



INVESTMENT OUTLOOK

May, 2003

REVISITING DOLLAR COST AVERAGING

We are now entering our fourth year of turbulent economic times punctuated by a weak stock market. If you have owned Variable Life or Variable Annuities during that time, as well as mutual funds and stocks, you probably feel that you have not been dealt with kindly. And yet, the past three years have represented a wonderful time for investors to take advantage of Dollar Cost Averaging.

Ernie Franz represented our company in Cincinnati during the 1970's. Ernie had a wonderful way of describing Dollar Cost Averaging. Ernie would say, "If you purchased 100 shares of some stock selling for whatever price, say \$50 per share, you immediately take on the mindset of a seller. You just invested \$5,000 and the only way you can make money is if the market goes up. But if you are investing \$50 per month, you take on the mindset of a buyer. The lower the market goes, the more shares you buy for your money, and those extra shares that you bought will ultimately put you way ahead."

Take a moment and think about your financial future. If investing in the stock market is part of your future, is there any way that you would end up believing that there never will be any down years. Think of the next ten, twenty, forty or sixty years, based upon your age, and just reflect for a moment on how ludicrous it would be to believe there will never be a bad year in the market. If history tells us that one out of every three and a half years will be a down year, then a twenty-year projection must include seven down years. A thirty-year projection must include ten or eleven down years. So if you know that those long term growth rates of 10% or 12% or possibly more all included bad years, then exactly what is your plan of action during a bad year going to be?

Our company got Beatrice Foods as a client in 1977. We were installing a plan in which the employees were buying Beatrice stock along with life insurance. I had a meeting with Jim Dutt, the President of Beatrice, in 1979 and he expressed surprise that even though Beatrice stock had dropped from 25 to 16 over the past two years, he hadn't heard a single complaint. We explained that in our offering of the stock, we first explained Beatrice as a company so that the employees were enthusiastic about becoming shareholders. It was obvious the employees understood that at 16 per share, their money was buying them more shares than they would have gotten at a price of 25. As it turned out, Beatrice was taken over in a leveraged buy-out in 1986 and all the shareholders were paid \$50 for their stock. They had acquired 50% more shares at 16 than they would have at 25.

Stock prices have always fluctuated and we all know that to make money, we must buy when prices are low and sell when prices are high. So what's stopping you? If you are like most people, it is *fear of the unknown*. "Just when is all of this nonsense going to stop?" we ask. I can answer you that to a great extent it has stopped. I cannot tell you how quickly the market will rebound, but I do have a few thoughts.

First of all, I do believe that the worst news is behind us. I may not be a fan of the current administration in Washington, but I must observe there was a level of competency in the speed and manner by which they took care of business in Iraq. It is also a political reality that the President must stand for election in just eighteen months and he has an economy to deal with. Clearly, it must be etched in his mind that his father lost his election after winning the Gulf War. The economic needs and concerns of a nation cannot be ignored and I believe that Richard Hoey of Dreyfus was correct when he projected a better economy in the second half of 2003 and an election boom in 2004. Will such a boom take us back to where we were in March 2000? I don't

know. What I do know is that if you take advantage of the remaining low prices and buy, then you don't have to get back to March 2000 prices to be financially restored.

Jeff is a participant in a 401(k) plan we manage. He was very concerned last Fall as he noticed that in spite of some very large personal and employer contributions to his plan, he was worth a lot less than he had been two years earlier. Jeff's plan had reached a high point in June 2000 and the September 2002 represented a new low. The cost to Jeff was over \$90,000 in value. I asked him if he had taken into account how many shares of stock he had purchased during the past two years in his various fund accounts. He had not. I pointed out that two of his funds were worth over 80 per share in June 2000 and both were in the mid 20's as of September 2002. At those lower prices, he had purchased many more shares. In order for him to regain his losses, those two funds only had to get back up to the low 50's. If they stayed in the 20's for another six months, his breakeven point would drop into the 40's. I don't know if either of those funds will get back into the 80's in the foreseeable future, but they don't have to. A price in the high 40's will now restore Jeff's losses and everything above that is pure gain... on a larger number of shares.

The technical reason that Dollar Cost Averaging works is that if you are buying at a fairly constant rate, be it monthly, annually, or whatever, your purchases at lower prices will buy you more shares while your purchases at higher prices will buy you fewer shares. This means that at any time, more of your shares will have been purchased at lower prices and fewer shares will have been purchased at higher prices. The operative phrase is that "the average cost of your shares will always be lower than the average of the prices that you paid for those shares."

To set your mind at ease, ask us to run a Morningstar analysis of your account that will show the Top Fifty holdings. We weight your account by how many dollars you have in each fund, look at the holdings of that fund, and then tell you what your overall account consists of. I've done this for a number of our clients and the companies that head the list always seem to include:

*Pfizer, Microsoft, Citigroup, Phillip Morris, General Electric, Johnson & Johnson
Exxon Mobil, Colgate Palmolive, Merck, Pepsico, Walmart, Coca-Cola*

Just what scares you about owning these companies? And if these companies currently are selling at such low prices, and you have available cash, then why aren't you buying? Certainly it makes no sense to say that you don't want to buy until after the prices have gone up.

Here are a few basics to keep in mind. Holding money in a tax-deferred account earns you more than in a taxable account because you don't have to truncate your growth each year by having to pay tax. If you are in the 33% bracket, then let me assure you that growing your money at 6% in a tax-deferred environment will give you better results than holding the same investment in a non-taxable environment and growing your money at a net 4%. Secondly, the permanent elimination of income tax on earnings inside a variable life insurance policy remains the best way to build your assets. The only way you can be hurt is if you do not make your scheduled investments. Remember, if you stick to your schedule, you are buying more shares at low prices which offsets the mortality expenses being paid by shares that are being redeemed at low prices. If you don't make your investments as you planned, the policy can be adversely affected... but that would have happened in an up market as well.

If you have questions on any of these ideas, please give me a call.

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