# The Wall Street Wish List Edition # 2

By Brady Willett & Todd Alway
Wish List 2002, December 26, 2001.

**None of the following pages should be taken as direct investment advice. We the producers are private investors, not professional investment advisors. Please make your own final investment decisions.**

**Preface:**

## Something Happened On The Way To The Bull Market Pen

Heading into 2001 expectations were high: Greenspan told us that the inventory glut was showing signs of correcting and that demand could soon pick-up, Abby said that the S&P would rise by 25% by year's end, and Bush & Company proclaimed that looming tax cuts would enable the consumer to spend, spend, spend. Suffice it to say, none of these things occurred as prescribed, and each party is still chanting their mantras proudly: the inventory glut continues to correct, the S&P 500 will rise in 2002, and consumers need not worry since more tax cuts are coming…

Beyond these 3 false prophets rests an even bolder speculation: after 11 Fed cuts the economy must soon rebound by default. While we do not disagree that the economy could soon rebound, it is the specific focus by many investors on previous monetary interventions that is troubling. The fact is, rate cuts do nothing more than lower interest rates. They do not absolve debt principle, force consumers to spend, or guarantee that economic conditions will improve.

In fact, as the Japanese case demonstrates, 'things' may get better or worse independent of interest rates. Rather, what is most important for economies and businesses is not interest rates per se, but the efficient allocation of capital. For instance, lower interest rates do not transform risky business practices into sound ones. Lower interest rates do not determine the utilization rate of embedded capital: demand does. Lower interests rates that are spun into capital to repurchase corporate shares do not determine how effective these initiatives are: the stock market does. Lastly, when debt loads are at record levels, personal savings are near all time lows, and increased corporate leverage is deemed "risk management", you get what we had last year: a low interest rate environment where there is a record amount of corporate and personal bankruptcy.

The fact is, the projected interest rate environment of 2002 needs to be framed in the context of the historically unprecedented borrowing binge of the 1990s. Ironically, hopes for an imminent economic rebound are based upon more borrowing and consequently more debt, not a change in the business practices that led to this mess in the first place. The interest rate on money may be low, but the cost to the economy of more borrowed capital, as 2001 will attest to, is high. The bulls will have difficulty charging back to the pen so long as they are yoked to the debt of the past.

## Stocks Are Inherently Risky, But Some Risks are Riskier Than Others

Warren Buffett, heralded by most as the greatest investor of all time, provided evidence that the face of the insurance industry has forever changed in light of the atrocities of September 11. We touch on Mr. Buffett's words to begin this year's report because we feel that they are helpful to the prudent investor:

*Only accept risks you are able to properly evaluate (stay within your circle of competence) and confine your underwriting to business that, after an evaluation of all relevant factors, including remote loss scenarios, carries the expectancy of profit.*

Warren Buffett, November 9, 2001
http://www.berkshirehathaway.com/qtrly/web1101.html

We feel that the same logic Mr. Buffett uses to guide the business of insuring must also guide the business of investing. Crystal ball momentum strategies or premonitions of a future technology which may be significant 20 years from now may be sufficient strategies for an investment industry with a vested interest in generating trading volume, but they are strategies based upon an unquantifiable element of risk. When investing is the goal, knowledge is the key. If it cannot be calculated, it cannot be known. How does one calculate where investing sentiment and momentum will lie two years from now? Given all the variables, who knows which internet business-model will gain a foothold 20 years into the future? Better yet, which companies within these unproven sectors will generate capital, disperse opportunities, and make money for the investor?

Even in brick and mortar businesses, unforeseen risks and industry blow-ups can occur from time to time; be it the shocking string of lawsuits knocking out companies related to 'asbestos', the lingering industry weakness that befell Bethlehem Steel, or the accounting trickery from Chainsaw Al that turned once powerful Sunbeam into an unviable stock. What emanates through each of these examples of corporate failure is the theme that <u>all</u> stocks carry risk.

That there is great risk in buying stocks should not come as a surprise. However, some risks and conversely some opportunities are more quantifiable than others. In our opinion, surface warnings in today's market include historically high valuations, instances of deep price wars developing in chip, auto, and grocery stocks, and ominous industry obsolescence trends. Additionally, there are countless other surface warnings which we will touch on in this report.

In terms of opportunities, companies with free-cash-flow, steady-to-strong return-on-equity, low premiums to solid assets, high quick ratios, low debt/equity levels, and in some cases, solid dividend rewards, offer to reduce the risk and may offer a positive destination for capital.

To this end, we aspire to turn the Wish List into a tool that can help you in making sound equity decisions by taking note of surface warnings and specific investment opportunities. The Wish List is not a cure for corporate unpredictability, nor is it a crystal ball whose vision is perfectly clear. Rather, and in light of Mr. Buffett's astute comments, we hope to offer a method which will assist in deciphering the corporate marketplace.

## <u>Recap of 2001 Wish List</u>

The last thing we want to do is make this introduction sound like a letter to shareholders. Rather, we will skip the 'we did a great job last year' innuendos and start off by saying that we did not expect, and we were certainly shocked as to how well last year's selections performed. No stock market investor in history can boldly claim that 50+% in any given year was planned for let alone take credit for such fantastic gains. That said, we were confident heading into the year that we were *investing in quality companies that carried a leadership role within their perspective industries*. That the end result was an immediate rise in all of our selections has been an added bonus.

Here is a brief breakdown of the eight companies we selected last year, and our opinions on each going forward. Refer to the 'what's new' section at www.wallstreetwishlist.com for further specifics on each company.

**<u>Correctional Properties:</u>** When we sold CPV on June 30 we believed it was paramount to secure the already fantastic gains rather than speculate that investors would continue to find appeal in CPV's somewhat risky dividend yield. We use the term 'somewhat risky' loosely as we feel that the company's leveraging and investment initiatives could prove dangerous. However, to date they have not.

Everything came together for the company in the 3Q01 – earnings were up, no immediate setbacks were reported from acquisitions, and they raised the quarterly dividend rate to 0.375 dollars. In hindsight, we ended up selling CPV too early.

**Stewart Enterprises:** We had liked Stewart for some time, and we were shocked at the roaring reception investors gave its share price in 2001. However, despite the *beginnings* of asset sales to pay down debt, Stewart by no means released material events that would support its share price rise. Rather, we think that investors latched onto its 'undervalued' story, and sent its share price into the stratosphere. Fueling the buying rampage was a Wall Street upgrade, and a solid bout of refinancing.

We do not feel that we sold Stewart too early, primarily because we cannot figure out why its share price kept rising after we sold. To be sure, revenues are stable yet dropping slightly, funeral margins are in steep decline, and more asset sales are needed. We feel that Stewart's 'undervaluation story' is over for now.

**ICU Medical:** ICU is another company we have liked for some time. However, due to what we felt was creeping overvaluation, we sold on June 26, 2001. Although we cannot comment on why ICU's shares are trading at a greater premium to ROE and earnings today, we do know that their CLAVE product is still superior to others, and affiliations with B.Braun continue to yield positive results. We are sincerely happy that we ran across ICU Medical back in early 2000 – not only because the company has outperformed all of our expectations, but because the Clave product is reminiscent of other great products and companies such as Coke and McDonalds. Placing all other aspects of investing aside, finding the excellent Clave product was all that mattered: when a truly superlative product or company is born it will gain marketshare, splinter old industries into new ones, and reward the investor handsomely. Melodrama aside, the Clave is such a product.

Our only fear in owning the stock today is near term valuations, the possibility of competition, or problems with B.Braun affiliations.

**HRP Properties:** On July 5 we said that 'HRP remains on the list but we think its share price may be nearing its momentum potential.' Suffice it to say; although we are not clairvoyant, HRP has slid ever since. While we are somewhat disappointed by the lack of momentum in HRP's stock price, we are not surprised by the company's ability to post stable operating results. That said, with the weakened business environment, HRP was removed from the Wish List on December 13, 2001. We feel that the company faces near term challenges as lease prices continue to drop in key areas.

**Barrick:** Although we pride ourselves on being long term oriented, we proved to possess a keen eye in selling Barrick on May 16. Since we disposed of Barrick, its share price has floundered miserably. During a year where gold did very little and Barrick was buying out companies, we feel confident that we stretched this investment to its maximum potential. Even so, we would still happily be holding Barrick if its share price had not spiked, and it may again be reaching attractive levels.

**Franco-Nevada:** We took Franco-Nevada off of the Wish List on Friday December 21, 2001. Our opinion of the company did not change in 2001. Rather, we felt that there was the risk that the proposed takeover by Newmont might fall through and/or the takeover price might slip prior to Feb 15, 2001 (takeover date).

**Meridian Gold:** Meridian remains on this year's list**.**

**Deswell Industries:** Deswell remains on this year's list.

While the above material represents a brief recap of last year's selections, later in the report we will be going into more detail on those companies that remain on this year's list.

## Introduction To The 2002 Wall Street Wish List

After finalizing our research this past week, we do not believe that there are many instances of severe undervaluation in the marketplace today. In fact, it took countless hours of research and many dead ends before we arrived at those stocks which did make it onto the list. Furthermore, the bulk of the companies that we like most are overvalued in terms of their current stock price. However, they do offer tempting targets for reevaluation should their stock price decline.

Quite often we will use the term 'overvalued'. There is no one measure we use to come to this conclusion. Rather, it is fashioned from our perceptions of the company, its fundamentals, and its relationship to the marketplace. This perception is grounded on the notion that a company trades with realistic and traditionally sound valuations. For instance, we all know that Coke is a fabulous company. However, its valuation leaves much to be desired. Coke trades with a PEG ratio of 2.45 (more than double the maximum we set as our standard). Furthermore, Coke trades at over 10 times book value and nearly 6 times sales; high by historical standards, especially for company of Coke's size. The dichotomy with Coke is that while indeed it is a great company, its days of rewarding shareholders with outsized gains may be over

With this in mind, we are particular in what we deem as 'undervalued'. Essentially, this means that we are attracted to companies that have strong ROE, a low debt burden, and a competitive corporate vision. When clarity and consistency is discovered within these three areas (more often than not), all other factors become increasingly more manageable. Furthermore, we try and find companies that are being misappraised by investors because of the onset of negative news, or unjustifiably negative perceptions surrounding the company. When such pressures develop on a stock, given that ROE, debt, and vision characteristics remain clear, the greatest opportunity is presented to the investor.

This is not to say that we will never buy a company that contradicts one or more of these factors, but that these measures provide the most consistent starting point in locating value.

Unlike last year, when many REITs carried high dividend yields and limited risk, most company shares have appreciated – thus, generally lower dividend yields and greater risk is now the theme. Likewise, many of the best gold companies have risen, tobacco stocks have rallied, and healthcare stocks are still overpriced. Suffice it to say, we believe that today's market offers less opportunity than last year's, and we think that the equity investor would do well to beat the yield on 30 year Treasuries in the upcoming year. This pessimism aside, we carried similar cautious notes last year and, as it turned out, our tepidly 'undervalued' selections roared.

Our sectoral opinions have not wavered much since December 26, 2000: we still think that the financial sector carries too much risk and too great a premium to forward earnings, we still believe that most consumer non/cyclicals are overvalued, and we still believe that while technology stocks may lead us out of the recession, their valuations remain catastrophically high. Exactly how the tech industry can be more overvalued today than when the Nasdaq was above 5,000 has to do with a steep decline in earnings across the board, and the partial recommencement of generally accepted balance sheet practices which eliminated many of the "intangibles" which companies counted as assets. As an example of the euphoria still present in tech stocks, on December 10, 2001 the tech sector carried an average P/E of 50, and an average ROE of 6%: these are, respectively, the highest and lowest readings of the 11 sectors we track.

However, while undervaluation is not running rampant, there is some optimism that can be fashioned. In particular, the transportation sector continues to near fair value and could potentially be a strong area in the near future, after global recession abates. To this end, we have examined a number of transportation industries and mapped out leadership. Furthermore, we have interrogated Tobacco, Alcohol, and Gold companies: areas of the marketplace that historically offer greater downside protection during uncertain economic times.

We have focused our attention on a greater array of industries and stocks this year, many of which did not make the final cut on this report. To be sure, we looked at more than 2000 individual companies: a daunting task that we hope will reap significant rewards in the future. However, even with this broadened scope we have selected fewer companies to buy this year (7 total). That said, we feel our reevaluation list of 13 companies will prove to be valuable over the next 12 months.

With these things in mind, the lists remain in much the same pattern as last year's. In terms of its layout, following a brief discussion of small cap versus large cap stocks we will go over our 7 selections; those stocks that have been selected as this year's recommendations. These are the stocks that we feel will reward the prudent investor. The sections following this highlight some of the relevant research findings in other industries along with our reevaluation picks and their prospective targets. In the final section we will recap both our primary recommendations and our reevaluation picks.

There are many investment terms and formulas used in our Wish List. While we take it for granted that everyone knows and fully understands what each of these mean, you can access the Wish List's Investor Resources page for further explanation. Click 'Introduction to Financial Statements', a guide that may help any investor beginners.

As always the initial data we use is from internet sources: it can be highly manipulated by accounting tricks or false internet calculations. When we zero in on specific companies, we calculate financial statistics using audited financial documents. There is no guarantee that any internet generated data is correct. Likewise there is no guarantee that our data is any more reliable. In sum, we have done our best to ensure that the data sets are valid, but errors are always possible. Please do your own research.

Listed below, are some of the general resources used in compiling the 2002 Wish List. Additionally, following each industry discussion specific resources are listed.

| **General Resources** | |
|---|---|
| http://www.hoovers.com/ | http://www.sec.gov/info/edgar.shtml |
| http://quote.yahoo.com/ | http://www.edgar-online.com/ |
| http://www.morningstar.com/ | http://www.kiplinger.com/ |
| http://www.moodys.com/ | http://www.marketguide.com/ |
| http://www.standardandpoors.com/ | http://www1.firstcall.com/ |

***   None of the information that follows constitutes direct investment advice.  Please make your own final decisions.**

*In order to gain knowledge of a specific industry we align the competitors within that industry, discover which companies are trading at the highest/lowest premiums, and hopefully determine the significance of their relative positions. However, this year we will begin first by peering into the prospects that different market-caps offer*

## Small Cap Focus

Companies Selected: 0    Reevaluation Targets: 1

To begin with, our focus was guided by the basic notion that smaller stocks appreciate more than other groups of stocks when the economy comes out of recession.  Moreover, we wanted to find companies that have already mapped out a success story and intend to draw on these achievements in a highly predictable manner in the future.  That said, it is worth noting that as an asset class U.S. 'small caps' outperformed all areas of the global marketplace in 2001.

### Forbes 200 Best Small Cap Stocks

In its methodology, Forbes states that *"The median 2002 estimated P/E of the 200 Best Small Companies is 18, about the same multiple as the average S&P500 company, even though smaller growth companies typically trade at much higher P/Es than the large caps."*  Actually, if Forbes had looked at the S&P 500 at the time, its P/E was trading with an average of 22 (markedly more than 'the same'). Additionally, since the mid-1980s large cap stocks have continually possessed higher P/E multiples than their smaller counterparts.  This is primarily because Wall Street focuses its attention on larger more liquid companies, a greater amount of indices (and thus funds) track larger stocks, and many newer investors, at least on some basic level, seem to equate the word 'size' with 'less risk'. These are important points for small cap enthusiasts to remember.

Above all else, we were disappointed with the Forbes list because of the 200 companies Forbes selected only 44 had *any* insider buying in 2001.  If these are really the best 200 small cap companies to own then why do employees and management not feel likewise?   Moreover, this number is artificially high when considering that we had to include companies such as QLGS in our breakdown (a mere 55 shares bought back in January). Needless to say, we are more attracted to companies where insiders are confident of the future and buying shares rather than selling at every waking moment.  This was not the case in most of the Forbes 200 companies. Rather in most instances insiders were jumping ship with abandon.

These complaints aside, we mention the Forbes list only because it enabled us to discover a few companies we did like.  Here is a listing of the companies we believe have some long-term appeal to the investor.  While we did not select any of these companies for the final recommendation list, we have quarantined these stocks to a 'small cap reevaluation list' to be reexamined on a quarterly basis.

**<u>Forbes 200 Best Small Cap Stocks - Top 17</u>** **Wish List 2002**

Data as of November 28, 2001

| ROE | Company | Sym | $ | P/E | P/B | D/E | Focus |
|---|---|---|---|---|---|---|---|
| 59.2 | Dynacq International Inc. | DYII | 21.9 | 38.49 | 13.52 | 0.02 | Healthcare |
| 25.68 | Suprema Specialties | CHEZ | 13.68 | 8.69 | 1.69 | 2.71 | Cheese |
| 23.64 | American Woodmark Corp. | AMWD | 44.51 | 14.39 | 3.07 | 0.16 | Kitchen cabinets |
| 22 | Chase Corporation | CCF | 11.75 | 8.13 | 1.68 | 0.36 | Industrial products |
| 20.35 | Medical Action Industries | MDCI | 17.8 | 32.9 | 5.7 | 0.21 | Sponges & Towels |
| 18.44 | RehabCare Group, Inc. | RHB | 23.93 | 16.16 | 2.32 | 0.01 | Healthcare staffing |
| 15.2 | Ambassadors International | AMIE | 18.7 | 6.64 | 1.3 | 0 | Travel services |
| 14.44 | Met-Pro Corporation | MPR | 11.4 | 10.12 | 1.41 | 0.14 | Pollution control |
| 14.12 | IHOP Corp. | IHP | 28.23 | 15.12 | 1.95 | 0.78 | House of Pancakes |
| 13.8 | Movado Group, Inc. | MOV | 16.95 | 9.49 | 1.25 | 0.56 | Watches |
| 13.2 | National Dentex Corp. | NADX | 22.17 | 13.24 | 1.64 | 0 | Dental laboratories |
| 12.93 | Curtiss-Wright Corp. | CW | 43.4 | 11.52 | 1.39 | 0.07 | Aerospace products/services |
| 12.71 | Triumph Group, Inc. | TGI | 29.89 | 9.53 | 1.11 | 0.42 | Aerospace related |
| 12.33 | American Italian Pasta (Current) | PLB | 43.35 | 23.2 | 3.1 | 0.97 | Pasta |
| 9.98 | Mercury Air Group Inc. | MAX | 4.45 | 8.95 | 0.87 | 2.23 | Aviation services |
| 9.11 | Modtech Holdings, Inc. | MODT | 8.75 | 10.99 | 0.89 | 0.29 | Modular buildings |
| 8.01 | Robert Mondavi Corp. | MOND | 34.74 | 18.42 | 1.39 | 0.79 | Wine |

Of these companies, one in particular represents a tempting target: American Italian Pasta. We believe that PLB has the infrastructure, both with distribution giant Sysco and developing operations in Europe, to succeed in the future. While many of its competitors are announcing plant closures and/or reductions in production, PLB is looking to add further capacity in late 2002. This is attributed to the fact that PLB is a low cost pasta producer: 'low cost' is a favorable term for a company within any industry. The company continues to gain market share, reduce costs, and build upon its new and old brands.

*"…it is important to note that in times of economic uncertainty, consumers appreciate the versatility, low cost, and nutritional benefits of pasta."* PLB CEO

Despite Mr. Webster's contention, we do not think that the words 'recession' and 'pasta' are perfectly correlated with one other, but there does seem to be a strong relationship. Pasta is a readily available, low cost consumer staple. Where the consumer has less surplus capital available for "conspicuous consumption", pasta companies should fare well.

Our primary concerns with PLB are that acquisitions will continue unfettered, and that any drop off in operating efficiencies will embellish the negative impact of acquiring higher debt/equity levels. In their latest conference call the company is pleased to report that interest rates are 'low' and that this should enable them to acquire more rapidly. However, it is worth remembering that the pasta business is heavily dependent on commodity prices and government regulation. This means that margins are prone to uncertainty in Durum prices, and regulatory policies, both domestic and international, could hamper PLB's new production facility in Italy.

With these thoughts in mind, we think that the company's stock price is too high, and would wait until a drop to buy the company for the long term. Our compliments go out to Forbes for not making their comprehensive list of small caps totally void of investment opportunity.

| | |
|---|---|
| http://www.pastalabella.com/ | http://www.durumgrowers.com/ |
| http://www.sysco.com/ | http://www.ndwheat.com/ |
| http://www.ers.usda.gov/ | http://www.ilovepasta.org/ |

## Large Cap Focus

Companies Selected: 0   Reevaluation Targets: 3

Market caps aside, there are two basic differences between large cap and small cap stocks: liquidity, and exposure. Your typical large cap Dow 30 stock is exposed to countless mutual funds, indices, and analyst rankings, while your typical small cap company is not. That said, there are always exceptions to the rule. For instance, the American Italian Pasta Company has a higher institutional ownership as a percentage of outstanding shares than Razor King Pin Gillette.

Nevertheless, the problem when looking at large cap stocks is that when a company does have a distinctive leadership role, you have to pay absurdly high valuations. As such, when these inflated giants do run into troubles the downside can be that much more severe. For instance, with recent blow-ups and/or earnings disappointments in Enron, Kroger, and Merck, holding many of the large cap issues within these industries (energy, grocery, and major drugs) proved unwelcome. Point being, many large cap issues rise and fall based upon industry momentum, not fundamentals per se. Obviously the same is true with smaller stocks as well, but not to the same extent since valuations are not stretched as high.

With this in mind, the large cap issues are regularly argued to have a 'safe haven' appeal when the market becomes volatile. For example, take Gillette. Please. One prominent fund manager said on December 14, 2001 that Gillette was an excellent buy because *'selling razor blades is largely independent of economic growth.'* However, while this argument may provide a rationale for why Gillette as a business will continue to thrive in a recessionary environment, it artificially conflates that business model with Gillette's stock price. Gillette the business may thrive even while the stock price does not. Given that as of December 14 Gillette had a trailing P/E of 55, a PEG of 3.33, and P/B value of 15, at what price does a safe-haven bet turn into a crap shoot? The fund manager does not even attempt to quantify Gillette's stock price. Rather he pontificates that capital will always swirl around the big-cap market, never exiting for other opportunities. We do not agree that is this investing.

Suffice it to say, we like companies that have low P/Es (below 20), attractive PEGs (1 or less), and comprehendible book values (less than 15 is the obvious example).

To this end, we believe that many fund managers have recently purchased Gillette solely on the notion that opportunity did not rest elsewhere. We believe that such fund managers are speculating for quick returns on a momentum area of the market. The momentum area now in focus appears to be those large cap stocks that will not see earnings decimation over the next 12 months. We do not wish to participate in this type of investing. Are we unreasonable to quickly damn most large cap stocks? Perhaps**…**

*"The reasonable man adapts himself to the world. The unreasonable one persists in trying to adapt the world to himself. Therefore all progress depends on the unreasonable man."* George Bernard Shaw

In conclusion, we did select a reevaluation level on Gillette last year of \$19-\$25 a share. On April 19 Gillette sunk below \$25 for the first, and only time in 2001.

With this in mind, we have set targets on some of our favorite large cap stocks for 2002. While it will take a serious bout of selling for such targets to be reached, we feel these levels would provide investors with an excellent opportunity to purchase, or at minimum, reevaluate the situation.

| Company | Sym | Market Cap ($Bill) | Current Price $ | Target $ |
|---|---|---|---|---|
| Gillette | G | 35.6 | 33.73 | 25-28 |
| General Motors | GM | 26.4 | 47.46 | 37-38 |
| Honneywell | HON | 26.9 | 33.1 | 22.15 |

## From Wall Street To Bay Street

Companies Selected: 1   Reevaluation Targets: 0

### Staffing Companies

To begin with, over the long term use of the internet clouds the sector. It is possible to argue that the internet decreases the need for these firms: if an employer can quickly and efficiently search for prospective employees using a simple online database, why the need for a headhunter? As for popular internet job sites monster.com, and hotjobs.com, we feel that their online leadership role can easily be duplicated, while current valuations in these online companies are too extreme.

That said, when a staffing company builds a relationship with a business, this relationship can takes precedence over more direct means of obtaining talent. When a growing firm needs the best applicant, often they would rather have a proven authority find this employee than search internet databases themselves. We believe that this type of relationship will ultimately be incorporated into an internet platform in the future. However, this relationship will not be completely severed.

We turned our eye to Bay Street for one company: Caldwell Partners International Inc. The company is an executive staffing services company that has been throttled by the global bear and may be undervalued.

**Caldwell Partners International Inc.**

| | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|
| Net Earnings | 2114 | 2851 | 3986 | 4164 | 5308 | 6439 | 5310 | 4032 | **778** |
| As a % of Revenues | 18.52 | 19.43 | 21.01 | **20.05** | 21.70% | 22.54 | **20.3** | **17.53** | ****3.41** |

** From unaudited 4Q01 number.

**Caldwell Partners International Inc.** — **Wish List 2002**

| Year-End Aug 31 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 Unaudited |
|---|---|---|---|---|---|---|
| Shareholders Equity | 22856.2 | 24656.1 | 27321.7 | 26034.9 | 22379.9 | ***19,919.1** |
| Cash-Flow | 2423.1 | 9977.9 | 674.5 | **-3888.4** | **-4885.3** | ***-2,872.01** |

* These numbers are neither audited, nor unaudited. Results due out in early 2002.

Caldwell has solid relationships with many prominent Canadian companies. Although the company has experienced some recent earnings setbacks and restructuring charges, we feel their standard of excellence will keep the company afloat. As well, we like the fact that the company is not leveraged and has little near-term financial risk: they have 94 cents a share in cash (roughly $1.24 when including securities), and no long term debt (according to company representative Kevin Hall, who was contacted as recently as December 21, 2001). The company currently trades for $1.14 CND.

Furthermore, on November 12, 2001 Caldwell issued a normal course issue bid to buy back 1,000,000 of its Class A (non-voting) shares. This represents roughly 8.2% of the public float. The company has 13,188,001 Class A shares outstanding, of which insiders hold 922,888, and 3,814,738 Class B shares of which 81.3% are held indirectly by CEO C. Douglas Caldwell. Lastly, J.C. Clark Ltd made a purchase of 1,085,100 Class A shares on November 29, 2001, and now owns 19.17% of the outstanding Class A shares for investment purposes.

In the statistics below are U.S. traded staffing firms and their basic valuations. In our opinion none are quite as attractive as Caldwell. With insiders entrenched, a normal course issue bid in place, and cash supplies strong, Caldwell is a rarity among staffing companies.

**Staffing Companies (from Business Services) - As of December 14, 2001**

Second to 'Schools' for highest average P/B average within the 25 Services industries.

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| **-11.2** | **Caldwell Partners International*** | **CWL.a** | **1.14** | **28** | **0.85** | **0** |
| 270,324 | TEAM Mucho, Inc. | TMOS | 4 | | 1.7 | 0.5 |
| 138 | AMN Healthcare Services | AHS | 25 | 275.2 | 8.6 | 1.6 |
| 78.8 | Right Mgt. Consultants | RMCI | 17.9 | 17.5 | 3.9 | 0.6 |
| 64.8 | Stratus Services Group | SERV | 0.9 | | 1.4 | 2.3 |
| 43.8 | Cross Country, Inc. | CCRN | 27.6 | 70.5 | 5 | 1.4 |
| 24.8 | Resources Connection Inc. | RECN | 27.9 | 36 | 6.2 | 0 |
| 19.7 | TeamStaff, Inc. | TSTF | 5.6 | 33.1 | 2 | 0.2 |
| 16.5 | Joule Inc. | JOL | 1.4 | 8.3 | 0.6 | 0.5 |
| 6.5 | TMP Worldwide Inc. (advertising) | TMPW | 41.5 | 69 | 3.8 | 0.06 |
| 2.7 | Adecco SA | ADO | 13.7 | | 8.6 | 2.1 |
| 1.9 | Staff Leasing, Inc. | GVHR | 2.2 | | 0.7 | 0 |
| 1.7 | Carlisle Holdings Ltd. | CLCH | 2.2 | | | |
| -5.2 | Manpower Inc. | MAN | 33.2 | 16.8 | 3.2 | 1.1 |
| -7.6 | Kelly Services, Inc. | KEYLA | 20.4 | 18.7 | 1.2 | 0.1 |
| -8.2 | On Assignment, Inc. | ASGN | 22.1 | 27.1 | 4.6 | 0 |
| -8.2 | Labor Ready, Inc. | LRW | 5.7 | 23.6 | 1.9 | 0.1 |
| -10.7 | COMFORCE Corporation | CFS | 1.1 | | 0.3 | 2.9 |
| -11.5 | Volt Information Sciences | VOL | 15.6 | 25.7 | 0.9 | 0.6 |
| -12.7 | Ablest Inc. | AIH | 4.6 | | 0.7 | 0 |
| -14.9 | RemedyTemp, Inc. | REMX | 13.2 | 14 | 1.2 | 0 |
| -16 | Professional Staff Plc. | PSTF | 2.5 | | 0.3 | 0.1 |
| -16.7 | Robert Half Int'l Inc. | RHI | 26.4 | 30.9 | 5.9 | 0 |
| -16.9 | Headway Corporate Res. | HEA | 0.4 | | 0.1 | 1.6 |
| -17.7 | Westaff, Inc. | WSTF | 2 | 7.3 | 0.4 | 0.4 |
| -18.3 | Diversified Corporate | HIT | 1 | | 0.2 | 0.7 |
| -18.8 | CDI Corporation | CDI | 20.2 | | 1.2 | 0.1 |
| -19.2 | Modis Professional Srvcs. | MPS | 7.3 | 38 | 0.5 | 0.1 |
| -19.8 | SOS Staffing Services | SOSS | 1 | | 0.2 | 0.6 |
| -22.5 | Personnel Grp. of America | PGA | 1 | | 0.1 | 0.6 |

*Caldwell statistics are estimates that take into account financial degradation since 3Q01.

| | | | | | | |
|---|---|---|---|---|---|---|
| -25 | HotJobs.com (computer services) | HOTJ | 10.7 | | 3.43 | 0.02 |
| -25.7 | Kforce, Inc. | KFRC | 5.8 | 40.6 | 1.2 | 0.2 |
| -29.4 | Heidrick & Struggles Int. | HSII | 19 | | 1.3 | 0 |
| -33.6 | Spherion Corporation | SFN | 10.3 | 6.3 | 0.5 | 0.2 |
| -35.4 | General Employment Ent. | JOB | 1.3 | | 0.5 | 0 |
| -37.2 | Korn/Ferry International | KFY | 9.7 | | 1.6 | 0.3 |
| -71.5 | Workstream, Inc. (cs) | WSTM | 4.2 | | 7.4 | 0.21 |
| | Webhire, Inc. (software) | HIRE | 1.1 | | 0.8 | 0.27 |

While staffing companies will likely face many challenges in the future, we believe Caldwell has built an infrastructure that is worth more than their current assets. Once restructuring initiatives (layoffs/charges) are completed and/or when executive activity picks up, Caldwell will likely rise rapidly. In sum, this tightly held 31 year old business is not about to vanish, even though shareholders have suggested as much by recently sending its stock price below cash.

One caveat: Typically dividends equated to 90% of net earnings. However, clearly dividends should not come at the expense of undermining shareholder value: meaning since the company is currently depleting its store of cash to run the business, it should not embellish this trend during rough times by sticking to its dividend policies. As such, Caldwell is likely to cut or even end their dividend until their business conditions improve. That said, we believe that this news has already been incorporated into the share price. Audited 4Q01 results are due out near the end of January.

http://www.caldwellpartners.com/
http://www.sedar.com/
http://www.sedi.ca/

## Casinos & Gaming

Companies Selected: 1 Reevaluation Targets: 1

### Insider Score

The first thing that caught our attention with this group is that ‘insider trading’ would be better termed as purely ‘insider selling’. Not what you would expect from this industry when considering that most companies possess high margin rates, and insiders are sure to know in advance information pertinent to customer volume and revenue flows.

However, the reason why insider buying is not rampant may have something to do with exceptionally strong industry performance. Most companies that have posted positive ROE over the last 12 months have witnessed outsized share price appreciation. We would attribute this to investors’ recent desire to be in companies with tangible earnings, and the overall search for ‘value’ going on in the marketplace in 2001. That said, the industry is set to enter 2002 on a weak note following September 11.

**Casino & Gaming - As of December 21, 2001** **Wish List 2002**

Leading Equipment Suppliers **(bold)**

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| **95.9** | **International Game Tech.** | **IGT** | **67.4** | **24.1** | **16.6** | **3.3** |
| 66.8 | Ameristar Casinos, Inc. | ASCA | 24.2 | 21.7 | 9.9 | 14.2 |
| 48.1 | Argosy Gaming Company | AGY | 32.7 | 16.6 | 6.2 | 6.8 |
| **46** | **Multimedia Games, Inc.** | **MGAM** | **38.4** | **45.2** | **12.5** | **0.3** |
| 45 | Nevada Gold & Casinos | UWN | 3.8 | 12.8 | 4.2 | 1.5 |
| 36 | MTR Gaming Group, Inc. | MNTG | 14.9 | 21.1 | 6 | 1.2 |
| **32.1** | **Shuffle Master, Inc.** | **SHFL** | **14.4** | **23** | **6.3** | **0** |
| 25.3 | Penn National Gaming, Inc | PENN | 29.3 | 21.4 | 4.7 | 4.9 |
| 22.6 | Station Casinos, Inc. | STN | 10.9 | 11.6 | 2.5 | 5 |
| 13.7 | Monarch Casino & Resort | MCRI | 7.9 | 19.4 | 2.4 | 2.3 |
| 12.6 | Isle of Capri Casinos | ISLE | 13.2 | 18.5 | 2.1 | 6.3 |
| 12.4 | Century Casinos, Inc. | CNTY | 2.3 | 12.6 | 1.4 | 0.9 |
| **11.6** | **WMS Industries Inc.** | **WMS** | **19.7** | **22.5** | **2.4** | **0** |
| 11.5 | Aztar Corporation | AZR | 17.7 | 14 | 1.5 | 1 |
| 10.9 | Interlott Technologies | ILI | 4.4 | 13.9 | 1.4 | 1.4 |
| 9.9 | Mandalay Resort Group | MBG | 21.3 | 15.4 | 1.5 | 2.6 |
| 9.8 | Churchill Downs, Inc. | CHDN | 32.6 | 21.4 | 1.9 | 0.6 |
| 8.5 | Black Hawk Gaming & Dvlp. | BHWL | 11 | 13 | 1 | 1.5 |
| 7.1 | Lakes Gaming, Inc. | LACO | 6.3 | 5.2 | 0.4 | 0 |
| 4.1 | Boyd Gaming Corporation | BYD | 5.9 | 26.5 | 1.1 | 3.2 |
| 3.5 | American Coin Merch., Inc | AMCN | 8.2 | 51.3 | 1.7 | 1.6 |
| 2.9 | The Sands Regent | SNDS | 2.3 | 12 | 0.3 | 0.3 |
| 1.7 | Magna Entertainment Corp. | MIEC | 6.5 | 53.9 | 0.9 | 0.2 |
| -0.4 | Park Place Entertainment | PPE | 9.1 | | 0.7 | 1.4 |
| -0.5 | Harrah's Entertainment | HET | 36.1 | | 3.1 | 2.9 |
| -3.5 | Pinnacle Entertainment | PNK | 6.2 | | 0.5 | 1.4 |
| **-7.5** | **Paul-Son Gaming Corp.** | **PSON** | **1.1** | | **0.3** | **0.1** |
| -25.9 | Sun International Hotels | SIH | 23.7 | | 0.9 | 0.7 |
| -31.9 | Riviera Holdings Corp. | RIV | 4.2 | | 1.2 | 18.2 |
| -36.8 | Trump Hotel/Casino Resort | DJT | 1 | | 0.2 | 18.9 |
| **-40.3** | **Scientific Games Corp.** | **SGM** | **7.8** | | **13.6** | **17.9** |
| **-57.9** | **Mikohn Gaming Corporation** | **MIKN** | **7.6** | | **2.5** | **2.7** |
| -78.5 | Youbet.com, Inc. | UBET | 0.5 | | 0.5 | 0 |
| **-177.4** | **Innovative Gaming Corp.** | **IGCA** | **0.3** | | **1** | **0.3** |
| -234.8 | Alpha Hospitality Corp. | ALHY | 14.5 | | 10.2 | 0.9 |
| | **Alliance Gaming Corp.** | **ALLY** | **26.8** | **27** | | |
| | **Anchor Gaming** (takeover by IGT) | **SLOT** | **67.2** | | | |
| | Hollywood Casino Corp. | HWD | 10.6 | | | |

| Gaming Industry - Gross Gambling Revenue (bill $) | | | |
|---|---|---|---|
| **Year** | **Casinos** | **All Gaming** | **Casino % of Rev** |
| 1990 | 8.3 | 26.6 | 31.20% |
| 1991 | 8.6 | 27.1 | 31.73% |
| 1992 | 9.6 | 30.4 | 31.58% |
| 1993 | 11.2 | 34.7 | 32.28% |
| 1994 | 13.8 | 39.8 | 34.67% |
| 1995 | 16 | 45.1 | 35.48% |
| 1996 | 17.1 | 47.9 | 35.70% |
| 1997 | 18.2 | 50.9 | 35.76% |
| 1998 | 19.7 | 54.9 | 35.88% |
| 1999 | 22.2 | 58.2 | 38.14% |
| 2000 | 24.3 | 61.4 | 39.58% |

Casino Revenue Growth Since 1990: **192.8%**
Total Gaming Growth: **139.8%**

Source: Christiansen Capital Advisors, LLC    Wish List 2002

## The Companies

Just as Mr. Trump's company appears to have turned the corner to profitability, New York State is unveiling plans for the *"biggest expansion of legalized gambling in the state's history"*. Consequently, with plans for three new casinos in the Catskills and slot machines at racetracks, DJT's stranglehold on the competition could soon be reversed. As well, as more surrounding states push to expand their gaming industries, Trump concludes that such initiatives *'could lead to a tremendous erosion of revenue.'*

If only Trump had the cash… possessing a 0.965 quick ratio with creditors already on your back is not a good place to be in while gambling dollars are already tight, and countless new avenues will entice people to stop and gamble before they complete the drive to Atlantic City. A quick ratio, or 'acid test' is simply current assets (less inventories) divided by current liabilities. DJT does not pass (a reading above 1) this test.

Is this the end of Donald Trump? Let's just say that while there is the possibility that Trump Hotels & Casino Resorts, Inc. will go bankrupt, Mr. Trump is not likely to miss too many meals.

Casino and gaming stocks are not all as risky as DJT. Rather, there are many companies within the group that have low leveraged qualities (SHFL, WMS), and others that are embedded inside of niche leadership roles (CHDN). Conversely, those companies that simply run a bunch of casinos splattered across America, or the globe for that matter, are not as predictable as the aforementioned types of companies. The demise of once popular Riviera Holdings Corp will attest to this.

We like one company within the group: WMS Industries Incorporated. The company makes video gaming machines, and video lottery terminals (VLCs), lives by the mantra of 'no debt', and has consistently showed solid gains in return-on-equity. Furthermore, we like the fact that WMS makes branded games such as Monopoly and has interests in Survivor: games that by all accounts equate to higher margin levels for makers because of the progressive and enthralling themes they present to casino gamblers.

We like WMS now because a recent software glitch has hit the company's financials as well as its stock price. We feel shares are reflective of this negative alone, not necessarily the future opportunities the company owns.

| WMS versus IGT | | | | | Wish List 2002 | |
|---|---|---|---|---|---|---|
| **As a % of Revenues** | | **Sep-00** | **Dec-00** | **Mar-01** | **Jun-01** | **Sep-01** |
| Gross Profit: | WMS | 50.2 | 50.1 | 52.2 | 54.1 | 54.4 |
| | IGT | 48.1 | 48.9 | 47.9 | 41.4 | 45.3 |
| Operating Margin: | WMS | 24.6 | 24.5 | 27.3 | **-** | **17.1** |
| | IGT | 28.6 | 31.1 | 28.5 | 20.2 | 22 |
| Net Profit Margin: | WMS | 15.9 | 16.3 | 18 | **4.9** | **12.5** |
| | IGT | 16.4 | 16 | 15.5 | 17.7 | 18.8 |

As the statistics show, prior to the software problem in June WMS compared well to that of IGT – only following these problems have margins in the middle and bottom of the income statements been hit. That said, WMS still consistently beats industry leader IGT in gross profit margin – a number that tells us one of two things: 1) customers are willing to pay a higher price for WMS's products versus IGT, and/or 2) WMS is the more efficient producer of the two. Either or, consistently higher gross profit margins is appealing.

However, to reiterate, software glitches have hit the company. This becomes increasingly evident as you work your way down their financial statements beginning June 30, 2001: when middle and bottom line margin levels were struck a violent blow that is just starting to show signs of subsiding. Our contention is that when these problems subside there is no reason to believe that the company will not go back to being run as efficiently as before.

Without doubt IGT controls the equipment market (roughly 65% of American sales). However, IGT has a $4.9 billion market cap while WMS hovers around $650 million. Point being, IGT has a mere $20 million more in shareholder equity than WMS. What this means is that if you broke each company up and sold all their parts at book value after debt payments, you would receive essentially the same amount of money. Did we mention that IGT has a $4.9 billion market cap versus WMS's $650 million? Furthermore, did we mention that when you back out intangible assets from IGT, WMS is actually worth roughly $150 million more than IGT on paper???

Shareholder equity aside, the primary difference between the two companies is that one (IGT) strives for super growth at all costs, while the other is content to be financially prudent all the time. While we feel that both companies can survive in this growing industry, it is WMS's conservative financial practices that we admire, and IGT's leveraged balance sheet and lofty valuations that we do not.

| **<u>Casino Equipment Suppliers</u>** | | | | **Wish List 2002** |
|---|---|---|---|---|
| Insider buy/sell for 2001* | **Sym** | **Purchased** | **Sold** | **Outstanding (Mill)** |
| International Game Tech. | IGT | 0 | 887,537 | 72.9 |
| Multimedia Games, Inc. | MGAM | 0 | 332,727 | 6.05 |
| Shuffle Master, Inc. | SHFL | 600 | 552,500 | 18.1 |
| WMS Industries Inc. | WMS | 1,531,700** | 97,000 | 32.2 |
| Alliance Gaming Corp. | ALLY | 5,000 | 967,170 | 22 |
| Anchor Gaming | SLOT | 0 | 36,744 | 14.9 |

*Does not include any options activity.

**Purchases made by Viacom CEO Sumner Redstone. Mr. Redstone owns 29.99% of outstanding shares.

We are selecting WMS as our number one casino stock for 2002 and beyond. As well, we have listed 1 other company we are attracted to because of their niche leadership role.

| Company | Sym | Reevaluation Target |
|---|---|---|
| Churchill Downs Incorporated | CHDN | $27-$28 |

| | |
|---|---|
| http://www.wmsgaming.com/ | http://www.americangaming.org/ |
| http://www.igtonline.com/ | http://www.gamingfloor.com/ |
| http://www.ustreas.gov/ | http://www.casinocity.com/ |

| Consumer Non/Cyclical - As of December 18, 2001 | + | - | Last 30 Days |
|---|---|---|---|
| Beverages (Alcoholic) | | | 14.99 (1.22%) |
| Beverages (Non-Alcoholic) | | | 5.68 (0.66%) |
| Crops | | | 6.47 (0.72%) |
| Fish/Livestock | | | 1.00 (0.10%) |
| Food Processing | | | 3.06 (0.32%) |
| Office Supplies | | | 6.73 (1.06%) |
| Personal & Household Prods. | | | 4.16 (0.68%) |
| Tobacco* | | | 2.40 (0.30%) |

*Tobacco has the highest ROE and Dividend yield within the group

## Tobacco

Companies Selected: 1   Reevaluation Targets: 2

The risks in owning tobacco are all too apparent: court developments could take a chunk out of future profits, and increased government taxation could lead to higher cigarette prices, prodding more people to quit smoking.

These worries aside for the moment, every single Tobacco stock was up in 2001. This occurrence did not happen, to the best of knowledge, in any other group. Usually there is some laggard that spoils a perfect year: not so for Tobacco.

For those of you who read last year's report, you may be surprised that we now like DIMON Incorporated. To be sure, DIMON is trading with a set of higher premiums today than at the same time last year. However, we are attracted to the company now because of its recent corporate strategy to reduce debt loads.

**Tobacco - As of December 17, 2001** — **Wish List 2002**

More attractive than last year (Higher ROE, lower $, lower P/E, P/B, and D/E)
Less attractive than last year
Not Available

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| 144.6 | | | | | | |
| 75.8 | UST Inc. | UST | 34.7 | 12.2 | 12.7 | 1.9 |
| 50 | Vector Group Ltd. | VGR | 34.3 | 39.8 | 13 | 3.5 |
| 26.3 | Philip Morris Companies | MO | 47 | 12.4 | 5.1 | 1 |
| 26.1 | Swedish Match AB (publ) | SWMAY | 51.9 | 16.8 | 4.4 | 1.4 |
| 21.9 | Star Scientific, Inc. | STSI | 2.8 | 23.8 | 5.4 | 1.1 |
| 17.7 | Universal Corporation | UVV | 36.9 | 8.7 | 1.8 | 1.4 |
| 7.6 | Standard Commercial Corp | STW | 18 | 8.6 | 1.3 | 1.8 |
| 5 | DIMON Incorporated | DMN | 6.9 | 10 | 0.7 | 1.4 |
| | R.J. Reynolds Tobacco | RJR | 57.3 | 14.3 | 0.7 | 0.2 |
| | Imperial Tobacco Grp. PLC | ITY | 26.5 | 11.1 | | |
| | British American Tobacco | BTI | 16.6 | 15.4 | | |
| | Gallaher Group PLC | GLH | 25.8 | 10.2 | | |

**DIMON Incorporated** — **Wish List 2002**

| Year-ended June 30 (In Millions) | 1999 | 2000 | 2001 | Sept 30,01 (Unaudited) |
|---|---|---|---|---|
| Revenues | 1,815.20 | 1,473.60 | 1,401.00 | 288.70 |
| Net Income | **-7.59** | 17.99 | 24.89 | *3.9 |
| Total Assets Less Intangibles | 1,276.63 | 1,088.45 | 1,015.12 | 1,021.34 |
| Outstanding Debt | 1,074.70 | 863.4 | 770.5 | 877.21 |
| Total Debt/Tangible Assets | 84.18% | 79.32% | 75.90% | 85.89% |

*Includes derivatives charge of 9.602

To begin with, DIMON's recovery must be placed into the context of a financially fragile company. Despite bold claims from management that they have already been reducing debt loads, this is simply not the case. Rather, as the above statistics will attest, total debt as a percentage of tangible assets is higher now than when debt reduction initiatives began. Furthermore, it should be noted that debt reductions that correlate to reductions in assets and business volumes are more costly than those funded solely from operations.

These points aside, we like DIMON in 2002 because they have built a platform for recovery. The company has recently exited from non-tobacco related businesses, and is now focused solely on tobacco. Furthermore, hits to revenue and operating results from restructuring appear to be abating: operating margins have been drifting higher in the last two quarters (10.9% and 9.1% respectively versus 4%, 5.5%, and 6.5% in the three previous quarters), and without derivatives charges in the 1Q02 the company would have posted 25 cents in earnings (or $12.2 million in net income). This increase was attributed, in part, to different shipment times for product. This is a constant theme for DIMON: volatile quarter-to-quarter results. However, annual revenues remain quite predictable, being in and around $1.4 billion.

If DIMON continues to keep a stranglehold on costs, we would expect the company to earn more than current corporate estimates of 61-65 cents a share for year-end June 2002. A similar situation to that of DIMON can be seen in Standard Commercial from 1999 to present. STW was facing adversity and quickly turned things around to see its stock price triple. While we do not believe that DIMON has this exact potential, we see similarities in that both stocks were depressed below tangible assets before they turned things around. Furthermore, as DIMON begins to turn its business around, it is also orchestrating a round of refinancing.

The derivative charges DIMON reported in 1Q02 are non-cash, and are reflective of changes in the value of its derivatives on the balance sheet. The company uses interest rate swaps to balance the impact of global currency fluctuations. As Enron will attest to, there can be great risk in anything related to derivatives. That said, DIMON's exposure is not unusual given its various properties around the globe. DIMON is the second largest independent tobacco leaf dealer in the world (Universal Corp, and Standard Commercial are number 1 and 3 respectively.)

Besides DIMON, we will be looking to reevaluate two of our perennial favorites in this industry: diversified leader Philip Morris, and chewing Tobacco kingpin UST.

| Company | Sym | Reevaluation Target |
|---|---|---|
| UST Inc. | UST | Low 30s |
| Philip Morris | MO | 42 |

| | |
|---|---|
| http://www.dimon.com/ | http://www.tobaccoleaf.org/ |
| http://www.tobaccojournal.com/ | http://www.ustobaccofarmer.com/ |
| http://www.tobacco.org/ | http://www.ontarioflue-cured.com/ |

## Water Transportation

Companies Selected: 1 Reevaluation Targets: 1

The two companies that have outperformed over the last 12 months, as evidenced by high readings in ROE, are typically 'spot charter' companies. Essentially these companies have vessels that float around empty until they get a contract to move product. The spot market is essentially (not always) more volatile given that demand can, and recently has, fallen off.

In the statistics below we have sectioned the industry into 'spot', 'mixed', and 'time'. This is not to say that companies focused on the spot or the time chartered markets will not change their focus in the future. However, heading into 2002 this is a rough estimate of their respective focus.

**Water Transportation - As of December 10, 2001**

Note: Highest Dividend Yield within the 5 transporation industries

| ROE | Company | Sym | $ | P/E | P/B | D/E | Classification |
|---|---|---|---|---|---|---|---|
| 88.9 | Excel Maritime Carriers | EXM | 3.4 | 1.5 | 1 | 0.7 | **SPOT** |
| 44.8 | Frontline Ltd. | FRO | 8.8 | 1.4 | 0.6 | 1.3 | Primarily **SPOT** |
| 35.5 | Teekay Shipping Corp. | TK | 31.7 | 3 | 0.9 | 0.7 | **MIXED** |
| 35.2 | Newport News Shipbuilding | NNS | 68.3 | 22.5 | 8 | 1.6 | Nuclear/Navy |
| 33.5 | OMI Corporation | OMM | 3.4 | 2.1 | 0.6 | 1.1 | **MIXED** |
| 24.1 | Knightsbridge Tankers Ltd | VLCCF | 15.5 | 4.1 | 1 | 0.5 | **TIME** |
| 22.1 | Transportacion Maritima | TMM | 8.9 | 14.6 | 3.1 | 8 | Diversified - Mexico |
| 19.9 | Todd Shipyards Corp. | TOD | 8.5 | 4.6 | 0.7 | 0 | Shipyards |
| 18.3 | Overseas Shipholding Grp. | OSG | 22.3 | 5.5 | 1 | 1 | **MIXED** |
| 16.6 | General Maritime Corp. | GMR | 8.3 | 5.2 | 0.6 | 0.7 | **MIXED** |
| 16.5 | Stelmar Shipping Ltd. | SJH | 13.7 | 4.2 | 0.8 | 1.8 | Primarily **TIME** |
| 13.9 | Kirby Corporation | KEX | 26.9 | 17.1 | 2.2 | 0.9 | Inland tank barges and towing vessels |
| 11.1 | Alexander & Baldwin | ALEX | 24.6 | 12.7 | 1.3 | 0.5 | Diversified - Food, Real Estate in Hawaii |
| 10.7 | Tidewater, Inc. | TDW | 29.8 | 13.3 | 1.3 | 0 | Services the offshore energy industry |
| 10.4 | Maritrans Inc. | TUG | 9.6 | 11.1 | 1.1 | 0.7 | |
| 10.1 | Seacor Smit, Inc. | CKH | 41.8 | 13.6 | 1.2 | 0.5 | Marine services to the oil and gas exploration and production industry |
| 8.5 | CP Ships Limited | TEU | 10.7 | 9.4 | 0.8 | 0.2 | Primarily **TIME** |
| 7.7 | MC Shipping Inc. | MCX | 0.9 | 3.3 | 0.2 | 1.7 | |
| 5.3 | Conrad Industries, Inc. | CNRD | 5 | 18.7 | 1 | 0.1 | Shipyards |
| 1.9 | Stolt-Nielsen S.A. | SNSA | 13.1 | 35.6 | 0.6 | 1.5 | Transportation Services, Subsea Services and Seafood |
| -0.9 | Sea Containers Ltd. | SCR.A | 10.5 | | 0.4 | 3.3 | Leasing, selling, and repairing of cargo containers |
| -8.3 | Seabulk International | SBLK | 4 | | 0.3 | 4.3 | |
| -41 | Int'l Shipholding Corp. | ISH | 6.3 | | 0.3 | 2.6 | Primarily **TIME** |
| -52 | B&H Ocean Carriers Ltd. | BHO | 5.4 | | 1.2 | 1.3 | |
| -167 | Trailer Bridge, Inc. | TRBR | 1.4 | | 3 | 9.5 | Puerto Rico: Trucking/Marine Freight |
| | Nordic American Tanker | NAT | 13.6 | 4.5 | | | **TIME** |

**Global Leaders**

A.P. Møller (Denmark)

Peninsular and Oriental Steam Navigation (Europe)

Mitsui O.S.K. Lines, Ltd. (Japan)

Besides the purely shipment oriented companies, there are a host of other businesses: namely the building, refueling of battleships (NNS), running of shipyards (TOD), and maintaining of water based operations (TDW). We stayed away from these types of companies for two reasons: you pay a hefty premium for government related companies that deal with large scale projects even when those projects are awarded on an unpredictable basis. Furthermore, with marine services and smaller inland carriers, it is unlikely that these companies will, map out a niche leadership role during a sluggish economic environment. In sum, without the threat of industry consolidation, something we do not think will occur in the foreseeable future, this industry presents few opportunities.

Instead, we focused our attention of those companies that possess transparent shipping models due to their use of spot/time/bareboats charters.

After looking first at the spot/mixed players, we found no competitor that has a clear advantage within their focus area. As well, certain companies have taken additional leverage assuming oil/global shipments will increase in the future: a notion we do not necessarily agree with. As an example, OSG has on order four VLCC's (Very Large Crude Carriers), and four other vessels. While this company is clearly looking to grow in the future, it is uncertain that their success will translate into margin levels similar to those that the industry has achieved in recent years.

As for the purely spot players, EXM has 6 aging (pre-1983) ships, FRO has a newer fleet of around 40 but their business is highly volatile, and while TK boasts about 71% utilization rates as of July 2001 ('the highest in the industry'), demand for shipments has dried up.

As for the 'chartered' players, we have identified what we feel to be the most attractive company: Nordic American Tanker (NAT). NAT owns 3 Suezmax oil tankers, and holds 7-year charters with BP Amoco. Expiration is set for September 2004, and the company 'guarantees' $1.35 in dividends per year. We like NAT more than the comparable Knightsbridge Tankers Ltd (VLCCF) because their charters are for a longer period of time, they carry less debt to assets, and management fees are radically smaller. VLCCF's CEO Mr. Ola receives $750,000.00 annually to run Knightsbridge – this for running a company that seemingly does nothing but paperwork, given that all its ships are under charter until February 2001.

We fully realize that both NAT, and VLCCF have been spun off from larger players in order to keep friends happy and reduce insurance exposures to potential catastrophes. That said, we believe NAT does a better job for shareholders by keeping costs lower.

Below are our projections for Knightsbridge Versus Nordic:

| **Knightbridge Tankers LTD.** | | **North American Tanker Shipping LTD.** | |
|---|---|---|---|
| | **Projected Results** | | **Projected Results** |
| Outstanding shares (mill): | **17.1** | Outstanding Shares: | **9.7** |
| Current Price: | **$16.05** | Current Price: | **$13.21** |
| *Annual Base Revenue (mill$): | **39.72** | *Annual Base Revenue: | **24.09** |
| **Annual Total Expenses: | **12.75** | Annual Total Expenses: | **11.2** |
| Total Debt: | **125** | Total Debt: | **30.2** |
| Income Available To Common: | **26.97** | Income Available To Common: | **12.89** |
| Dividend Per share: | **$1.57** | **Dividend Per share: | **$1.32** |
| Current Forward Yield: | **9.50%** | Current Yield: | **10.22%** |
| *For 2002-Feb 2004. | | *For 2002-Sept 2004. | |
| **Management/related expenses, and interest on debt. | | **$1.35 minimum dividend per share. | |
| **Wish List 2002** | | | |

NAT can act as a fixed investment for the cautious investor that does not wish to simply hold cash. Just as last year we selected CPV and HRP largely for their dividends, so too do we now like NAT. Furthermore, as the charter rates creep above $22,000, there is the possibility that BP Amoco will be forced to pay a higher rate as per the contract (this has enabled the company to report significantly larger than base revenues in the past). We have no opinion on whether shipment rates will rebound. We like NAT regardless of this possibility.

The company owns 3 Suezmax oil tankers which typically average 25 years in life, and as older vessels come off the market, or demand picks up, there is the possibility of a renewal with BP Amoco or other parties. These 3 vessels carry a current book value of $47 million each, and come 2004 (based on amortization, the state of the market, and the condition of the vessels) these assets could vary from $70 million to $100 million. NAT currently has a market cap of $128 million, and $30 million in total debt: meaning even by the best estimates you are paying $58 million over 2004 book. We do not mind this risk given the current yield, and the fact that these vessels should be able to produce returns in some form or other beyond 2004. That said, we like NAT as a fixed investment in 2002, but perhaps not beyond. For the added risk of owning NAT instead of a 30 year Treasury you receive roughly double the return. If 2004 arrives and the global shipments market remains depressed, owning NAT could prove risky as they fight for 'spot' market revenues.

We would look to sell NAT after any spike in share price, or when better alternatives in the marketplace present themselves. We do not have a firm opinion on which direction the company's share price will point in 2002: we like the company for their quarterly distributions, and hopefully a stagnate share price. Please make your own decision.

| **Company** | **Sym** | **Reevaluation Target** |
|---|---|---|
| Teekay Shipping | TK | $26 |

http://www.uns.no/nat.htm
http://www.tradewinds.no/

## Oil/Gas Pipelines

Companies Selected: 1 Reevaluation Targets: 1

**~ Oil Well Services & Equipment - As of December 21, 2001**
**~ Oil & Gas Operations/ Integrated**
**~ Natural Gas Utilities**

**Companies that have some key 'pipeline' interests.**

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| 56.3 | Kaneb Services LLC | KSL | 18.2 | 6.8 | 5.8 | 8 |
| 43.6 | Mitchell Energy & Develp. | MND | 52.1 | 8.6 | 3.2 | 0.4 |
| 40.3 | PanCanadian Energy Corp | PCX | 25.5 | 6.2 | 2.7 | 0.4 |
| 40.2 | Ultramar Diamond Shamrock | UDA | 49.9 | 5.7 | 2.1 | 0.8 |
| 37.8 | Atlas Pipeline Partners | APL | 23.8 | 9.4 | 3.5 | 0.1 |
| 34.1 | Quicksilver Resources Inc | KWK | 18.2 | 13.6 | 3.7 | 2.6 |
| 32.3 | Shamrock Logistics LP | EDL | 39.4 | 8.8 | 2.5 | 0.1 |
| 31.8 | Kaneb Pipe Line Partners | KPP | 40.1 | 13 | 3.7 | 1.2 |
| 27.7 | BJ Services Company | BJS | 31.4 | 15 | 3.7 | 0.1 |
| 27.7 | Unocal Corporation | UCL | 34.8 | 10.7 | 2.6 | 0.9 |
| 27.7 | Enterprise Products Part. | EPD | 46.4 | 14.5 | 3.5 | 0.7 |
| 27 | TEPPCO Partners, L.P. | TPP | 30 | 13 | 3.3 | 3.4 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 20.2 | Buckeye Partners, L.P. | BPL | 37.2 | 14.8 | 2.9 | 1 |
| 19.5 | Enbridge, Inc. | ENB | 27.1 | 13.9 | 2.7 | 2.4 |
| 17.4 | Westcoast Energy Inc. | WE | 26.4 | 11.1 | 1.7 | 1.7 |
| 16.6 | Plains All Amer. Pipeline | PAA | 25.2 | 22.6 | 3.4 | 1.7 |
| 16.1 | TC Pipelines, LP | PCLPZ | 24.9 | 10.7 | 1.7 | 0.1 |
| 12.9 | TransCanada PipeLines Ltd | TRP | 12.6 | 14.1 | 1.8 | 1.7 |
| 12.4 | Delta Natural Gas Company | DGAS | 20.1 | 12.7 | 1.6 | 2.4 |
| 12 | Chesapeake Utilities | CPK | 19.5 | 13.5 | 1.6 | 1.3 |
| 11.4 | Northern Border Partners | NBP | 37.8 | 15.7 | 1.6 | 1.5 |
| 8.9 | Kinder Morgan Energy Ptnr | KMP | 37.7 | 24.9 | 1.6 | 0.8 |
| 5.3 | Enbridge Energy Partners, | EEP | 40.4 | 41.5 | 2.2 | 1.4 |
| 2.2 | El Paso Energy Partners | EPN | 36.8 | 367.6 | 8 | 1.7 |

When oil and natural gas prices rise, it does not take long before additional capacity comes online. For instance, in 2000, when natural gas prices skyrocketed the number of rigs immediately and rapidly began to increase. As a result, when economic activity and demand for energy products slowed this year, the added supply built into the system helped in depressing prices. These are pertinent considerations for most natural gas and energy companies. However, even as prices tumble and many poorly run exploration companies get crushed, product still needs to be piped to the customer.

Accordingly, we do not care to pontificate about future rig counts and micro supply/demand fluctuations. Rather, we took a long-term view of increasing demand trends, looked within four different industries, and mapped out pipeline exposure. To note: many energy exploration and production companies have pipeline interests as a part of their midstream and downstream business models. However, we stayed away from companies that did not produce the majority of their revenues from pipeline and related (terminal) activities.

**Wish List 2002 -- The Primarily Pipeline Players**

| Company | Sym | Focus |
|---|---|---|
| Atlas Pipeline Partners | APL | 12 Natural Gas pipelines (1,000 miles) - Eastern Ohio, Western New York and Western Pennsylvania. |
| Buckeye Partners, L.P. | BPL | Pipeline common carrier with various interests. |
| Chesapeake Utilities | CPK | Subsidiary Eastern Shore Natural Gas Company. 281-mile interstate pipeline system. |
| El Paso Energy Partners | EPN | Total midstream energy services. Quality assets. |
| Enbridge Energy Partners, | EEP | 99% limited partner interest in Lakehead Pipe Line Company. Primarily crude oil from western Canada to the United States and Ontario. |
| Enbridge, Inc. | ENB | World's longest crude oil and liquids pipeline system |
| Kaneb Pipe Line Partners | KPP | Pipeline/Terminalling. Kansas, Nebraska, Iowa, South Dakota, North Dakota, Colorado and Wyoming. |
| Kinder Morgan Energy Ptnr | KMP | 10,000 miles of product pipelines / 20 associated terminals. |
| Northern Border Partners | NBP | 70% general partner interest in Northern Border Pipeline Company |
| Plains All Amer. Pipeline | PAA | Crude oil pipeline/terminalling. California, Texas, Oklahoma, Louisiana, Illinois and the Gulf of Mexico |
| Shamrock Logistics LP | UDL | Refined product pipeline: Texas, Oklahoma, New Mexico, and Colorado. Pipes product for Ultramar Diamond Shamrock (Sym: UDS) |
| TC Pipelines, LP | TCLPZ | United States-based pipeline assets. 30% interest in Northern Border Pipeline Company and a 49% interest in Tuscarora Gas Transmission Company. |
| TEPPCO Partners, L.P. | TPP | Refined products and liquefied petroleum gases transportation, and crude oil and natural gas liquids transportation and marketing. |
| TransCanada PipeLines Ltd | TRP | 38000 kilometers of pipeline. Western Canada |

In many cases, those businesses that are focused primarily on pipeline operations have a more predictable business model than most energy companies. Moreover, given the unpredictability that has ensued following the collapse of Enron, some pipeline companies still offer to benefit from current energy trends without necessarily facing the added risk from energy related trading/investing practices. To be sure, many energy companies are quick to report that setbacks resulting from the Enron debacle will be temporary. However, who is to say that the entire industry is any safer today than yesterday? Who is to say that another Enron is not lurking around the corner?

With this in mind, we are selecting TC Pipelines, LP**.** We had debated selecting Enbridge Energy Partners as well. However, the company is acquiring assets at a rapid and potentially reckless pace. S&P recently downgraded Enbridge Energy Partners' debt and placed it on its 'negative' watch. Moreover, the company feels comfortable producing negative cash-flow in favor of paying dividends. We like TC Pipelines because it has an attractive distribution payment, and there is no immediate threat that can stop the company from benefiting from increased pipe-flows in the future.

TC Pipelines, LP has a 30% interest in the Montana-Saskatchewan pipeline system run by Northern Border Pipeline (NBO holds remaining 70% stake), and a 49% interest in Tuscarora Gas Transmission Company. The NBP pipeline pumps roughly 22% of all natural gas from Canada to the U.S. Furthermore, the system was recently expanded (Project 2000). As a result, NBR, and TCLPZ now have a deeper reach into the Mid-West.

NBP was not completely immune to the Enron debacle. The partnership expects to take a $12.1 million hit over the next year, which equates to nearly 3% of earnings. No, the company is not going to go under because of this exposure, but yes, these numbers are 'material' enough for investors to consider: both NBP, and TCLPZ face near term challenges.

**Covered Call Considerations**

Kinder Morgan trades at $38.50 a share, and the June 2002 $40 calls are bid at $1.50 a share. For those long-term investors buying KMP solely for distribution payments (dividends), writing covered calls seems like an excellent idea**.** While the projected dividend rate on KMP is approximately 7% for 2002, writing covered $40 June 02 calls add another 3.9% to this total.

That said, although we liked KMP's assets, we were turned off by its balance sheet: last quarter its quick ratio dipped below 1. Perhaps we are being overly pessimistic. We have set a reevaluation target of $32.

| | |
|---|---|
| http://www.tcpipelineslp.com/ | http://www.fe.doe.gov/oil_gas/im_ex/otherinfosources.html |
| http://www.aga.org/ | http://www.gasindustries.com/economics/economic.htm |
| http://tonto.eia.doe.gov/oog/info/ngw/ngupdate.asp | http://intelligencepress.com/ |

## Gold: The Misunderstood Metal

Companies Selected: 1 Reevaluation Targets: 2

The story goes that during times of crisis, be it the great depression in the 1930s or rampant stagflation in the 1970s, owning gold can yield a profitable return. However, to many investors buying gold as a hedge against crisis has lost its appeal. Such investors conclude that if gold could not even rally above $300 during the downing of the WTC, anthrax exposures, and terrific stock follies, why would anyone still think that the metal has 'safe haven' qualities?

Herein lies the fault in valuing gold: its credibility as an investment is most often measured by its immediate reaction to 'crisis' like events, not its stability regardless of such events. To be sure, gold naysayers often look at the terrific decline in the metal following a brief peak at $875 an ounce back in 1980. Moreover, the metal has become so misunderstood that most of Wall Street has slashed its weighting down to zero percent within their model portfolios in recent years, central banks have begun selling en masse, and gold producers began to hedge, or actually bet against the price of gold.

It should be noted that the gold naysayers are particular in their slander. They neglect to mention that for the year as of October 2001, the average gold fund had increased by 29.5% while the S&P had lost almost the same amount. 29.5% is an incredible return by any stretch of the imagination. Furthermore, even with the rally in the markets since late September, the XAU index is ahead of the Nasdaq and the Dow for 2001. Granted, the XAU is not ahead by much (up 6% to date). However, it is still ahead.

It could also be said that we are being 'particular' in that such a comparison of the XAU to the leading U.S. markets is myopic. After all, the actual price of gold is only marginally higher now than it was at the beginning of the year. However, for those of you looking back over the last two years, the 'best' gold stocks have proved an excellent hedge. The aware gold investor in 2001 has benefited handsomely while the markets plunged, and there is no reason not to believe that if stock prices fall further the best run companies will further appreciate.

With these things in mind, we have fashioned a belief that gold is a misunderstood metal: No, gold shares do not go up 1000% and vindicate the rambunctious goldbugs' belief that global finance needs to be backed by gold, not confidence in paper. Rather, gold will probably never see $875 ounce again unless the U.S. dollar ceases to exist. Likewise, even when the broader stock markets flounder, owning the 'best run' gold companies could prove profitable, but perhaps not 'internet mania' profitable. As such, perhaps the naysayers should remember that profit with limited risk is the goal, not visions of grandeur…

This is all that we feel investing in gold related instruments is: a hedge against financial uncertainty and/or a viable investment when alternatives are few. We continue to look at the gold industry fondly, but not irrationally…

## Gold/Silver Industry

*'Probably the best place to start when looking at this group is to ask yourself 'what do I have to lose' – if you had bought at the wrong time this year (or attempted to trade rather than invest in the best names) you lost quite a lot.'* WSWL 2001

Last year proved that you can be bullish on gold companies, yet carry no definite opinion on the immediate direction of the underlying metal. We continue to fashion such an opinion, and to date no serious flaws have been exposed in our logic. As for simple data, those companies that performed the best last year were in the upper quadrant of those companies that dropped the least in the year prior (2000). This is not a complicated idea to understand: the best run companies consistently drop least during the bad times, and rise the most during mediocre times. As for the 'good times', we are not sure when exactly they will arrive.

**Gold & Silver - As of December 21, 2001**

**Companies that increased shareholder value in 2001.**

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| 34.5 | Meridian Gold Inc. | MDG | 10.3 | 20.2 | 5.7 | 0 |
| 21.6 | Anglo American PLC | AAUK | 15.1 | 6.8 | 1.5 | 0.2 |
| 19.3 | Goldcorp, Inc. | GG | 12 | 37.3 | 6.4 | 0 |
| 15.5 | U.S. Energy Corp. | USEG | 3.9 | 33.5 | 4.6 | 0.4 |
| 8.4 | Franco-Nevada (TSE) | FN.TO | 23.5 | 28.41 | 2.5 | 0.2 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 5.5 | Royal Gold, Inc. | RGLD | 5.3 | 107.7 | 5.7 | 0 |
| 3.5 | Harmony Gold Mining Co. | HGMCY | 6.7 | 47.7 | 1.7 | 0.3 |
| 0 | Compania de Minas Buenav. | BVN | 20.3 | | 3.5 | 0.2 |
| 0 | Barrick Gold Corp. | ABX | 16.3 | | 2.7 | 0.3 |
| -1.3 | Crystallex International | KRY | 1.8 | | 1.5 | 0.2 |
| -1.8 | Agnico-Eagle Mines Ltd. | AEM | 9.6 | | 3 | 0.9 |
| -1.9 | TVX Gold, Inc. | TVX | 0.4 | | 0.4 | 0.2 |
| -2.3 | Newmont Mining Corp. | NEM | 19.5 | | 2.6 | 0.9 |
| -3.7 | Silver Standard Resources | SSRI | 2.5 | | 3.1 | 0 |
| -6.4 | Apex Silver Mines Limited | SIL | 9.6 | | 2.5 | 0 |
| -10.9 | Gold Fields Limited | GOLD | 5 | | 3.9 | 0 |
| -14.1 | AngloGold Limited | AU | 18.3 | | 0 | 0.8 |
| -14.5 | Echo Bay Mines Ltd. | ECO | 0.6 | | 0.7 | 0.2 |
| -16.8 | Pan American Silver Corp. | PAAS | 4 | | 2.4 | 0.1 |
| -19.5 | Lihir Gold Limited | LIHRY | 11.9 | | 1.8 | 0.2 |
| -30.7 | Bema Gold Corporation | BGO | 0.3 | | 0.4 | 0.4 |
| -34.1 | Kinross Gold Corporation | KGC | 0.8 | | 0.7 | 0.3 |
| -35.8 | Placer Dome Inc. | PDG | 11.3 | | 2.8 | 0.7 |
| -36.7 | Richmont Mines Inc. | RIC | 1 | | 1 | 0 |
| -38.1 | Glamis Gold Ltd. | GLG | 3.7 | | 3 | 0 |
| -38.8 | Ashanti Goldfields Co. | ASL | 3.6 | | 1.3 | 1.3 |
| -45.4 | Canyon Resources Corp. | CAU | 1 | | 0.4 | 0.1 |
| -73.8 | Cambior, Inc. | BGJ | 0.4 | | 0.4 | 0.5 |
| -109.3 | Hecla Mining Company | HL | 1 | | 1.2 | 0.3 |
| -111.4 | Dayton Mining Corporation | DAY | 0.3 | | 0.5 | 0.1 |
| -148.4 | Vista Gold Corporation | VGZ | 0.1 | | 0.6 | 0 |
| -279.2 | Coeur d'Alene Mines Corp. | CDE | 0.8 | | 0.8 | 3.5 |
| | Durban Roodepoort Deep Lt | DROOY | 1.3 | | | |
| | Randgold & Exploration Co | RANGY | 2.4 | 6.2 | | |
| **Other** | Normandy | NDY | | | | |

We have rummaged through the gold/silver industry many times over the years, and we always learn something new. For instance, we did not know that Goldcorp would feel so strongly about the value of gold that they would actually warehouse the metal. However, this is exactly what is happening: at the end of 3Q01 Goldcorp stated that they are holding back 28,000 ounces of gold in their inventory because they believe the price has significant upside potential. If only more companies felt like Goldcorp perhaps the metal wouldn't be wallowing below $300 an ounce.

Meridian is our sole gold selection for 2002. The company has cleared its hedge book, has no long-term debt, and is one of the lowest cost producers in the business. If gold acts as it did in 2001 Meridian's share price may stagnate, but earnings should cushion any wide-spread selling from developing. If gold were to sustain a rally, we believe that Meridian would be one of the best stocks to own.

After taking Franco-Nevada off of the list on December 21, we have set a reevaluation target of $21. If the Newmont takeover goes through we fully realize that this target will not be met. Our opinion of the company did not change last year.

Our final suggestion is Goldcorp, or the company that is beginning to store token amounts of gold awaiting a price spike higher. Goldcorp's mining costs are comparable to that of Meridian, the company is unhedged, debt free, and has strong reserves. We have set a reevaluation target of $10.50-$11 a share.

We believe that consolidation will continue in the industry in 2002, albeit at a slower pace than in 2001.

## Deswell Industries (DSWL)

From Wish List 2001: *"We think we have found a diamond in the rough with Deswell Industries."*

We continue to believe that China based Deswell is an industry leader when it comes to the injection molding business. No, the company does not have the widespread capabilities and capacity of the mid-sized Canadian company Husky. However, Deswell does have cheap labor, quality management (a rarity in China), and is acquiring new machinery all the time. To note: the company acquires new things with cash, not debt…

| Deswell Industries | | | | | | | | Wish List 2001 |
|---|---|---|---|---|---|---|---|---|
| Year-end March | **1994** | **1995** | **1996** | **1997** | **1998** | **1999** | **2000** | **2001** |
| Revenues ($ Mill) | 16.2 | 21 | 30.6 | 44.5 | 66.2 | 53.4 | 61 | 80.8 |
| Earnings ($ Mill) | 3 | 4 | 5.9 | 8.7 | 13 | 9.5 | 10.3 | 12.8 |
| Dividends Per Share | | 0.36 | - | 0.6 | 0.7 | 1.08 | 0.88 | 0.88 |
| Div As a % of Earnings | | 30.5 | - | 32.4 | 29.17 | 62.8 | 46.6 | 37.3 |
| Book Value Per Share | | - | 4.64 | 6.14 | 8.25 | 8.91 | 9.91 | 11.41 |
| Long Term Debt | nil | nil | nil | nil | nil | nil | nil | nil |

Here is a quick comparison of Deswell to related competitors:

| Company (Alphabetical) | Sym | Current Story |
|---|---|---|
| Alltrista Corp | ALC | Selling off assets. |
| Atlantis Plastics, Inc. | AGH | Profits sliding. |
| Berry Plastics | Private | Quick ratio below 1 |
| Clarion Technologies Inc. | CLAR | Weakest balance sheet in the business. Possible chapter 11 |
| **Deswell Industries** | **DSWL** | **Profits down, but strong. Expanding with cash. Dividends.** |
| Hoffer Plastics Corporation | Private | |
| Husky | HKY.to | Consistently losing money. Shcad needs to go. |
| International Smart Sourcing | ISSG.OB | Outsourcing work to China for U.S. companies. |
| Solectron Corporation | SLR | Earnings in tailspin. Recent S&P downgrade. Now planning $1.5 billion financing package |
| Summa Industries | SUMX | Earnings in slide. Just completed convertible preferred offering. |

The above companies do many of the same things Deswell does, minus the pristine balance sheet. Not unlike how WMS Gaming possesses a conservative approach to its business, so too is Deswell wary of taking on debt. However, this fear of debt does not translate into lost opportunities. Rather, just the opposite.

We see no reason to sell Deswell at this time. The company's stock price may decline or rise in 2002, but we feel that management is building a solid business for the future. Since 1995 employment has gone from 1,221 to roughly 4,089 today. We look for this total to expand in 2002, and for Deswell to post stable/strong financial results if global currency prices and demand trends remain much the same.

Our only complaint would be with regards to steadily dropping operating margins: these peaked at 19.6% in 1997 and 1998. By contrast, operating margins were 15.8% for year-end 2001 (Mar), and have only ticked up slightly for the six months ended September 30, 2001 (17.6%). Obviously a 19.6% operating margin is better than 17.6% (about $876 thousand dollars better for the six months ended September 30, 01). We hope, as evidence by note 9 on the latest balance sheet, that management enjoyed the new cars shareholders bought them in 2000. Enough pampering, lets get back to 19.6%…

## Deswell Industries - Balance Sheet - Year End March 31

| Assets | 1998* | 1999* | 2000 | 2001 |
|---|---|---|---|---|
| **Current assets:** | | | | |
| ~~ Cash and cash equivalents | $21,902 | $27,600 | $27,156 | $25,330 |
| ~~ Restricted cash (collateral for unused credit lines) | - | - | 2,129 | 1,988 |
| ~~ Marketable securities (ACM) | - | - | 1,308 | |
| ~~ Accounts receivable - net of allowance for doubtful accounts of 2000 - $87 and 2001 - nil | - | 7,800 | 10,607 | 15,777 |
| ~~ Inventories (FIFO - Primarily raw materials) | 6,415 | 5,900 | 10,932 | 12,034 |
| ~~ Prepaid expenses and other current assets | - | 7,000 | 2,295 | 1,833 |
| ~~ Income taxes receivable | - | - | 164 | 428 |
| **Total current assets** | - | 48,300 | 54,591 | 57,390 |
| ~~ Property, plant and equipment-net | - | 15,600 | 16,701 | **25,563** |
| ~~ Goodwill - net of accumulated amortization of 2000 - $142 and 2001 - $177 | - | 400 | 549 | 513 |
| **Total assets** | **59.144** | **64,300** | **$71,841** | **$83,466** |
| **Liabilities & Shareholders' Equity** | | | | |
| **Current liabilities:** | | | | |
| Accounts payable | - | $2,900 | $5,401 | $4,274 |
| Accrued payroll and employee benefits | - | - | 1,417 | 1,837 |
| Customer deposits | - | - | 1,745 | 1,850 |
| Other accrued liabilities | - | 4,300 | 1,200 | 1,776 |
| Income taxes payable | - | - | 101 | 297 |
| **Total current liabilities** | 7,213 | 7,200 | 9,864 | 10,034 |
| - | | | | |
| Deferred income taxes | - | - | 15 | 15 |
| Commitments and contingencies | | | | |
| Minority interests | - | - | 8,931 | 9,540 |
| **Total liabilities** | 13,933 | 15,500 | 18,810 | 19,589 |
| - | | | | |
| **Shareholders' equity:** | | | | |
| Common Shares $0.01 par value-authorized 20,000,000 shares, shares issued and outstanding March 31, 2000 - 5,347,931; March 31, 2001 - 5,597,931 | - | - | 53 | 56 |
| Additional paid-in capital | - | - | 24,100 | 26,843 |
| Retained earnings | - | - | 28,878 | 36,978 |
| **Total shareholders' equity** | **45,211** | **48,800** | **53,031** | **63,877** |

* Data is incomplete

**Deswell: P, P and E:** As many North America molding companies are laying off workers, and reporting dismal earnings results, Deswell continues to use cash to expand:

| **At cost:** | **2000** | **2001** |
|---|---|---|
| Leasehold land and buildings | | |
| Plant and machinery 17,533 21,571 | $3,475 | $4,940 |
| Furniture, fixtures and equipment | 7,697 | 9,722 |
| Motor vehicles | 1,227 | **2,355** |
| Leasehold improvements | 2,035 | 3,187 |
| Total | **31,967** | **41,775** |
| Less: accumulated depreciation and amortization | -15,266 | -18,952 |
| Construction in progress – | -- | 2,740 |
| **Net book value** | **$16,701** | **$25,563** |

# Trucking

Companies Selected: 0 Reevaluation Targets: 1

**Trucking - As of December 21, 2001**

Highest ROE of the 6 transportation industries.

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| 43.5 | Landstar System, Inc. | LSTR | 73 | 13.3 | 5.6 | 1 |
| 26.1 | United Parcel Service | UPS | 55.3 | 25.4 | 6.4 | 0.5 |
| 24.4 | Forward Air Corporation | FWRD | 33.1 | 33.7 | 7.1 | 0.1 |
| 17.4 | Heartland Express, Inc. | HTLD | 28.9 | 25.7 | 4.1 | 0 |
| 16.8 | Arkansas Best Corporation | ABFS | 29.4 | 13.4 | 2.2 | 0.4 |
| 15.3 | Knight Transportation | KNGT | 28.2 | 38.6 | 5.4 | 0.3 |
| 15.2 | P.A.M. Transportation | PTSI | 12.4 | 10.7 | 1.5 | 1 |
| 12.6 | Roadway Corporation | ROAD | 35.9 | 15.9 | 2 | 0 |
| 11.9 | Motor Cargo Industries | CRGO | 12.1 | 11.2 | 1.3 | 0 |
| 10.9 | Marten Transport, Ltd. | MRTN | 18 | 10.3 | 1.1 | 1 |
| 8.5 | Werner Enterprises, Inc. | WERN | 25.7 | 26.4 | 2.1 | 0.1 |
| 8.1 | Old Dominion Freight Line | ODFL | 11.7 | 9.4 | 0.7 | 0.7 |
| 8.1 | USFreightways Corp. | USFC | 31.5 | 15.9 | 1.2 | 0.4 |
| 6.4 | Yellow Corporation | YELL | 24.5 | 20 | 1.2 | 0.5 |
| 5.9 | J.B. Hunt Transport Svcs. | JBHT | 23 | 32.1 | 1.8 | 0.9 |
| 4.1 | Swift Transportation Co. | SWFT | 23.2 | 71.3 | 2.8 | 0.5 |
| 4.1 | Dynamex, Inc. | DDN | 2.1 | 8.8 | 0.4 | 0.7 |
| 3.7 | Patriot Transportation | PATR | 19.6 | 23 | 0.8 | 0.7 |
| 3.3 | Covenant Transport, Inc. | CVTI | 16 | 41 | 1.3 | 0.7 |
| 1.2 | Transport Corp. of Amer. | TCAM | 6.4 | 70.1 | 0.6 | 1.2 |
| -0.8 | Frozen Food Express Ind. | FFEX | 2 | | 0.4 | 0.2 |
| -1.1 | USA Truck, Inc. | USAK | 9.7 | | 1.3 | 1 |
| -2.4 | U.S. Xpress Enterprises | XPRSA | 8.2 | | 0.7 | 1.2 |
| -4.2 | Boyd Bros. Transportation | BOYD | 3.5 | | 0.4 | 1.4 |
| -5.1 | Alternate Marketing Ntwks | ALTM | 1.4 | | 0.8 | 0 |

| | | | | | |
|---|---|---|---|---|---|
| -6.3 | Avalon Holdings Corp. | AWX | 2.8 | 0.2 | 0 |
| -8.6 | Celadon Group, Inc. | CLDN | 5.2 | 0.7 | 1.9 |
| -11.3 | Landair Corporation | LAND | 13 | 1.9 | 0.4 |
| -14.1 | Smithway Motor Xpress | SMCX | 1.6 | 0.2 | 1.5 |
| -19.3 | CNF, Inc. | CNF | 32.1 | 1.8 | 0.7 |
| -20.6 | Asche Transportation Svcs | ASHE | 0 | 0 | 1.9 |
| -21.8 | Intrenet Inc. | IRNE | 0 | 0 | 1.5 |
| -31.4 | Consolidated Freightways | CFWY | 5 | 0.6 | 0.6 |
| -53.6 | The Morgan Group, Inc. | MG | 2.6 | 1 | 0.2 |
| -58.6 | Cannon Express, Inc. | ABFS | 0.5 | 0.2 | 5.5 |
| -59.8 | CD&L, Inc. | CDV | 0.3 | 0.3 | 2.7 |
| -70 | Simon Transportation | SIMN | 1.4 | 0.3 | 1.6 |
| -103.7 | Allied Holdings, Inc. | AHI | 2.1 | 0.8 | 16.5 |

We talked with a few companies back in late November in the guise of 'Truckers' – to note: if you plan on doing this to research companies, figure out what licenses and experience you need to say you have beforehand. To our surprise one company was looking to hire in almost all areas: Heartland Express. This was an impressive discovery given that the more touted Forward Air Corporation was only hiring in two areas: Cincinnati, and Columbus (hiring in Sacramento began in December). Forward Air is solely an owner operator versus Heartland which is primarily (68%) company-owned tractors.

The reason why we posed as out of work truckers when calling these companies is that it allowed us to talk to someone who was not trying to pump the stock. Most IR people are, to put it frankly, snakes. By contrast, employee relations people do not fabricate facts when someone is looking for work.

As for Forward Air Corporation, the company benefits from the current market environment in two respects: first, following the September 11 attacks air shipment weights were reduced due to FDA weight restrictions and various other psychological reasons. Two, FedEx spillover volume oftentimes lands with FWRD. However, these benefits could be temporary.

While we did not select a company in this industry, we have selected the industry leader for reevaluation**:** all signs point to Heartland Express Incorporated. Heartland has three qualities which we believe will continue to enhance the company's success story:

1) Highest pay rate in industry
2) Loyal customer base / Cult Like Workforce
3) The company's mantra is 'no debt'.

| **Heartland Express Incorporated** | | | | | | | | **Wish List 2002** | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Year** | **91** | **92** | **93** | **94** | **95** | **96** | **97** | **98** | **99** | **2000** |
| Revenues (mill$) | 73.9 | 96.5 | 116 | 224.2 | 191.5 | 229 | 263 | 264 | 261 | 274.8 |
| Net Earnings (mill$) | 9 | 11.6 | 14.7 | **10.1** | 20.6 | 25 | 30.1 | 33.1 | 33.1 | 34.2 |
| Book Value | 1.13 | 1.45 | 1.86 | 2.08 | 2.66 | 3.3 | 4.1 | 4.98 | 5.28 | 6.15 |

Although we did not get a chance to talk with all of Heartland's employees, we did get the feeling that this is not an ordinary company from the people we did speak with. Not unlike the way every Wal-Mart cult member sings a song before they start work, HTLD has a similar doctrine: *"our passion is to provide the best transportation service in America."* If such a vision holds firm, the company's success is virtually guaranteed.

Heartland does not believe in amassing debt to fund its expansion plans. Rather, CEO Mr. Gerdin, who owns 38% of the outstanding shares, prefers to expand with cash-flow; taking baby steps rather than leveraged leaps.

Holding minimal amounts of debt on the balance sheet is a definite plus going into what could be a prolonged economic slowdown. This is especially true when considering that as the industry enters a consolidation phase Heartland could choose to expand comfortably. The industry could reach such consolidation in the near future as many financially weak companies (CFWY) may decide that it is more prudent to be acquired than to try and finance new capital spending initiatives on their own during trying times.

'No debt' has certainly not kept HTLD from running its business effectively. After recently acquiring 100 tractors and 300 trailers with cash, the average age of the company's fleet is now just 18 months. With this young fleet of trucks and history of customer satisfaction, it is not difficult to envision Heartland being a strong company for many years to come.

We look to reevaluate Heartland on a quarterly basis, or when its stock price nears $20 a share. We believe an opportunity to buy the company could present itself sometime early this year given the fact that near-term valuations are rich, and shipment trends historically bottom out in the month of January. The company is trading at 22 times consensus 2002 earnings estimates, and is expected to grow earnings by an average of 10% over each of the next 5 years.

http://www.heartlandexpress.com/
http://www.bts.gov/
http://www.truckline.com/
http://www.bidc.state.tx.us/HighwayTruckingStatistics.htm
http://www.ops.fhwa.dot.gov/freight/regulate/sw/index.htm

## Beverages Alcoholic

Companies Selected: 0   Reevaluation Targets: 1

Last year we reviewed this industry but decided not to include any final suggestions except to say that BUD was the industry leader. At the time we felt that the premiums in the larger companies were too steep, and the future in smaller companies and foreign players was too uncertain.

However, what has changed over the last year is that investors have taken premiums in some of the best companies down a notch. Accordingly, in the statistics below we have included a quick comparison to last year's numbers.

**Beverages (Alcoholic) - As of December 14, 2001**

**More attractive than last year (Higher ROE, lower $, lower P/E, P/B, and D/E)**
**Less attractive than last year**
**Same as last year**
**Not Available**

| ROE | Company | Sym | $ | P/E | P/B | D/E |
|---|---|---|---|---|---|---|
| 40.4 | Anheuser-Busch Companies | BUD | 42.9 | 22.9 | 8.9 | 1.3 |
| 24.4 | Diageo plc | DEO | 42.6 | 20.2 | 4.8 | 1.5 |
| 19.5 | Brown-Forman Corporation | NF.B | 60.2 | 18 | 3.3 | 0.2 |
| 16.8 | Constellation Brands Inc. | STZ | 39.9 | 14.3 | 2 | 1.7 |
| 16.2 | The Boston Beer Co., Inc. | SAM | 13.8 | 17.9 | 2.7 | 0 |
| 13.2 | Vina Concha y Toro S.A. | VCO | 35.8 | 25.6 | 3.4 | 0.5 |
| 12.5 | Adolph Coors Company | RKY | 55.8 | 17.6 | 2.1 | 0.1 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 12.1 | Central European Dist. | CEDC | 10.9 | 23.2 | 2.6 | 0.6 |
| 10.9 | Todhunter International | THT | 8.6 | 7.6 | 0.8 | 1 |
| 10.9 | Quilmes Industrial S.A. | LQU | 12.4 | 9.6 | 1 | 0.5 |
| 10.7 | Compania Cervecerias Uni. | CU | 18 | 17.9 | 1.9 | 0.2 |
| 9 | LVMH Moet Hennessy L.V. | LVMHY | 7.9 | 33.5 | 3 | 1.5 |
| 8 | The Robert Mondavi Corp. | MOND | 35.4 | 18.8 | 1.4 | 0.8 |
| 7 | Big Rock Brewery Ltd. | BEERF | 3.1 | 18.4 | 1.2 | 0.1 |
| 5.4 | Golden State Vintners | VINT | 5.3 | 15 | 0.8 | 0.8 |
| 2.9 | Chalone Wine Group, Ltd. | CHLN | 10 | 46.9 | 1.4 | 1 |
| -0.9 | Geerlings & Wade, Inc. | GEER | 1 | | 0.4 | 0.3 |
| -3.6 | Pyramid Breweries Inc. | PMID | 2.3 | | 0.7 | 0 |
| -3.9 | Redhook Ale Brewery, Inc. | HOOK | 1.8 | | 0.2 | 0.1 |
| -30 | Genesee Corporation | GENBB | 19.1 | | 0.7 | 0.1 |
| -67 | MBC Holding Company | MBRW | 0.6 | | 3.2 | 3.2 |
| | Kirin Brewery Company, Lt | KNBWY | 68.3 | 26.3 | | |
| | **Not listed in 2000** | | | | | |
| 28.1 | AmBev | ABV | 20 | 32.5 | 8 | 0.8 |
| *Share price comparison to that of December 29, 2000. | | | | | | |

When not including gains from dividends, an amount that could have been topped by any available U.S. treasury note, share prices in 3 of the best names (BUD, BF.B, RKY) have declined year-over-year. Suffice it to say, we are absolutely thrilled by this development as it makes for a more attractive sector.

With this in mind, we are selecting the most depressed issue: Brown-Forman Corporation. Unlike the massive BUD, we feel that BF.B's share price is more firmly rooted to fundamentals. As well, BF.B is a more nimble company with regards to market positioning. This is especially true when considering that recent advertising trends seem to suggest that liquor advertising will be given the same playground as that of beer (NBC broke an unwritten law in late 2001 when it announced that it would begin putting liquor ads on television). If this trend continues it will only be to BF.B's benefit.

**Brown-Forman**

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|
| Sales $Mil | 1,490 | 1,644 | **1,606** | 1,672 | 1,793 | 1,824 | 1,906 | 2,009 | 2,134 | 2,118 |
| EPS | 1.76 | 1.88 | **1.63** | 2.15 | 2.31 | 2.45 | 2.67 | 2.93 | 3.18 | 3.40 |
| Div/Share | 0.78 | 0.86 | **0.93** | 0.97 | 1.02 | 1.06 | 1.10 | 1.15 | 1.21 | 1.28 |
| Return on Equity | 21.3 | 20.4 | 20.4 | 30.1 | 27.5 | 25.2 | 24.3 | 23.6 | 22.4 | 21 |
| Economic Goodwill | 12.22 | 11.9 | **10.45** | 11.59 | 11.6 | 11.83 | 12.38 | 11.64 | 12.1 | 12.01 |
| Div/EPS | 44.3% | 45.7% | **57.1%** | 45.1% | 44.2% | 43.3% | 41.2% | 39.2% | 38.1% | 37.6% |

We like BF.B for three simple reasons:

1) They have paid a quarterly cash dividend without exception for 56 years in a row.
2) They have quality, recognizable brands that should continue to thrive for many years to come.
3) The 911 disaster hurt its consumer durables businesses, and has made its stock price more attractive.

To note: we do not like BF.B's consumer durables business. For a company so strongly positioned with wine and spirits, we would hope that they would exit this area and focus on what they are good at. Trying to sell Jack

Daniels, and luggage at the same time? It boggles the mind…

That said, its Lenox department (fine China and related products) is noteworthy, and is perhaps worth saving. However, its contribution to future earnings is not nearly as predictable as the booze: quite frankly, we believe people will always consume the company's liquor products, and opportunities overseas continue to develop.

To this end, we want to buy BF.B on weakness. Such weakness could arrive with another earnings setback next quarter, a broad sell-off in U.S. stocks, or an announcement from the company concerning developments/closures, or potential restructuring.

The company has already enacted previous stock repurchase plans, but we feel that they may not be as willing to buy more shares this go around, and/or such purchases will not readily turn the stock around.

| Date | Average Price | Shares Purchased (Class A, and B) |
|---|---|---|
| 20-Feb-01 | $68.05 | 13,358 |
| 23-Jul-01 | $66.65 | 189,916 |

Price as of December 24, 01 -- $63.15

In sum, we want to see any corporate misstep before we step in to buy their brands: such a misstep could arrive at any moment, and we initially are looking to reevaluate the company near its 52-week low of $57. While buying the company now could prove wise for the long-term investor we believe that recent industry trends suggest a better opportunity will arrive shortly. To note: during 1994 the company suffered terrible setbacks in both revenue, and earnings, but this did not impact the dividend (the company simply paid a higher percentage of earnings out in dividends). We feel that such a precedent will be repeated when, and if, further setbacks arrive. It is encouraging for a new shareholder to know that a) the company is financially strong, and b) they are prepared for setbacks.

## Wish List Companies and Conclusions

### The 2002 Wall Street Wish List

| Company | Sym | Current $ |
|---|---|---|
| Caldwell Partners International Inc | CWL.a (TSE) | 1.14 (CND) |
| WMS Industries Inc. | WMS | 19.98 |
| DIMON Incorporated | DMN | 7.39 |
| Nordic American Tanker | NAT | 13.21 |
| TC Pipelines, LP | TCLPZ | 25.00 |
| Meridian Gold Inc. | MDG | 10.45 |
| Deswell Industries, Inc. | DSWL | 17.99 |

**Reevaluation Targets** — **Wish List 2002**

| Company | Sym | Current $ | Target $ |
|---|---|---|---|
| American Italian Pasta | PLB | 43.35 | 36 - 38 |
| Gillette | G | 33.73 | 22 - 25 |
| General Motors | GM | 47.46 | 37 - 38 |
| Honneywell | HON | 33.10 | 22.15 |
| Churchill Downs, Inc. | CHDN | 33.00 | 27 - 28 |
| UST Inc. | UST | 35.49 | Low 30s |
| Philip Morris | MO | 46.37 | 42.00 |
| Teekay Shipping | TK | 34.43 | 26.00 |
| Kinder Morgan | KMP | 38.06 | 32.00 |
| Franco-Nevada | FN (TSE) | 23.58 | 21.00 |
| Goldcorp Incorporated | GG | 12.20 | 10.50 - 11.00 |
| Brown-Forman Corporation | BF.B | 63.15 | 57-59 |
| Heartland Express | HTLD | 28.92 | 20-22 |

Beyond our 7 selections, it is our contention that the prudent investor should remain highly liquid and prepared for when better opportunities arrive. With this in mind, Heartland Express is truly our favorite company, but one that we cannot bring ourselves to buy at this level. We feel that Heartland, which has only acquired four companies since 1986, will make key asset acquisitions in the near future, when other trucking companies are scratching to stay alive. Furthermore, with its young fleet of trucks and precise management in place, we believe that owning this company at a good price is far and away the best investment we have identified.

We hope that the Wish List has presented you the investor with some investment ideas. The list's intention is to take an honest look at opportunity, not necessarily to foretell of a serious crash or bear market that looms. To be sure, we spend the entire year at FallStreet.com warning investors about the dangers of investing in the U.S. financial markets – come Christmas time we express our opinions on where we believe opportunity rests.

We feel that the 7 companies we have selected have the potential to produce solid returns in 2002. Of course, there is no guarantee that this will be the case. However, this report will hopefully provide you with a starting point when doing you own investment research.

Some of the stocks we have selected appear to be overbought (MDG, WMS, and DSWL). Suffice it to say, we are not market technicians. Rather, we believe that these companies will do better business tomorrow than they do today. As such, they are on the list regardless of any misgivings we may possess concerning short-term price fluctuations. If our opinion changes you will receive an e-mail notifying you as much.

As for the other companies and industries we continue to monitor, you will receive an e-mail when, and if, we add them to the list. The prospective 'targets' for each company are levels where we believe serious reevaluation is needed. However, we may choose to add these companies to our 2002 portfolio before these levels are struck.

We wish you the very best in 2002.

Sincerely,

Brady Willett
Todd Alway

*"Investment success is not synonymous with infallibility. Rather, it comes about by doing more things right than wrong."*
Robert G. Hagstrom, The Warren Buffett Way.