



**December 31, 2002**

**RE: 2003 Outlook & Other Issues**

**Dear Valued Client,**

As you know, 2002 was another bad year for most stocks and a good year for bonds and real estate investments. In fact, the S&P 500 and NASDAQ were down 23% and 32%, while the Dow Jones Corporate Bond Index was **up 11%** in 2002. The last time the stock market had three consecutive down years was during World War II.

In the July, 2002 client letter, it was pointed out that aggressive economic stimulus through tax reductions, low interest rates and the increasing growth of the nation's money supply (i.e. America's economic heart beat), would give the stock market the fuel needed to make up most of the ground lost in 2001. Unfortunately, the escalation of the war on terrorism, and its uncertain outcome, are expected to dominate the stock and bond markets for the foreseeable future.

**Stock Outlook:**

We are expecting the economy to grow at a slow to moderate rate over the next three to five years, and we expect the S&P 500 to reflect this by trading in a **range between 1200 and 800**. History has repeatedly shown that after a big stock market decline (i.e. the Great Depression, World War II and the 1970's recession), the stock market moves "sideways" for several years.

On the positive side, this is what Wall Street calls a "stock picker's market". It can be profitable to focus on companies that are financially performing well in this environment, and taking potential profits on these stocks at significant price points identified by our research. In addition, we have also increased our use of long term stock options as a way to "lock in" today's low stock prices without a full financial commitment for several years.

**Bond Outlook:**

Since 2000, we have been encouraging all of our clients to increase their investment in bond and equity income holdings to **at least 33%**. Although we feel the investment climate will continue to be good for bond investors, due to consistently low interest rates caused by slow economic growth and low inflation, there are several key issues that need to be considered before further investment is made:

1. **Corporate Bonds:** One of the few positive surprises from last year was how well most of our corporate bond investments maintained their value during the accounting crisis. Although it requires patience, we have been able to find 3-5 year bonds paying up to 7% and 6-10 year bonds yielding up to 8.5%. In addition, we have structured hedging strategies in order to help maintain the value of bond holdings in margin accounts if interest rates rise unexpectedly.

2. **Municipal Bonds:** We are very concerned about the high valuation of most municipal bonds, and we estimate that the financial problems plaguing state and local governments nationwide could cause municipal bond prices to drop 15% from today's levels. We are recommending that clients avoid additional investment in this area, sell all existing municipal bond mutual funds, sell bonds with maturities exceeding 2013 and seriously consider the use of hedging strategies to protect the remaining holdings in accounts with margin capabilities.
3. **Other Income Investments:** Throughout this year we intend to increase investment in preferred stocks, real estate investment trusts, master limited partnerships and real estate backed trust deeds on properties in Marin County, California. These investments are yielding between 7-10% as of 12/31/02.

#### **Other Issues:**

**Client Restricted Investments:** One of the advantages of working with Winans International is the ability to combine into one portfolio client directed investments with investments selected by us. Please keep in mind that any investments listed under "Client Holdings" on your Portfolio Overview report are considered restricted, and thus we have no authority to sell these holdings without client direction. In addition, these investments have not met our selection requirements and thus are not treated the same way as investments that we make on behalf of the client. If you have any restricted investments, please let us know what your objectives are for these holdings.

**Stop-Loss Orders:** Several years ago, we decided to switch from using automatic stop-loss orders to a manual approach for reducing stock losses, because the current market's extreme level of volatility had rendered stop loss orders useless in many instances. We will continue to deal with investment losses using the manual approach until a more "normal" market condition returns.

**Investor Class Action Lawsuits Against Corporations:** Due to last year's corporate accounting crisis triggered by the bankruptcy of Enron, shareholder lawsuits have been filed against a few of the companies that we held in client portfolios such as Tyco International and Elan PLC. We have notified the brokerage firms holding your accounts, as well as the law firms involved, that we want our clients to be included as plaintiffs in these cases. If you receive any documents regarding these lawsuits, please forward copies of the information to us. Hopefully, there will be investor compensation for the disgraceful conduct of many companies and/or their officers.

**Improving Client Communication:** As a general policy, we try to respond to all client requests during weekdays within 24 hours. As our business has grown, so has the volume of phone calls, voicemail, e-mail and faxes. In order to facilitate this growth, we have tried to better organize our effort in the following ways:

**1) Phone Calls:** During a normal day, I have set aside from 11:00-12:00 and from 1:30 – 4:00 to speak directly with clients. In order to make our conversation more efficient and effective, please schedule a time and tell Gloria what needs to be discussed. Please keep in mind that Karen, Bart and Gloria are available much of the time and can assist you with most requests.

**2) Voice Mail:** We check voicemail in the mornings and early afternoons. If you have a matter that needs immediate attention, please call back and talk to a staff member on weekdays from 8:00 to 5:00(PST).

**3) Emails & Faxes:** We check for emails and faxes in the morning and our deleted email files once a week. Due to our virus protection software, emails with attachments are usually sent to the deleted file. If you are sending us important, time-sensitive material by email or fax, please call us to confirm that it was received.

**Please review thoroughly the information contained with this letter before our meeting. It is important that we mutually agree on a future course of action that reflects today's opportunities and risks.**

As a final thought, I have entered my 22<sup>nd</sup> year as an investment professional and clearly remember the terrible stock market conditions of the early 80's, "the 87 crash" and the Gulf War, as well as, the future predictions of "doom and gloom" made by the experts of the time. Contrary to these opinions, the situation reversed and produced great investment opportunities. If history and the consistency of human nature are any kind of guide "This too shall pass!"

I look forward to seeing you during our next meeting, and call us if you have any questions.

**Sincerely,**

**Kenneth G. Winans  
Founder & President**