

MJB ASSET MANAGEMENT LLC

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January 31, 2004

Dear Clients and Friends:

What will the markets do this year? A recent newspaper article surveyed five prominent analysts – including strategists at Goldman Sachs and Smith Barney – for their views.¹ Two of the analysts expect the markets to increase by 20% this year; one expects a 12% increase; one expects a 4% increase; the fifth expects an 8% decline. One advises to “stop chasing stocks of cyclical companies;” another advises to “hold onto stocks of cyclical companies.” Three advise that interest rates will rise; one says the rise will hurt stock prices, while two say it won't.

Such predictions are nothing more than guesses. The future is unknown; the fact that five well-known market professionals offer such contradictory views demonstrates the absurdity of the exercise. At MJB Asset Management we prefer to focus on what is known as opposed to guessing about what is not. We observe the markets, economic conditions and the world around us; develop investment strategies that reflect current conditions; and integrate the strategies with each of our clients' unique goals and circumstances to create individualized investment plans. When markets and/or client circumstances change, we adjust our strategies and client portfolios accordingly. We call this “investing in the moment.” It keeps us from getting locked into “predictions” about the future, and provides us with flexibility to make changes as the future becomes the present.

At present, we remain in a jobless recovery. The U.S. economy grew 8% in last year's third quarter, and appears to have grown again in the fourth quarter.² Yet this growth produced virtually no new jobs. Domestic manufacturers have been shedding jobs for decades. But now service jobs are starting to go, as technology enables firms to reduce back office staff and/or move technical jobs to lower wage locales.³ Layoffs continue⁴ while utilization rates remain at three quarters of capacity. Absent new jobs, the economy cannot kick into full gear. As a result,

¹“On the Street, Optimism Prevails for Stocks Through 2004,” *New York Times*, January 2, 2004, p. C14.

² Here again, the folly of “predictions.” Economist expected 5% growth; the actual numbers came in at a “disappointing” 4%.

³ Two experiences illustrate this point. (1) I recently visited an orthopedist for x-rays after injuring my hand. Unlike older x-ray machines that use film, this machine created a digital picture of my bones that emerged from a printer in the next room, and could have been transmitted electronically to a printer anywhere in the world for review by a radiologist. (2) Several weeks later, I called Dell tech support twice for my office computer. Both times, I was connected within minutes to Dell technicians -- one in the Philippines, one in India.

⁴ Eastman Kodak recently announced 15,000 layoffs; Kraft Foods announced 6,000 layoffs.

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the Federal Reserve has kept short term interest rates low to encourage growth; the bond market has kept longer term rates low as long as inflation remains subdued.⁵

But now, longer term rates are facing upward pressure from a different source -- the combination of federal income tax cuts and massive increases in military and homeland security spending. The tax cuts are an attempt to spur the economy and create jobs; the military and homeland security spending are not, but might have that effect. Either way, the combination has created an enormous budget deficit -- estimated by the Congressional Budget Office to be half a trillion dollars this year. The government will finance this deficit by borrowing from the public, which likely will push interest rates higher. Should the economy begin creating new jobs and higher wages, rates will likely increase further as bond investors begin to anticipate renewed inflation down the road. Should rates move up, most bond prices -- which move inversely to interest rates -- will drop. Stocks are also at risk. Higher rates eat away at corporate profits by increasing corporate borrowing costs and making it less attractive for consumers to buy on credit.

At current levels, we see discordance between stock prices and underlying economic fundamentals. Given this discrepancy, we took advantage of substantial price increases to trim positions in Intel, IBM and Texas Instruments for clients with individual stocks last quarter. We also trimmed McDonalds after the discovery of a cow in the U.S. food chain infected with mad cow disease. For clients with equity mutual funds, we continue to favor "value" strategies that preserve principal over more volatile "growth" strategies. We also continue to invest in funds that pursue alternative strategies with low correlations to the movements of the general stock market, including the Merger, Gabelli ABC and Hussman Strategic Growth funds.

For clients with bonds and/or bond funds, we have moved to shorter maturities to protect principal as domestic interest rates rise. We also have kept positions in high yield bonds, which already have high interest payments and are less likely to drop as rates rise. To diversify away from the U.S. bond market, we are adding positions in the Pioneer Strategic Income Fund, which selectively invests in less expensive bonds overseas. We will maintain this strategy until we see evidence that interest rates in the U.S. are leveling off.

Thank you for investing with MJB Asset Management. As always, we invest side by side with all of our clients in the same stocks and funds. We look forward to discussing your portfolios and investment goals.

Sincerely,

Richard Bregman

MJB Asset Management is registered with the Securities and Exchange Commission. We are happy to provide you with a copy of our most recent SEC Form ADV upon request.

⁵ The Fed controls short term rates. Supply and demand in the bond market determines longer term rates.