

Good News? Slide 1

- Wal-Mart – Sales up strongly, but people are trading down-bad news.
- General Motors – Earnings beat the street, but all income is from lending money.
- Bankers – Earnings very strong, but most come from trading profits & that does not add to economic growth. Trading is a zero sum game.
- General Electric – Earnings beat the street, but were 11% below a year ago. They are in a broad section of the economy, which indicates the economy is not doing well.

Good News?

- Wal-Mart
- General Motors
- Bankers
- General Electric

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Average Hourly Wage Slide 2

Wage rates worldwide will converge in a global economy. Wages & salaries are under pressure in the US. Estimates are that 3.3 million service jobs in the US will be lost over the next 10 years. Consumer spending has been fueled by loans, not income.

Average Hourly Wage

United States	\$20.32
Australia	\$13.15
Ireland	\$13.28
South Korea	\$8.09
Singapore	\$7.77
Hong Kong	\$5.96
Thailand	\$0.50
Indonesia	\$0.37
China	\$0.30
India	\$0.24

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Preconditions Slide 3

These are things that have happened over the years, which have led to the feeling that government will always bail out the economy. That being the thought, market and economic participants have assumed more & more risk using more & more leverage. Such action on the part of the government creates a moral hazard, which is now coming to a head.

The Bubble Road Map Preconditions

- 1913 – Federal Reserve Act
- 1920's – Excess credit bubble
- 1930's – Keynesian economics
- 1940's – WWII halts depression
- 1950's – Marshall Plan – global economy
- 1960's – Good then Bad
 - Tax cuts
 - Guns & Butter

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Preconditions (cont.)

- 1970's – Nixon “We are all Keynesian now”
 - Gold delinked
 - Wage & price controls
 - Greenspan WIN
 - Carter – G. William Miller
- 1980's – Supply side revolution
 - Too big to fail
 - Oil, Farmland
 - Gold to \$850
 - 1986 Tax Increase
 - S&L bailout

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Preconditions (cont.)

- 1990's – The Last Straws
 - Tax Increase
 - Deregulation – Glass Stegal
 - Greenspan / Rubin & Wall Street
 - Bail Outs everywhere
 - Y2k
 - New Paradigm
 - Creative Accounting
 - Excess Credit

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Final Blow Off

- Stock options – currency of record
- IPO craze
 - 1986-1990 – 90 avg. – earnings history
 - 1996 – 2000 – 390 avg. – just a plan, no earnings history
 - Example: ivillage 24 to 56 in 1 day
 - \$15MM sales – lost \$43.7MM 1st year public
 - Example: PriceLine – bought tickets from airlines and sold them at a loss.
- Capital Spending Boom 1992 – 2000 +74%

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Final Blow Off Slide 4

The 1996 to 2000 final conditions led to the largest economic & market bubble in world history. The bull market in common stocks created the smartest investors in history. It was a “greater fool theory” perpetuated by the Wall Street minions. Investors often don’t get what they seek, but get what they deserve. Public dot com offerings doubled & tripled over night & created a capital spending boom in assets that today have little to no value. These types of blow offs take years and years to correct.

Global Imbalance Slide 5

For seven years the total global economy grew by \$3.164T and the US was 96% of that growth or \$3.045T. Much of this growth came from spending that was financed by the use of debt. How long can we keep up that rate of spending? How long will the rest of the world continue to loan us the money we need to spend in such a manner?

The rest of the world, particularly China, has built their business model on selling to us with little internal growth of their own. Will that change? If they don’t, where will future worldwide growth come from?

Global Imbalance

- Years 1995-2002, 7 years
 - U.S. 96% of global increase in GDP
 - “Normal” share is 33%
 - Numbers: \$3.164T World, \$3.045T U.S.
- The question is: Where will growth come from?
 - Japan – no reforms yet
 - Europe – high unemployment; no demand
 - China – no domestic demand
 - U.S. – low savings, high debt, no multiplier effect
 - Answer: The rest of the world has to pick up demand and the U.S. has to start saving

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2nd Q 03 Non-Market Debt Growth Slide 6

Debt, Debt, Debt. The fed’s low interest rates through their easy money polices are encouraging participants to lend and borrow. On an annualized basis the creating of debt was at the highest rate in history during the 2nd Q of 2003 (latest info available). Our fear is that the assets purchased will lose their value as markets correct, but the debt will remain. This is extremely deflationary.

2nd Quarter 2003 Non-Market Debt Growth Annualized*

Commercial Banks	\$819.1B	11.00%
Corporate Loans (\$74.3B)		
Mortgages \$355.4B		
Agencies \$283.9B		
Others \$254.1B		
Credit Unions		16.70%
Finance Companies		17.00%
REITS		34.70%
Federal Reserve		11.00%
GSE's		9.30%
FF's and Repo's		43.00%

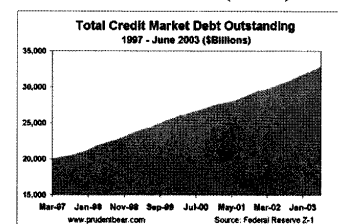
*Highest growth in history

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Charts Slide 7

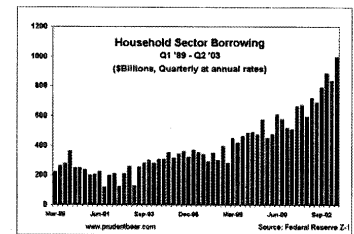
These are charts showing the huge increase in debt over the last several years. The first has to do with market debt as opposed to non-market debt depicted in the previous table. The second is household sector debt growth and the last mortgage debt. As of now, 41% of all debt outstanding has to do with mortgage debt. The amount of equity the average person has in his home is 16% if you exclude those who own their homes in full. Normal cyclical declines in housing markets in the past have been around 30%. We believe a housing bubble blow off is now taking place.

Debt Growth (cont.)



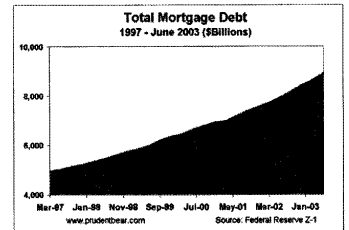
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Debt Growth (cont.)



7

Debt Growth (cont.)



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Measures of Debt Slide 8

These are various measures indicating the extreme amount of debt assumptions that has been taken. Debt is deflationary therefore remains a major risk to the economy. With little income growth on the part of individuals and profit growth on part of business, the economic outlook remains unexciting. A tipping point may be very close.

Measures of Debt

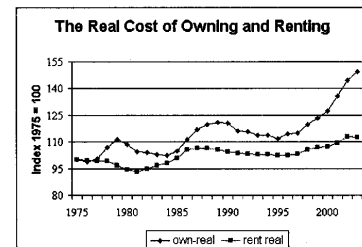
	% of GDP	
	1980	2002
Non Federal Debt	110%	170%
Federal Debt	25%	40%
	% of PDI	
	1980	2002
Household Debt	70%	110%
	% of Cash Flow	
	1980	2002
NonFinancial Corp	400%	650%
	% of Assets (Liquidity)	
	1980	2002
Securities - Banks	23%	29%

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Housing Slide 9

Cost to own is accelerating while the cost to rent has leveled off. In the past, this has been an extremely good indicator of a housing decline correction to come. We believe we will see these lines converge and do so primarily when the cost of owning comes down due to a large decline in the value of existing homes. "Bubble, bubble, boil, and trouble."

Housing



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What Wall Street Says About the Economy Main Stream Analysis Slide 10

Absolutely wrong headed and frankly hard to believe anyone with any ability to view our economy independently would buy into. It's classic buy side Keynesian & University of Chicago mantra. Please pay particular attention to "why this is wrong."

Main Stream Analysis

- Nothing has changed
- Mildest post WWII recession
- Fed prevented real trouble

WHY IS
THIS
WRONG?

What is Different This Time? Slide 11

Note where profits appear in the sequence of events “normal” vs. this time (2000-2001). There are two very important points. First, the last time profits went down as soon as they did in 2000-2001 was the 1930’s. This indicates that profits or lack there of is the main reason the economy went south. Secondly, please note inflation was not the reason the feds tightened this time. They did raise rates a bit, but always-made money available – this is much different than the past. We believe we may be approaching a 1930’s type of economy.

What is Different This Time?
A Different Kind of Recession
(In Order of Occurrence)

“Normal”		2000 – 2001	
Inflation	Up	Inflation	Down
Tight Money*	Up/Down	Tight Money*	Up/Up
Housing	Down	Profits	Down
Inventories	Down	Capital Spending	Down
Consumer Spending	Down	Inventories	Down
Profits	Down	Housing	Down?
Capital Spending	Down	Consumer Spending	Down?

* Two components – interest rates and availability

What is Different This Time Slide 12

This enumerates the short falls to date in this recovery versus previous recoveries. We believe although GDP numbers have been better since 12/31/01 the recovery in the business community is near non-existent.

What is Different This Time?
(cont.)

Industrial Production	
This time from recession trough	-1.0%
Past recessions	+0.6%
Imports	
This time from recession trough	+15.7%
Past recession	+7.2%
Employment	
This time from recession trough	-1,300,000
Past recessions	+2,800,000
Short in wages & salaries	\$240B

What is Different This Time Slide 13

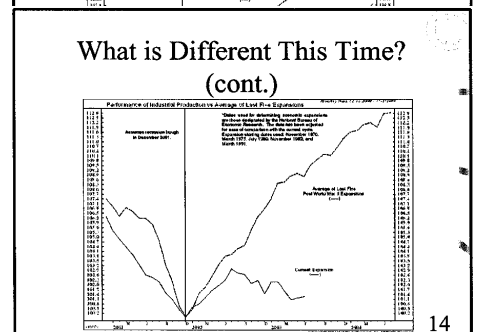
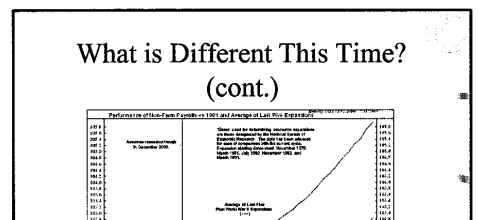
In the old days the economy drove the financial markets. This time the financial markets are driving the economy. This is very dangerous as the financial markets are not growth oriented in their own right. These markets are a zero sum game – for every winner, there is a loser. Economic growth comes from non-financial activity and this is what is suffering. Note that 40 % of all financing is for financial institutions – in 1998, it was only 25%. Most of this is for speculative activity and not real economic endeavors. This is not good.

What is Different This Time?
(cont.)

Entity	1998	1999	2000	2001	2002
Non-Financial	75.10%	71.50%	67.80%	63.60%	59.70%
Financial	24.90%	28.50%	32.20%	36.40%	40.30%
Total	100.00%	100.00%	100.00%	100.00%	100.00%

What is Different This Time Slide 14

These charts are two measures of the recovery vs. prior recoveries. Although Wall Street is convinced we are experiencing strong growth, this indicates otherwise. We believe another recession is close at hand.



Keynesian Analysis Slide 15

Gross Domestic Product is the broad economic gage that Wall Street follows closely. The problem is the devil is in the details. Dollars spent are not created equal, but this doesn't seem to matter in most analytical models. Please note that the consumer is approximately 70% of total, however, is not nearly as important as capital spending is in the grand scheme of things. Note our comment re: the importance of dollar spent.

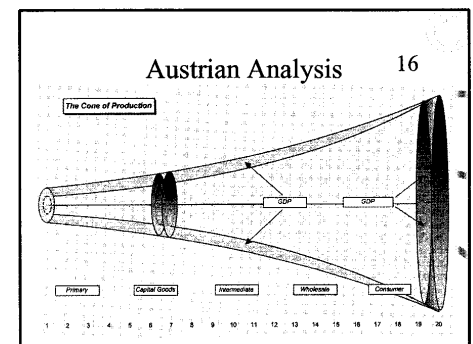
Keynesian Analysis	
GDP Sector Shares	
Consumer Spending	70%
Capital Spending	10%
Housing	5%
Net Exports	(5%)
Government	20%
	<hr/> 100%

Based on 2nd Quarter '03 current \$

- Does every \$ of GDP Count the Same?**
1. Consumer spending – no multiplier effect
 2. Capital spending – does have multiplier effect
 3. Military spending – adds very little value
 4. Trial lawyers – redistributing income
 5. Wall Street – new issues – multiplier effect
 6. Government – mixed – infrastructure
 7. B to B – much of it has multiplier effect

Austrian Analysis Slide 16

The Austrian economic model is by far, in our opinion, the best analytical approach to the study of economics. What it says is that one cannot properly determine the strength and/or weakness in the economy by looking only at the broad aggregate (GDP). If you will note in the cone of production, there are two basic elements. One is the time element from primary production at the left to the consumer at the extreme right. The other is that activity in between which is such things as capital goods, intermediate goods, and wholesale activity. Much of this is not counted in the GDP. If it were, consumer spending would be something like 35 to 40% rather than 70%.



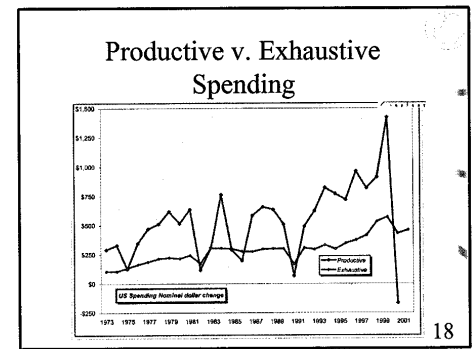
Total Business Costs Slide 17

Theses are the various costs that are not fully accounted for in the GDP aggregate numbers. There are some duplicates, but the best one can estimate is that some 60% of these costs are not counted. These are business-to-business expenses, which is where profits or losses occur. This is the area of our current problem. The remaining 40%, which are counted show up in, the final GDP sections classified as something else (see 15 Keynesian analysis).

Total Business Costs	
Gross Domestic Output	\$17.3T
Add Imports	1.4
100% Business Revenues	\$18.7T
Less Profits	1.5T
Depreciation	0.9
Business Costs	2.4T
Add Capital ex spending	1.2T
Total Business Activity costs	\$17.5T
Personal Consumption Expenditures	\$7.0T
Business to Personal	2 1/2 or 71% / 29%

Productive vs. Exhaustive Spending Slide 18

This is an Austrian classification between spending, which is productive, (has a multiplier effect) and that which is final consumptions such as retail sales. Final sales (exhaustive) keep only those presently employed, employed. Productive are located at the left end of the production cone and have high multiplier effect as they move towards final consumption. Note what has happened in 2000 and beyond. This represents trouble.



The Problem Slide 19

We are experiencing good GDP numbers but they don't indicate profits. The business of America is business and if no profit growth occurs, we can look forward to very slow economic times. This seems to currently be the case.

The Problem

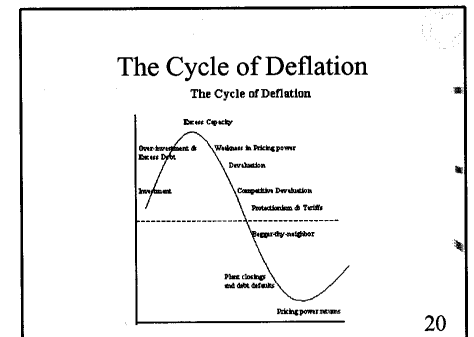
Headlines from Reuters 9/26/03

- 2nd quarter final GDP revised up, spending strong, 3.3% vs. 1.4% from preceding period
- 2nd quarter final after tax profits fell 5.0% from preceding period

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Cycle of Deflation Slide 20

We are approaching the dotted line on the right hand side of the chart. President Hoover & Roosevelt policies are welling up in Washington D.C. Beware of the blame game. China and other Asian countries will probably be the political scapegoat.



The Road to Investment Disaster Slide 21

Wall Street and the consulting industry picked up on the academic studies of those mentioned in these tables and sold it to the investing public. Never has so many been misled by such absurd and illogical investment theories. A very profitable cottage industry developed from the works of these academicians. Nobel prize winners were created on the backs of individual investors losses. It begs the question – where are all the customers yachts? We fear that only a long and major market decline from here (S&P 500) will awaken the investing public to the gross injustice perpetuated by those who may or at least should know better.

The Road to Investment Disaster

- University of Chicago
 - Eugene Fama: Efficient Markets
 - Harry Markowitz: Modern Portfolio Theory
 - Roger Ibbotson: Mathematical Bible
 - Milton Friedman: Quantity Theory of Money
- Others
 - Supply Siders: Caught Potomac Fever
 - Jeremy Siegel: Stocks for the Long Term
 - Scholes & Merton: Nobel economics LTCM
 - LTCM = US Economy today

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The Road to Investment Disaster (cont.)

- Consulting Industry
 - Performance: wedge issue
 - Acceptance of Chicago school
 - Insulation against beneficiaries
- Wall Street Killing Field
 - 800,000 vs. handful

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