SIGMA INVESTMENT COUNSELORS

Sigma Summaries

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Investment Perspective

It didn't take long for us to be reacquainted with the misery inflicted by a bear market environment. Clearly, the NASDAQ market pain has been felt for the better part of the past twelve months. Recently, the more seasoned companies (the NASDAQ companies tend to be faster growing and more volatile) populating the Standard & Poor's 500 stock index (S&P 500) declined to a level representing over a 20% drop from its high, pushing this broad market benchmark also into bear territory.

The only good that we can posit about this kind of market activity is that it eventually comes to an end. That is why we have reproduced the chart that appears on the inside of this month's Sigma Summaries. It helps to have a little perspective, and we think this gives an illuminating snapshot. We were reminded of the value of this chart by a prospective new client (who happens to be a practicing investment professional and a CFA Charterholder). He mentioned that he studies this chart during difficult market periods just to remind himself that all bear markets do end and the path of equity prices over the long term is irregularly higher.

We recognize that the chart provides more comfort to those investors who began investing prior to 1999 since they have had an opportunity to benefit from the previous bull market. Notwithstanding this, it is actually more important for new investors to maintain a long-term outlook and not be panicked into selling. Indeed, after having experienced this pain, it would be regrettable to miss the next up-leg of what we believe will be an improving market.

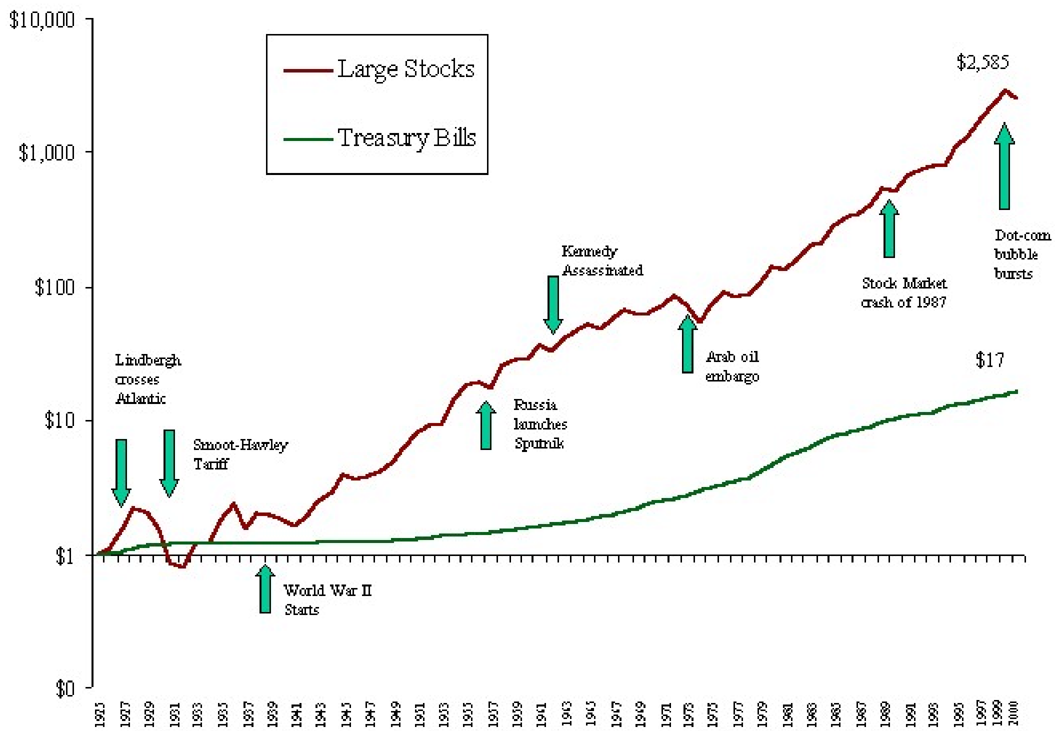
Our confidence in the long-term trend is bolstered by the many positive global economic developments we have observed during the past two decades. As is well known, it was during these two decades that the United States shirked off the yoke of economic malaise and inflation and embarked upon a path which restored economic global growth. The benefits of those operating improvements are now being coupled with exciting technological developments to stimulate further longer-term productivity growth.

More immediately, our analysis has led us to conclude that the broad market, as measured by the S&P 500, has substantial upside potential, notwithstanding the fact that there is still some additional downside risk. Our fundamental valuation work indicates that a continuation of market anxiety could lead the S&P500 from its present levels, around 1140, to around 1050, an 8% decline. However, if one can assume that the earnings growth of the S&P500 will average 9% over the next five years (compared to 15% over the last five years), the S&P500 could advance to around 1650 producing a gain of 45%.

No one knows the near term outlook for the markets. Also, repeatedly we have reminded investors that successful investing requires making a multi-year commitment to stocks of successful companies selling at defensible valuations. While more and more companies are reporting profit warnings, once the current inventory and oversupply imbalances within some industries are worked through, the profit slowdown should reverse. Further, we are confident that markets ultimately work, and they will force the various authorities to make the right monetary, fiscal and political decisions to enable prosperity to continue. These factors should allow the seventy-year trend of the S & P 500 depicted below.

Written by: Robert M. Bilkie Jr., CFA

LONG TERM HISTORICAL RETURNS – VALUE OF ONE DOLLAR INVESTED IN 1925



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