

Index Fund Strategies

ASSET CLASS

A monthly update of asset class performance, trends, & topics for long-term investors

Index Returns

	1999	2000	2001	Last 9 yrs.	2/15 2002
Bonds					
Short-term	4.6	6.7	5.8	5.5	0.5
S-T Global	3.7	6.7	5.9	7.3	1.0
Intermediate	-3.6	13.5	8.2	7.1	1.6
Long-term	-7.9	16.6	8.2	8.1	2.4
U.S. stocks					
Large Market	20.8	-9.3	-12.1	13.3	-3.2
Large Value	4.8	10.2	3.8	14.1	-0.4
Small Micro	29.8	-3.6	22.8	14.8	-1.6
Small Market	25.4	2.5	12.7	12.6	-3.4
Small Value	13.1	9.0	22.7	15.6	-0.2
Real estate	-2.0	28.4	13.2	9.6	1.0
Int'l stocks					
Large Market	28.5	-14.0	-20.8	6.3	-4.6
Large Value	16.3	-0.2	-15.3	8.6	-0.9
Small Market	21.9	-5.4	-10.5	3.1	1.1
Small Value	19.0	-3.1	-4.6	3.6	2.1
Emerg. Mkts.	71.7	-29.2	-6.8	5.1	4.1

Descriptions of Indexes

Short-term bonds	DFA One-Year Fixed Income fund
S-T Global bonds	DFA Five-Year Global Fixed
Intermediate bonds	DFA Intermed. Gov't Bond fund
Long-term bonds	Vanguard Long-term Bond Index
U.S. Large Market	DFA US Large Co. (S&P 500)
U.S. Large Value	DFA Large Cap Value fund
U.S. Small Micro	DFA US 9-10 fund
U.S. Small Market	DFA US 6-10 fund
U.S. Small Value	DFA US 6-10 Value fund
Real Estate	DFA Real Estate Securities fund
Int'l Large Market	DFA Int'l Large Cap fund
Int'l Large Value	DFA Int'l Large Cap Value fund
Int'l Small Market	DFA Int'l Small Company fund
Int'l Small Value	DFA Int'l Small Cap Value fund
Emerging Markets	DFA Emerging Markets fund

"Last 9 yrs." returns are ended 12/31/01 and for U.S. Large Value (3/93), U.S. Small Value (3/93), Int'l Large Value (3/93), Int'l Small Market (10/96), Int'l Small Value (1/95), and Emerging Markets (5/94) include simulated data prior to fund inception (in parentheses).

This information is obtained from sources we believe are reliable, but we cannot guarantee its accuracy.

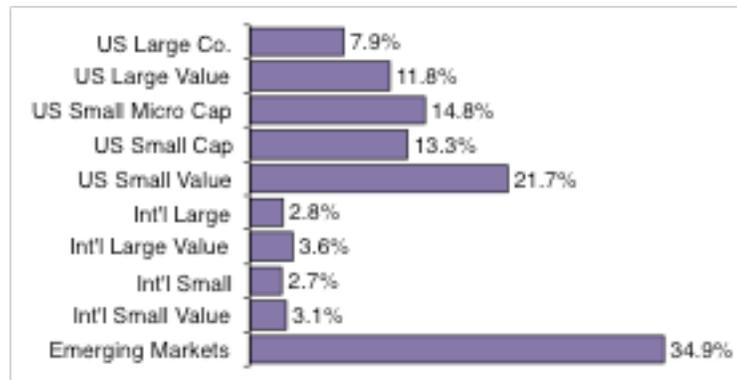
Past performance does not guarantee future returns.

This newsletter is published by
TAM Asset Management, Inc.
 1100 Mar West St., Suite D
 Tiburon, CA 94920
 phone: 415-435-5045
 Efax: 781-623-4691
 email: trout@tamasset.com
 Web Site: www.tamasset.com
 Editor: Jeffrey C. Troutner

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Markets Update Tuesday, February 19, 2002

Asset Class Returns 9/17/01 to 2/14/02 (first close after 9/11)



Enron, Screwy Tax Policy & Stock Speculators

Jeff Troutner, TAM Asset Management, Inc.

I don't know about you, but I have absolutely given up on the national news media's ability to report on any story in a complete and fair manner. I agree with Bernard Goldberg (author of *Bias: A CBS Insider Exposes How the Media Distort the News*) that there is a huge liberal slant to the national network news and among the major metropolitan newspapers. It's not so much a liberal bias that bugs me as much as there is a slant one way or the other. You simply don't get the whole story and what you do get is based more on shock value than fact. So it seems that on any business-related issue the solutions always come down to more government control, more regulations, higher costs, and higher taxes for hardworking Americans. Enron is just the latest example.

If you listen to Dan Rather, the whole problem with Enron boils down to crooked corporate executives and greedy big time accountants with conflicts of interest. Both were simply looking to enrich themselves at the expense of the "little guy"—Enron employees and shareholders. And only more government regulation and control can possibly fix the problem. But is this really the case?

There is no question that Ken Lay at Enron and the boys at Arthur Andersen were enriching themselves and deceiving the public as to the real risks of Enron's business structure. For this they should be made to pay financially to the point of personal bankruptcy and serve hard time if it is found that they violated securities laws. The news organizations have this part right.

The only other part of the story getting any airtime is the connection of Enron to politicians. The big obsession, of course, is a Cheney/Bush connection, but that seems to be losing steam. After all, what big name CEO doesn't

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try to kiss up to national politicians anytime they can (and vice versa). As a shareholder or employee you expect that. No one's complaining about Jack Welch's onetime influence at GE. It goes with the territory. Even Bill Gates has started to exert more influence in Washington after Microsoft's experience with the anti-trust suit. If we want less corporate influence of politicians we should change laws. Of course, we should also not whine if our local congresspersons fail to attract more jobs to our local communities or the president fails to protect American jobs from unfair foreign competition and other threats.

If nothing else, the political connection provides some good laughs. Our local Marin County equivalent to Pravda reported recently that Governor Gray Davis' spokesman defended his boss's acceptance of a large campaign contribution from Enron by stating that Republican candidate and former Los Angeles mayor Richard Riordan lured the *Democratic* National Convention to LA and that Enron had donated \$100,000 to the cause. Hmm. Oh yea, Riordan accept a campaign contribution of \$500 from Enron, which he returned. Davis didn't return his \$119,500 Enron gift.

Enron didn't fail because they were allowed to skirt the law or were granted special exemptions by their political buddies. They failed because they were buried in debt. And they were buried in debt because their accountants tried to take full advantage of this country's screwy tax laws. Jeremy Siegel, a Wharton School professor and author of the excellent book, *Stocks for the Long Run*, explains this very well in an article in the February 13 *Wall Street Journal*.

As Siegel points out, our tax laws allow companies to deduct interest expense on debt, but not dividends paid to shareholders. So dividends are taxed twice: first as earnings for the company and then to shareholders. Rather than issue additional equity shares and pay the holder of those shares a return in the form of dividends, companies like Enron take on much more debt than they might otherwise. Enron's stupid, but legal, way of keeping their share price high was to keep the debt off their books through the use of something called MIPS—Monthly Income Preferred Shares. MIPS are just the latest big moneymaking scheme concocted by those wizards on Wall Street, in this case Goldman Sachs. Enron reported the MIPS to the IRS as debt and could deduct the interest expense. But they were allowed to report the securities as equity to the rating agencies and shareholders. And it's all perfectly legal—for now.

Changing the tax laws to eliminate the double taxation of dividends won't eliminate greed and mismanagement.

But it would give companies less of an incentive to devise such esoteric and complex securities and make the whole process more transparent. Apparently most other countries think so. As Siegel notes in his article, 62.5% of all other countries provide complete or partial offset to the double taxation and another 25% give shareholders a break on the dividend taxation.

Which brings us to the Enron shareholders. Frankly, I have little sympathy for any of them. First, it is my understanding that the Enron stock portion of the employees' 401(k) accounts was a company match. This is a voluntary contribution by the company. Second, if the argument is that the employees should have been told what the executives already knew (and the public evidently did not) so that they could dump their stock at the pre-disclosure high prices, isn't that simply shifting the loss to some other unsuspecting investor? Where's the ethics in that? It could be argued then that the restriction on sale of the stock gift to employees saved other investors from significant loss.

Clearly, the restriction on sale of the Enron stock in the 401(k) plan did not discourage employees from contributing to the plan. The smart ones invested their own contribution in a diversified stock and bond portfolio. To change the rules governing 401(k) plans in light of the Enron debacle would be a huge mistake in my view. Many companies would simply eliminate or reduce the voluntary company contribution if company stock is not an option or if it's too restrictive.

As far as non-employee shareholders, you would think the high tech/dot-com crash since March 2000 would have convinced them not to concentrate their assets in just a few stocks. Price speculation involves significant risk. You can win big or lose big. Enron speculators only got what they should have expected as part of the game.

Other News: It's the Growth Managers' Turn...

The 1995-1999 period was pretty tough on value-oriented money managers. I know TAM's net asset growth wasn't what I had hoped for. Too many investors hopped on the growth train and only got off when the train left the tracks in March of 2000. Starting around 1998 we saw a large number of experienced and successful value managers simply retire rather than continue taking the abuse for "poor returns" from their shareholders and colleagues.

Well, now it's the growth managers' turn. Poor returns have forced the managers of the AIM Weingarten, Janus Enterprise, Putnam OTC Emerging Growth fund, and several other big-name funds to step aside. I guess Kenny Rogers was right. Gamblers gotta know when to hold 'em and know when to fold 'em.