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Equity Performance
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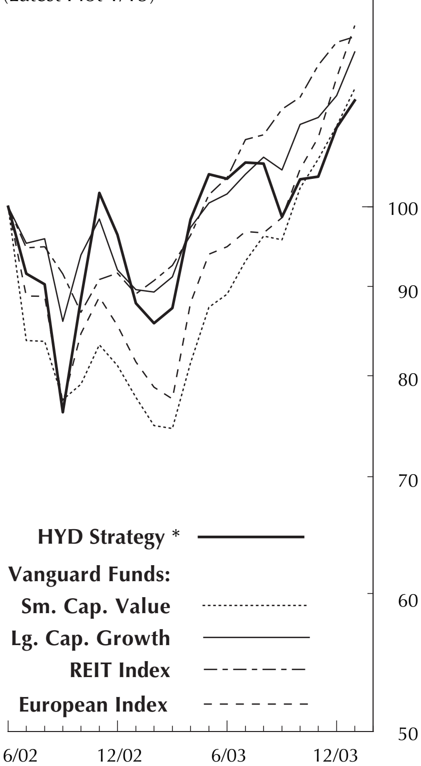
(Latest Plot 1/15)



*** HYD is a hypothetical model based on back-tested results. See p. 6 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.

Online: www.americaninvestment.com

Health Savings Accounts: Opportunities for Investors

A new way to pay for health care that was introduced by the Medicare Reform Act in December combines an insurance component with an intriguing savings kicker. The new plans, called health savings accounts (HSAs) are designed to help individuals save for qualified medical and retiree health expenses on a tax-favored basis. Contributions to these accounts are federally tax-deductible, and earnings accumulate tax-free. Withdrawals are also tax-free, as long as they are used to pay for qualified medical and retiree health expenses. This equivalent of a tax home run—tax-deductible contributions, tax-free accumulation of earnings, and tax-free withdrawals—is truly unique to any type of savings plan.

The major catch: HSAs must be used in conjunction with a high-deductible health insurance plan, which shifts a greater share of medical costs from insurance companies to individuals and families. For individuals under age 65 who purchase self-only policies, a qualified health plan must have a minimum deductible of $1,000 with a $5,000 cap on out-of-pocket expenses. For family policies, a qualified health plan must have a minimum deductible of $2,000 with a $10,000 cap on out-of-pocket expenses. These amounts are indexed annually for inflation. A taxpayer must be under age 65 to open an account.

Beginning January 1, health savings accounts replace Archer MSAs, an earlier type of medical savings account that never really took off because of its restricted availability and complexity. Below are some notable features of the newer, more user-friendly HSAs:

- Beginning this year, individuals can make annual tax-deductible contributions of as much as $2,600 ($5,150 for families) to a health savings account, regardless of whether they itemize on their Federal tax returns. Employer contributions are made on a pretax basis and are not taxable to the employee. This means employers can make deposits to HSAs on behalf of employees, and receive the full employer health insurance deduction for such deposits.

  Currently, 23 states permit tax deductions for contributions to Archer MSAs, according to Scott Krienke, Vice President of individual medical services with Fortis Insurance, an early entrant into the HSA market. Krienke anticipates that many of these states will amend their laws to allow tax-deductible contributions to HSAs as well.
- In addition to the maximum contribution amount, individuals between age 55 and 65 may make additional "catch up" contributions of up to $500 in 2004, increasing to $1,000 annually in 2009 and thereafter. A married couple can make two catchup contributions as long as both spouses are at least age 55. The maximum amounts are indexed annually for inflation.
- Distributions made for nonmedical purposes are subject to income tax and a 10 percent penalty. The penalty is waived for distributions made by individuals age 65 and older, or in the case of death or disability. Medical

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expenses that qualify for tax-free withdrawal treatment include amounts paid for the diagnosis and treatment of disease, prescription drugs, long-term-care insurance and long-term-care services, continuation coverage required by Federal law under COBRA, and health insurance for the unemployed.
- Funds not used in one year can be rolled over into the next to help pay for future expenses. This treatment differs from more familiar flexible spending accounts, whose "use or lose" provisions require participants to empty their accounts each year. Money in flexible spending accounts also earns no interest. By contrast, health savings account investments can include interest-bearing securities or mutual funds.
- The maximum annual contribution to the health savings account may not exceed the amount of the deductible, and is computed monthly. For example, if the annual deductible for an individual policy is $2,600, the maximum monthly contribution to the health savings account in 2004 would be $216.67 ($2,600/12). This means that if one opens a health savings account on June 1, one can contribute a maximum of $1,516.69 ($216.67 x 7) for that year. Although the annual contribution is determined monthly, the maximum contribution may be made on the first day of the year.

"Health Care Savers" and "Health Care Spenders"

As with an IRA, early contributions to a health savings account are advantageous because the money has more time to take advantage of tax-free compounding of earnings. Over time, the account balance can grow significantly. *While the savings account may be used to cover health care costs, there is no requirement that these costs be covered through withdrawals taken from this valuable nest-egg. If you have the means to cover these costs with after-tax dollars, you can leave this savings account alone to compound tax free.*

Assume, for example, that a family of four contributes $5,000 annually to a health savings account, generating an initial tax savings of $1,250 if they are in the 25 percent tax bracket. Instead of making withdrawals from the health savings account, they pay for medical and dental expenses not covered by insurance with after-tax dollars. With an average annual return of 8 percent, the health savings account would be worth $78,225 after 10 years and $247,115 after 20 years. With an annual deposit of $3,000 at the beginning of each year, the account would be worth $46,935 after ten years and $148,269 after 20 years.

Under an ideal health savings account "savers" scenario, someone might accumulate a sizable balance in anticipation of a medical rainy day, pay all or most medical expenses with after-tax dollars, and reach age 65 in robust health. At that point, he could withdraw the money tax-free to pay for long-term-care insurance or expenses not covered by Medicare. Or, he might decide to use all or part of the account for living expenses or a vacation, and pay income taxes on the withdrawals used for those purposes. Even if withdrawals are eventually subject to income taxes, tax-deductible contributions and tax-free accumulation of earnings provide savings incentives and benefits similar to those offered by 401(k) plans.

But health savings accounts were not designed as an estate planning tool. If an account beneficiary's surviving spouse is the named beneficiary on the account, the spouse becomes the new account owner. Although the account passes to the spouse tax-free, it continues to be subject to regular health savings account distribution rules. If the health savings account passes to a person other than the account beneficiary's surviving spouse, it is no longer a health savings account and the heir is required to include in gross income the fair market value of the assets as of the date of death. The includable amount may be reduced by any payments from the account made for the decedent's qualified medical expenses, if paid within one year after death.

In reality, however, most people cannot afford to pay uninsured medical expenses with after-tax dollars, and leave their HSAs untouched. According to the IRS, 73 percent of MSA accounts are set up by those who had been uninsured for six months or more and who probably have no other options. Initially, the most likely candidates for health savings accounts will be the self-employed, the uninsured, and those working for smaller companies who might not otherwise be able to afford a higher-cost, traditional health-insurance plan. This "health spenders" group will pay the lower premiums associated with a high-deductible health insurance plan. If they have some financial leeway, they might contribute all or part of their premium savings over a traditional plan to a health savings account, and use most of the account to pay for ongoing medical expenses.

Others will no doubt be drawn to HSAs for their significant tax benefits. This "health-savers group" could make sizable tax-deductible contributions to the account and pay some or all of their medical expenses from after-tax dollars, leaving the balance to grow largely untouched. For those in a financial position to consider such a strategy, the question is whether or not the tax advantages offered by health savings accounts, combined with the premium savings policy holders realize by opting for a high-deductible policy, outweighs the monetary and emotional costs associated with shouldering a higher portion of one's medical bills. Those considering using a health savings account mainly as a tax-sheltered savings plan should consider several factors:

- **How healthy you are.** Younger, healthier individuals with few medical expenses are obviously better candidates for high-deductible policies than those with more pressing medical needs, such as young families or those with chronic illnesses. But even a healthy individual could suddenly develop an expensive, chronic illness and get stuck paying the maximum deductible for a very long time. At that point, the door to a more traditional health plan may already be closed because of a preexisting condition.
- How wealthy you are. The tax benefits of HSAs are obviously more valuable to those in higher tax brackets. The saver's strategy also works best if you are fairly certain that your income

Several firms are offering policies designed for Health Savings Accounts. While we do not endorse any particular product, readers can get more information from the following firms:

Fortis—800-800-1212; www.fortishealth.com
Aetna—860-273-0123; www.aetna.com
Golden Rule Insurance—800-444-8990; www.goldenrule.com

and assets are substantial enough to pay medical expenses up to the deductible from monies outside the plan for an extended period, should the need arise.

- **How much you can save on premiums.** High-deductible health-insurance policies typically cost between 20 and 50 percent less than traditional plans. At Fortis Insurance Company, which offers both traditional and high-deductible policies, a family of four consisting of two 37-year-old adults and two children would pay a $600 monthly premium for a traditional insurance policy with a $500 annual copayment. A policy with a $5,000 annual deductible would cost $250 a month.

  The previous example illustrates a best-case example of a healthy couple purchasing a non-group policy with a very high deductible. Group policies, as well as those with lower deductibles, typically provide less dramatic savings over traditional health plans.
- **How comfortable you feel paying for medical costs yourself.** Most Americans who have health insurance are used to going to the doctor and paying copayments of $10 or $15 for a typical office visit. Without insurance, even routine healthcare costs can add up to hundreds or even thousands of dollars fairly quickly. Regardless of the tax advantages HSAs offer, you have to be comfortable with the practical reality of digging into your own pocket to pay for medical expenses.

A Bright Future?

HSAs and their MSA predecessors in theory have the potential to help reign in health care costs. If the consumer is paying the first dollar of health care out of his pocket (or out of his health savings account) he will, in theory, be more attentive to costs when shopping for services than would a third-party payor, be it an insurance company or the government.

Yet it remains unclear whether HSAs will take off, or languish in the obscurity suffered by the Archer MSA. Companies were reluctant to offer Archer MSAs because of sunset provisions and limitations on enrollment. With these restrictions removed, HSAs face a brighter future. But don't expect to see large employers offering health savings account this year. Many already had their benefit plans mapped out for 2004 by the time the legislation passed late last year, and aren't likely to alter their insurance options before 2005.

The longer-term future of health savings accounts, and their appeal as an investment to those with the resources to maximize their tax benefits, depends in part on whether banks, brokerage firms, or mutual fund companies jump in to offer competitive products with a broad choice of investment options. Right now, only a handful of health insurance companies are marketing HSAs, and those that do typically put contributions into accounts that pay a low, fixed rate of interest.

Fortis, which offers medical savings accounts with over 8,000 mutual-fund investment options, plans to extend those options to health savings accounts as well. Its MSAver plan provides a glimpse of just how investor-friendly these accounts can be. The MSAver account connected to the plan offers Internet trading, stock quotes, access to phone representatives, and other features associated with mainstream brokerage accounts. Participants can pay for out-of-pocket medical expenses with a healthcare-only debit card or dedicated checking account. No claim forms are necessary.

Critics worry that HSAs could have a negative impact on the health care industry and medical costs. They contend the plans will raise the costs of traditional coverage, relegate the older and sicker to expensive comprehensive insurance, and appeal only to the "healthy and wealthy." Others say that early detection of illnesses could be placed in jeopardy if individuals avoid seeking treatment when they have to pay for it themselves.

Another potential fly in the ointment is the IRS, which is considering how to coordinate other benefit-plan components, such as flexible-spending accounts, with health savings accounts. The IRS could throw a curve ball by saying that flexible-spending accounts cannot be used in conjunction with health savings accounts, according to Andy Anderson, an attorney with Hewitt Associates, a benefits consulting firm. Anderson expects guidance from the IRS on this issue some time in June.

QUARTERLY REVIEW OF INVESTMENT POLICY

Money-Market Funds

Cash-equivalent assets continued to provide meager returns as interest rates remained low throughout the quarter. Nevertheless, in order to meet your liquidity needs, whether they are planned or unanticipated, there is no substitute for this asset class. The most convenient way to maintain exposure to this asset class is through a money-market fund. Money-market funds are mutual funds that invest in short-term securities such as Treasury bills, bankers' acceptances, commercial paper, or negotiable certificates of deposit of major commercial banks. As of mid-January taxable money-market funds were paying an annualized yield of only 0.52 percent. The Federal Reserve has not changed its Fed Funds target rate since June, and has indicated that it intends to keep rates low.

Intermediate-Term Bonds

We continue to counsel investors to avoid "reaching for yield." It would be unwise to either assume greater credit risk or to extend the maturity of your fixed-income portfolio. The bond allocations in the accompanying table should be confined to U.S. Government-issued securities or high-grade corporate or municipal bonds with five years or fewer remaining until maturity.

For many investors, any of the three fixed-income mutual funds on p. 8 will provide a suitable means for holding bonds. Investors with more substantial investment portfolios might consider building a bond ladder. Equal amounts should be invested in bonds with maturities ranging from six months to five years, in six- to twelve-month intervals. As these bonds mature, the proceeds can be reinvested in new five-year bonds. Alternatively, you could follow a "variable maturity" strategy (see the March 2001 *Investment Guide* for a full discussion of this approach) designed to pro-

Yields on U.S. Treasury Securities

	06/30/03	*9/30/03*	*12/31/03*
3-month	0.84	0.95	0.91
6-month	0.96	1.01	1.01
1-year	1.02	1.13	1.18
10-year	3.55	3.96	4.26
30-year	4.56	4.88	5.07

RECOMMENDED PORTFOLIO ALLOCATION PERCENTAGES

	Conservative	*Moderate*	*Aggressive*
Money-Market Funds	30	20	10
Intermediate-Term Bonds	35	25	15
Income Equities	10	5	0
Large-Cap Value Stocks	20	30	35
Small-Cap Value Stocks	0	5	10
Growth Stocks	5	5	10
Foreign Equities	0	5	10
Gold-Related	0	5	10
	100	100	100

Note: Most investors should adopt values between the extreme conservative and aggressive percentages shown above. What is best for an individual investor will depend on one's circumstances and tolerance for risk.

vide the highest expected return per unit of volatility assumed. The strategy, however, is not simple to implement; the only cost-effective means of implementing this approach is offered through the mutual funds of Dimensional Fund Advisors (DFA). DFA offers domestic, global, and municipal-bond funds that adopt this variable-maturity strategy. The DFA funds are not available to "retail" investors, but may be purchased through our Professional Asset Management (PAM) program.

Income Equities

Real Estate Investment Trusts (REITs) and the Duff and Phelps Select Income Fund should be included in most investors' portfolios. In addition to enhancing the stability of your portfolio's value, these investment vehicles provide a steady level of income. The accompanying table reveals that since the second quarter of 2001 REITs have provided at total return of over 58 percent; they have been one of the top-performing asset classes over that period. Our investment vehicle of choice is the Vanguard REIT Index fund (symbol VGSIX). It is currently yielding 5.14 percent. In addition to providing an attractive yield, REITs are not strongly correlated with those of other income-producing securities such as bonds, so they deserve inclusion in many portfolios.

The Duff and Phelps Select Income Fund holds predominantly bonds and stocks of public utilities. Investors might find its monthly dividend to be an attractive feature. The fund is currently yielding 6.94 percent on an annual basis. The fund is able to maintain this high payout because, in addition to its common shares, management issues relatively low-cost remarketed preferred stock, which leverages the earnings available for common shareholders.

Common Stocks

Domestic equities ended the year with a strong quarter. The S&P 500 Index rose 12.18 percent, the Dow Jones Industrial Average gained 13.40 percent and the NASD Composite gained 12.11 percent. The Lipper Large Cap Value Index returned 13.42 percent.

During the fourth quarter the HYD model generally fell back in line with market averages, with a total return* of 12.50 percent. Eastman Kodak's share price has rebounded after falling sharply when management cut the firm's dividend in the third quarter. This is consistent with the general pattern of previous HYD stocks that cut their dividends.

The "Kodak moment" nonetheless had a significant effect on returns for calendar year 2003. After a notably strong performance in 2002, the model significantly underperformed the overall market this year, as well as other large-cap-value benchmarks.

The hypothetical HYD model has outperformed the S&P 500 during just 10 of the last 18 calendar years (the longest period for which comparative data is available) but over the entire period the model returned 16.95 percent annually, versus 10.20 percent for the S&P 500. Moreover, the volatility for these two measures was identical; both had a standard deviation of 21.9. This suggests that episodes such as Kodak's recent swoon might occur occasionally, but are not a valid reason to question to efficacy of the HYD approach over long time periods.

Total Returns	***2002***	***2003***
HYD Model	**-3.36%**	**+15.19%**
S&P 500 Index	**-22.10%**	**+28.68%**
S&P 500/BARRA Value Index	**-20.85%**	**+31.79%**
Lipper Large Cap Value Index	**-19.68%**	**+28.27%**

HYD is a hypothetical model based on back-tested results. See p. 6 for a full explanation.

For the quarter the Vanguard Value Index Fund (large-cap) gained 13.93 percent. Large-cap growth stocks were up as well. The Vanguard Growth Index gained 10.33 percent.

The Russell 2000 (small-cap) Index gained 14.52 percent, while the Vanguard Small-Cap Value Index returned 16.19 percent. International stocks were the stel-

Total Returns (%)

	2001			*2002*				*2003*				*Total Return Entire Period*
	2Q	*3Q*	*4Q*	*1Q*	*2Q*	*3Q*	*4Q*	*1Q*	*2Q*	*3Q*	*4Q*	*2Q 2001-4Q 2003*
Vanguard Short-Term Corporate	1.25	3.34	0.17	0.26	1.25	**2.27**	1.34	**1.39**	0.02	0.40	0.46	14.91
Vanguard REIT Index	10.66	-2.56	4.72	8.08	4.79	-8.48	0.10	1.01	12.27	9.47	9.27	58.93
Vanguard Value Index	4.41	-16.26	7.89	1.32	-10.69	-20.45	9.88	-5.57	20.27	2.24	13.93	-1.34
High-Yield Dow 4/18*	10.24	-16.09	9.19	6.92	-6.20	-23.79	**26.42**	-9.21	18.59	-4.90	12.50	12.43
Vanguard Small Cap Value Index	**13.25**	-16.63	**21.22**	**9.59**	-4.15	-22.50	4.62	-7.98	19.39	7.48	16.19	34.89
Vanguard Growth Index	7.70	-13.26	12.97	-0.87	-16.30	-14.07	7.04	-0.91	11.57	3.24	10.33	1.43
Vanguard European Stock Index	-1.87	-12.09	9.48	0.05	-4.05	-22.85	10.77	-9.25	**22.30**	3.89	**20.30**	7.49
Gold (London PM Fix)	5.01	**8.31**	-5.66	9.01	**5.67**	1.63	7.75	-3.56	3.33	**12.14**	7.28	**62.26**

The highest returns provided in each period are in **Bold Face Type**. * HYD is a hypothetical model based on back tested results. See p. 6 for a full explanation.

lar performers for the quarter. The MSCI EAFE Index finished the fourth quarter up 17.11 percent. The Vanguard European Stock Index fund rose 20.30 percent. The euro again boosted the value of euro-denominated holdings, rising roughly 8 percent against the dollar, closing the quarter at $1.23.

Gold-Related Investments

The gold price surged during the quarter, rising from $388 to $417. The price benefited from the weaker dollar. We do not recommend that investors "load up" on gold (or any other asset class) in anticipation of future events. Gold is an extremely volatile asset and should only be held as a small proportion of an investment portfolio (see our recommended portfolio allocation table).

Total Returns: AIS-Recommended Gold-Related Stocks

	2002	***2003***
Barrick Gold Corp.	-2.22%	49.05%
Newmont Mining Co.	52.60%	68.26%
Rio Tinto PLC (ADR)	4.73%	45.23%
Placer Dome Inc.	6.49%	57.15%
Anglogold Ltd. (ADR)	97.84%	41.45%
Gold Fields, Ltd. (ADR)	197.04%	2.24%

We have long recommended direct ownership of gold coins for individuals. This is not so much to make money as to have money in all circumstances. Bullion coins should be purchased for this purpose rather than numismatic coins. Alternatively, investors can purchase shares of our recommended precious-metals mining companies. Our recommended shares include only well established, producing, dividend-paying companies.

FOURTH-QUARTER ECONOMIC REVIEW

Overall, our appraisals of the statistical indicators suggest that the economic recovery remains on firm footing. Ten of the ten leaders with a clear trend were appraised as probably or clearly expanding and 80 percent of the coinciders were expanding. As a result of two upgrades in the appraisals of the lagging indicators, two of the six for which a trend is evident are appraised as probably or clearly expanding, versus only one of six the previous month.

Industrial Activity

Industrial output continued to rise smartly, with the prospect of further gains ahead. The Federal Reserve's index of industrial production increased at a 6.2 percent annual rate during the quarter, led by gains in the production of consumer durables materials (14.1 percent) and construction supplies (7.6 percent). The Fed's capacity utilization index reported further progress in the absorption of idle resources, reaching 75.8 percent by the end of the fourth quarter. It had been at 74.9 percent in September, and 74.0 percent in June.

Housing

For a change there was a mixed picture in the housing sector. Through the first two months of the fourth quarter, measures of home-building activity were higher than they'd been in the third quarter, but the pace of home sales declined. Housing starts grew 8.3 percent over the third quarter's average, while building permits were up 3.4 percent. Sales of new homes, however, were down 5.3 percent from the third quarter's level, while resales of single-family homes were 3.4 percent below the third-quarter rate.

Labor Markets

December's gain of only 1,000 jobs suggested continuing sluggishness in the job market. However, there was a bit of good news during the fourth quarter. As measured by the payroll survey, employment growth continued throughout the quarter, averaging 48,000 per month. And the unemployment rate declined to 5.7 percent in December; its most recent peak was 6.3 percent in June. But the way the rate declined–with more than 300,000 ending their search for work—points to continuing weakness in the job market.

It is interesting to note the implications of two explanations for the labor market's lackluster performance in the current recovery. One line of argument emphasizes the increasing importance of global competition for both manufacturing- and service-sector jobs in high-wage Western economies. Although official data on the subject are scarce, there is a good deal of anecdotal evidence on the relocation of jobs, many of which had been thought to be insulated from foreign competition. In recent months, there has been a steady stream of announcements that corporations are relocating the work done in U.S.-based call centers, back-office operations, and other functions to overseas locations. These relocations have occasionally included software development and other activities further up the corporate food chain.

Another explanation—not necessarily inconsistent with the global labor view—is that employment growth, particularly in the manufacturing sector, responds to the combination of business fixed investment (spending on plant and equipment) and export demand. This second view suggests a hopeful outlook. Business investment spending increased in the second and third quarters of 2003 at annual rates of 7.0 percent and 12.8 percent respectively. And the weaker dollar suggests there could soon be a resumption of growth in U.S. exports. If there is any merit to the global labor cost argument, however, any resulting pickup in employment growth will be smaller than suggested by historical relationships.

International Trade and the Dollar

During the fourth quarter, the dollar's exchange value declined against a wide range of currencies. The USD/EUR rate rose from $1.13 at the end of the third quarter to $1.23 at the end of the year, an 8 percent decline in the dollar's value against the European currency. The dollar also declined against the Japanese yen, with the JPY/USD rate going from 115 to 108 over the same interval, representing a 7 percent decline.

The dollar has been losing value for almost two years now. The Federal Reserve's broad dollar index, which weights the currencies of U.S. trading partners according to their importance in trade flows with the U.S., has declined by 12.8 percent since March of 2002.

U.S. exporters look forward to reaping the benefits of the lower dollar: As the currency's exchange value declines, so do the prices of U.S. exports in foreign markets. The improved business prospects brought on by the dollar's decline are a key feature of the optimistic outlook in export-oriented sectors. At the same time, however, participants in the financial markets are again recalling the consequences of a too-rapid decline in the dollar's exchange value: higher interest rates, lower equity prices, and the prospect—however slim—of a disruption in U.S. financial markets.

THE HIGH-YIELD DOW INVESTMENT STRATEGY

We are convinced that long-term, common-stock investors will receive superior returns on the "large-capitalization-value stock" 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 of the four highest-yielding Dow issues, excluding General Motors and Altria (formerly 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 Altria 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, Altria has never ranked lower than fourth on the list, whatever its ups and downs, and, given the circumstances, using Altria 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. Of the four stocks eligible for purchase this month, only **AT&T and Merck** were not eligible for purchase 18 months earlier (in July 2002). Investors following the model should find that the indicated purchases of **AT&T** and **Merck** and sales of **Eastman Kodak** and **Dupont** are sufficiently large to warrant trading. In larger accounts, a rebalancing in **SBC** may be warranted as the model calls for adding to positions that have lagged the entire portfolio. Investors with sizable holdings 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 the table if prospective commissions will be less than, say, one percent of the value of a trade. By making such adjust-

As of January 15, 2004

					Percent of Portfolio*	
	Rank	*Yield*	*Price*	*Status*	*Value*	*No. Shares*[1]
Altria Group	1	5.01%	54.25	*		
SBC Comm.	2	4.67%	26.74	Holding**	24.29	27.24
AT&T	3	4.49%	21.16	Buying	17.26	24.46
General Motors	4	3.70%	54.00	*		
JP Morgan Chase	5	3.49%	38.92	Holding**	30.23	23.29
Merck	6	3.22%	45.93	Buying	2.97	1.94
DuPont	7	3.15%	44.47	Selling	8.91	6.08
CitiGroup	8	2.83%	49.50			
General Electric	9	2.50%	30.33			
Exxon Mobil	10	2.48%	40.28			
Eastman Kodak	13	1.92%	26.07	Selling	14.12	16.25
Caterpillar	16	1.78%	83.38	Holding	2.19	0.78
					100.0	100.0

Change in Portfolio Value[2]

	1 mo.	*1 yr.*	*5 yrs.*	*10 yrs.*	*15 yrs.*	*From 12/63*	*Std. Dev.*
HYD Strategy	9.52%	10.24%	6.08%	12.68%	15.68%	15.65%	19.43
Dow	5.44%	23.68%	4.25%	12.53%	13.46%	10.68%	16.98

* The strategy excludes Altria and General Motors. ** Currently indicated purchases approximately equal to indicated purchases 18 months ago. [1] 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. [2]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.

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.

ments 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, AT&T, J.P. Morgan Chase and Merck—account for roughly 75 percent 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

		Market Prices			12-Month		Latest Dividend			Indicated	
	Ticker Symbol	1/15/04	12/15/03	1/15/03	High	Low	Amount	Record Date	Paid	Annual Dividend	Yield† (%)
Altria Group	MO	**$54.25**	53.36	41.12	55.03 *H*	27.70	0.680	12/22/03	1/09/04	2.720	5.01
★ SBC Comm.	SBC	**$26.74**	24.87	28.54	29.99	18.85	0.313	1/10/04	2/02/04	1.250	4.67
★ AT&T (r)	T	**$21.16**	18.98	27.46	27.72	13.45	0.238	12/31/03	2/02/04	0.950	4.49
General Motors	GM	**$54.00**	48.93	40.20	55.55 *H*	29.75	0.500	11/13/03	12/10/03	2.000	3.70
★ J. P. Morgan Chase	JPM	**$38.92**	35.26	27.08	39.95 *H*	20.13	0.340	1/06/04	1/31/04	1.360	3.49
★ Merck	MRK	**$45.93**	43.70	59.29	63.50	40.57	0.370	12/05/03	1/02/04	1.480	3.22
☆ DuPont	DD	**$44.47**	44.06	42.50	46.17 *H*	34.71	0.350	11/15/03	12/14/03	1.400	3.15
Citigroup	C	**$49.50**	47.78	37.45	50.52 *H*	30.25	0.350	11/03/03	11/26/03	1.400	2.83
General Electric	GE	**$32.00**	30.33	25.19	32.42	21.30	0.200	12/31/03	1/26/04	0.800	2.50
Exxon Mobil	XOM	**$40.28**	37.80	34.93	41.63 *H*	31.58	0.250	11/12/03	12/10/03	1.000	2.48
International Paper	IP	**$43.86**	40.78	37.91	45.01 *H*	33.09	0.250	11/21/03	12/15/03	1.000	2.28
Honeywell Intl.	HON	**$36.48**	30.83	25.27	36.90 *H*	20.20	0.188	11/20/03	12/10/03	0.750	2.06
☆ Eastman Kodak	EK	**$26.07**	23.45	39.14	41.08	20.39	0.250	11/03/03	12/12/03	0.500	1.92
Johnson & Johnson	JNJ	**$51.84**	49.46	55.00	59.08	48.05	0.240	11/18/03	12/09/03	0.960	1.85
Procter & Gamble	PG	**$99.51**	97.82	85.90	100.49 *H*	79.57	0.455	10/24/03	11/14/03	1.820	1.83
☆ Caterpillar	CAT	**$83.38**	78.52	47.18	85.16 *H*	41.24	0.370	10/20/03	11/20/03	1.480	1.78
Coca-Cola	KO	**$49.73**	49.79	44.90	50.99 *H*	37.01	0.220	12/01/03	12/15/03	0.880	1.77
Alcoa	AA	**$35.47**	34.94	22.20	39.44 *H*	18.45	0.150	11/07/03	11/25/03	0.600	1.69
McDonald's	MCD	**$25.15**	25.42	16.69	27.01	12.12	0.400	11/14/03	12/01/03	0.400	1.59
Boeing	BA	**$43.04**	39.20	33.35	43.70 *H*	24.73	0.170	11/14/03	12/05/03	0.680	1.58
3M Company (s)	MMM	**$84.30**	82.00	63.51	85.40 *H*	59.73	0.000	11/21/03	12/12/03	1.320	1.57
United Tech.	UTX	**$95.40**	91.55	64.40	96.75 *H*	53.51	0.350	11/14/03	12/10/03	1.400	1.47
Hewlett-Packard	HPQ	**$25.30**	22.01	20.25	25.80 *H*	14.18	0.080	12/17/03	1/07/04	0.320	1.26
Walt Disney	DIS	**$24.82**	22.83	17.99	25.08 *H*	14.84	0.210	12/12/03	1/06/04	0.210	0.85
American Express	AXP	**$49.68**	45.31	37.67	49.75 *H*	30.90	0.100	1/02/04	2/10/04	0.400	0.81
Home Depot, Inc.	HD	**$35.43**	34.35	21.87	37.89	20.10	0.070	12/04/03	12/18/03	0.280	0.79
IBM	IBM	**$94.02**	92.11	87.59	95.65 *H*	73.17	0.160	11/10/03	12/10/03	0.640	0.68
Wal-Mart Stores	WMT	**$53.49**	50.74	50.59	60.20	46.25	0.090	12/19/03	1/05/04	0.360	0.67
Microsoft Corp. (s)	MSFT	**$27.54**	26.74	28.14	30.00	22.55	0.160	10/17/03	11/07/03	0.160	0.58
Intel Corp.	INTC	**$33.06**	30.24	17.35	34.60 *H*	14.88	0.020	11/07/03	12/01/03	0.080	0.24

★ BUY. ☆ HOLD. † Based on indicated dividends and market price as of 1/15/04. *H* New 52-week high. *L* New 52-week low. (s) All data adjusted for splits. (r) All data adjusted for reverse splits. * SBC paid an extra dividend of .10 on 11/3/03 that is not included in the annual yield.

Note: The issues indicated for purchase (★) are the 4 highest-yielding issues (other than Altria Group 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

	1/15/04	Mo. Earlier	Yr. Earlier
Gold, London p.m. fixing	**412.50**	407.50	351.00
Silver, London Spot Price	**6.32**	5.56	4.73
Copper, COMEX Spot Price	**1.08**	1.00	0.76
Crude Oil, W. Texas Int. Spot	**33.65**	33.18	33.21
Dow Jones Spot Index	**175.59**	173.64	150.85
Dow Jones-AIG Futures Index	**137.41**	136.33	114.49
CRB-Bridge Futures Index	**264.41**	260.84	239.74

Interest Rates (%)

U.S. Treasury bills -	91 day	**0.86**	0.89	1.18
	182 day	**0.95**	0.99	1.22
	52 week	**1.15**	1.25	1.30
U.S. Treasury bonds -	15 year	**4.55**	4.82	4.78
Corporates:				
High Quality -	10+ year	**5.47**	5.77	5.91
Medium Quality -	10+ year	**5.80**	6.15	6.75
Federal Reserve Discount Rate		**2.00**	2.00	0.75
New York Prime Rate		**4.00**	4.00	4.25
Euro Rates	3 month	**2.10**	2.16	2.85
Government bonds -	10 year	**4.19**	4.38	4.19
Swiss Rates -	3 month	**0.26**	0.28	0.63
Government bonds -	10 year	**2.62**	2.79	2.28

Exchange Rates

British Pound	**$1.813900**	1.746900	1.606700
Canadian Dollar	**$0.771500**	0.758300	0.651600
Euro	**$1.248500**	1.233600	1.056700
Japanese Yen	**$0.009429**	0.009297	0.008473
South African Rand	**$0.135400**	0.158500	0.113000
Swiss Franc	**$0.797200**	0.794600	0.723400

Securities Markets

	1/15/04	Mo. Earlier	Yr. Earlier
S & P 500 Stock Composite	**1,132.05**	1,068.04	918.22
Dow Jones Industrial Average	**10,553.85**	10,022.82	8,723.18
Dow Jones Transportation Average	**3,018.48**	2,950.77	2,360.51
Dow Jones Utilities Average	**266.17**	254.34	221.36
Dow Jones Bond Average	**178.68**	173.91	159.34
Nasdaq Composite	**2,109.08**	1,918.26	1,438.80
Financial Times Gold Mines Index	**1,641.30**	1,772.90	1,233.62
FT African Gold Mines	**2,532.40**	2,648.78	2,310.99
FT Australasian Gold Mines	**3,474.68**	3,316.54	1,776.21
FT North American Gold Mines	**1,300.78**	1,437.29	929.99

Coin Prices

	1/15/04	Mo. Earlier	Yr. Earlier	Premium
American Eagle (1.00)	**$434.65**	416.45	360.55	5.37
Austrian 100-Corona (0.9803)	**$413.83**	396.63	343.43	2.34
British Sovereign (0.2354)	**$103.55**	99.35	86.35	6.64
Canadian Maple Leaf (1.00)	**$434.90**	416.70	360.80	5.43
Mexican 50-Peso (1.2057)	**$510.50**	489.30	423.80	2.64
Mexican Ounce (1.00)	**$423.30**	405.70	351.30	2.62
S. African Krugerrand (1.00)	**$429.65**	411.85	356.95	4.16
U.S. Double Eagle-$20 (0.9675)				
St. Gaudens (MS-60)	**$512.50**	485.00	410.00	28.42
Liberty (Type I-AU)	**$675.00**	675.00	675.00	69.13
Liberty (Type II-AU)	**$482.50**	482.50	410.00	20.90
Liberty (Type III-AU)	**$455.00**	450.00	390.00	14.01
U.S. Silver Coins ($1,000 face value, Circulated)				
90% Silver (715 oz.)	**$4,345.00**	3,920.00	4,550.00	-3.85
40% Silver (292 oz.)	**$1,747.50**	1,582.50	1,587.50	-5.31
Silver Dollars	**$6,575.00**	6,400.00	6,112.50	34.48

Note: Premium reflects percentage difference between coin price and value of metal in a coin, with gold at $412.50 per ounce and silver at $6.32 per ounce. The weight in troy ounces of the precious metal in coins is indicated in parentheses.

Recommended Mutual Funds

	Ticker Symbol	1/15/04	Month Earlier	Year Earlier	52-Week High	52-Week Low	Distributions Latest 12 Months Income	Distributions Latest 12 Months Capital Gains	Yield (%)
Short-Term Bond Funds									
★ iShares Lehman 1-3 Yr Treasury	SHY	**$82.71**	82.37	82.06	83.04	81.82	1.3142	0.0000	1.59
★ USAA Short Term Bond	USSBX	**$9.12**	9.09	9.03	9.23	9.00	0.3393	0.0000	3.72
★ Vanguard Short-term Corporate	VFSTX	**$10.83**	10.80	10.77	10.96	10.72	0.4361	0.0000	4.03
Income Equity Funds									
★ DNP Select Income[1, 2]	DNP	**$11.20**	10.80	10.54	11.27	9.69	0.7800	0.0000	6.96
★ Vanguard REIT Index	VGSIX	**$15.20**	15.28	11.67	15.39	11.28	0.7800	0.0000	5.13
Large Cap. Value Equity Funds									
★ iShares S&P 500 Value Index[3]	IVE	**$56.66**	53.05	45.06	56.85	37.44	0.8873	0.1472	1.57
★ Vanguard Value Index	VIVAX	**$19.05**	18.33	15.35	19.22	13.09	0.3720	0.0000	1.95
Small Cap. Value Equity Funds									
★ iShares Sm. Cap. 600 Value Index[3]	IJS	**$103.88**	96.42	73.81	104.14	45.57	0.7612	0.3430	0.73
★ Vanguard Sm. Cap Value Index	VISVX	**$11.65**	11.42	8.67	11.72	7.39	0.1980	0.0000	1.70
Growth Equity Funds									
★ iShares S&P 500 Growth Index[3]	IVW	**$56.74**	53.78	46.76	56.89	41.25	0.6069	0.1124	1.07
★ Vanguard Growth Index	VIGRX	**$25.29**	24.27	20.76	25.46	18.59	0.1760	0.0000	0.70
Foreign Equity Funds									
★ iShares S&P Europe 350 Index[3]	IEV	**$66.00**	62.55	48.16	67.49	39.52	2.5127	0.0000	3.81
T Rowe Price European Stock	PRESX	**$17.96**	16.82	13.07	17.97	10.81	0.2200	0.0200	1.22
★ Vanguard European Stock Index	VEURX	**$22.74**	20.94	16.57	22.74	13.64	0.4600	0.0000	2.02

Recommended Gold-Mining Companies

	Ticker Symbol	1/15/04	Month Earlier	Year Earlier	52-Week High	52-Week Low	Distributions Latest 12 Months	Distributions Frequency	Yield (%)
Anglo American PLC, ADR	AAUK	**$21.69**	20.56	14.81	23.12	13.45	0.480	Semiannual	2.21
★ Anglogold Ltd., ADR	AU	**$41.15**	47.29	34.01	49.95	27.10	1.329	Semiannual	3.23
ASA Ltd.[1]	ASA	**$42.45**	45.18	38.80	48.00	31.76	0.600	Quarterly	1.41
★ Barrick Gold Corp.†	ABX	**$20.56**	22.15	15.15	23.70	14.10	0.187	Semiannual	0.91
★ Gold Fields Ltd.	GFI	**$13.45**	13.72	13.25	15.52	9.52	0.318	Semiannual	2.36
★ Newmont Mining	NEM	**$42.59**	47.22	27.50	50.28	24.08	0.200	Quarterly	0.47
★ Placer Dome†	PDG	**$16.03**	16.90	11.00	19.23	8.71	0.085	Semiannual	0.53
★ Rio Tinto PLC‡	RTP	**$107.15**	103.00	79.56	116.33	71.70	2.420	Semiannual	2.26

★ Buy. ☆ Hold. (s) All data adjusted for splits. † Dividend shown is after 15% Canadian tax withholding. ‡ Not subject to U.K. withholding tax. na Not applicable.
[1] Closed-end fund, traded on the NYSE. [2] Dividends paid monthly. [3] Exchange traded fund, traded on ASE.

The information herein is derived from generally reliable sources, but cannot be guaranteed. American Investment Services, the American Institute for Economic Research, and the officers, employees, or other persons affiliated with either organization may from time to time have positions in the investments referred to herein.