

INVESTMENT GUIDE

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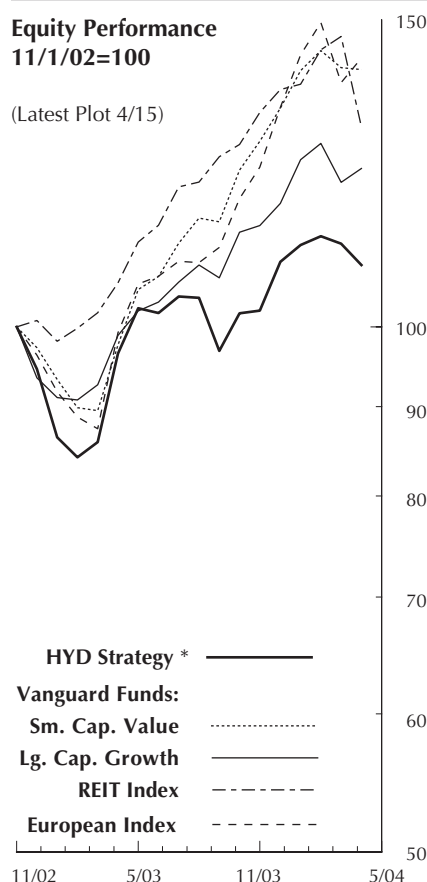
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Great Barrington, Massachusetts 01230

April 30, 2004

Equity Performance 11/1/02=100

(Latest Plot 4/15)



* HYD is a hypothetical model based on back-tested results. See p. 30 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

Tweaking the Dow

On April 8 the 30 component companies of the venerable Dow Jones Industrial Average (DJIA) were changed for the first time since 1999. Eastman Kodak, AT&T, and International Paper were dropped while Pfizer, Verizon and American International Group (AIG) were added. Although two of the firms that were replaced were in our high-yield Dow model, the changes will not necessitate any drastic action on the part of investors who follow our methodology.

The editors of the *Wall Street Journal* try to maintain the DJIA as an index that will remain a legitimate proxy for the broader market. They focus, therefore, on providing a selection of firms that are representative of the overall U.S. economy. Most recently healthcare (Pfizer) and finance (AIG) have grown increasingly important in the economy, while industries such as basic materials (International Paper) have become less important.

Two stocks that are being dropped from the index are currently in our high-yield Dow model; Eastman Kodak accounts for roughly 12 percent of the model's value, and AT&T 18.6 percent. However, the change will not generate a sudden shift in holdings. We will simply continue to sell off Eastman Kodak month-by-month, a process begun in the fall when the firm cut its dividend sharply. AT&T will be sold off month-by-month as well, beginning in August, 18 months after it was first purchased. Verizon immediately moved into the four highest yielding stocks in the Dow, and is now included in our recommended high-yield Dow portfolio (see table on page 30). High-yield Dow investors should make their first purchase this month.

Yield and Market Capitalization

	Symbol	Yield (Percent)	Market Cap (\$ Billions)
Out	Eastman Kodak	1.94	7.31
	AT&T	5.03	15.50
	International Paper	2.38	20.75
In	Pfizer	1.82	272.75
	Verizon	4.16	103.74
	AIG	0.35	197.97

We remain optimistic regarding the model's prospects. While "value" investing has returned to favor in general, the recent change in the tax law has generated a great deal of interest in high-yielding stocks in particular, and we think the tax break is likely to prompt more firms, including those in the DJIA, to increase their payouts.

TAXING CAPITAL GAINS: WHAT'S NEXT?

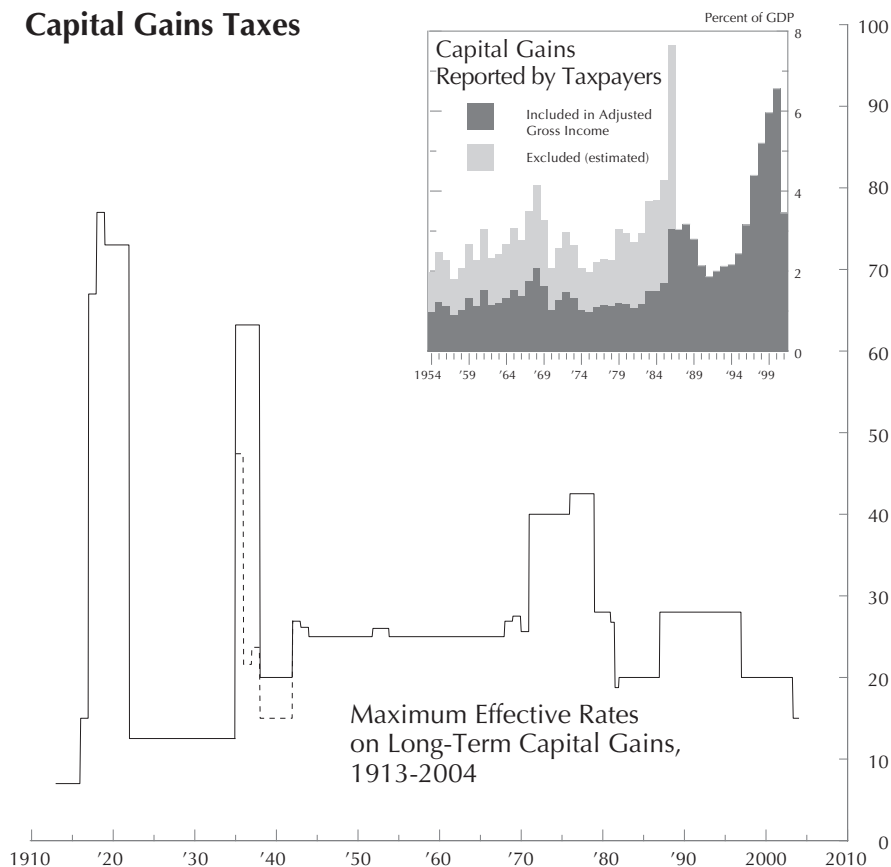
Beginning last year investors whose federal marginal income tax bracket exceeded 15 percent saw their long-term Federal tax rate paid on capital gains fall from 20 to 15 percent. The levy on those in lower brackets fell from 10 to five percent. Unless the present law is extended, rates will return to 20 percent and 10 percent levels beginning in 2009.

We cannot predict what action congress might take over the next five years, but we can look to history as a guide. There is little hope that spending by the Federal government will be reigned in. This suggests that rates will be allowed to climb; on the other hand, a large proportion of (voting) households now have a stake in the stock market, which might generate enough political pressure to forestall a return to higher rates.

The accompanying box demonstrates that tax rates have been anything but stable since they were first introduced. We suspect that uncertainty will continue, which will complicate long-term financial planning.

In this environment a passive approach to investing makes eminent sense; it provides an ideal means of minimizing your realized gains regardless of the tax rates that will prevail. By investing in index funds and utilizing a passive asset allocation strategy, trading will be held to a minimum. You will also be able to "swap" investment vehicles within asset classes at year end, enabling you to take full advantage of any realized losses without sacrificing exposure to any asset class (see September 2003 *Investment Guide* "Smart Tax Strategies" for more detail).

Capital Gains Taxes



Notes: Prior to 1922 and for 1988-1990, the rates shown are the highest applicable to ordinary income. For other years the effective rate was lower, either because a portion of long-term gains was excluded from taxable income (the excludable portion was deemed a "tax preference" subject to the alternative minimum tax during the years 1971-1979), because the maximum tax on such gains was "capped" at a rate below that on ordinary income, or both. The minimum holding period to qualify for a long-term gain has varied over the years. Currently it is one year. From 1922 through 1935 it was two years. During 1935-37, and from 1977 to 1985 it was one year. From 1938 through 1942 it was 18 months. From 1943 through 1976 and in 1986 and 1987 it was 6 months. During the years 1935 through 1941, larger reductions from ordinary income tax rates were granted on holding periods greater than the minimum, with the lowest rates (plotted as the dashed curve for those years) on assets held as long as 10 years. Prior to 1987, the maximum effective tax rate on long-term gains applied to relatively few taxpayers with very high incomes — most taxpayers faced a lower rate. Since 1987, the maximum rate on long-term gains has applied to a much larger proportion of taxpayers. The current top rate is generally 15 percent for taxpayers whose regular tax bracket exceeds 15 percent.

QUARTERLY REVIEW OF INVESTMENT POLICY

Money-Market Funds

Cash-equivalent assets continued to provide minuscule returns as interest rates remained low throughout the first quarter. However, most investors cannot afford to forego cash-equivalent assets. Liquidity is extremely important in order to meet unanticipated expenditures. Money-market funds remain the optimal means of providing exposure to this asset class. 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-April taxable money market funds were paying an annualized yield of only 0.51 % on average.

Intermediate-Term Bonds

Interest rates generally fell throughout the quarter until mid-March, when macroeconomic indicators began signaling stronger growth. On April 9 a bombshell employment report for March revealed 308,000 new jobs were created, far exceeding Wall Street's expectations. Rates

have reversed course dramatically, as the markets now appear convinced that any ambiguity regarding economic growth has been erased.

In the face of rising rates it might be tempting to forego additional commitments to, or even to sell bonds, since bond prices and interest rates are inversely related. However, we do not recommend alterations from our recommended allocations on page 27. The recent spike in rates merely confirms our contention that markets respond virtually instantaneously to new information.

Since all information is reflected in current security prices, future changes in interest rates will be driven by news, which is unknown by definition. In the case of interest rates, expectations regarding interest rates are enormously important. The recent employment report, suggesting further growth and possible price inflation, was largely unexpected. By selling bonds now one would be simply placing a bet that subsequent unanticipated news will reveal price inflation even higher than that currently anticipated by the bond market.

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 fixed-income mutual funds on page 33 will provide a suitable means of 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 simply 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) an approach designed to provide 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 a registered investment advisor.

Interest Rates

	April 16	Month Ago	Year Ago
U.S. Government Obligations			
3-month Treasury Bill	0.93%	0.93%	1.15%
6-month Treasury Bill	1.07	1.00	1.16
2-year Treasury Note	1.98	1.51	1.68
5-year Treasury Note	3.36	2.73	2.93
10-year Treasury Bond	4.34	3.77	3.96
3-year Treasury Bond	5.17	4.71	4.89
Inflation Spread*	2.50		

* The difference between the nominal yield on 10-year U.S. Treasury notes and the real (inflation-adjusted) rate on 10-year Treasury Inflation-protected securities provides a measure of anticipated annual price inflation.

These funds are available through our Professional Asset Management (PAM) program.

Income Equities

Over the past several quarters Real Estate Investment Trusts (REITs) have been the overall stellar performers among our recommended asset classes (see accompanying table of asset class returns), and during the first quarter they provided the strongest returns by far. However, as the accompanying chart indicates, REITs took a big hit in early April. The cause of this drop was not readily apparent to us; the spike in interest rates might have played a roll, though historically REITs have not been as interest-rate sensitive as bonds, despite their generous yield. In any event, the sudden drop in REIT prices, while significant, does not suggest that investors should alter their strategies. While over the very long term those asset classes that bear the most risk can be expected to provide the highest returns, over shorter time spans the "winners" among these various asset classes will alternate, and recent winners inevitably "revert to the mean" as part of this process.

Our investment vehicle of choice is the Vanguard REIT Index fund (symbol VGSIX). At the end of March the fund was yielding 4.69 percent.

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. However, due to its significant holdings of common stocks of public utilities and bonds, its share price is strongly correlated to interest rates; and indeed the fund's share price took a steep decline in early April amidst fears of higher interest rates. Nevertheless the fund is currently yielding 7.3 percent on an annual basis and pays dividends monthly, which many investors find convenient. The fund is able to maintain its 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

The first quarter brought considerable volatility to the stock market. News regarding the war, the economy, oil prices, and presidential politics all contributed. In the end, our recommended funds managed small gains. Among large-cap value stocks the Vanguard Value Index and the hypothetical high-yield Dow model provided total returns of 2.12 percent and 2.34 percent, respectively; the Lipper Large Cap Value Index, a composite measure of large-cap value mutual funds, returned 2.81 percent. The Vanguard Small Cap Value Index managed a more generous 7.14 percent while the Vanguard Growth Index and the Vanguard European Stock Index provided 1.49 percent and 0.82 percent, respectively.

The major indexes behaved similarly. The S&P 500 Index rose 1.69 percent, while the Dow Jones Industrial Average fell 0.31. The NASDAQ fell 0.46 percent.

Gold-Related Investments

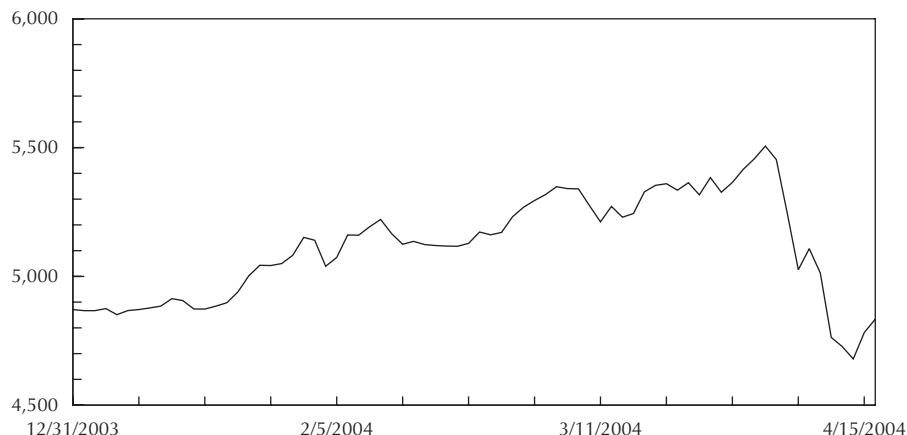
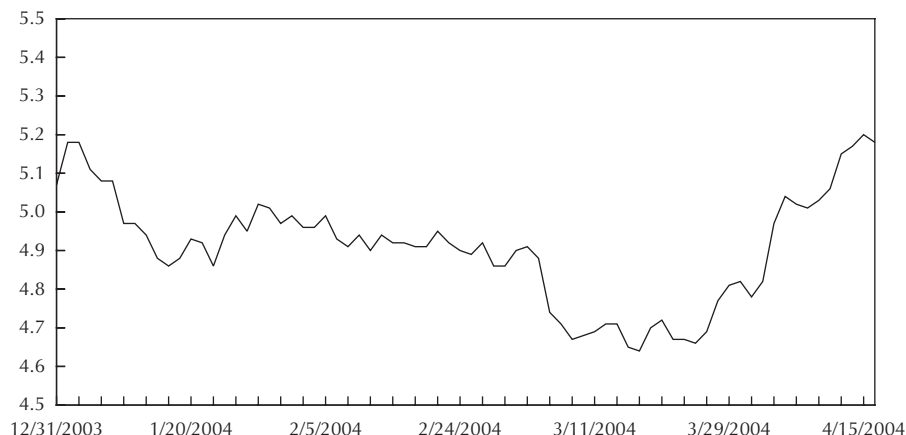
The gold price began the quarter at \$416.25 and closed the quarter at \$423.70 but had faded to \$408 by mid-April.

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.

NAREIT Equity Index

30-Year Treasury Bond Yield
(Adjusted Close)

Gold is an extremely volatile asset class. For example, between January 1968 and December 2003, gold, as measured by the end of month London P.M. fix, provided a total annual return of 7.1 percent. During the same period Treasury bills provided exactly the same return. But gold was far riskier, its standard deviation, which measures volatility, a form of risk, was *over ten times* that of Treasury bills.

So why hold gold at all? Because gold

moves quite independently of other asset classes, so despite the extremely volatile nature of its price changes, it can actually add stability to a properly constructed portfolio. We recently examined the results of a passively managed portfolio composed of large-cap stocks (as measured by the S&P 500), large-cap value stocks, and small-cap value stocks, (size defined by market cap, and value determined by book-to-price measures),

in equal amounts rebalanced annually for the same 36 years 1968-2003. We considered two additional portfolios; one with the same mix but with 10 percent gold bullion (with the monthly returns based on the end-of-month London P.M. fix), and another with 10 percent in six month Treasury Bills. The addition of 10 percent gold reduced the total portfolio return by 0.07 percent, but reduced the risk, as measured by standard deviation, by 2.31 percent. The addition of 10 percent Treasury bills reduced the total return by 0.49 percent but reduced the risk (standard deviation) by only 1.82 percent.

Thus even though gold, in absolute terms, is far more volatile than Treasury bills, it has the potential to reduce the magnitude of the swings in your overall portfolio. Because of gold's inherent volatility, our allocations are limited to those shown in the table.

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.

We are sometimes asked why our recommended conservative portfolio has no allocation to gold related assets. The reason is that gold is a form of portfolio insurance; it is designed to protect the stability of your portfolio's value over time, especially in light of unanticipated needs for cash that can occur along the way. As one grows older and investment horizon grows shorter, the need for this insurance diminishes. We save so that, ultimately, we can spend; so investors should be converting their more volatile holdings to cash and short-term bonds.

Total Returns (%)

	—2001—		—2002—				—2003—				2004	Total Return Entire Period 3Q 2001- 1Q 2004
	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	
Vanguard Short-Term Corporate	3.34	0.17	0.26	1.25	2.27	1.34	1.39	1.89	0.39	0.46	1.53	15.23
Vanguard REIT Index	-2.56	4.72	8.08	4.79	-8.48	0.10	1.01	12.27	9.47	9.27	11.75	60.49
Vanguard Value Index	-16.26	7.89	1.32	-10.69	-20.45	9.88	-5.57	20.27	2.24	13.93	2.12	-3.50
High-Yield Dow 4/18**	-16.09	9.19	6.92	-6.20	-23.79	26.42	-9.21	18.59	-4.90	12.50	2.34	4.37
Vanguard Small Cap Value Index	-16.63	21.37	10.41	-4.15	-22.50	4.62	-7.98	19.39	7.48	16.19	7.14	27.60
Vanguard Growth Index	-13.26	12.97	-0.87	-16.30	-14.07	7.04	-0.91	11.57	3.24	10.33	1.49	-4.42
Vanguard European Stock Index	-12.09	9.48	0.05	-4.05	-22.85	10.77	-9.25	22.30	3.89	20.30	0.82	10.44
Gold (London PM Fix)	8.31	-5.66	9.01	5.67	1.63	7.26	-3.56	3.33	12.14	7.28	1.79	56.58

The highest returns provided in each period are in **Bold Face Type**. * HYD is a hypothetical model based on back tested results. See p. 30 for a full explanation.

A READER INQUIRES

In our December 2003 issue we published "Investing and the Science of Economics." A reader responded with two questions that go to the heart of the notion of passive investing:

The discussion of Markowitz and Sharpe left me confused. If return depends on riskiness, then if you diversify to reduce risk, doesn't that reduce return? What did you mean when you said Markowitz could construct an "optimal" portfolio?

The answer to the first question is that while an investor can increase his expected returns by assuming additional risk, it is not necessarily true that by assuming additional risk one will increase expected returns.

To make this clear it is first important to understand the distinction between different types of risk. *Company-specific risk* is the risk of investing in an individual company. There are random events that could occur—a lawsuit, a fire, the death of a key executive—that would primarily affect only that company. Indeed you could lose your entire investment in a stock if the news were dire enough to result in bankruptcy. *Industry risk* is similar except that it refers to broader economic events that adversely affect an entire industry. Beginning in early 2000, for example, technology firms suffered declines far greater than the rest of the stock market. *Both types of risk are diversifiable*; by owning hundreds of stocks among several industries, for every bit of "bad" news affecting a particular stock or industry, there would be an equal chance of offsetting "good" news emerging for another firm or industry in the portfolio. A well-diversified portfolio could be rendered worthless only by an economy-wide collapse.

Now consider how markets work; consider two hypothetical securities of comparable risk, stock A and stock B. If security A had higher expected returns than B, then investors would flock to security A and abandon security B; the price of A would rise accordingly and B would fall until the securities were priced at levels that produced equivalent expected returns. The market maintains an equilibrium whereby all securities within a given asset class have the same expected returns. In this environment, an investor purchasing just one stock instead of the entire asset class would be unnecessarily

Test Your Investment Knowledge

The total market capitalization of the 30 constituent stocks that comprise the Dow Jones Industrial Average constitute approximately what percentage of the entire market capitalization of all 6,645 stocks traded on the NYSE, AMEX, and NASDAQ and OTC combined?

- A. 5.0 % B. 18.0% C. 0.60% D. 3.0%

Answer: B. As of mid-April the Dow 30 stocks had a combined market value of roughly \$3.741 trillion dollars, or roughly 18 percent of the combined market value of all domestically traded stocks.

assuming individual and industry specific risk. This would be irrational since he could purchase the entire asset class and garner the same expected return while dispensing with all of the risk attributable to that particular firm as well as the risk associated with its industry. Thus by choosing an individual security over an entire asset class, one would be assuming risk that is uncompensated by additional expected return.

Modern portfolio theory posits that an investor cannot, however, dispose of the (non-diversifiable) risk associated with the entire stock market. This *market risk* is the risk common to all stocks, such as business cycle fluctuations. You can purchase an S&P 500 Index fund, thereby eliminating all company and industry specific risks associated with the firms held by the fund. However, you would still be subject to the fortunes of the broader stock market. So, once you have assembled an adequately diversified portfolio, you can increase your expected returns only by increasing the level of your investment; e.g. by assuming greater market risk.

Subsequent research identified factors other than market risk that explained the returns to financial assets. Stocks could be categorized into asset classes defined by size and style (growth vs. value). Each of these asset classes (e.g. small-cap value stocks) represent potential portfolios of stocks that can provide investors with the opportunity to assume additional and unique forms of non-diversifiable (com-

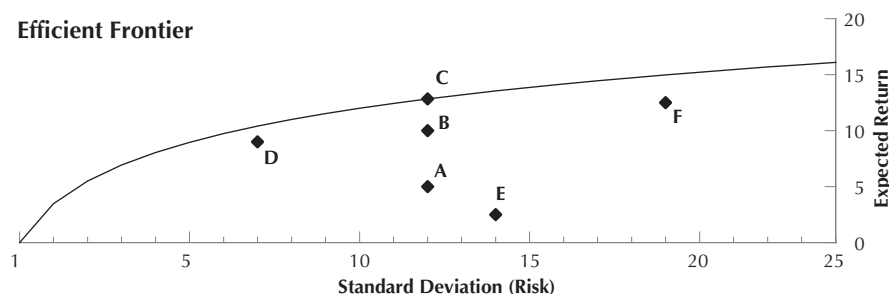
pensated) risk; these were explained at length in the December article.

The answer to the second question builds on the point made previously: it is possible to assume risk without being compensated with additional expected return. Ideally, then, one can build a portfolio that is efficient, in the sense that one is deriving the maximum amount of expected return per unit of risk, by fully "diversifying away" all such uncompensated risk. For a given set of assets (e.g. cash, bonds, small-cap stocks), an infinite number of possible portfolios (points on the chart below) can be created depending on the percentage allocation assigned to each asset. Points A through F represent the total return and volatility (a form of risk measured by standard deviation) that could be expected from six such hypothetical portfolios based on the historical returns of each asset.

In theory, investors should be striving for any portfolio on the frontier, such as point C. Point C represents a portfolio that "dominates" portfolio's A and B, since C has a greater expected return for the same level of risk. Similarly, points D, E, and F are sub-optimal, since they are "inside" the efficient frontier and portfolios directly "above" them on the frontier have higher expected returns for the same level of risk assumed.

Once "on" the frontier, an investor can achieve a higher expected return only by accepting greater volatility. Such portfolios are therefore said to be "efficient."

Efficient Frontier



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 **Citigroup** was not eligible for purchase 18 months earlier (in November 2002), and **Verizon** was not in the Dow. Investors following the model should find that the indicated purchases of **Verizon** and **Citigroup** and sales of **Eastman Kodak** are sufficiently large to warrant trading. In larger accounts, rebalancing positions in **JP Morgan Chase**, **SBC** and **Dupont** may be warranted as the model calls for adding to positions that have lagged the entire portfolio and selling positions that have done better. 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 adjustments from time to

As of April 15, 2004

	Rank	Yield	Price	—Percent of Portfolio*—		
				Status	Value	No. Shares ¹
SBC Comm.	1	5.13%	24.36	Holding**	24.23	27.76
Altria Group	2	4.89%	55.59	*		
General Motors	3	4.41%	45.39	*		
Verizon	4	4.16%	37.06	Buying	1.52	1.15
JP Morgan Chase	5	3.51%	38.77	Holding**	29.68	21.37
CitiGroup	6	3.21%	49.92	Buying	3.12	1.74
Merck	7	3.15%	46.98	Holding	3.11	1.85
DuPont	8	3.11%	45.07	Holding**	8.59	5.32
General Electric	9	2.60%	30.76			
Exxon Mobil	10	2.29%	43.68			
AT&T	NA	5.09%	18.64	Holding	18.54	27.75
Eastman Kodak	NA	2.00%	24.95	Selling	<u>11.18</u>	<u>12.51</u>
					100.0	100.0

Change in Portfolio Value²

	1 mo.	1 yr.	5 yrs.	10 yrs.	15 yrs.	From 12/63	Std. Dev.
HYD Strategy	-1.42%	15.92%	2.25%	12.80%	14.96%	15.40%	19.36
Dow	2.75%	26.04%	1.65%	12.95%	12.93%	10.58%	16.95

* 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.

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, Verizon, J.P. Morgan Chase, and Citigroup—account for roughly 58 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

	Ticker Symbol	Market Prices			12-Month		Latest Dividend			Indicated	
		4/15/04	3/15/04	4/15/03	High	Low	Amount	Record Date	Paid	Annual Dividend	Yieldt
★ SBC Comm.	SBC	\$24.36	24.18	21.25	27.73	19.65	0.313	4/10/04	5/03/04	1.250	5.13
Altria Group	MO	\$55.59	53.77	32.45	58.96	29.87	0.680	3/15/04	4/12/04	2.720	4.89
General Motors	GM	\$45.39	44.97	35.17	55.55	32.84	0.500	2/13/04	3/10/04	2.000	4.41
★ Verizon	VZ	\$37.06	37.30	34.54	41.35	31.10	0.385	4/09/04	5/03/04	1.540	4.16
★ J. P. Morgan Chase	JPM	\$38.77	40.93	26.87	43.84	25.88	0.340	4/06/04	4/30/04	1.360	3.51
★ Citigroup	C	\$49.92	49.12	39.25	52.88 H	37.50	0.400	2/02/04	2/27/04	1.600	3.21
☆ Merck	MRK	\$46.98	44.85	56.93	63.50	40.57	0.370	3/05/04	4/01/04	1.480	3.15
☆ DuPont	DD	\$45.07	41.01	40.81	46.25	38.60	0.350	2/13/04	3/13/04	1.400	3.11
General Electric	GE	\$30.76	30.30	28.30	34.57	26.90	0.200	3/01/04	4/26/04	0.800	2.60
Exxon Mobil	XOM	\$43.68	41.78	35.05	43.83 H	34.26	0.250	2/11/04	3/10/04	1.000	2.29
Honeywell Intl.	HON	\$34.50	32.59	22.39	37.65	21.45	0.188	2/20/04	3/10/04	0.750	2.17
Coca-Cola	KO	\$51.20	47.71	42.53	52.78	39.00	0.250	3/15/04	4/01/04	1.000	1.95
Procter & Gamble	PG	\$106.12	102.52	89.88	107.39 H	86.51	0.500	4/23/04	5/14/04	2.000	1.88
Caterpillar	CAT	\$80.80	73.98	52.70	85.70	50.19	0.370	4/26/04	5/20/04	1.480	1.83
Pfizer	PFE	\$37.34	34.95	32.21	38.89	29.43	0.170	2/11/04	5/05/04	0.680	1.82
Alcoa	AA	\$33.00	34.11	22.59	39.44	21.28	0.150	2/06/04	2/25/04	0.600	1.82
Johnson & Johnson	JNJ	\$54.52	50.57	55.98	57.99	48.05	0.240	2/17/04	3/09/04	0.960	1.76
3M Company (s)	MMM	\$82.85	74.87	66.82	86.20	60.26	0.330	2/20/04	3/12/04	1.440	1.74
Boeing	BA	\$41.53	39.78	27.29	45.10	26.03	0.170	2/13/04	3/05/04	0.680	1.64
United Tech.	UTX	\$88.14	87.90	63.71	97.84	59.30	0.350	5/21/04	6/10/04	1.400	1.59
McDonald's	MCD	\$26.93	28.45	15.85	29.98	15.45	0.400	11/14/03	12/01/03	0.400	1.49
Hewlett-Packard	HPQ	\$21.89	21.71	15.57	26.28	15.20	0.080	3/17/04	4/07/04	0.320	1.46
Wal-Mart Stores	WMT	\$57.79	57.90	55.29	61.31	50.50	0.130	5/21/04	6/07/04	0.520	0.90
Walt Disney	DIS	\$24.70	25.33	18.31	28.41	17.45	0.210	12/12/03	1/06/04	0.210	0.85
American Express	AXP	\$49.75	50.95	36.90	53.98	34.60	0.100	4/02/04	5/10/04	0.400	0.80
Home Depot, Inc.	HD	\$35.86	35.41	27.16	37.89	25.75	0.070	3/11/04	3/22/04	0.280	0.78
IBM	IBM	\$93.97	91.82	82.79	100.43	78.16	0.160	2/10/04	3/10/04	0.640	0.68
Microsoft Corp. (s)	MSFT	\$25.22	25.16	24.61	30.00	23.60 L	0.160	10/17/03	11/07/03	0.160	0.63
Intel Corp.	INTC	\$26.66	27.10	17.13	34.60	16.65	0.040	5/07/04	6/01/04	0.160	0.60
AIG	AIG	\$74.68	70.06	53.98	77.36	53.82	0.650	6/04/04	6/18/04	0.260	0.35
☆ AT&T (r)	T	\$18.64	18.87	13.73	23.18	13.45	0.240	3/31/04	5/03/04	0.950	5.09
☆ Eastman Kodak	EK	\$24.95	25.72	31.67	32.46	20.39	0.250	11/03/03	12/12/03	0.500	2.00

† Based on indicated dividends and market price as of 4/15/04. 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

	4/15/04	Mo. Earlier	Yr. Earlier
Gold, London p.m. fixing	398.25	398.10	325.45
Silver, London Spot Price	6.86	7.11	4.52
Copper, COMEX Spot Price	1.29	1.35	0.73
Crude Oil, W. Texas Int. Spot	37.57	37.44	29.29
Dow Jones Spot Index	190.42	189.48	145.89
Dow Jones-AIG Futures Index	148.49	148.29	113.47
CRB-Bridge Futures Index	276.87	278.36	231.73

Interest Rates (%)

U.S. Treasury bills -	91 day	0.93	0.95	1.17
	182 day	1.11	1.00	1.18
	52 week	1.41	1.11	1.24
U.S. Treasury bonds -	15 year	4.96	4.34	4.60
Corporates:				
High Quality -	10+ year	5.84	5.29	5.84
Medium Quality -	10+ year	6.25	5.67	6.44
Federal Reserve Discount Rate		2.00	2.00	2.25
New York Prime Rate		4.00	4.00	4.25
Euro Rates	3 month	2.05	2.07	2.52
Government bonds -	10 year	3.88	4.03	4.17
Swiss Rates -	3 month	0.27	0.26	0.30
Government bonds -	10 year	2.62	2.46	2.53

Exchange Rates

British Pound	\$1.785100	\$1.818800	1.576600
Canadian Dollar	\$0.742500	\$0.751900	0.690800
Euro	\$1.192900	\$1.235100	1.084200
Japanese Yen	\$0.009217	\$0.009144	0.008313
South African Rand	\$0.152400	\$0.149300	0.130000
Swiss Franc	\$0.767900	\$0.787800	0.722220

Securities Markets

	4/15/04	Mo. Earlier	Yr. Earlier
S & P 500 Stock Composite	1,128.84	1,104.49	890.81
Dow Jones Industrial Average	10,397.46	10,102.89	8,402.36
Dow Jones Transportation Average	2,913.94	2,790.44	2,316.62
Dow Jones Utilities Average	271.98	274.68	216.82
Dow Jones Bond Average	175.54	180.69	165.42
Nasdaq Composite	2,002.17	1,939.20	1,391.01
Financial Times Gold Mines Index	1,588.20	1,592.70	1,104.49
FT African Gold Mines	2,195.74	2,335.57	1,826.61
FT Australasian Gold Mines	3,193.67	3,077.85	1,715.65
FT North American Gold Mines	1,314.78	1,296.22	873.55

Coin Prices

	4/15/04	Mo. Earlier	Yr. Earlier	Premium
American Eagle (1.00)	\$430.25	\$410.35	329.75	8.04
Austrian 100-Corona (0.9803)	\$425.35	\$390.83	314.13	8.95
British Sovereign (0.2354)	\$102.55	\$97.95	79.25	9.39
Canadian Maple Leaf (1.00)	\$430.50	\$410.60	330.00	8.10
Mexican 50-Peso (1.2057)	\$505.40	\$482.10	387.70	5.25
Mexican Ounce (1.00)	\$419.10	\$399.80	321.40	5.24
S. African Krugerrand (1.00)	\$425.35	\$405.85	326.75	6.80
U.S. Double Eagle-\$20 (0.9675)				
St. Gaudens (MS-60)	\$480.00	\$480.00	440.00	24.58
Liberty (Type I-AU)	\$675.00	\$675.00	675.00	75.19
Liberty (Type II-AU)	\$492.50	\$505.00	440.00	27.82
Liberty (Type III-AU)	\$455.00	\$455.00	395.00	18.09
U.S. Silver Coins (\$1,000 face value, Circulated, year earlier uncirculated)				
90% Silver (715 oz.)	\$5,530.00	\$4,870.00	4,550.00	12.74
40% Silver (292 oz.)	\$2,180.00	\$1,955.00	1,587.50	8.83
Silver Dollars	\$6,675.00	\$6,500.00	6,112.50	25.78

Note: Premium reflects percentage difference between coin price and value of metal in a coin, with gold at \$398.25 per ounce and silver at \$6.86 per ounce. The weight in troy ounces of the precious metal in coins is indicated in parentheses.

Recommended Mutual Funds

	Ticker Symbol	4/15/04	Month Earlier	Year Earlier	— 52-Week — High Low	Distributions Latest 12 Months Income Capital Gains	Yield (%)
Short-Term Bond Funds							
★ iShares Lehman 1-3 Yr Treasury	SHY	\$82.22	\$82.92	82.22	83.08 81.82	1.3251	1.61
★ USAA Short Term Bond	USSBX	\$9.06	\$9.14	9.04	9.23 9.02	0.3203	3.54
★ Vanguard Short-term Corporate	VFSTX	\$10.76	\$10.88	10.79	10.96 10.72	0.4115	3.82
Income Equity Funds							
★ DNP Select Income ^{1,2}	DNP	\$10.57	\$11.11	10.05	11.42 9.90	0.7800	7.38
★ Vanguard REIT Index	VGSIX	\$14.75	\$16.40	12.27	16.98 12.06	0.7900	5.36
Large Cap. Value Equity Funds							
★ iShares S&P 500 Value Index ³	IVE	\$56.66	\$56.09	42.89	58.88 41.71	0.9246	1.63
★ Vanguard Value Index	VIVAX	\$19.12	\$19.26	14.61	19.91 14.15	0.4020	2.10
Small Cap. Value Equity Funds							
★ iShares Sm. Cap. 600 Value Index ³ IJS		\$104.79	\$103.48	69.49	109.15 45.57	0.8487	0.81
★ Vanguard Sm. Cap Value Index	VISVX	\$11.91	\$12.11	8.17	12.48 7.99	0.1980	1.66
Growth Equity Funds							
★ iShares S&P 500 Growth Index ³	IVW	\$56.25	\$54.72	46.25	58.01 45.26	0.6160	1.10
★ Vanguard Growth Index	VIGRX	\$25.50	\$25.15	20.53	26.09 20.10	0.1460	0.57
Foreign Equity Funds							
★ iShares S&P Europe 350 Index ³	IEV	\$64.58	\$63.20	47.43	69.20 45.98	2.5127	3.89
★ T Rowe Price European Stock	PRESX	\$17.41	\$17.55	12.80	18.68 12.38	0.2200	1.26
★ Vanguard European Stock Index	VEURX	\$22.14	\$22.08	16.09	23.57 15.58	0.4600	2.08

Recommended Gold-Mining Companies

	Ticker Symbol	4/15/04	Month Earlier	Year Earlier	— 52-Week — High Low	Distributions Latest 12 Months Frequency	Yield (%)
Anglo American PLC, ADR	AAUK	\$23.74	\$23.22	14.60	26.69 13.46	0.510	2.15
★ AngloGold Ltd., ADR	AU	\$36.77	\$40.40	28.55	49.95 27.70	0.985	2.68
ASA Ltd. ¹	ASA	\$39.46	\$40.07	34.81	48.00 33.75	0.650	1.65
★ Barrick Gold Corp.†	ABX	\$21.77	\$20.87	15.42	24.16 14.76	0.220	1.01
★ Gold Fields Ltd.	GFI	\$12.18	\$11.65	10.73	15.52 9.85	0.192	1.58
★ Newmont Mining	NEM	\$43.05	\$41.99	26.38	50.28 25.95	0.180	0.42
★ Placer Dome†	PDG	\$16.41	\$16.06	9.97	19.23 9.56	0.100	0.61
★ Rio Tinto PLC‡	RTP	\$96.55	\$98.35	78.37	116.33 72.30	2.560	2.65

★ 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.

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