

MJB ASSET MANAGEMENT LLC

950 Third Avenue, New York, NY 10022 (212) 421-4042

RICHARD BREGMAN, CFA, *Chief Executive Officer*

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Dear Clients and Friends:

Last quarter we wrote about the recession's end; the impending economic recovery; and a stock market poised for a rebound. Three months later, the recession is behind us and the recovery has begun, but the markets continued to decline. The three month period ended June 30th saw the Dow Jones Industrial Average decline by 10.7%, the S&P 500 index of large U.S. stocks decline by 13.4% and the NASDAQ composite index drop by 20.7%.

What happened? For two years, weary investors had trudged through a market weighed down by recession and the unwinding of the largest speculative bubble in recent memory. Now, just as the economy was beginning to recover, we have been hit by revelations that numerous high-ranking corporate officials have been lying for years about their companies' earnings, while reaping staggering fortunes at the expense of the shareholders to whom they lied. Adding insult to injury has been the discovery that many of the institutions on which investors rely to protect against such lies – e.g., the supposedly independent boards of directors, auditors and Wall Street stock analysts – have also been lying. The mounting disclosures of fraud and investigations -- which have moved beyond former dot.com darlings to engulf blue chip stalwarts such as Citigroup and JP Morgan – have turned out to be the straw that broke the camel's back. Though limited to a comparatively few companies, the corporate misdeeds have led to the loss of billions of dollars of wealth. More damaging has been the incalculable – though clearly enormous – loss of faith in the markets. Investors have reacted by fleeing stocks, evidenced by a \$30 billion outflow from equity mutual funds in the first three weeks of July alone.¹

Investor confidence remains fragile, with many taking a wait and see attitude before re-entering the markets. Economic signals continue to point toward a mild recovery, as interest rates and inventories are low, consumers continue to spend and the housing market remains robust. Yet global economic and political risks remain, including the continuing lag in corporate expenditures and the uncertainty caused by the war on terrorism and the strife in the Middle East. In the face of this uncertainty, we manage our clients' assets by focusing on things that we can control, including asset allocation, security selection and perhaps most importantly, the way in which we react to things that we cannot control.

¹ Credit Suisse First Boston, "U.S. First Edition Research Note," July 25, 2002.

We start by properly allocating each client's portfolio among stocks (individual equities and/or equity mutual funds), bonds and cash in a manner that is consistent with their risk tolerance and time horizon. Generally speaking – though by no means universally, for it is always dependent on each client's unique circumstances -- clients with longer time horizons or a higher tolerance for risk have a larger portion of their portfolios allocated to stocks. Conversely, clients with shorter time horizons or lower risk tolerances have a smaller allocation to equities.

After determining each client's asset allocation, we select securities and/or funds for each portfolio. In selecting individual equities, we look for high quality blue chip stocks with the opportunity for growth that are trading at prices 40% or more below their most recent high prices. As a stock approaches its former high price or if its fundamentals deteriorate, we sell and replace it with a new stock selling at or below 40% off. During the past quarter, we added Clear Channel Communications (CCU) and Xerox Corporation (XRX) to our portfolios. Clear Channel owns more than 1,200 independent radio stations across the United States; has a dominant position in the outside advertising market (i.e., billboards, etc.); and is an increasingly prominent owner of live entertainment venues (e.g., stadiums and theaters) and sponsor of live entertainment events. As economic activity increases, CCU is well positioned to benefit from corresponding increases in local and/or national advertising. And CCU's live entertainment division should benefit from increased attendance at concert and other live events as consumers begin to increase their discretionary spending in a recovery.

Xerox Corporation (XRX) is one of the most recognized companies in America. Until recently, however, it had become one of the worst managed. Among other things, an insular corporate culture, poor sales management and lack of product innovation in the face of new imaging technologies left Xerox a weak competitor against its nimbler and more creative rivals Canon and Ricoh. Questionable accounting for multi-year lease revenues led to an SEC investigation, a \$10 million fine and a restatement of earnings dating back to 1997, and left Xerox's stock price down more than 80% from its former highs. Analysts questioned whether Xerox would survive. In response, Xerox replaced its top management, shed non-strategic assets, reduced payroll expenses dramatically and reorganized and re-incentivized its sales teams. With a re-focus on its core competencies and a reduced cost structure, Xerox reported positive earnings this quarter for the first time in over a year. We believe the price of Xerox stock has room for substantial appreciation as the broad market begins to recognize the company's revival.

One stock on which we have been wrong is Bristol Myers (BMY). We purchased Bristol after the Food and Drug Administration delayed approval for Erbitux, the potential blockbuster cancer drug that BMY was developing with biotechnology firm ImClone. Subsequently, Bristol announced that another of its potential blockbuster drugs, Vanlev, was not significantly more effective than existing medications. Several days after that, BMY disclosed it had induced drug wholesalers to buy advance quantities of other BMY drugs, thereby inflating current earnings at the expense of future earnings. At the same time, ImClone came under federal investigation; its co-founder was arrested for fraud and insider trading; and the story made the tabloids as Martha Stewart came under scrutiny for selling her ImClone stock just prior to the announcement about Erbitux. At this point, Bristol Myers has gone from being a premier pharmaceutical company to

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a floundering giant with a weak pipeline and poor management. Its strong sales force and stable of existing drugs make it a potentially attractive acquisition for an overseas drug company that seeks to improve its product mix and distribution capabilities in the United States. And so we will hold Bristol Myers as a takeover candidate for a short while more.

For clients with mutual funds, we seek managers with rational and consistent investment strategies who have proven to be top quartile performers over multi-year periods. Our search covers various investment sectors (e.g., large, small, domestic, international, etc.) and styles (e.g., growth, value, growth at a reasonable price, etc.). Given the breadth of the market drop this past quarter, most mutual funds had negative returns. Within that context, international funds and domestic small cap value funds performed better than other sectors and styles. Next came large cap value funds; growth funds large and small brought up the rear. For owners of mutual funds it is particularly important to remain patient. Funds tend to be style specific. When their particular segment of the market is "hot," they are hot with it; when their segment is cold, they are cold. Keep in mind it was little more than two years ago that this year's last place growth funds were leading the pack with triple digit gains. Conversely, the small cap value funds that are winners this year were losing money in 1999 and early 2000 while their growth counterparts rocketed off the charts. We have maintained an overweighting towards value style funds for all of our client portfolios and will continue to do so for the foreseeable future. However, as always, we will maintain exposure to all types of funds, for ultimately it is the manager's skill that we seek and not the asset class in which the manager operates.

At MJB Asset Management we invest in the same stocks and funds as all of our clients, and understand the increased levels of frustration, anxiety and anticipation that many investors have felt over the past couple of years. Much of it can be traced to a feeling that we cannot control the markets. Combined with a prolonged market decline, that feeling can create an overwhelming temptation to pull out. Yet these market movements provide us with enormous opportunities to execute long term investment plans by buying and/or selling mis-priced securities and adjusting asset allocations to take advantage of less expensive parts of the market. We remain optimists and excited by the opportunities and choices that this and all markets provide for long term investors.

Thank you for your continued confidence. We look forward to speaking with you about your investment portfolios.

Sincerely,

Richard Bregman