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Commentary
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The Markets

The first nine months of this new year of the new millennium has been like a roller-coaster ride. The most volatile stock benchmark is the technology driven NASDAQ average. During the first three months of the year, the NASDAQ gained 12% and it has proceeded to lose 20% over the next 6 months. The most widely known of the stock market indicators is the Dow Jones Industrial Average, which started the year with a three month return of (5%) and now stands at a positive 2% gain. Compared to last year at this time when the Dow was up 12.6% and the NASDAQ had gained 25.2%, this has been a pretty tough year. The more broadly diversified Standard and Poors 500 Index began the year 2000 up 2% and is now down 2%. To give a picture of just how much things are changing, the NASDAQ lost 3% in July, gained 9% in August and lost 14% in September.

The Rikoon composite portfolio returns for the first nine months of the year 2000 continued to be above market. In the U. S. Large Company area, our portfolios returned (1.92%)versus the Standard and Poors year-to-date result of (2.23%). In international stocks, our stocks showed a (9.3%) decline versus the international blue chip stock market decline of (12.58%). Rikoon clients had an 8.1% return so far this year in taxable bonds versus the Lehman Brothers bond index return of 5.57%. In the tax-free area, our portfolios were up 4.37% versus the market's increase of 6.50%. There is generally much less fluctuation in bond returns than in stocks. Even though interest rates have gone up during the first 9 months of this year, we are pleased that people relying on their bond portfolios have seen their first increase in total value.

With rising oil prices, inflation jitters have begun to appear in investor's minds. While the nation's unemployment level is fairly stable, other consumer prices are being watched closely, because if they start to rise, the Fed may well raise interest rates again causing further concern for stocks. For the last three years, people have had increasing enthusiasm for most technology stocks and there was and still is the feeling that we are in a "new economy," one not subject to recession or inflation. This should soon disappear. From our point of view, the analysts on Wall Street and other members of the investment community are partially to blame for the high level of volatility because they give investors unrealistic expectations of the market.

Intel is a good example of a company doing a tremendous job running its business, and preparing for a future when stand-alone desk top computers are as obsolete as typewriters. Wall Street, however, demands ever increasing rates of growth. When Intel reported a shortfall in sales growth, that is actual receipts even though their profitability did not decrease, it lost a hundred billion dollars in market value in one day! Nothing fundamentally changed about Intel from one day to the next, only the short term view of “professionals” on the Street. As the disappointment spread, the price of all technology companies tumbled. Intel blamed its small reduction in sales growth on a weak Euro, not fundamental demand for its products; Wall Street could not care less!

This points to two real problems in the stock market today: unrealistically high expectations and lack of good information. In regard to information, under new disclosure rules, companies can no longer give Wall Street analysts advance information about their upcoming financial performance. It must be disseminated simultaneously to the general public and to Wall Street as well. The big firms soon will not have any better information than individual investors. As far as accuracy goes, unless Wall Street does a good deal more leg work ahead of time, such as calling a company’s suppliers, competitors and customers, the numbers jitters that are now causing Intel such problems are likely to get more unsettled, and not just for Intel.

In the not too distant past, companies had to make money in order for their stock to go up. What we have seen is that the boom in technology has driven expectations of future growth to higher and higher levels, to the point of being impossible to achieve. By focusing on increased sales or increased market share, some new investors were taking for granted that someday, somehow, these companies would make money. In order to meet these unrealistic expectations, companies have had to boost their profits by using accounting devices and non-reoccurring gains. This is not the kind of growth that long-term investors should value. Intel is not alone. Telecom giant Lucent is down 64%, and Cisco is 30% from its high, while Microsoft and AT&T have also had sharp drops for different reasons.

Economics and the Environment

Recently, I wrote an article for the local newspaper about the combined efforts of corporations with environmental groups to help protect the world’s commercial forests. Since many of you might not see the article, I thought you would be interested in reading it.

Many people have a strong desire to help preserve our natural resources and quality of life. For some investors, the main way this urge gets expressed is through a desire to invest in companies and businesses that do not promote environmental degradation. For all the good intent of socially responsible investing, very little in the way of actual influence makes its way into the real world. Tobacco companies, defense contractors, and nuclear utility companies have all not done well over the past decade, but it is the economics of these businesses, driven by consumer purchasing preferences, that has created this effect.

Some take a more proactive position by initiating proxy actions and attending annual meetings. If you are interested in these initiatives, contact the Interfaith Center on Corporate Responsibility. Another proactive option available is to invest in alternate energy companies such as Fuel Cell or Energy Conversion Devices. Both firms are actively pursuing alternatives to the internal combustion engine and with rising oil prices, demand for shares in these companies is on the increase.

It is quite encouraging that one can now vote for environmental preservation with one’s own spending dollars. This focus approach was highlighted in a recent Wall Street Journal article about how Home Depot and environmental activists joined together to try to protect the world's forests. Jim Carlton wrote in the September 26, 2000, edition about the activities of the Forest Stewardship Council (FSC). It related a heartening example of how people interested in changing corporate behavior can act effectively through a combination of analysis, communication, strategy, and bravado.

The purpose of the FSC is to protect endangered forests without impeding on the livelihoods of loggers, processors, or marketers of wood products. What kind of power and influence does it take to have an effect on the health of the world's forest? The Forest Stewardship Council's first step was to evaluate harvesting and growing practices of loggers and then to research how companies buy and market wood products throughout the United States. The FSC then established their criteria for sustainable logging, proper worker's conditions, and a ban on chemicals, which are destructive to the environment. They certify as "FSC Approved" only those practices which contribute to the long-term health of forests.

Making progress with Home Depot was not easy. First, activists associated with FSC snuck into the retail warehouses and highjacked the P.A. system to make comments like "Attention Shoppers, on aisle seven you will find mahogany ripped from the heart of the Amazon." This brought attention to what was a mostly unknown aspect of Home Depot's operations. After several such sneak attacks, Home Depot decided to sit down with the FSC and decide whether it would make sense to associate their company with the FSC and its certification process as opposed to being its target.

When environmentalist groups and businesses come together, large organizations such as the World Bank and the World Wildlife Fund are willing to contribute to the costs of bringing their efforts to fruition. The marketing of environmental causes in such a way as to match up with the public relations goals of corporations is the key. One common good of these two very different groups is to have consumers agree to pay more for environmentally safe and ecologically sustainable products.

FSC built their credibility by being onsite and hands on. Atlanta-based Home Depot eventually did decide to inform its suppliers that they did not want to use endangered wood species. The desired time frame for dealing with the situation was different for the two organizations. After deciding <u>not</u> to bring a boycott against Home Depot, the FSC brought in some media celebrities to further prod the company towards action, which was an ongoing concern.

Consumer buying habits are greatly influenced by celebrity advertising and many actors and artists are willing to donate their time to causes such as the FSC. Showing up at annual meetings with celebrities allowed the FSC to gain media attention. Home Depot then decided that rather than fight, it would be better business to accept and promote the FSC's agenda. Once Home Depot decided to play ball with the FSC, it was presented as a business decision. "Look, we sell a lot of wood and we want to make sure that we will have wood to come for a long time," said a Home Depot spokesperson. Certain competitors of Home Depot realized that with FSC certification they would be able to counter Home Depot's current marketing advantage, so they too are climbing aboard.

Industry lobbying efforts against the FSC took an extremely intelligent form. Several large paper companies formed a competing organization called Sustainable Forestry Initiative (SFI). Because membership in the SFI is mandatory for companies in the American Forest and Paper Association, there was and is confusion about which certification is genuine. The industry-sponsored group does not believe in curtailing the use of herbicides and allows for more severe timber cutting practices than the FSC standards. While the grassroots FSC has nine staff members, its activities cover the entire globe. The jury is still out, but I believe that the work of environmental groups will be enhanced as consumer purchasing decisions get integrated with social goals. It is heartening to see that people acting within the law, and in concert with business, are helping bring about positive changes for all of us.

Good News

The last several months have brought two projects to completion. Our business merger with Carret and Company of New York City is now underway. We are very happy to have partners of the caliber and integrity that the people at Carret exemplify. I look forward to introducing many of them to you over the upcoming years. Our clients should be assured that our investment process and client services will not change except that some enhancements will become evident over time. By early next year, we will be using an upgraded portfolio management and reporting system, as working with Carret moves up the time table for utilizing this system.. We are also in development of a client-directed website. This will be fast, easy to use, and convenient. It will permit those who prefer to view accounts and communicate over the Internet with an opportunity to do so.

Another development is in the financial planning area. Juliana Henderson and Stephen Madeyski are enrolled in the Certified Financial Planning program. Our clients in Albuquerque will have the opportunity to be served by our Albuquerque branch, which we plan to open in 2001.

On a personal level, I hope soon to return to painting before the markets open. My current project is a series of painting for a non-denominational chapel, which will take about 5 years to complete on movable panels, using the egg-tempera medium. Our dog Sadie enjoys the egg whites, which are not used in the paint making process. By the way, the "chapel" building to receive the work has not yet been located and any suggestions of a suitable site would be welcome!

Please note that our next afternoon "tea" gathering will be on Tuesday, November 21st. It will be oriented towards youthful investors so we will start a little later than usual, at 3:30 p.m. All those ages 8 and older are welcome to join us as we discuss the basic concepts of stock and bond analysis.

As you can see by the flyer, we are pleased to announce our move to new quarters. We will be across the street from the southwest corner of the State Capitol building. This historic house was formerly headquarters for Blue Sky Beverage Company, New Mexico's nationally regarded natural beverage manufacturer. The structure dates from the 1930's, and although it has been renovated to include modern conveniences and telecommunications capabilities, it retains much of its original character. The new location has trees, a great flagstone patio, and more street parking. We look forward to hosting many of you at our new offices, located at 510 Don Gaspar.

Best wishes for a glorious Autumn.