March 31st, 2004

"Those who do not forget the past are the masters of the future." Sima Qian

At Disciplined Equity Management, we constantly study history in order to avoid the mistakes of investors who have gone before us. Every examination of financial history reveals that no one has ever successfully predicted the short-term movements of the market over any meaningful period of time. Consequently, one of the tenets of our disciplined investment approach is that making predictions about the equity markets is not only a waste of time, but actually detrimental to successful investing.

In contrast, consider what life is like for the vast majority of equity investors who do not follow a disciplined investment approach such as ours. Despite history, most investors continue to believe that the path to financial success somehow lies buried in the news of the day and the resulting short-term market fluctuations. These investors hang on every word of the financial experts in order to profit from (or avoid the loss from) from current events. After all, they say, why own stocks during the bad periods when they are universally expected to go down?

The fatal flaw in this approach is that all currently known **and** expected information about world events is already priced into securities. *Un-anticipated* events are what move the global equity markets. And until someone invents a reliable time machine, predicting the future will continue to be impossible. Why then, do self-proclaimed market gurus continue to make market forecasts? Note the following quotes from some of the world's most well respected financial experts over the past year:

> *"I do not believe a long-term investor will make money in this market because it is a secular bear market."*
> Felix Zuelauf of Zuelauf Asset Management. Source: "On the Money—Roundtable Part II," *Barron's* (January 2003).
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> *"I suspect that 2003 will end up being the fourth consecutive down year for the first time since 1932."*
> Jeremy Grantham of Grantham, Mayo, Van Otterloo & Co. Source: "Is The Bear Market Over?" *Smart Money* (January 2003): 71.
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> *"These stocks still are way ahead of themselves. I am not at all sure we have seen the bottom; I think we could see new, lower lows."*
> John Rutledge of Evergreen Investments. Source: E.S. Browning, "Experts Duel Over Fate of Bellwether Rally," *The Wall Street Journal,* (June 2003).

Far from being the predicted debacle, 2003 instead proved to be one of the very best years on record for both the major stock market indexes and our quantitative portfolios. Once again, heeding the advice of the prognosticators proved to be the exact wrong thing to do.

History teaches us to: Commit to a disciplined approach. Diversify broadly. Ignore the noise.

As a postscript, this newsletter gives us the opportunity to unveil our new corporate image with our stationery. To view the entire package, please visit our new interactive website at www.DEMgt.com.

Don Davey   Jeff Kopp