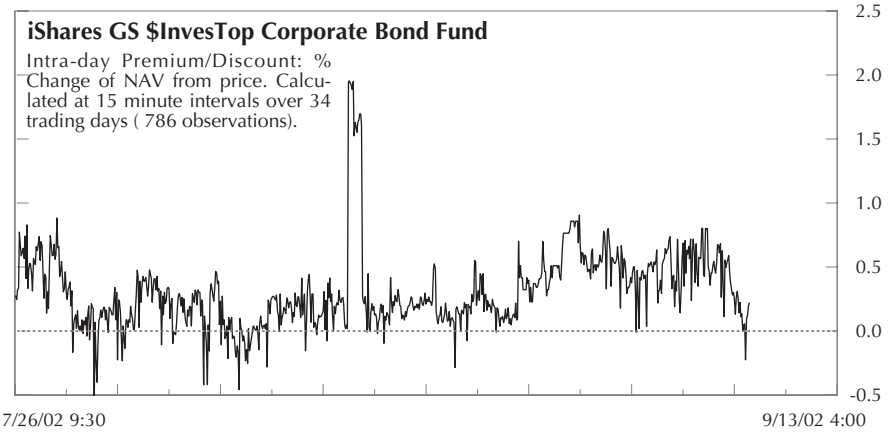
nomic picture and corporate scandals, Barclays Global Investors came to market with the first four fixed-income ETFs in the United States. Despite historically low interest rates, the new ETFs were met with great enthusiasm as one fund alone captured well over a billion dollars in assets within two weeks of its debut, making it one of the largest ETFs trading on the American Stock Exchange. True to form of past ETFs, this new array will enable investors to target fairly specific segments of the bond market with varying ranges of maturity and credit quality. Three of the four ETFs invest in U.S. Treasuries and represent nearly the entire spectrum of the yield curve with short-, medium-, and long-term funds. The fourth fund captures the broad investment grade corporate bond market as represented by the Goldman Sachs $ InvesTop index.

Role of ETFs in a Portfolio

Bonds play an important role in reducing portfolio risk. In the 7 years ending June 30th, a hypothetical all-equity portfolio would have returned 10.6% with a volatility of over 16%. Shifting one third of the assets into bonds would reduce the portfolio's volatility to 8.6% and still return over 8%[1]. The trade-off is nearly 80% of the return for little more than half of the volatility. This simple example illustrates the benefits of fixed-income in a portfolio context. With the introduction of exchange-traded bond funds, investors have a tool to build a comprehensive asset-allocation strategy using both equity and fixed-income funds.

The advantages of bond funds in this regard are similar to traditional mutual funds. While bond funds have no maturity, per se, they are more efficient than managing a portfolio of individual bonds, which is cumbersome to say the least. For example, cash flows from interest payments need to be reinvested at a competitive yield, maturing bonds replaced, and credit quality monitored. This can all be accomplished with one trade in a bond fund. Bond funds can also capture a specific maturity range or entire market segment, thus different funds can be utilized to match the needs of a particular investor.

Barclays announced that three additional bond funds are on the way and other companies such as Nuveen are reportedly quick at work to launch more. Since there is little need for numerous funds of the same index, it would not be surprising for fixed-income ETFs to proliferate just as equity funds have. Future launches could include mortgage and asset-backed securities, municipals, high-yield corporates and industry or country specific bonds. Barclays has also had requests to "fill the gap" with a Treasury fund that would span the 3-7 year "gap" in the yield curve currently uncovered by the new funds.



A Few Points to Ponder

1) Costs: Investors should always be aware of the impact of costs on investments, particularly in fixed-income investments. Each of the new bond ETFs has a 0.15% expense ratio. This is competitive with funds available from the low-cost providers such as Vanguard and minuscule compared to corporate- and government-bond funds, which according to Morningstar have a 1.0% average expense ratio. ETF management fees are likely to remain low for the foreseeable future. First, they are passively managed, keeping turnover and expenses low, and trading costs are minimized from economies of scale. Furthermore, since ETFs have little need to hold cash for redemptions as traditional mutual funds do, after-tax returns are enhanced and "cash drag" (the returns lost to lower-yielding cash investments) is minimized. In the long run bond returns are enhanced by maintaining low expenses. However, the cost advantage of ETFs can be easily eroded by trading commissions if they are too actively traded.

2) Premium/Discount: ETFs have an innovative secret weapon termed the "creation unit," which is the mechanism used to create and redeem shares. This is a simplified version of how they work: An *authorized participant* (a large financial firm) purchases the underlying securities in the index, delivers them to a custodian bank, and receives ETF shares in return. Redemption is the same process in reverse. Creation units allow the number of shares to expand and contract to meet demand. This mechanism gives institutional investors the ability to take advantage of any disparity between the value of ETF shares and their underlying securities. All of this serves to minimize the difference between the market price of a fund and its NAV. The factors that determine how well all this serves its purpose are liquidity of the underlying securities and the size of the fund (in short the ease with which market makers can utilize the creation-unit mechanism).

While it is no guarantee that this mechanism will work under all market conditions, the transparency of ETFs enable easy evaluation on a fund by fund basis. NAVs are estimated every 15 seconds (which can be viewed with a separate ticker symbol) and calculated at the end of every trading day. Of the bond ETFs, the GS $ InvesTop Corporate Bond Fund displays the greatest variance between closing price and NAV, at an average of 0.72% between July 26 and September 10, 2002. However, on an intraday basis, (15 minute intervals, 786 valid observations) the standard deviation of premiums and discounts was quite low at 0.31%. In other words, there was a modest price disparity between NAV and price for the fund, but that disparity remains fairly constant, so investors who buy at a modest "premium" have had little risk of selling at a significantly lower premium. Still, ongoing observations through varying market conditions will be worthwhile.

3) Taxes: The tax benefit of exchange-traded funds over traditional funds is highly

[1] Stocks are represented by the S&P 500 and bonds are represented by the Lehman Brothers 7-10 year bond index. Volatility is annualized standard deviation.

touted. However, fixed-income funds have higher income and a higher turnover rate than equity index portfolios do because the composition of the underlying securities will change more often as bonds mature or are dropped from the index. Thus fixed-income ETFs may be less tax efficient than their equity counterparts.

4) Tracking error: Index funds are often managed by a technique called representative sampling. Notice from the box above that some of the funds have little more than half of the holdings of the index, while others have more. The fund's prospectus dictates only that the characteristics of an index be replicated, but not necessarily its exact makeup. Fund managers appreciate this flexibility as buying bonds for a portfolio can be quite a different exercise than declaring them fit for an index. Particularly as bonds do not trade on an exchange are thus not as transparent as equities. But sampling could come at a cost if there is a sustained variation between the return of the fund and that of the index. This variation is termed "tracking error" and should be negligible for index funds (excepting for fees, which indexes don't have). While we would not anticipate a problem with this set of funds as they hold very liquid securities, they have not had enough history for thorough evaluation. As new funds are issued, investors should at least periodically monitor this aspect of each fund's performance.

A Final Word

Purchasing ETFs as opposed to traditional mutual funds may be a matter of preference or a function of individual fund characteristics. ETFs have merit as a low cost and flexible vehicle for those who wish to capture specific segments of the bond market or maintain a particular risk profile as part of a long-term asset allocation strategy. Active Traders or those who invest small amounts regularly could easily erode any cost advantage over traditional mutual funds by incurring excessive trading commissions. Also remember that when it comes to any exchange traded fund, each should be evaluated on its own merits and not be judged by the whole. An ETF based on the S&P 500 may not have the same characteristics as one based on Singaporean equities and the same will hold true as we see new varieties of exchange-traded bond funds.

While the four fixed-income ETFs currently available are acceptable investment vehicles, many investors might wait until a broader selection becomes available. We continue to recommend that fixed-income investors "stay short"; that is, their fixed income holdings should generally not have a weighted maturity that exceeds five years (see box). Of the four new funds, only one meets this criterion (the Lehman 1-3 YR Treasury Bond fund). We will continue to monitor these funds going forward.

(For more information on equity exchange-traded funds and their various structures, see the Investment Guides of September and November 2001)

FIXED INCOME INVESTMENT VEHICLES

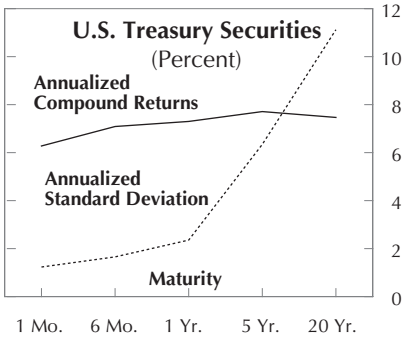
Characteristic	Individual Bond	Fixed-Income ETF	Open-end Bond Mutual Fund	Closed-end Bond Mutual Fund
Liquidity	Sell at market any time, some bonds less liquid	Liquid. Real-time intra-day prices.	Liquid. Priced at end-of-day Net Asset Value.	Liquid. Real-time intra-day prices.
Diversification	No	Yes, portfolio of bonds based on broad index.	Depends on structure, could be less diversified if actively managed vs. index.	Depends on structure, could be less diversified if actively managed vs. index.
Costs	"Spread" charged at purchase or sale	Low expense ratio, brokerage commission at purchase or sale	Expense ratio can be high if actively managed. Possible brokerage commission	Expense ratio can be high if actively managed. Brokerage commission
Minimum Investment	Usually $5,000 and increments of $5,000	None	Possible, varies by fund	None
Reinvestment	Investor must perform	Investor must perform	Automatic if requested	Investor must perform
Income Payments	Semi-annual except zero coupon bonds	At least monthly	Varies by fund	Varies by fund
Pricing	Market price with broker discretion	Real-time, intra-day	Net Asset Value	Real-time, intra-day
Accessibility	Most brokerage firms	Most brokerage firms	Through fund, some brokerage firms	Most brokerage firms

Source: Barclay's Global Investors, Fixed Income Securities, Inc.

WHY STAY SHORT?

Because their periodic interest payments are fixed, bond prices are inversely related to interest rates; as prevailing interest rates rise, bond prices fall, and vice versa. Furthermore, long-term bonds are more interest-rate sensitive than are shorter-term bonds, because their longer time to maturity renders them more vulnerable to fluctuating rates.

The chart below demonstrates that fixed-income securities with longer maturities have tended to provide only mod-

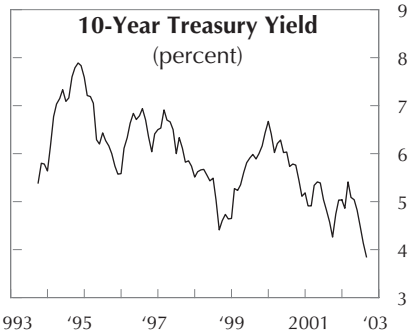


estly higher returns over time, but the risk of those securities, as measured by their volatility, or standard deviation, has been significant. In light of this risk/return environment we recommend that investors, as a rule of thumb, avoid fixed-income assets with maturities in excess of five years.

This recommendation is based on an historical review of the evidence, and it reflects our view of how to invest in bonds regardless of the interest rate environment. It is not a temporary strategy based on our view of current market conditions, since in our view predicting interest rates is a hopeless endeavor. Nevertheless, the current interest-rate environment may well be poised to once again present a lesson to those who "reach for yield" by extending maturities.

Consider the following: Ten-year U.S. Treasury notes are currently providing a meager 3.8% yield to maturity. The chart above right shows yields since October 1993, when these notes on average yielded roughly 5.9% annually, ranging from as high as 8.2% to their current low. Clearly, if interest rates were to simply revert to the mean, bond prices would fall, and owners of bond portfolios would be in for a rough ride.

The 7-10 year Treasury Bond iShares are currently providing a 30-day SEC yield of 3.84% versus 1.83% for the 1-3 year Treasury Bond iShares. An investor might



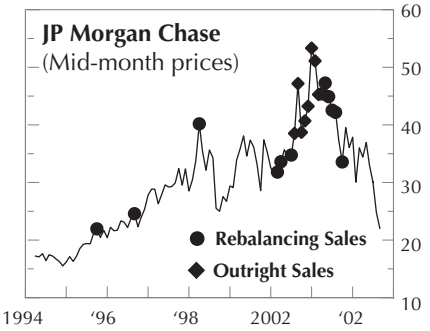
be tempted to purchase the longer-term shares if he simply focused on yield. However, the 7-10 year shares have an effective duration of 6.08 versus 1.54 for the 1-3 year shares. In other words, *the longer-term securities yield just over twice that of the shorter-term securities, but are almost four times as risky if interest rate sensitivity (as measured by duration) is used to assess risk*. Suppose 10-year yields were indeed to revert to their mean, and increase by 2%, and that yields along the entire yield curve from 1 month to 10 years similarly increased by 2%. Using duration as a rough gauge, the 7-10 year iShares would fall in value by 12.2% (duration of 6.08 X 2%), while the 1-3 year iShares would fall by only 3.1% (1.54 X 2%).

JP MORGAN IN THE HYD PROGRAM

This month J.P. Morgan Chase (JPM) issued an earnings warning that sent its share price reeling. Considering that its share price is at its lowest point in many months and that JPM shares have been in the our "4-for-18" model for over eight years, investors might not realize that it has in fact been a profitable holding. Here we analyze its history to demonstrate that, as is the case with all the stocks, the model will systematically "buy low" and "sell high" even those stocks that remain in the model for extended periods. This is demonstrated in the chart above.

Through September 2002, JPM generated dividends equal to the 16.3% of the total purchase cost of the stock in the model. The proceeds of the JPM shares sold from the model totaled 59.5% of that total purchase cost, and it happens that the value of remaining holdings of JPM as of September 2002 also equaled 59.5% of the cost. The sum of these three percentages is 135.4% of the cost (a total return of 35.4% on the amounts invested over the entire 102 month period).

In terms of a more conventional measure, the total annualized rate of return for JPM



during the period was 11.2%. (Annualized rate of return is actually calculated as an internal rate of return.) Imagine a savings account in which the deposits equaled the purchases and the withdrawals equaled the sales and dividends of JPM within the "4-for-18" model. Such an account would have had to have paid 11.2% per year for its current balance to equal to the current value of the JPM stock in the model portfolio.

The first purchase of what is now J.P. Morgan Chase occurred in April 1994, just 35 months after J.P. Morgan and Co. was first included in the Dow Jones Industrial Average. JPM was eligible for purchase by the model during 94 of the 102 succeeding months.

During 68 of the 94 months when JPM was eligible for purchase, it had also been eligible 18 months earlier, *i.e.*, it was a "hold." However, the model "rebalances" every month so that its purchases and holdings of the four eligible stocks each month are of equal value. Rebalancing positions for the months when JPM was a "hold" resulted in either the sale of some shares when JPM's stock price had performed better than the other stocks in the portfolio during the prior 18 months, or the purchase of additional shares if it had underperformed.

Sales generated from such "rebalancings" occurred during 12 months. During 8 months the model sold all the shares it had purchased and/or retained 18 months earlier. The chart shows both types of sales.

The salient point of all these numbers is this: J.P. Morgan's price has been volatile, to the advantage of HYD investors. The model mechanically buys low and sells high. Investors who have adhered to its discipline by buying in the face of headline-grabbing bad news (when yield is skyrocketing) and selling while yields have fallen, have enjoyed the ride.

THE HIGH-YIELD DOW INVESTMENT STRATEGY

We are convinced that long-term, common-stock investors will receive superior returns on the "large-capitalization-value stocks" component of their holdings when they consistently hold the highest-yielding Dow stocks. The fact that a given company's stock is included in the Dow Jones Industrial Average is evidence that the company is a mature and well-established going concern. When a Dow stock comes on the list of the highest-yielding issues in the Average, it will be because the company is out of favor with the investing public for one reason or another (disappointing earnings, unfavorable news developments, etc.) and its stock price is depressed. A High-Yield Dow (HYD) strategy derives much of its effectiveness because it forces the investor to purchase sound companies when they are out of favor and to sell them when they return to relative popularity.

Selecting from the list will not be cut and dried if the timing of purchases and sales reflects individual prejudices or other *ad hoc* considerations. These usually come down to "I'm not going to buy *that*" or "goody, this fine company has finally come on the list and I'm going to load up." Our experience with investing in the highest-yielding Dow stocks has shown that attempts to "pick and choose" usually do not work as well as a disciplined approach.

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, they found that the best combination of total return and low risk (volatility) was obtained by purchasing the four 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", $12.)

The model portfolio of HYD holdings set forth in the accompanying table reflects the systematic and gradual accumulation the four highest-yielding Dow issues that are neither General Motors nor Philip Morris. 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 exclude Philip Morris because, in present circumstances, it seems unlikely that there will be sufficient "good news" for it to be sold out of the portfolio. For more than eight years, Philip Morris has never ranked lower than fourth on the list, whatever its ups and downs, and, given the circumstances, using Philip Morris in the strategy amounts to a buy-and-hold approach. The HYD strategy, to repeat, derives much of its superior performance from buying cheap and selling dear.

In the construction of the model, shares purchased 18 months earlier that are no longer eligible for purchase are sold. The hypothetical trades used to compute the composition of the model (as well as the returns on the model and on the full list of 30 Dow stocks) are based on mid-month closing prices, plus or minus $0.125 per share. This month, two of the four stocks eligible for purchase, **SBC Communications** and **JP Morgan Chase,** were not eligible for purchase 18 months earlier (in December 2000), and two issues that were eligible for purchase 18 months ago, **Caterpillar** and **International Paper**, are not eligible this month. Investors following the model should find that the indicated purchases of SBC and Morgan, and the indicated sales of Caterpillar and International Paper are sufficiently large to warrant trading. In larger accounts, rebalancing positions in **Eastman Kodak** and **Dupont** may warrant additional trades, as the model calls for adding to positions that have lagged the entire portfolio and lightening up on positions that have done better than the portfolio as a whole.

Investors with sizable portfolios may be able to track the exact percentages month to month, but smaller accounts should trade less often to avoid excessive transactions costs, only adjusting their holdings toward the percentages in

As of September 13, 2002

					——*Percent of Portfolio**——	
	Rank	*Yield*	*Price*	*Status*	*Value*	*No. Shares†*
Eastman Kodak	1	6.35%	28.36	Holding**	25.9	27.5
JP Morgan Chase	2	6.17%	22.04	Buying	19.6	26.7
Philip Morris	3	5.53%	46.30	*		
General Motors	4	4.54%	44.08	*		
SBC Comm.	5	4.40%	24.55	Buying	9.7	12.0
Dupont	6	3.49%	40.08	Holding**	28.8	21.6
Caterpillar	7	3.44%	40.64	selling	12.5	9.3
Honeywell Int'l	8	3.18%	23.56			
Merck & Co.	9	2.92%	49.27			
Alcoa	10	2.73%	21.99			
Int'l Paper	11	2.70%	37.04	Selling	3.5	2.9
					100.0	100.0

Change in Portfolio Value‡

	1 mo.	*1 yr.*	*5 yrs.*	*10 yrs.*	*15 yrs.*	*From 12/63*	*Std. Dev.*
Strategy	-7.2%	-16.9%	3.1%	11.6%	13.6%	15.3%	19.0
Dow	-5.6%	-12.0%	3.1%	11.6%	10.8%	10.3%	17.0

* 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 a very exacting stock selection strategy, and are gross of any management fees. They do not reflect returns on actual investments or previous recommendations of AIS. Past performance may differ from future results.

the table if prospective commissions will be less than, say, one percent 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.

The process of *starting* to use the strategy is not as straightforward. The two most extreme approaches are: 1) buy all the indicated positions at once or 2) spread purchases out over 18 months. Either choice could be said to represent an attempt at market timing, i.e., buying all at once could be construed as a prediction that (and will look good in retrospect only if) the prices of the shares go up after the purchases are made. On the other hand, if purchases are stretched out and stock prices increase, the value of the investor's holdings will lag behind the strategy's performance. We believe that most attempts to time the market are futile, and the best course lies somewhere in between the extremes.

Some portion of the shares now held in the strategy will be sold within a few months. The shares most likely to be sold are those whose indicated yields are too low to make them currently eligible for purchase. This usually means that their prices have risen (and their yields have fallen) in relative if not absolute terms, since they were purchased. If such stocks are purchased now and are sold within a few months, the investor will receive only a portion of the profit, or sustain a greater loss, than the strategy. On the other hand, if the stocks not currently eligible for purchase are bought and the strategy does not call for selling them soon, it will usually be because their prices have decreased so that their indicated yields render them again eligible for purchase. In other words, buying a stock that is not currently among the top four means that it will very likely be sold during the months ahead (perhaps at a gain, perhaps not, but with payment of two commissions either way). Alternatively, if the price decreases so that the issue again becomes eligible for purchase, then the investor's initial purchase would be likely to be held in the portfolio at a loss for some period of time. In the latter situation, the investor would have been better off waiting.

Accordingly, for new HYD clients, we usually purchase the complement of the currently eligible stocks without delay. (This month, the four eligible issues—SBC Communications, Dupont, Eastman Kodak, and J.P. Morgan Chase—account for over 80% of the total portfolio value). Any remaining cash will be held in a money-market fund pending subsequent purchases, which will be made whenever the client's holdings of each month's eligible stocks are below the percentages indicated by the strategy by an amount sufficient to warrant a trade.

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

THE DOW JONES INDUSTRIALS RANKED BY YIELD

	Ticker Symbol	Market Prices 9/13/02	Market Prices 8/15/02	Market Prices 9/10/01	12-Month High	12-Month Low	Latest Dividend Amount	Latest Dividend Record Date	Latest Dividend Paid	Indicated Annual Dividend	Yield† (%)
★ Eastman Kodak	EK	**$28.36**	30.24	43.23	42.00	24.40	0.900	6/03/02	7/16/02	1.800	6.35
★ J. P. Morgan Chase	JPM	**$22.04**	24.79	37.26	40.95	18.22	0.340	7/05/02	7/31/02	1.360	6.17
Philip Morris	MO	**$46.30**	50.91	48.15	57.79	40.30	0.640	9/16/02	10/10/02	2.560	5.53
General Motors	GM	**$44.08**	45.71	51.58	68.17	39.17	0.500	8/16/02	9/10/02	2.000	4.54
★ SBC Comm.	SBC	**$24.55**	28.06	43.43	47.50	22.20	0.270	7/10/02	8/01/02	1.080	4.40
★ DuPont	DD	**$40.08**	41.74	38.39	49.80	32.64	0.350	8/15/02	9/12/02	1.400	3.49
☆ Caterpillar	CAT	**$40.64**	44.16	48.10	59.99	39.05	0.350	7/22/02	8/20/02	1.400	3.44
Honeywell Intl.	HON	**$23.56**	32.13	35.70	40.95	22.15	0.188	8/20/02	9/10/02	0.750	3.18
Merck	MRK	**$49.27**	50.58	66.10	70.60	38.50	0.360	9/06/02	10/01/02	1.440	2.92
Alcoa	AA	**$21.99**	25.43	33.80	40.50	21.05 *L*	0.150	11/08/02	11/25/02	0.600	2.73
☆ International Paper	IP	**$37.04**	39.24	37.84	46.20	30.70	0.250	8/23/02	9/16/02	1.000	2.70
Exxon Mobil	XOM	**$34.08**	37.14	41.24	44.58	29.75	0.230	8/13/02	9/10/02	0.920	2.70
General Electric	GE	**$27.05**	32.29	39.35	41.84	23.02	0.180	9/27/02	10/25/02	0.720	2.66
Citigroup	C	**$29.38**	35.84	42.45	52.20	24.48	0.180	8/05/02	8/23/02	0.720	2.45
Hewlett-Packard	HPQ	**$13.50**	15.00	17.89	24.12	10.75	0.080	9/18/02	10/09/02	0.320	2.37
3M Company	MMM	**$119.83**	126.80	102.20	130.60	85.86	0.620	8/23/02	9/12/02	2.480	2.07
Boeing	BA	**$35.58**	37.49	43.46	51.07	27.60	0.170	8/16/02	9/06/02	0.680	1.91
Procter & Gamble	PG	**$92.00**	91.32	74.20	94.75	67.00	0.410	7/19/02	8/15/02	1.640	1.78
United Tech.	UTX	**$58.00**	61.75	66.20	77.75	40.10	0.245	8/23/02	9/10/02	0.980	1.69
Coca-Cola	KO	**$49.65**	51.41	49.95	57.91	43.50	0.200	9/15/02	10/01/02	0.800	1.61
Johnson & Johnson	JNJ	**$54.14**	55.97	55.62	65.89	41.40	0.205	8/20/02	9/10/02	0.820	1.51
Walt Disney	DIS	**$15.50**	15.15	23.58	25.17	13.48	0.210	12/07/01	12/21/01	0.210	1.35
AT&T	T	**$12.72**	10.55	17.65	20.00	8.20	0.038	9/30/02	11/01/02	0.150	1.18
McDonald's	MCD	**$20.53**	24.16	28.92	30.72	19.89 *L*	0.225	11/15/01	12/03/01	0.225	1.10
American Express	AXP	**$34.19**	37.45	35.01	44.91	24.20	0.080	7/05/02	8/09/02	0.320	0.94
IBM	IBM	**$72.50**	76.50	96.47	126.39	65.70	0.150	8/09/02	9/10/02	0.600	0.83
Home Depot, Inc.	HD	**$33.45**	28.93	40.55	52.60	26.10	0.050	9/05/02	9/19/02	0.200	0.60
Wal-Mart Stores	WMT	**$54.40**	54.71	46.23	63.94	42.00	0.075	9/20/02	10/07/02	0.300	0.55
Intel Corp.	INTC	**$16.03**	18.61	26.07	36.78	15.03 *L*	0.020	11/07/02	12/01/02	0.080	0.50
Microsoft Corp.	MSFT	**$47.91**	49.77	57.58	70.62	41.41	0.000	-	-	0.000	0.00

★ BUY. ☆ HOLD. † Based on indicated dividends and market price as of 9/13/02. *H* New 52-week high. *L* New 52-week low. (s) All data adjusted for splits.

Note: The issues indicated for purchase (★) are the 4 highest yielding issues (other than Philip Morris and General Motors) qualifying for purchase in the top 4-for-18 months model portfolio. The issues indicated for retention (☆) have similarly qualified for purchase during one or more of the preceding 17 months, but do not qualify for purchase this month.

RECENT MARKET STATISTICS

Precious Metals & Commodity Prices

	9/13/02	*Mo. Earlier*	*Yr. Earlier*
Gold, London p.m. fixing	**318.80**	312.65	271.50
Silver, London Spot Price	**4.60**	4.49	4.18
Copper, COMEX Spot Price	**0.69**	0.68	0.65
Crude Oil, W. Texas Int. Spot	**29.81**	29.06	27.63
Dow Jones Spot Index	**138.20**	132.53	104.16
Dow Jones-AIG Futures Index	**106.39**	102.20	101.16
CRB-Bridge Futures Index	**227.08**	216.67	197.62

Interest Rates (%)

U.S. Treasury bills -	91 day	**1.67**	1.61	3.18
	182 day	**1.67**	1.61	3.12
	52 week	**1.70**	1.66	3.11
U.S. Treasury bonds -	15 year	**4.60**	4.86	5.38
Corporates:				
High Quality -	10+ year	**6.06**	6.35	6.75
Medium Quality -	10+ year	**7.09**	7.45	7.43
Federal Reserve Discount Rate		**1.25**	1.25	3.00
New York Prime Rate		**4.75**	4.75	6.50
Euro Rates	3 month	**3.32**	3.33	4.27
Government bonds -	10 year	**4.47**	4.38	4.84
Swiss Rates -	3 month	**0.75**	0.81	3.18
Government bonds -	10 year	**2.75**	2.80	3.33

Exchange Rates

British Pound	**$1.543300**	1.534400	1.456400
Canadian Dollar	**$0.632600**	0.640800	0.640900
Euro	**$0.970000**	0.982400	0.897900
Japanese Yen	**$0.008189**	0.008516	0.008207
South African Rand	**$0.093300**	0.093700	0.117000
Swiss Franc	**$0.660100**	0.671000	0.592900

Securities Markets

	9/13/02	*Mo. Earlier*	*Yr. Earlier*
S & P 500 Stock Composite	**889.81**	930.25	1,092.54
Dow Jones Industrial Average	**8,312.69**	8,818.14	9,605.51
Dow Jones Transportation Average	**2,246.87**	2,319.97	2,676.49
Dow Jones Utilities Average	**225.63**	242.50	335.48
Dow Jones Bond Average	**148.98**	143.49	103.66
Nasdaq Composite	**1,291.40**	1,345.01	1,695.38
Financial Times Gold Mines Index	**1,265.52**	1,114.26	808.85
FT African Gold Mines	**2,207.69**	1,784.54	809.27
FT Australasian Gold Mines	**1,632.57**	1,498.00	946.98
FT North American Gold Mines	**992.38**	900.50	776.27

Coin Prices

	9/13/02	*Mo. Earlier*	*Yr. Earlier*	*Premium*
American Eagle (1.00)	**$329.55**	322.25	281.75	3.37
Austrian 100-Corona (0.9803)	**$313.93**	307.03	268.53	0.45
British Sovereign (0.2354)	**$79.25**	77.55	68.15	5.60
Canadian Maple Leaf (1.00)	**$329.80**	322.50	282.00	3.45
Mexican 50-Peso (1.2057)	**$387.50**	378.90	331.50	0.81
Mexican Ounce (1.00)	**$321.20**	314.10	274.80	0.75
S. African Krugerrand (1.00)	**$326.55**	319.35	279.65	2.43
U.S. Double Eagle-$20 (0.9675)				
St. Gaudens (MS-60)	**$385.00**	375.00	317.50	24.82
Liberty (Type I-AU)	**$675.00**	675.00	675.00	118.84
Liberty (Type II-AU)	**$385.00**	385.00	425.00	24.82
Liberty (Type III-AU)	**$359.50**	355.00	297.50	16.55
U.S. Silver Coins ($1,000 face value)				
90% Silver (715 oz.)	**$4,600.00**	4,600.00	4,200.00	39.86
40% Silver (292 oz.)	**$1,575.00**	1,575.00	1,550.00	17.26
Silver Dollars	**$6,025.00**	6,025.00	6,050.00	69.31

Note: Premium reflects percentage difference between coin price and value of metal in a coin, with gold at $318.80 per ounce and silver at $4.60 per ounce. The weight in troy ounces of the precious metal in coins is indicated in parentheses.

Recommended Mutual Funds

	Ticker		*Month*	*Year*	*— 52-Week —*		*Distributions Latest 12 Months*		*Yield*
Short-Term Bond Funds	*Symbol*	*9/13/02*	*Earlier*	*Earlier*	*High*	*Low*	*Income*	*Capital Gains*	*(%)*
★ Fidelity Target Time Line 2003	FTARX	**$9.54**	9.52	9.52	9.68	9.41	0.4054	0.0000	4.25
★ USAA Short Term Bond	USSBX	**$9.12**	9.01	9.97	10.04	8.95	0.5338	0.0000	5.85
★ Vanguard Short-term Corporate	VFSTX	**$10.74**	10.67	10.91	11.03	10.62	0.6124	0.0000	5.70
Income Equity Funds									
★ DNP Select Income[1, 2]	DNP	**$10.16**	10.35	10.84	11.62	7.85	0.7800	0.0000	7.68
★ Vanguard REIT Index	VGSIX	**$12.67**	12.35	12.25	13.69	11.17	0.6696	0.1105	5.28
Large Cap. Value Equity Funds									
★ iShares S&P 500 Value Index[3]	IVE	**$43.02**	45.12	54.48	56.94	37.07	0.7824	0.1472	1.82
★ Vanguard Value Index	VIVAX	**$14.73**	15.38	18.75	19.46	13.21	0.3060	0.1070	2.08
Small Cap. Value Equity Funds									
★ iShares Sm. Cap. 600 Value Index[3]	IJS	**$74.85**	75.80	78.74	99.67	66.35	0.6224	0.3430	0.83
★ Vanguard Sm. Cap Value Index	VISVX	**$8.84**	8.92	9.55	11.66	8.14	0.0650	0.3810	0.74
Growth Equity Funds									
★ iShares S&P 500 Growth Index[3]	IVW	**$45.98**	48.18	55.12	61.21	40.02	0.4389	0.1124	0.95
★ Vanguard Growth Index	VIGRX	**$20.46**	21.36	24.53	27.09	18.25	0.2170	0.0000	1.06
Foreign Equity Funds									
★ iShares S&P Europe 350 Index[3]	IEV	**$47.30**	51.00	57.30	60.78	44.10	0.9307	0.0000	1.97
T Rowe Price European Stock	PRESX	**$12.73**	13.33	15.35	16.55	12.47	0.3600	0.0000	2.83
★ Vanguard European Stock Index	VEURX	**$16.36**	17.31	19.47	20.91	15.67	0.4400	0.0000	2.69

Recommended Gold-Mining Companies

	Ticker		*Month*	*Year*	*— 52-Week —*		*Distributions*		*Yield*
	Symbol	*9/13/02*	*Earlier*	*Earlier*	*High*	*Low*	*Latest 12 Months*	*Frequency*	*(%)*
Anglo American PLC, ADR	AAUK	**$12.70**	12.50	12.75	19.61	9.46	0.460	Semiannual	3.62
★ Anglogold Ltd., ADR	AU	**$27.90**	23.70	15.82	34.66	15.28	0.649	Semiannual	2.33
ASA Ltd.[1]	ASA	**$33.90**	29.08	17.31	40.44	17.00	0.600	Quarterly	1.77
★ Barrick Gold Corp.†	ABX	**$17.55**	16.00	16.11	23.49	13.46	0.220	Semiannual	1.25
★ Gold Fields Ltd.	GFI	**$13.98**	11.70	3.86	17.15	3.98	0.111	Semiannual	0.79
★ Newmont Mining	NEM	**$29.34**	27.00	21.15	32.75	18.52	0.120	Quarterly	0.41
★ Placer Dome†	PDG	**$10.73**	9.40	11.10	14.74	7.91	0.100	Semiannual	0.93
★ Rio Tinto PLC‡	RTP	**$69.65**	67.85	68.59	86.00	53.70	2.350	Semiannual	3.37

★ 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. [1] Closed-end fund, traded on the NYSE. [2] Dividends paid monthly. [3] Exchange traded fund, traded on ASE.