INVESTMENT GUIDE

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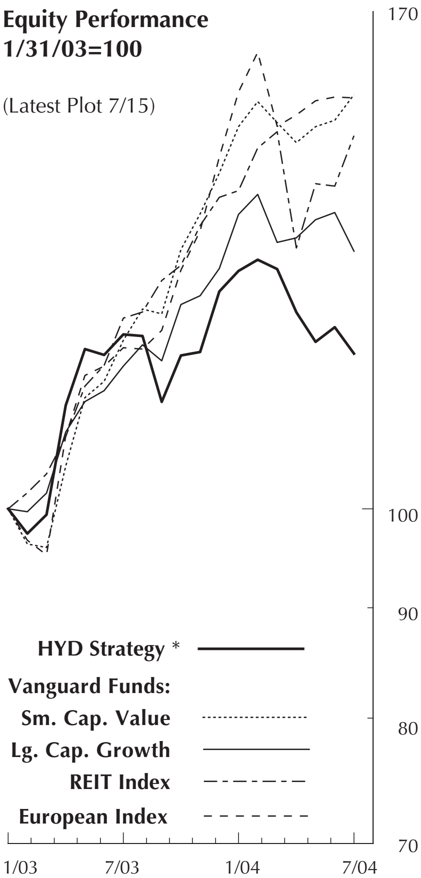
Equity Performance
1/31/03=100

(Latest Plot 7/15)



*** HYD is a hypothetical model based on back-tested results. See p. 54 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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Microsoft Comes of Age

Not long ago, during the late 1990s, tech stocks were all the rage and common stock dividends were regarded by many to be archaic. But sentiment changes quickly; on July 20 Microsoft announced an unprecedented onetime payout of $32 billion to shareholders, or $3 per share, and doubled its regular dividend to $0.32 per share. The company also announced plans to buy back $30 billion of its own stock over the next four years.

Why the change of heart? Many factors may have prompted this decision, but shareholders have eyed the firm's mountain of cash for some time, and we suspect that their voices were amplified by last year's tax change that reduced the tax on qualified dividends to 15 percent. It is also possible that Microsoft accelerated the payout (the stock goes exdividend November 18) through the massive onetime lump sum, rather than further increase its regular dividend, out of concern that a new administration in Washington would push for a repeal of the lower levy on dividends as early as next year. If that is the case other firms could follow suit before year-end, perhaps after the election should a new administration prevail.

Microsoft was added to the Dow in late 1999, along with Intel, Home Depot and SBC. In the October 1999 ***Investment Guide*** we wrote:

> "Some analysts have noted that most of the recent additions to the Dow pay little in the way of dividends (Microsoft has never paid a dividend). The notion is that as older 'smokestack' stocks have been replaced by 'information-based' issues, the dividend yield somehow will become less related to total return. We believe that, 1) the recent lagging of the HYD stocks relative to the Average does not even come close to providing sufficient evidence of this, and 2) *it is most unlikely that there has been a fundamental or lasting change in how the market values common stocks for the long term*."

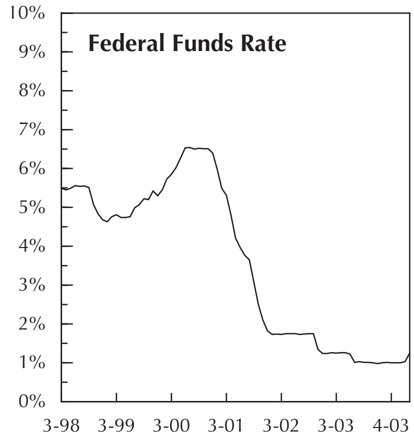
Our commitment to the latter proposition remains firm. Notably, using mid-month prices, as of July 15, the HYD model would have outperformed Microsoft, in total return, by 14.3 percent, since Microsoft became a Dow component. The fact is investors demand a premium for assuming greater risk, and it is risky stocks, as opposed to growth stocks, that have higher than average expected returns. We have no illusions that Microsoft will become a component in our HYD model any time soon. It is certainly difficult to imagine Microsoft becoming a "distressed stock," given what is known today. But many of the stocks that have been in our model were at one time considered "go go" growth stocks, and it would not surprise us if one day Microsoft were to enter our model.

QUARTERLY REVIEW OF INVESTMENT POLICY

The Economy

During the second quarter, several economic indicators came in below levels that had been forecast by Wall Street, and the nation's Gross Domestic Product (GDP) in the first quarter was revised downward to 3.9 percent. Nevertheless the economic indicators of our parent, the American Institute for Economic Research (AIER) point to a far greater likelihood of continued economic expansion versus contraction. As if mid-July, 11 out of 11 leading indicators with a discernable trend were pointing to continued expansion. Five hit new highs. The cyclical score, a purely mathematical analysis of all 12 leading indicators, was a robust 88, after surging to 86 from 79 in June (a score below 50 would indicate that contraction is more likely than expansion, a score above 50 points to continued expansion). Of the six coincident indicators, 100 percent (five out of five) of those with a clear trend were pointing to expansion, up from 83 percent in June. The percentage of lagging indicators pointing to expansion was up from 25 percent in June to 33 percent in July. On June 30 the Federal Reserve Board raised the target for the Federal funds rate by 0.25 percent to 1.25 percent, a move that was widely anticipated. In the face of accelerating growth the Fed had been sending signals for weeks that rates would be coming off of their historic lows and that monetary tightening would begin. The change marked the first increase in four year.

Asset classes of all stripes had a difficult quarter, as indicated in the accompanying table. Foreign equities were the strongest performing asset classes, but only managed a 2.25 percent total return. REITs, gold, and the high-yield Dow strategy all fell by more than 5 percent.



Money-Market Funds

Cash-equivalent assets are again providing negative returns in real terms, but investors should not ignore this asset class. While it may be tempting to "reach for yield" by moving out of money-market funds and into a higher-yielding short-term bond fund, this temptation should be avoided. Short-term interest rates are unpredictable, but during periods of rising rates money-market funds outperform short-term bonds. This "downside protection" is extremely valuable, not only for conservative investors, but for anyone, since liquidity is extremely important in order to meet unanticipated expenditures. Despite a current average yield of only 0.59 percent, money-market funds remain the optimal means of providing exposure to this asset class.

Taxable 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. The shares of money market funds are issued and redeemed at a Net Asset Value (NAV) of $1.00 per share. These funds have certain built-in safeguards. Under the Investment Company Act of 1940 a fund's maturity cannot exceed 90 days, nor can it invest in any security with a maturity of more than 13 months. Diversification rules prevent money-market funds from investing more than five percent of their assets in any single non-U.S. government issue. These funds should not be confused with money-market deposit accounts offered by banks, which are essentially interest-bearing checking accounts, insured by the Federal Deposit Insurance Corporation (FDIC) and subject to minimum-balance requirements and limited check-writing privileges.

Most brokers offer their customers a money-market fund for a "sweep" account. Dividends, interest, and deposits are used to purchase additional shares in this fund, which may be redeemed to pay for purchases and withdrawals from the account. Similarly, mutual funds in "families," which have the same sponsors and management companies, such as Vanguard, will include several money-market funds among their offerings. These typically include municipal money-market funds, which earn income that is exempt from Federal, and sometimes state and local income taxes.

Short/Intermediate-Term Bonds

Bonds prices took a hit during the quarter, as interest rates reversed course. Interest rates and bonds move in opposite directions and the Vanguard Short-Term Investment Grade Fund had its first negative quarter in 3 years.

With interest rates in the news, investors might feel pressured to "do something" in anticipation of the next move in rates. This would be unwise. The market's best guess regarding the Fed's next move, future price inflation, or any other variable that could affect interest rates, is already reflected in current rates. Future changes in interest rates, and therefore in bond prices, will be therefore be driven by news, which is unknown by definition.

The bond allocations in the accompanying Recommended Portfolio Allocation 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.

RECOMMENDED PORTFOLIO ALLOCATION PERCENTAGES

	Conservative	*Moderate*	*Aggressive*
Money-Market Funds	30	20	10
Short/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.

For many investors, any of the fixed-income mutual funds on page 56 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 June 2004 ***INVESTMENT GUIDE*** for a full discussion) 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. DFA's expenses are among the lowest in the mutual-fund industry, so even when these are combined with the fee assessed by a low-cost advisor the total cost of owning these funds is reasonable. These funds are available through our Professional Asset Management (PAM) program.

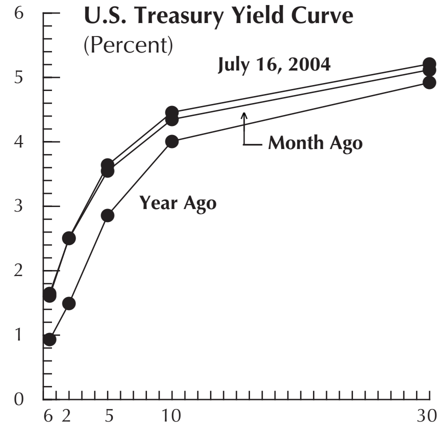
Income Equities

During the second quarter REITs' total return tumbled nearly six percent, ending a long "winning streak." Commercial real estate values have been strong over the past three years, but the market's enthusiasm for REITs apparently waned as interest rates moved higher. Historically REIT price changes have not been closely tied to interest rates. Indeed we include these precisely because their risk/return profile is quite different from both bonds and equities.

Investors should not alter their target REIT allocation in response to this reversal. 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. REITs were the winners over several recent quarters, but during the second quarter they simply demonstrated that at some point winners will inevitably "revert to the mean."

Our investment vehicle of choice is the Vanguard REIT Index fund (symbol VGSIX). As of July 15 the fund was yielding 5.2 percent.

The Duff and Phelps Select Income Fund (DNP) had a volatile second quarter, as its share price gyrated with interest rate expectations. The fund's price began the quarter at $11.14 but had tumbled to $9.69 by May 7, before rebounding. As of July 15 the price stood at $10.90 with a yield of 7.2 percent. The 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. 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. The fund is trading at a relatively high premium (its market price divided by its net asset value) of roughly 39 percent; since 1990 the premium has averaged 10.7 percent. Nevertheless, the fund's yield and monthly payout provide a consistent cash flow, and we continue to recommend it for investors if held as a small portion of their total portfolio. It would be reasonable for investors to divide their income equity allocation (see the accompanying Recommended Portfolio Allocation table) equally between the Vanguard REIT fund and DNP.



Common Stocks

Relative to recent quarters, the stock market was relatively tame during the past three months. Among large-cap value stocks the Vanguard Value Index and the hypothetical high-yield Dow model provided total returns of 1.56 percent and -6.19 percent, respectively; the Lipper Large Cap Value Index, a composite measure of large-cap value mutual funds, returned -0.47 percent. The Vanguard Small-Cap Value Index managed 0.89 percent while the Vanguard Growth Index and the Vanguard European Stock Index provided 1.51 percent and 2.25 percent, respectively.

The major indexes showed little change. The S&P 500 Index rose 1.30 percent, while the Dow Jones Industrial Average advanced 1.24 percent. The NASDAQ rose 2.70 percent.

The disparity between the HYD model's performance and that of the other value indexes (the S&P/Barra Value Index and the Lipper Large Cap Value Index) is not alarming, considering the current

Total Returns (%)

	2001	*—2002—*				*—2003—*				*—2004—*		*Total Return Entire Period 4Q 2001-*
	4Q	*1Q*	*2Q*	*3Q*	*4Q*	*1Q*	*2Q*	*3Q*	*4Q*	*1Q*	*2Q*	*2Q 2004*
Vanguard Short-Term Inv Grade	0.17	0.26	1.25	**2.27**	1.34	**1.39**	1.89	0.39	0.46	1.53	-1.30	10.06
Vanguard REIT Index	4.72	8.08	4.79	-8.48	0.10	1.01	12.27	9.47	9.27	**11.75**	-5.95	**54.90**
Vanguard Value Index	7.89	1.32	-10.69	-20.45	9.88	-5.57	20.27	2.24	13.93	2.12	1.56	17.04
High-Yield Dow 4/18**	9.19	6.92	-6.20	-23.79	**26.42**	-9.21	18.59	-4.90	12.50	2.34	-6.19	16.67
Vanguard Small-Cap Value Index	**21.37**	**10.41**	-4.15	-22.50	4.62	-7.98	19.39	7.48	16.19	7.14	0.89	54.43
Vanguard Growth Index	12.97	-0.87	-16.30	-14.07	7.04	-0.91	11.57	3.24	10.33	1.49	1.51	11.85
Vanguard European Stock Index	9.48	0.05	-4.05	-22.85	10.77	-9.25	**22.30**	3.89	**20.30**	0.82	**2.25**	28.45
Gold (London PM Fix)	-5.66	9.01	**5.67**	1.63	7.26	-3.56	3.33	**12.14**	7.28	1.79	-6.58	35.04

The highest returns provided in each period are in **Bold Face Type**. * HYD is a hypothetical model based on back tested results. See p. 54 for a full explanation.

composition of the portfolio. The model currently holds eight stocks; historically this has provided adequate diversification among industries, since the 30 stocks in the Dow are specifically constructed to represent all industries, and the stocks in the model are selected from among these stocks. However, of these eight stocks the model currently holds, three are telecommunications stocks and two bank stocks. Thus, it is not surprising that the model might experience much larger short-term swings versus the much broader indexes. We regard this as an anomalous situation and that over time we expect that the model will revert to a broader representation of industries. In the meantime, we would expect there will be equal probability of "upside swings" that could dwarf those of the indexes, comparable in proportion to this "downside swing" experienced this quarter.

Gold-Related Investments

The gold price began the quarter at $423.70 per ounce and closed the quarter at $395.80 before modestly rebounding to $403.15 by mid-July.

We recommend gold because it 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. 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.

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 one's investment horizon grows shorter, the need for this insurance presumably diminishes. This is why we do not recommend gold in our conservative portfolio allocation plan. This is only a guide, however; gold may be entirely acceptable for those who consider themselves conservative investors, but we strongly recommend that in that case gold be limited to no more than five percent of a portfolio's value.

SPONTANEOUS ORDER AND INVESTMENT RULES*

Investment research may not be "rocket science," but it has become increasingly complex as analysts borrowing from both the hard and soft sciences employ a variety of techniques in an attempt to make sense of financial markets. At one end of the research continuum are quantitative analysts who have applied concepts such as Brownian Motion and the heat exchange equation to model option prices, while at the other are behavioral- finance researchers who utilize laboratory experiments derived from clinical psychology to explain financial market phenomena.

Studies have shown that the typical individual investor is a relatively poor intuitive statistician. However, even if all investors had graduate level training in statistics, the conclusions drawn from the research still depend on the quality of the numbers being crunched. The phrase "garbage in, garbage out" applied to much of the data and investment analyses disseminated to the public at the peak of the stock market bubble. On the heals of last years financial reporting scandals have come widespread charges of after hours trading in the mutual fund industry. These latest revelations of misconduct are particularly damaging given the growth in the industry and the perception that mutual funds are a relatively safe haven for unsophisticated individual investors unable to digest the mountains of raw data and complex research at the disposal of professional investment experts.

If individual investors are unable to decipher much of the analysis that passes as investment research, and cannot trust chief financial officers, auditors, financial analysts or mutual fund managers, how do they make knowledgeable investment decisions? The answer is that most individual investors make decisions the same way they always have: by relying on codified investment rules.

The Price System

Perhaps the most important contribution of Nobel economist Friedrich A. Hayek (1889-1992) was his insight into the use of knowledge in human decision making. He believed that knowledge was so widely dispersed across the population that no centralized decision maker or expert could hope to acquire enough of it to bring about an allocation of resources more efficient than the one achieved by the price system.

Hayek's challenge to central planning came at a time in the 1930s when many in and out of government were beginning to question the role of markets. For Classical economists, the price system was a method for overcoming a shortage of altruism. By virtue of the invisible hand, market participants who pursued self interest were simultaneously maximizing social welfare. Gordon Gekko's assertion in the movie *Wallstreet* that "greed is good" essentially echoes this position.

In contrast, Hayek did not see the price system so much as a way to resolve a shortage of altruism but as a means to overcome deficits in the knowledge of market participants. His ideas on knowledge and price discovery have important implications for how relatively unsophisticated individual investors are able to utilize information embodied in sophisticated market research.

For example, financial research has shown that the futures market for orange juice concentrate does a better job forecasting weather patterns in Florida than do meteorologists. This is because the market aggregates all available knowledge, including knowledge possessed by experts. According to this view, the controversial proposal for a futures market in terrorism makes good sense if the fundamental problem in fighting terrorism is a shortage of information. Hayek believed that the knowledge provided by the price system was morally neutral. Terrorism experts in the Pentagon, Department of State, or Central Intelligence Agency may be competent analysts, but they are often captured by organizational politics, and their knowledge, like expert meteorologists', is incomplete compared

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* This article is by Michael Devaney, Ph.D., CFA, is a professor of finance at Southeast Missouri State University in Cape Girardeau. He acknowledges The American Institute for Economic Research in Great Barrington, Mass., and its summer conference "Hayek, Dewey and Embodied Cognition: Experience, Beliefs and Rules." Reprinted with permission, InvestmentNews, June 14, 2004. Copyright, Crain Communications, Inc.

to the aggregated knowledge of the market.

In few endeavors do so many "experts" provide such an array of conflicting views as in the area of securities investment. Hayek expressed little faith in non-market institutions and harbored a distrust of experts. It is not so much that he believed them to be dishonest, but he thought that a system as complicated as international equity markets could be fully understood only through an even more complex system. Hayek believed that much of the most valuable knowledge utilized by economic actors was "tacit knowledge" that could not be easily communicated to others. One can convey a recipe for spaghetti sauce written on a card, but it is difficult to communicate to another the information required to ride a bicycle.

Spontaneous Order

However, this does not mean that tacit knowledge is lost to those without specialized expertise the relevant field. Hayek argued that tacit knowledge can be aggregated into codified rules of behavior that constitute what he called a "spontaneous order". For example, one way of dealing with the mass of conflicting investment research generated daily is to simply ignore it. Rather than market timing and liquidity trading—which attempt to interpret conflicting information that drives short run asset prices—many individual investors employ a rule based on a long-term buy and hold.

This rule incorporates sophisticated capital market research which has shown that much of the positive return generated in the stock market over the last 75 years occurred during a relatively small percentage of total trading days. Hence the greatest danger of market timing is being out of the market when positive trading days occur. Employing an investment strategy that incrementally acquires stock over both bull and bear market cycles—rather than attempting to time market turns—should result in an average acquisition cost that largely mitigates market bubbles.

Similarly, the 60%-40% stock-to-bond split that has become conventional wisdom in portfolio allocation for individual investors is derived from research on the long-term equity risk premium. Individual investors need not understand all of the arcane research surrounding risk pricing to exploit this information.

Perhaps the most well known codified rule of investing is the concept of diversification. Virtually every undergraduate investment text illustrates how most of the diversifiable risk in a randomly selected equity portfolio can be eliminated with only 15 to 20 issues. Although the concept is based on abstract statistical measures such as mean, variance and covariance many individual investors correctly interpret security diversification as nothing more than an extension of the common sense notion of not "putting all of your eggs in one basket." The "risk spreading" benefits of diversification also serve to reduce some of the uncertainty associated with the dissemination of inaccurate data by ethically challenged market participants.

Growth in equity mutual funds, especially indexed funds, testifies to the market's acceptance of diversification as a codified investment rule. Similarly, academic research, which found that the returns for small firms exceed those for larger firms (the "small firm effect"), has spawned the creation of numerous small capitalization mutual funds. One reason the mutual fund scandal has been so damaging is because the mutual fund ownership structure has been a particularly useful vehicle for implementing rules that benefit individual investors.

The codification of investment knowledge into simple operational rules evolves after an extended period of investigative research, followed with testing by investment practitioners. As equity ownership has spread from Wall Street to Main Street, the importance of this process in advancing investor confidence and social welfare should not be taken lightly.

Long-run shifts in the market risk premium or the dissipation of the small firm effect may suggest changes in codified rules, but only after due process. Ultimately, the real arbiters of significant investment research are not the editors of prestigious academic journals but the public.

I would like to thank the American Institute for Economic Research in Great Barrington, MA and its summer conference on "Hayek, Dewey and Embodied Cognition: Experience, Beliefs and Rules."

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** and **Verizon**, which were not then Dow components, were not eligible for purchase 18 months earlier. 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.

As of July 15, 2004

	Rank	Yield	Price	Status	——Percent of Portfolio*—— Value	No. Shares[1]
Altria Group	1	5.64%	48.20	*		
SBC Comm.	2	5.43%	23.00	Holding**	25.40	28.77
General Motors	3	4.55%	43.94	*		
Verizon	4	4.42%	34.81	Buying	6.07	4.54
JP Morgan Chase	5	3.78%	36.00	Holding**	28.13	20.36
CitiGroup	6	3.62%	44.21	Buying	7.46	4.39
Merck	7	3.31%	44.71	Holding	3.14	1.83
DuPont	8	3.28%	42.62	Holding	4.75	2.90
General Electric	9	2.40%	33.37			
Exxon Mobil	10	2.38%	45.32			
AT&T	NA	6.50%	14.60	Holding	15.41	27.50
Eastman Kodak	NA	1.90%	25.82	Selling	9.58	9.66
					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	-3.93%	-3.68%	0.04%	12.06%	14.00%	15.11%	19.31%
Dow	-1.92%	13.43%	-0.02%	12.45%	12.07%	10.46%	16.91%

* 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.

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, Verizon, J.P. Morgan Chase, and Citigroup — account for roughly 67 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	*7/15/04*	*6/15/04*	*7/15/03*	*High*	*Low*	*Amount*	*Record Date*	*Paid*	*Annual Dividend*	*Yield† (%)*
Altria Group	MO	**$48.20**	47.55	40.50	58.96	38.72	0.680	6/15/04	7/09/04	2.720	5.64
★ SBC Comm.	SBC	**$23.00**	24.47	24.80	27.73	21.16	0.313	7/10/04	8/02/04	1.250	5.43
General Motors	GM	**$43.94**	47.64	36.25	55.55	35.03	0.500	5/14/04	6/10/04	2.000	4.55
★ Verizon	VZ	**$34.81**	35.94	36.95	39.54	31.10	0.385	7/09/04	8/02/04	1.540	4.42
★ J. P. Morgan Chase	JPM	**$36.00**	37.25	37.29	43.84	32.40	0.340	7/06/04	7/31/04	1.360	3.78
★ Citigroup	C	**$44.21**	47.02	46.83	52.88	42.48	0.400	5/03/04	5/28/04	1.600	3.62
☆ Merck	MRK	**$44.71**	47.95	61.87	62.30	40.57	0.370	6/04/04	7/01/04	1.480	3.31
☆ DuPont	DD	**$42.62**	43.57	42.08	46.25	38.60	0.350	5/14/04	6/12/04	1.400	3.28
General Electric	GE	**$33.37**	31.81	27.67	34.57	26.90	0.200	6/28/04	7/26/04	0.800	2.40
Exxon Mobil	XOM	**$45.32**	44.08	35.19	45.59 *H*	34.90	0.270	5/13/04	6/10/04	1.080	2.38
Honeywell Intl.	HON	**$35.70**	35.97	27.88	37.65	25.94	0.188	5/20/04	6/10/04	0.750	2.10
Pfizer	PFE	**$32.58**	35.09	33.86	38.89	29.43	0.170	8/13/04	9/03/04	0.680	2.09
Caterpillar	CAT	**$79.40**	75.39	58.07	85.70	57.78	0.410	7/20/04	8/20/04	1.640	2.07
Johnson & Johnson	JNJ	**$55.35**	56.21	52.55	57.28	48.05	0.285	5/18/04	6/08/04	1.140	2.06
Coca-Cola	KO	**$50.84**	51.23	43.99	53.50	42.28	0.250	6/15/04	7/01/04	1.000	1.97
Alcoa	AA	**$32.88**	31.14	24.75	39.44	24.00	0.150	8/06/04	8/25/04	0.600	1.82
Procter & Gamble (s)	PG	**$55.01**	55.52	44.38	56.34 *H*	43.25	0.250	7/23/04	8/16/04	1.000	1.82
Hewlett-Packard	HPQ	**$19.65**	21.70	22.90	26.28	19.10	0.080	6/16/04	7/07/04	0.320	1.63
Boeing	BA	**$49.14**	49.25	33.44	51.49 *H*	31.00	0.200	8/13/04	9/03/04	0.800	1.63
3M Company (s)	MMM	**$88.62**	85.55	64.04	90.29 *H*	63.40	0.360	5/21/04	6/12/04	1.440	1.62
United Tech.	UTX	**$91.00**	89.28	71.92	97.84	71.58	0.350	8/20/04	9/10/04	1.400	1.54
McDonald's	MCD	**$27.91**	26.68	21.08	29.98	20.40	0.400	11/14/03	12/01/03	0.400	1.43
Wal-Mart Stores	WMT	**$52.33**	56.71	57.32	61.31	50.50	0.130	8/20/04	9/07/04	0.520	0.99
Home Depot, Inc.	HD	**$34.33**	35.77	33.17	37.89	30.10	0.085	6/10/04	6/24/04	0.340	0.99
Walt Disney	DIS	**$23.87**	24.70	21.35	28.41	19.78	0.210	12/12/03	1/06/04	0.210	0.88
IBM	IBM	**$84.02**	90.54	86.44	100.43	78.73	0.180	5/10/04	6/10/04	0.720	0.86
American Express	AXP	**$48.90**	51.22	45.14	53.98	42.36	0.100	7/02/04	8/10/04	0.400	0.82
Intel Corp.	INTC	**$23.15**	28.43	24.10	34.60	23.14	0.040	5/07/04	6/01/04	0.160	0.69
Microsoft Corp.	MSFT	**$27.87**	27.41	27.27	30.00	24.01	0.160	10/15/03	11/07/03	0.160	0.57
AIG	AIG	**$69.53**	72.15	59.30	77.36	56.16	0.750	9/03/04	9/17/04	0.300	0.43
☆ Eastman Kodak	EK	**$25.82**	25.42	26.56	31.55	20.39	0.250	6/01/04	7/15/04	0.500	1.90
☆ AT&T	T	**$14.60**	16.18	19.60	23.18	14.12	0.024	6/30/04	8/02/04	0.950	6.50

† Based on indicated dividends and market price as of 7/15/04. *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

	7/15/04	Mo. Earlier	Yr. Earlier
Gold, London p.m. fixing	**403.15**	**386.50**	348.25
Silver, London Spot Price	**6.54**	**5.63**	4.78
Copper, COMEX Spot Price	**1.29**	**1.20**	0.79
Crude Oil, W. Texas Int. Spot	**40.97**	**37.19**	31.62
Dow Jones Spot Index	**146.47**	**182.86**	146.49
Dow Jones-AIG Futures Index	**185.02**	**144.14**	116.11
CRB-Bridge Futures Index	**273.38**	**266.62**	233.12

Interest Rates (%)

U.S. Treasury bills -	91 day	**1.33**	**1.33**	0.89
	182 day	**1.67**	**1.67**	0.96
	52 week	**1.95**	**2.10**	1.05
U.S. Treasury bonds -	10 year	**3.71**	**3.88**	3.93
Corporates:				
High Quality -	10+ year	**5.91**	**6.06**	5.50
Medium Quality -	10+ year	**6.37**	**6.52**	6.03
Federal Reserve Discount Rate		**2.25**	**2.00**	2.00
New York Prime Rate		**4.25**	**4.00**	4.00
Euro Rates	3 month	**2.11**	**2.10**	2.13
Government bonds -	10 year	**4.19**	**4.33**	3.87
Swiss Rates -	3 month	**0.48**	**0.34**	0.27
Government bonds -	10 year	**2.84**	**2.92**	2.33

Exchange Rates

British Pound	**$1.859000**	**$1.828100**	1.591200
Canadian Dollar	**$0.756500**	**$0.728100**	0.716100
Euro	**$1.235300**	**$1.205700**	1.113500
Japanese Yen	**$0.912600**	**$0.908000**	0.008447
South African Rand	**$0.166100**	**$0.152900**	0.127900
Swiss Franc	**$0.808800**	**$0.791200**	0.719200

Securities Markets

	7/15/04	Mo. Earlier	Yr. Earlier
S & P 500 Stock Composite	**1,106.69**	**1,132.01**	1,000.42
Dow Jones Industrial Average	**10,163.16**	**10,380.43**	9,128.97
Dow Jones Transportation Average	**3,125.39**	**3,039.84**	2,573.97
Dow Jones Utilities Average	**279.99**	**272.27**	238.63
Dow Jones Bond Average	**175.90**	**173.29**	171.40
Nasdaq Composite	**1,912.71**	**1,995.60**	1,753.21
Financial Times Gold Mines Index	**1,522.58**	**1,387.71**	1,262.89
FT African Gold Mines	**1,915.58**	**1,801.15**	2,037.14
FT Australasian Gold Mines	**3,584.43**	**2,967.13**	2,181.40
FT North American Gold Mines	**1,281.87**	**1,167.30**	1,000.75

Coin Prices

	7/15/04	Mo. Earlier	Yr. Earlier	Premium
American Eagle (1.00)	**$402.25**	**$403.35**	356.85	-0.22
Austrian 100-Corona (0.9803)	**$383.03**	**$384.13**	339.93	-3.08
British Sovereign (0.2354)	**$96.05**	**$96.35**	85.55	1.21
Canadian Maple Leaf (1.00)	**$402.50**	**$403.60**	357.10	-0.16
Mexican 50-Peso (1.2057)	**$472.60**	**$473.90**	419.50	-2.77
Mexican Ounce (1.00)	**$391.80**	**$392.90**	347.80	-2.82
S. African Krugerrand (1.00)	**$397.85**	**$398.95**	353.35	-1.31
U.S. Double Eagle-$20 (0.9675)				
St. Gaudens (MS-60)	**$460.00**	**$470.00**	410.00	17.93
Liberty (Type I-AU)	**$675.00**	**$675.00**	675.00	73.06
Liberty (Type II-AU)	**$487.50**	**$487.50**	440.00	24.98
Liberty (Type III-AU)	**$425.00**	**$425.00**	390.00	8.96
U.S. Silver Coins ($1,000 face value, circulated, year earlier uncirculated)				
90% Silver (715 oz.)	**$4,230.00**	**$4,182.50**	4,450.00	-9.54
40% Silver (292 oz.)	**$1,730.00**	**$1,725.00**	1,587.50	-9.41
Silver Dollars	**$6,500.00**	**$6,500.00**	6,137.50	28.48

Note: Premium reflects percentage difference between coin price and value of metal in a coin, with gold at $403.15 per ounce and silver at $6.54 per ounce. The weight in troy ounces of the precious metal in coins is indicated in parentheses.

Recommended Mutual Funds

	Ticker Symbol	7/15/04	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	**$81.76**	**$81.45**	82.46	83.08	81.14	1.4744	0.0000	1.80
★ USAA Short Term Bond	USSBX	**$8.99**	**$8.97**	9.13	9.17	8.95	0.2995	0.0000	3.33
★ Vanguard Short-Term Inv. Grade	VFSTX	**$10.67**	**$10.62**	10.87	10.91	10.59	0.3858	0.0000	3.62
Income Equity Funds									
★ DNP Select Income[1, 2]	DNP	**$10.90**	**$10.75**	11.04	11.42	9.60	0.7800	0.0000	7.16
★ Vanguard REIT Index	VGSIX	**$15.83**	**$15.36**	13.57	16.98	13.35	0.8200	0.0000	5.18
Large Cap. Value Equity Funds									
★ iShares S&P 500 Value Index[3]	IVE	**$55.76**	**$56.86**	49.23	58.88	47.32	0.9564	0.0000	1.72
★ Vanguard Value Index	VIVAX	**$19.14**	**$19.24**	16.72	19.91	16.26	0.4420	0.0000	2.31
Small Cap. Value Equity Funds									
★ iShares Sm. Cap. 600 Value Index[3]	IJS	**$105.99**	**$105.19**	85.81	109.90	81.85	0.9237	0.0000	0.87
★ Vanguard Sm. Cap Value Index	VISVX	**$12.10**	**$11.91**	9.76	12.48	9.45	0.1980	0.0000	1.64
Growth Equity Funds									
★ iShares S&P 500 Growth Index[3]	IVW	**$54.75**	**$56.83**	50.96	58.01	48.66	0.6288	0.0000	1.15
★ Vanguard Growth Index	VIGRX	**$24.76**	**$25.55**	22.86	26.09	21.86	0.1360	0.0000	0.55
Foreign Equity Funds									
★ iShares S&P Europe 350 Index[3]	IEV	**$64.73**	**$65.73**	52.31	69.20	51.50	1.1110	0.0000	1.72
T Rowe Price European Stock	PRESX	**$17.63**	**$17.53**	14.25	18.68	13.97	0.2200	0.0200	1.25
★ Vanguard European Stock Index	VEURX	**$22.77**	**$22.42**	18.09	23.57	17.73	0.4600	0.0000	2.02

Recommended Gold-Mining Companies

	Ticker Symbol	7/15/04	Month Earlier	Year Earlier	— 52-Week — High	Low	Distributions Latest 12 Months	Frequency	Yield (%)
Anglo American PLC, ADR	AAUK	**$21.25**	**$20.52**	15.91	26.69	15.53	0.570	Semiannual	2.68
★ Anglogold Ashanti Ltd., ADR	AU	**$33.57**	**$31.79**	30.77	49.95	29.89	0.996	Semiannual	2.97
ASA Ltd.[1]	ASA	**$36.61**	**$34.95**	36.02	48.00	33.47	0.600	Quarterly	1.64
★ Barrick Gold Corp.†	ABX	**$20.55**	**$19.26**	16.98	24.16	16.67	0.220	Semiannual	1.07
★ Gold Fields Ltd.	GFI	**$10.09**	**$10.27**	11.00	15.52	9.75	0.118	Semiannual	1.17
★ Newmont Mining	NEM	**$41.90**	**$37.97**	31.84	50.28	31.01	0.300	Quarterly	0.72
★ Placer Dome†	PDG	**$17.06**	**$15.31**	11.48	19.23	11.38	0.100	Semiannual	0.59
★ Rio Tinto PLC‡	RTP	**$103.46**	**$94.95**	81.76	116.33	79.24	2.720	Semiannual	2.63

★ 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.