

Thoughts from

Hanson Investment Management Inc.

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Markets Don't Mind Bad News . . .

WHAT THEY MIND IS **UNCERTAINTY**. Unfortunately uncertainty is what we are getting plenty of now. Take a look at the chart to the right. Our biggest problem today is Iraq and until there is some resolution the economy and market will sit on its hands frozen in place.

Back in 1921 the economist Frank Knight differentiated between risk and uncertainty. Risk is something you can calculate, where you can apply probabilities and make educated guesses. Uncertainty is where the odds of success or failure are completely incalculable. This is the case with Iraq.

If we go to war we would like to think it would be short and followed by a decisive victory. This is how the last one went. But there are many more worse-case scenarios including a protracted war that draws in Israel and the rest of the region and where Islamists take control of some of the oil and hold us hostage. So we sit and stew unsure what to do. And there is nothing that gets the gloomy juices going like sitting and stewing.

I am hoping Iraq will get settled one way or another soon and we will move from uncertainty to more traditional risk assessment. Business spending has been anemic for three years and there are capital spending projects that need to get done. If the dam breaks and some of this spending is released, the consumer will not have to shoulder all of the work of the recovery. This would be good. A more balanced recovery is healthy and renewed capital spending would increase confidence and lead to higher stock prices. But all this requires

the big uncertainty of Iraq to be out of the way first. All fingers and toes are crossed on this one.

BEHIND THE GLOOM

Why has early-January confidence suddenly turned into pessimism?

IRAQ JITTERS The increasing likelihood of a war with Saddam has spooked markets and helped send consumer confidence to its lowest ebb in nine years.

PROFITS HICCUP Although cost-cutting helped boost average earnings of S&P 500 companies an estimated 13% in the fourth quarter of 2002, economists say profit growth will fall to an estimated 9% in the first quarter of 2003 and to 6% in the second.

SLOWING GROWTH Data due out Jan. 30 were expected to show that economic expansion slowed from 4% in the third quarter to below 1% in the fourth. Estimates are now being ratcheted down to 2% to 2.5% for the first half, and fears of a double-dip recession are returning.

WEAK CAPITAL SPENDING

Worried about Iraq and seeing no uptick in demand, companies continue to delay new spending on plants and equipment.

POLITICAL UNCERTAINTY With President Bush's stimulus package running into stiff opposition in Congress and his Administration seemingly preoccupied with Iraq, confidence in his handling of the economy is plunging.

Source: Business Week

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Hanson Investment Management is an investment counsel firm managing portfolios for individuals and institutional clients. The firm also consults with individuals on financial planning and works with self-directed retirement plans on investment options.

2000 Revisited. . .

This party was quite a doozy . . .

MARCH 10 MARKS THE THIRD anniversary of the peak of the NASDAQ Composite at 5048. The Standard & Poor 500 hit its high on March 24 at 1527. As the chart to the

in the face of such wealth destruction.

The chart to the left was on page one of our newsletter in May 2000. It shows how extreme the blow off in high tech prices was. Cisco was the most valuable company in the world at that time at \$550 billion. Its market cap equaled that of

twenty-five major 'old economy' companies. Today it is a much different story. The market cap of Cisco has fallen to \$93 billion while the value of the twenty-five old-line companies has stayed relatively stable at \$503 billion. The 75% decline in the NASDAQ and the 47% decline in the Standard & Poor 500 rank among history's major Bear Market episodes.

I wouldn't be surprised however that when some of the uncertainties lift (*see page 1*) this market could rally sharply. This often happens even in the depths of a Bear market. Interest rates and inflation are very accommodating now and if business spending kicks in even marginally we could see good growth in GDP and the stock market.

A second surprise could be that the laggards of the past cycle could be solid contributors to this rally. I am not banging the drum necessarily for high technology but when capital spending gets

unleashed a lot of it will occur in technology (*see chart below*) and this will be a big boost to the stocks. On the other hand, financial stocks are now more than 20% of the overall market. Typically when one group gets to this concentration like energy did in the 1980's and technology in the 1990's, the market tends to correct. I would not be overly heavy in finance. But healthcare interests us. The demographics are moving in the industry's favor. We are all getting older and using more drugs and the sector has been out of favor for such a long time that the stocks are much cheaper than in the past.

Hunkering down and doing nothing is not the answer in this environment. Neither is acting unusually boldly. The best course is to keep your wits about you, keep your long term objective in clear focus and look for opportunities that may well be right in front of you but covered by the fog of market gloom.

(UN)HAPPY ANNIVERSARY

► Below are some key figures showing the declines in equity wealth and stock valuations, and the diminished risk appetite of investors, since the broad market peaked nearly three years ago on March 24, 2000.

	THEN*	NOW**
S&P 500	1527	837
US stock-market cap	\$17.8 Tril	\$9.7 Tril
Mkt cap as % of US GDP	184%	90%
1-yr fwd S&P est. oper. earns.	\$57/shr	\$52/shr
Forward P/E ratio	26.2	16.0
10-yr Treasury yield	6.17%	3.78%
Schwab avg. daily trade vol.	320,000 shrs	126,000 shrs
Investors intelligence bulls/bears	55%/26%	40%/36%

*As of 3/24/00 or most recent figures. **As of 2/27/03 or latest available figures.

Source: Barrons

THE NEW ECONOMY

Company	Ticker	3/23/00 Market Cap (\$B)
Cisco	CSCO	550
Total		550.00
Price/Sales		36.00
Price/Earnings		213.00

THE OLD ECONOMY

Company	Ticker	3/23/00 Market Cap (\$B)
Ford	F	53.75
Texaco	TX	27.70
Merrill Lynch	MER	39.56
DuPont	DD	57.36
Aetna	AET	8.24
International Paper	IP	16.08
Sara Lee	SLE	16.42
Raytheon-Class B	RTN.B	6.34
Caterpillar	CAT	14.19
AMR	AMR	4.71
FedEx	FDX	11.53
Minnesota Mining & Mfg	MMM	35.03
McDonald's	MCD	47.64
Archer-Daniels-Midland	ADM	6.52
Goodyear Tire & Rubber	GT	3.67
Morgan (JP)	JPM	23.80
Anheuser-Busch	BUD	28.14
Lilly	LLY	70.20
Staples	SPLS	9.74
Fox Entertainment	FOX	18.74
Consolidated Edison	ED	7.02
Apple Computer	AAPL	22.73
Maytag	MYG	2.66
Hilton Hotels	HLT	2.81
Dow Jones	DJ	6.66
Total		541.24
Price/Sales		1.01
Price/Earnings		14.82

Source: Ned Davis Research Source: Morgan Stanley Dean Witter

right shows the U.S. stock market has lost over \$8 trillion since, equal almost to an entire year's GDP. Maybe we should be impressed how well the economy has done

SIGNS OF A TELECOM RECOVERY

The industry is wracked by bankruptcy and scandal, but new trends point toward recovery. Here's why:

MORE CYCLICAL

Telecom once depended on voice service, a staple in good times and bad. Services like Net access now account for most telecom traffic. As the economy improves, spending will rise.

IMPROVING PROFITS

They're uneven, but profits are picking up, especially in wireless. Nextel Communications just posted its second quarterly profit. And giant Vodafone beat industry expectations.

STABILIZING PRICES

While pricing power is still weak, carriers say prices are stabilizing. And on some international routes, like New York to London, prices have increased during the past few months.

NEW PRODUCTS

The adoption of new offerings, including broadband service, is rising. And a new generation of wireless phones with color screens and cameras could spark demand.

Source: Business Week

The New U.S. Economy . . .

Cómo se dice this is our future? . . .

THE CENSUS BUREAU recently reported that Hispanics have surpassed African Americans as the largest U.S. minority group. It is estimated for instance that there are 23 million Mexicans in the United States. Vicente Fox, the President of Mexico, likes to say these Mexicans produce an estimated \$400 billion of output in America. Mexico's home output is around \$600 billion. So the influence of Mexico and Hispanics in general is significant.

I am no expert on all this but I am fascinated by the potential. The chart in the upper right shows total U.S. Hispanic population at 37 million and their purchasing power is growing rapidly. Companies on both sides of the border are going to be taking advantage of this. Marketers spent \$2.5 billion last year on ads targeting Hispanic consumers, up 11% from 2001. The biggest spenders were Proctor & Gamble followed by Altria (the old Philip Morris) General Motors, AT&T and McDonalds. Cable sports giant ESPN will launch ESPN Deportes (Spanish for sports) on a twenty-four hour basis this year.

You can measure the increasing wealth of Hispanics by the amount of money they send back to their home countries. It is estimated that Mexicans in the United States remit \$11 billion a year. This is the third largest source of income for the country after oil exports and tourism.

Foreign companies are entering the U.S. market at a growing rate. The *Wall Street Journal* recently estimated that Latino disposal income nationwide has grown 160% since 1990 to \$580 billion even higher than the estimate in the chart in the upper right. An obvious beneficiary of this is media companies broadcasting in Spanish.

Univision (traded here, symbol UVN) has already corralled a lot of the early advertising market. Univision is a Los Angeles based company with over twenty television stations and an 80% share of the Spanish-speaking television audience. Another company to watch is Grupo

Televisa (traded in the U.S., symbol TV) a Mexican supplier of broadcast content as well as an investor in Univision.

Food will be a big part of the Hispanic market. Haagen Daz got the jump on Ben & Jerry's by introducing Dulce De Leche (caramel) ice cream recently. This is South America's favorite flavor. Supermarket chains from Mexico are also moving into the U.S. now. Gigante (pronounced Hee-gan-tay), the country's third largest grocer has opened stores in Southern California and will be branching out soon. In fast food Pollo Campero, a Guatemala City seller of spicy chicken has three outlets in Los Angeles, with new stores going in in Houston and Washington DC. Two Mexican chains, El Tizoncito, a vendor of roasted pork tacos and Gorditas Dona Tota, which sells tortilla dough filled with meat or cheese, plan to start operating in the U.S. by the end of the year.

More Hispanic consumers

As the U.S. Hispanic population increases, so does its purchasing power:

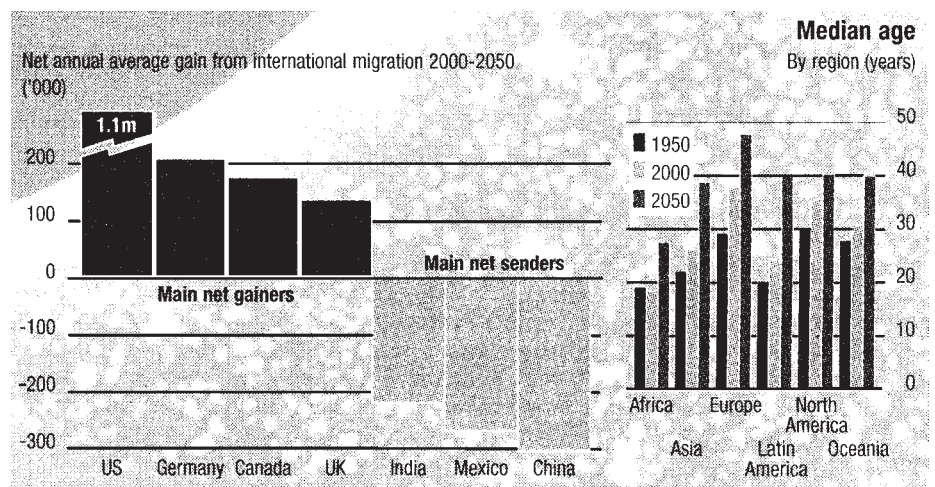
U.S. Hispanic population (in millions)		Purchasing power (in billions)	
1999	31.3	1999	\$446.9
2002	37.0	2002	\$540.0

Source: *Hispanic Business* magazine

By Frank Pompa, USA TODAY

Globalization is often seen as U.S. companies or products strong-arming their way into emerging markets. But with the Hispanic market the process may work in reverse. Look for more Spanish/South American influence on almost everything here. I think the two most important languages this century after English are going to be Chinese and Spanish. Chinese will cover a rather narrow but large niche in Southeast Asia. Spanish on the other hand will have influence over a much wider area including South America, Spain and the Philippines. And here in the U.S. employers are already looking for bilingual help to bridge the gap between America and the new Hispanics. Young people had better pay attention. This could be your future.

MIGRATION



Source: Financial Times

Investment Trends . . . Searching for Value . . .

I JUST RETURNED FROM Raymond James 24th Annual Institutional Investor Conference. This event held in Orlando, Florida brings together senior managers from over 225 companies, equity analysts and portfolio managers.

What did I learn? Well first, despite three down years in a row, the investment business appears alive and well. Without a doubt, the tone was more sober, but the attendance list of approximately 430 institutional investors was about the same as in the past.

From an economic perspective, general business conditions do not appear quite as bad as the media would have us believe. I arrive at this conclusion taking into account the natural “optimism” expressed by presenting CEOs whose objective in part is to attract investment capital.

On the negative side, many industries continue to experience pricing pressure. In technology and telecommunications, excess capacity and price competition remain the order of the day. In healthcare, regulatory reforms threaten to slow the rate of inflation. Most manufacturers going head to head with Asian competitors consider price increases a thing of the past. Rising healthcare and energy costs are also starting to rear their ugly head. While these costs do not represent a large percentage of most company’s overall cost structure, they are growing and managements have little control over the rate of increase.

So why be optimistic given the negatives discussed above? First, although most presenting companies admitted to having little insight into future economic conditions, they did report stable to slightly increased order rates. Second, every company I saw is working aggressively to reduce costs. In the manufacturing sector, firms are realigning production methods to eliminate redundancy and improve efficiency. Sophisticated software is helping companies more closely manage inventories. Improving cash flow is the

order of the day. Debt is being paid down and balance sheets repaired.

Over the course of the three days, I found a number of companies that look interesting even in today’s low growth environment. Many of these firms are

Raymond James 24th Annual Institutional Investors Conference

low cost producers with leading market shares. Furniture Brands, for example, is the country’s largest manufacturer of residential furniture while Polaris is a leader in the market for All-Terrain Vehicles, snowmobiles and watercraft. Strong brand recognition and innovative product development are helping these firms ward off competitors and both are aggressively managing costs. Furniture Brands has significantly reduced costs by moving production to China while Polaris has consolidated manufacturing of key product lines. Recently, the uncertain economic environment has caused consumers to cut back purchases of both company’s products. But longer term we expect that growing after tax incomes and low interest rates will support a rebound in consumer spending. When this happens, these two market leaders will benefit.

Despite the generally weak economic

backdrop, a number of industries continue to experience solid gains. According to healthcare consultant IMS, the rapidly aging population will drive solid 11%-14% annual increases in pharmaceutical spending over the next decade. Drug distributors Amerisource Bergen (ABC) and Priority Healthcare will benefit from this trend. ABC, the nation’s largest pharmaceutical distributor, resulted from the recent merger between Amerisource and Bergen Brunswig. The company continues to realize significant cost savings from distribution and overhead consolidation and is branching into higher growth markets. Priority operates in a much smaller and faster growing market distributing specialty pharmaceuticals for chronic diseases such as Hepatitis C.

Finally, a number of companies, such as Manhattan Associates, appear well positioned given the current economic downturn. Manhattan is the leading provider of software designed to optimize the efficiency of distribution centers. Sales of Manhattan’s products are growing steadily as companies seek to better manage inventory and free up cash. Manhattan is not without risks. The company is small and operates in the fast moving software industry. But we think strong end-market demand, the company’s market leadership and reasonable valuation make it worth another look.

– Anne Williams Doremus, CFA

LEADERS OF THE PACK

Company	Ticker	Price	52-Week Range	Market Capitalization	Price to Earnings	Debt to Total Capital	Yield
Amerisource-Bergen	ABC	\$51.05	(83-50)	\$5.6 Billion	12.8x	32%	0.2%
Furniture Brands	FBN	\$18.55	(43-17)	\$1.0 Billion	7.9x	30%	0.0%
Manhattan Associates	MANH	\$19.50	(40-12)	\$563 Million	19.1x	0%	0.0%
Polaris	PII	\$45.11	(77-45)	\$1.0 Billion	9.4x	6%	2.8%
Priority Healthcare	PHCC	\$24.10	(30-18)	\$1.0 Billion	18.4x	0%	0.0%

Source: Hanson Investment Management