

Monthly Chartbook

March 2004

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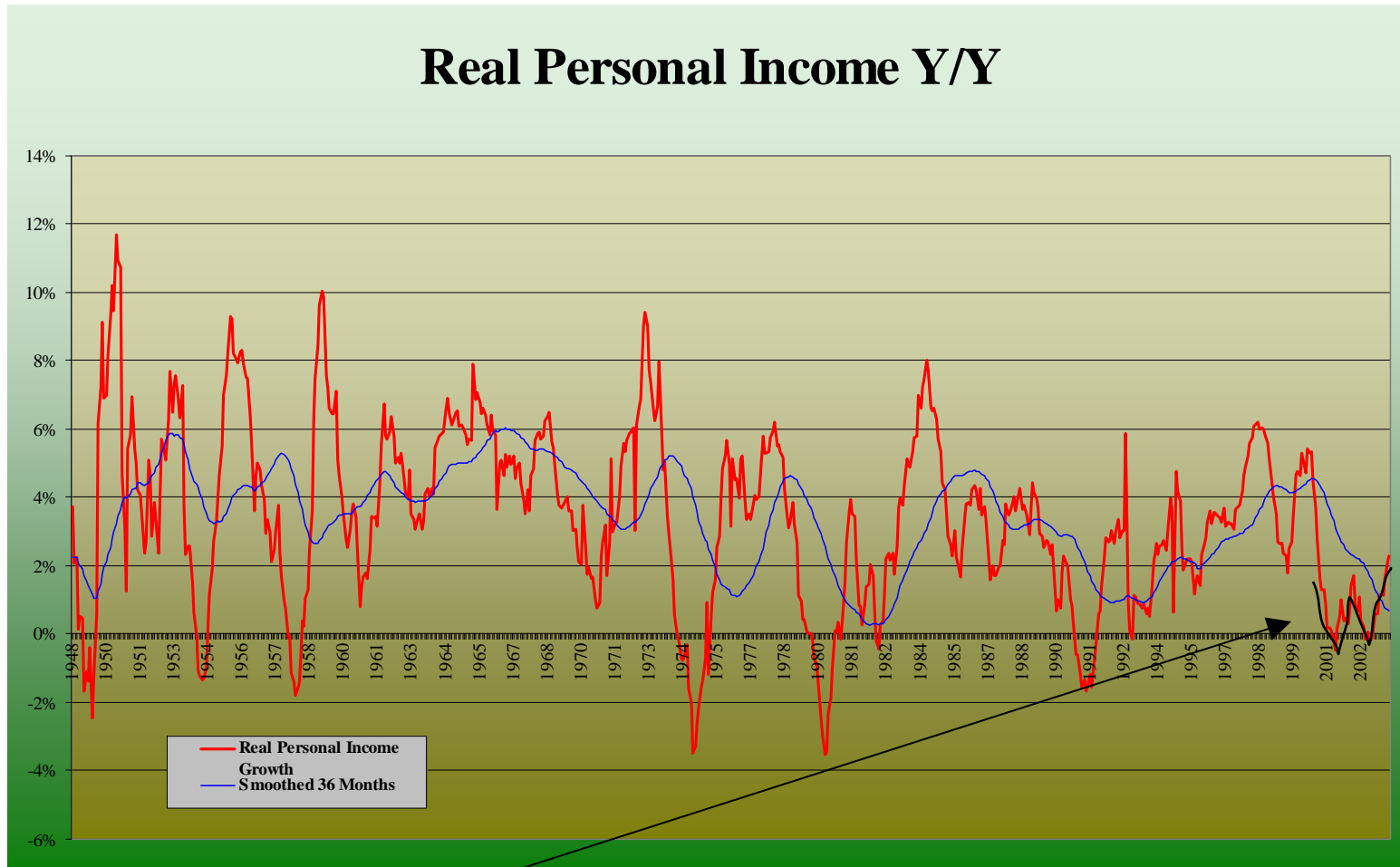
Executive Summary

In the middle of a “W” recovery

- No pun intended. Events over the last 12-18 months (like the war in Iraq) delayed robust growth.
- Economy bottomed in October of 2001 and again in April of 2003... “W” recovery.
- Double bottom explains some of jobs lag against robust GDP growth.

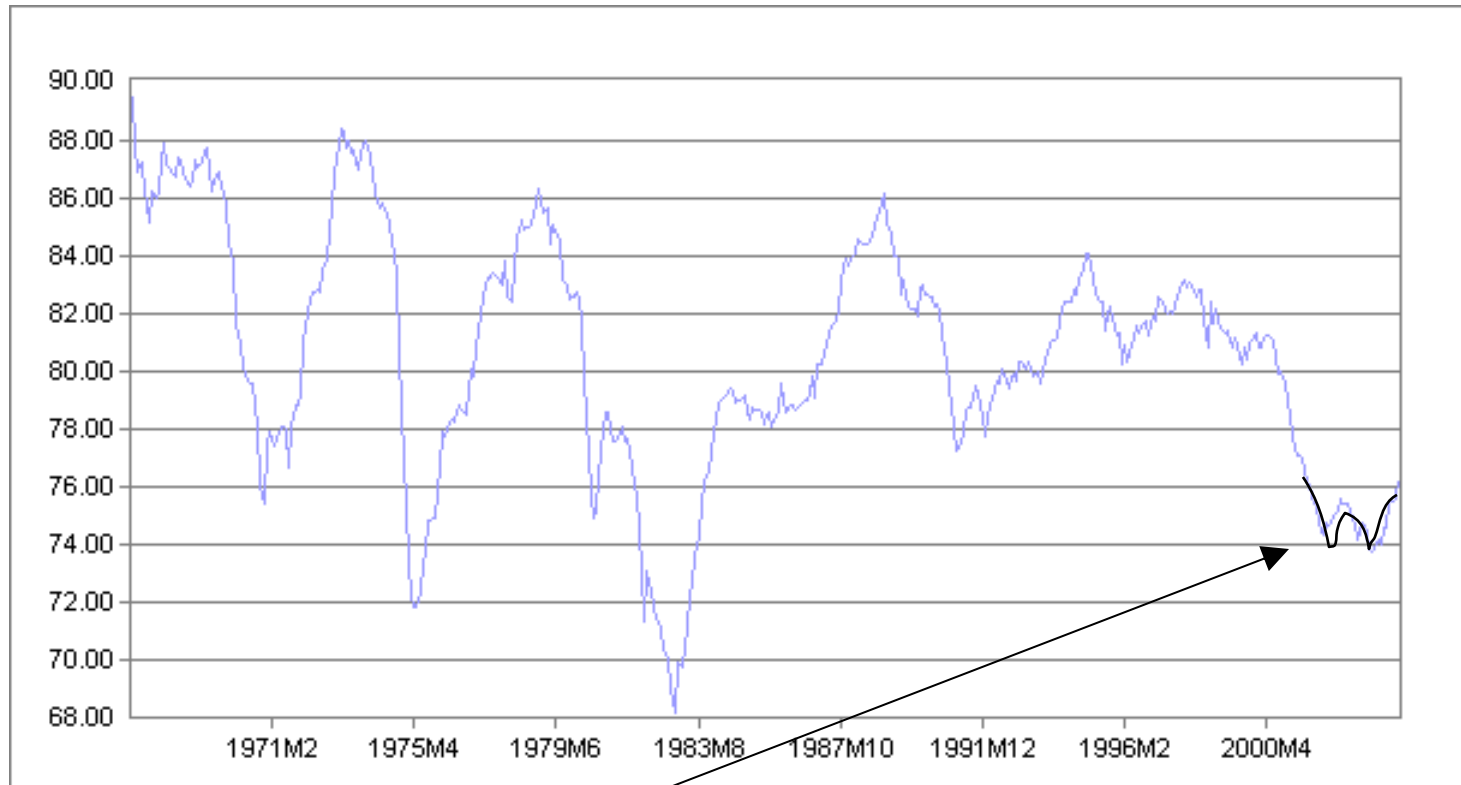
Executive Summary

- First half of the year growth looks strong; strength of the rest of 2004 in question.
- Labor markets improving, but not as swiftly as after past recessions.
- Inflation is low, but critical prices are rising.
- *Growth is status quo.*

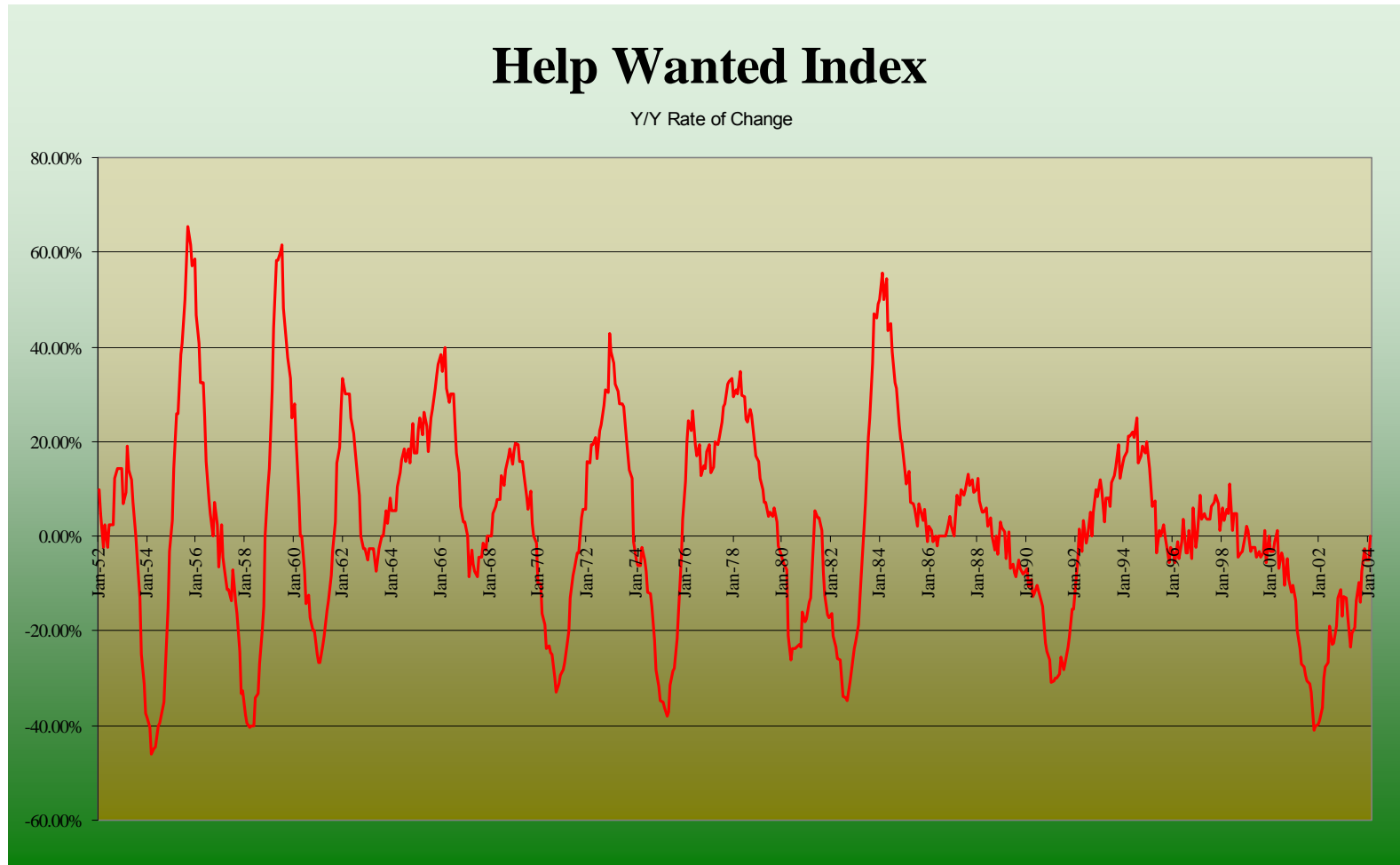


Confidence and events surrounding the war on terror led to a double bottom in the economy in October of 2001 and again in April of 2003, delaying effects of robust growth even as GDP moved higher.

Macro-economic Research



US manufacturing Capacity Utilization Ex. High Tech. This series has had a fit of misstarts after the first bottom leading to a lack of confidence in manufacturing hiring.



The help wanted index bottomed in October of 2001 and again in April of 2003 consistent with the “W” recovery. If this index continues its trend higher, it should indicate robust job growth.

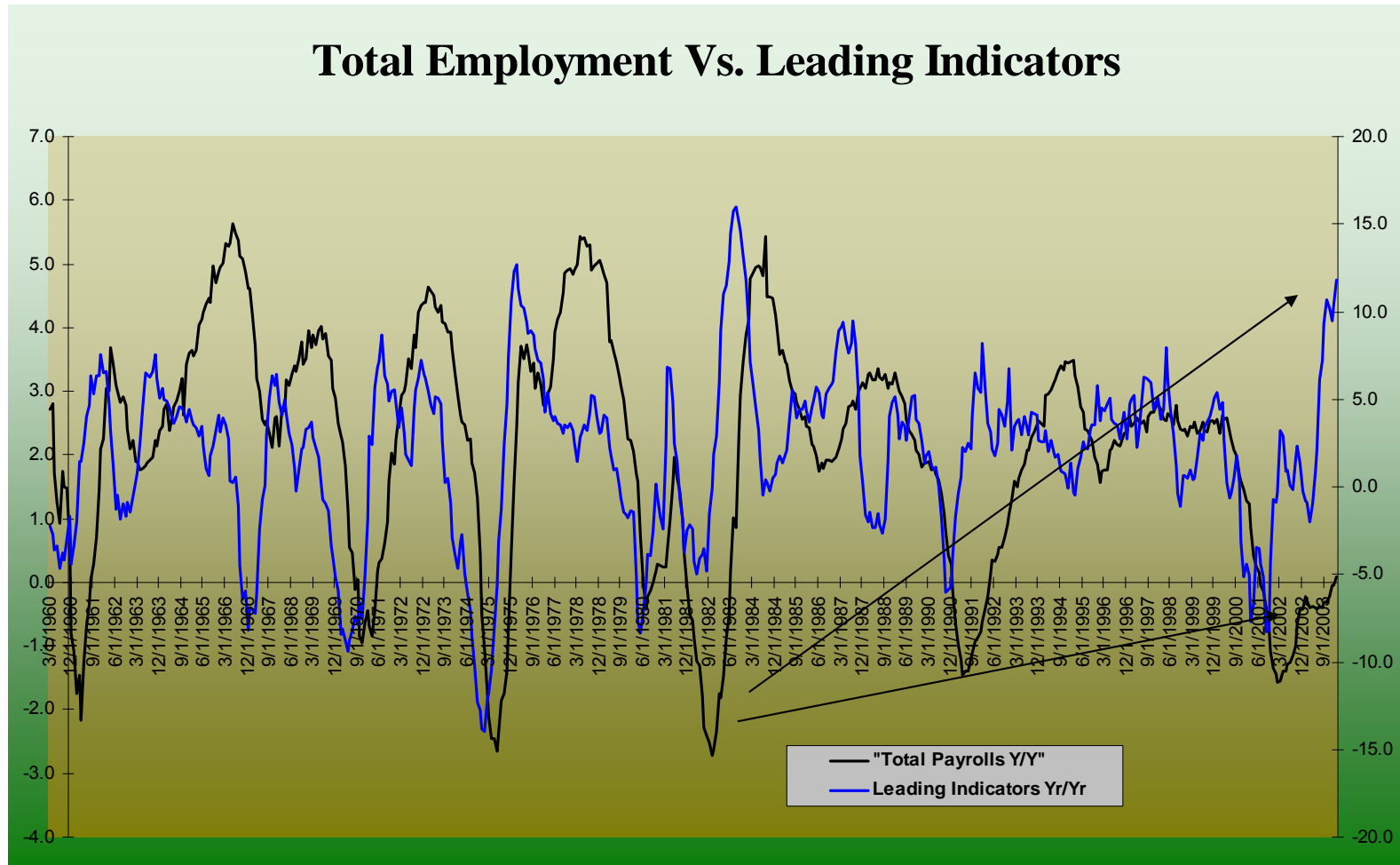
Where the jobs are:

Percentage of employers who expect to hire more workers in the second quarter of the year.

Construction	42%
Education	15%
Finance	23%
Manufacturing (durables)	31%
Manufacturing (non-durables)	27%
Mining	21%
Public Administration	21%
Services	30%
Transportation/Utilities	23%
Wholesalers/Retailers	30%

Source: Manpower International

The Employer Outlook Survey by Manpower International, a Milwaukee-based staffing company. The quarterly survey notes that 28 percent of employers expect to hire more workers from April to June. This is the third consecutive quarter that employers reported an up tick in hiring.



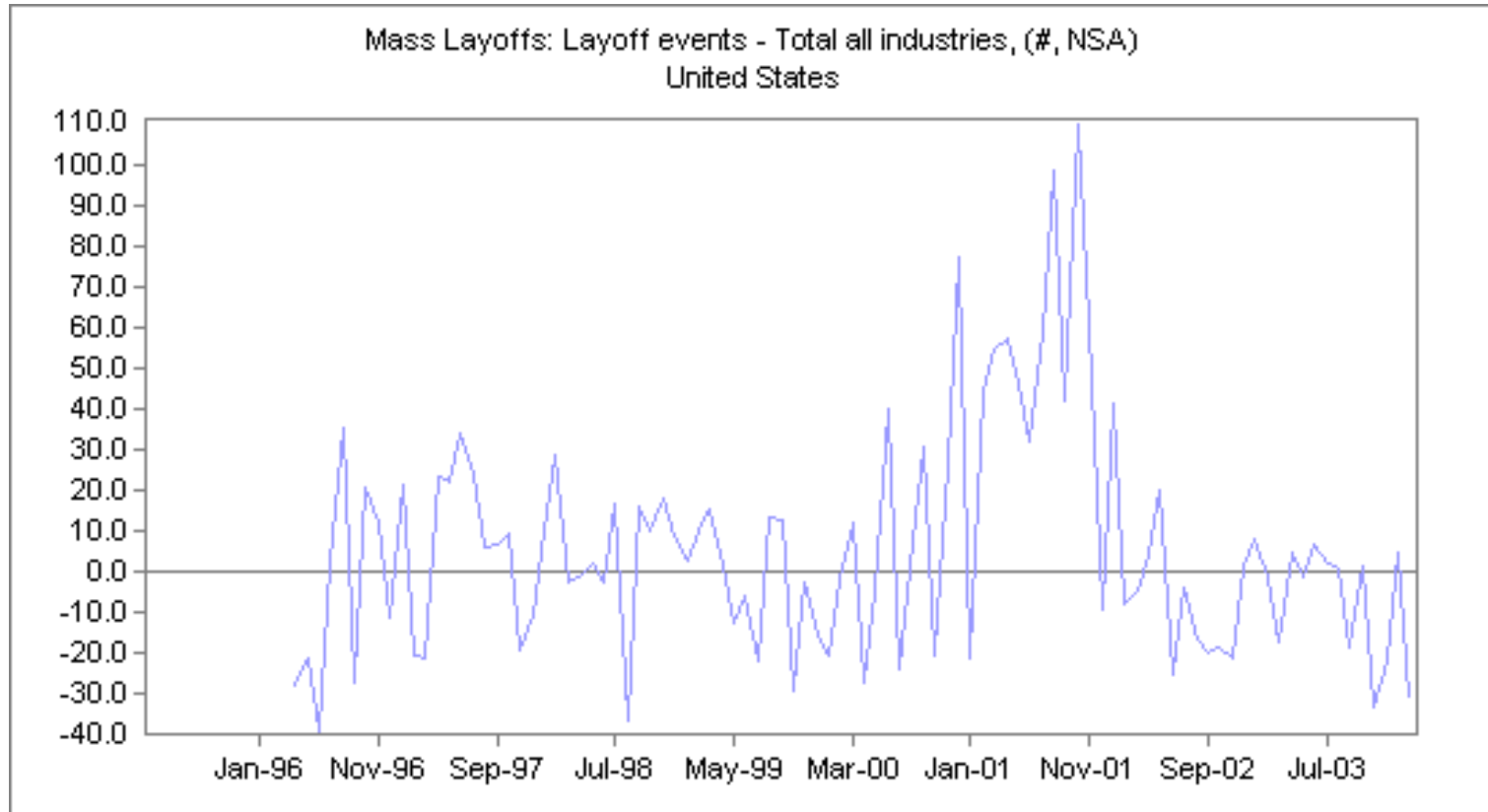
Employment lags and IS following the broader economy higher.

Macro-economic Research



Persistent joblessness has been stubborn and has only improved to levels consistent with job growth in the last three months. Index levels above 1 are consistent with improving labor market conditions.

Macro-economic Research



Monthly mass layoffs are trending down, consistent with other improving labor indicators we follow.

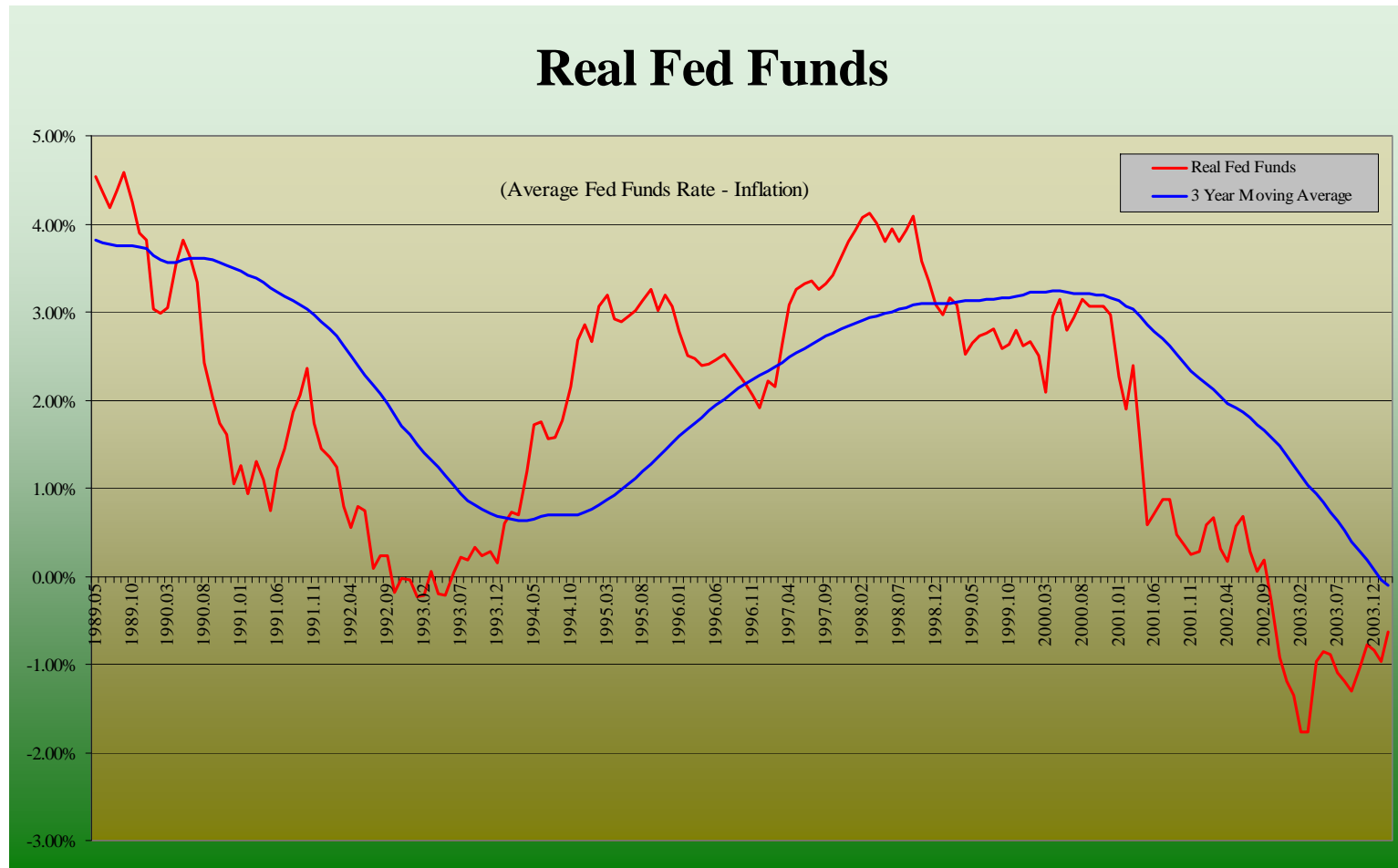
Capital Markets Expectations

Index	Current	Forecast		Range	Time Frame
S&P 500	1126.21	Trading range	↔	1090-1240	10-12 Months
Ten Year Treasury	3.86%	Bottomed June 2003	↑	4.00%-4.625%	10-12 Months
Inflation (all Urban)	1.64%	2.25%	↑	1.75%-2.25%	12-18 months
Fed Funds	1.00%	1.00%-1.50%	↑	1.00%-1.75%	6-10 months
S&P 500 Earnings	\$49.32	\$53.50	↑	\$51-55	1q2004
	Legend:	↑ "Good"	↓ "Bad"	↔ "Indifferent"	

Federal Reserve Watch

- Real Fed Funds are moderating as inflation has fallen.
- Monetary policy is still accommodative, but look out for marginal tightening going forward.
- Everyone “expects” higher rates and higher inflation and a tighter FED. Is this a danger sign if you are contrary?
- As the election approaches, the Greenspan question is going to be asked again and again. If Dr. G is looking for an out, election time is it.

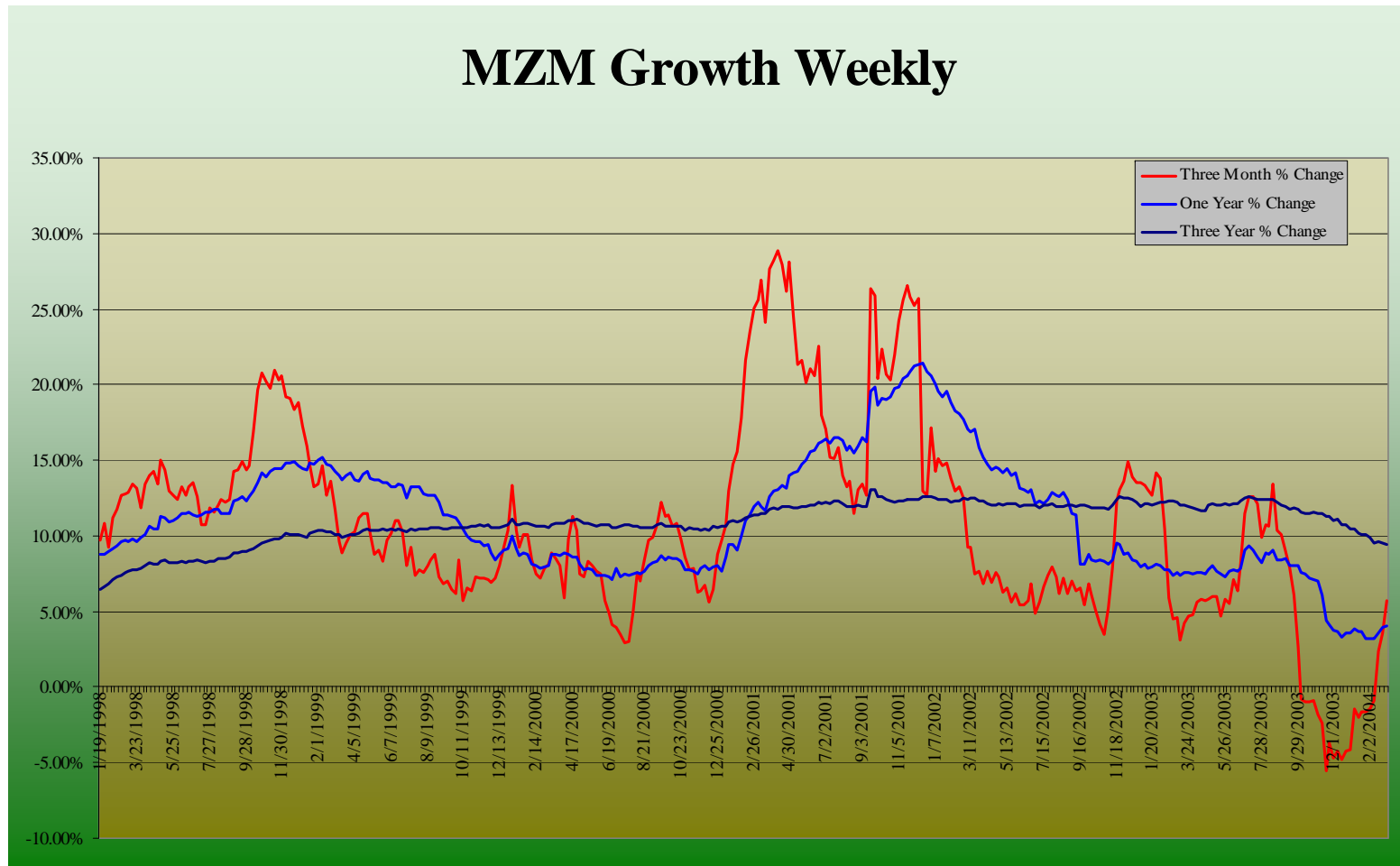
Federal Reserve Watch



The negative Fed Funds Rate explains why Bank & Money Market Yields are so low.

We believe the Fed will have few reasons to keep real interest rates negative as employment and output improve. The 30 year average for Real Fed Funds is 2.72% -- significantly above current levels.

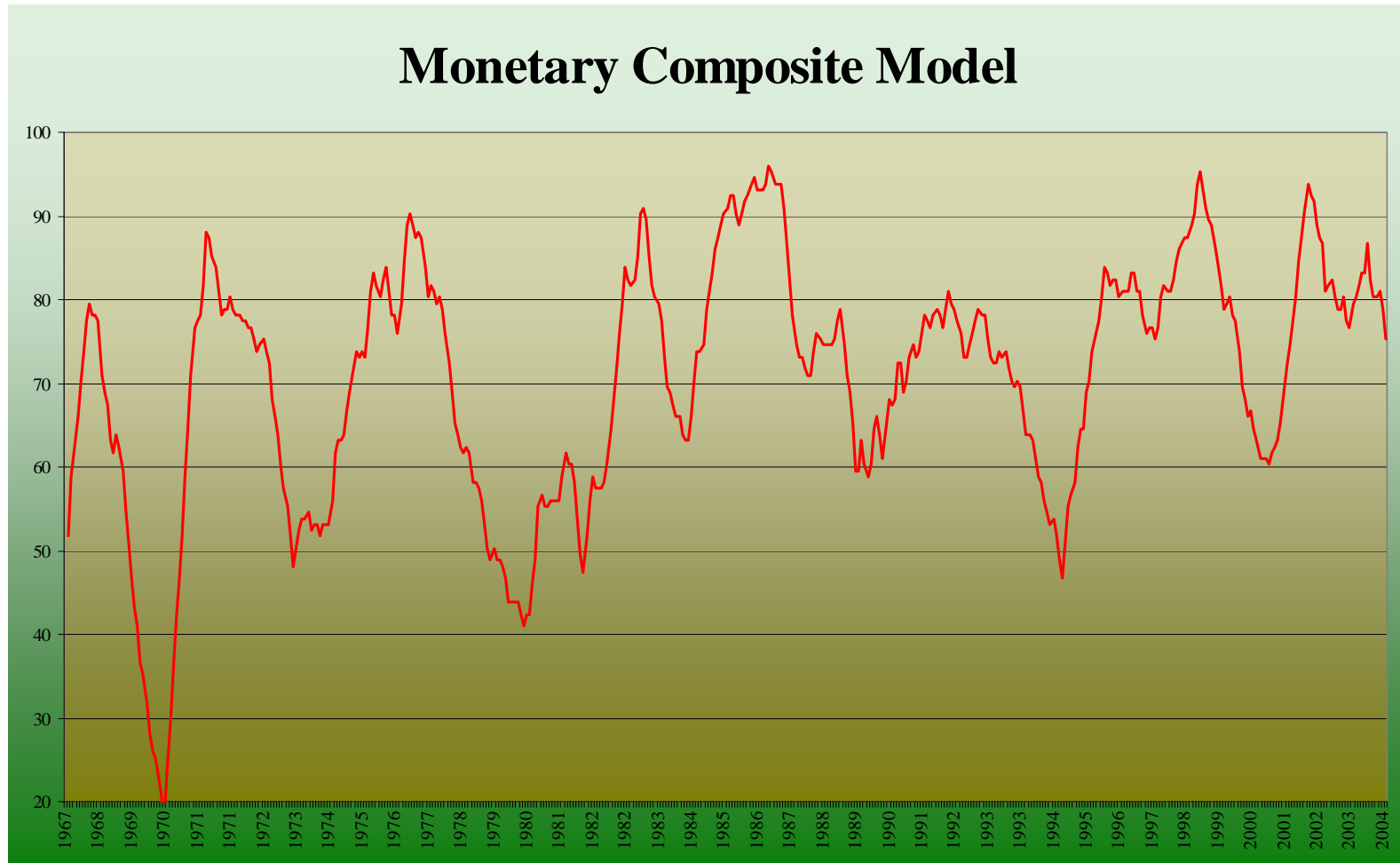
Federal Reserve Watch



Money Zero Maturity (MZM) is a broad measure of liquidity that is significant to lending, business activity, and equity prices.

The 3 month growth rate of money supply continues to improve considerably.

Federal Reserve Watch



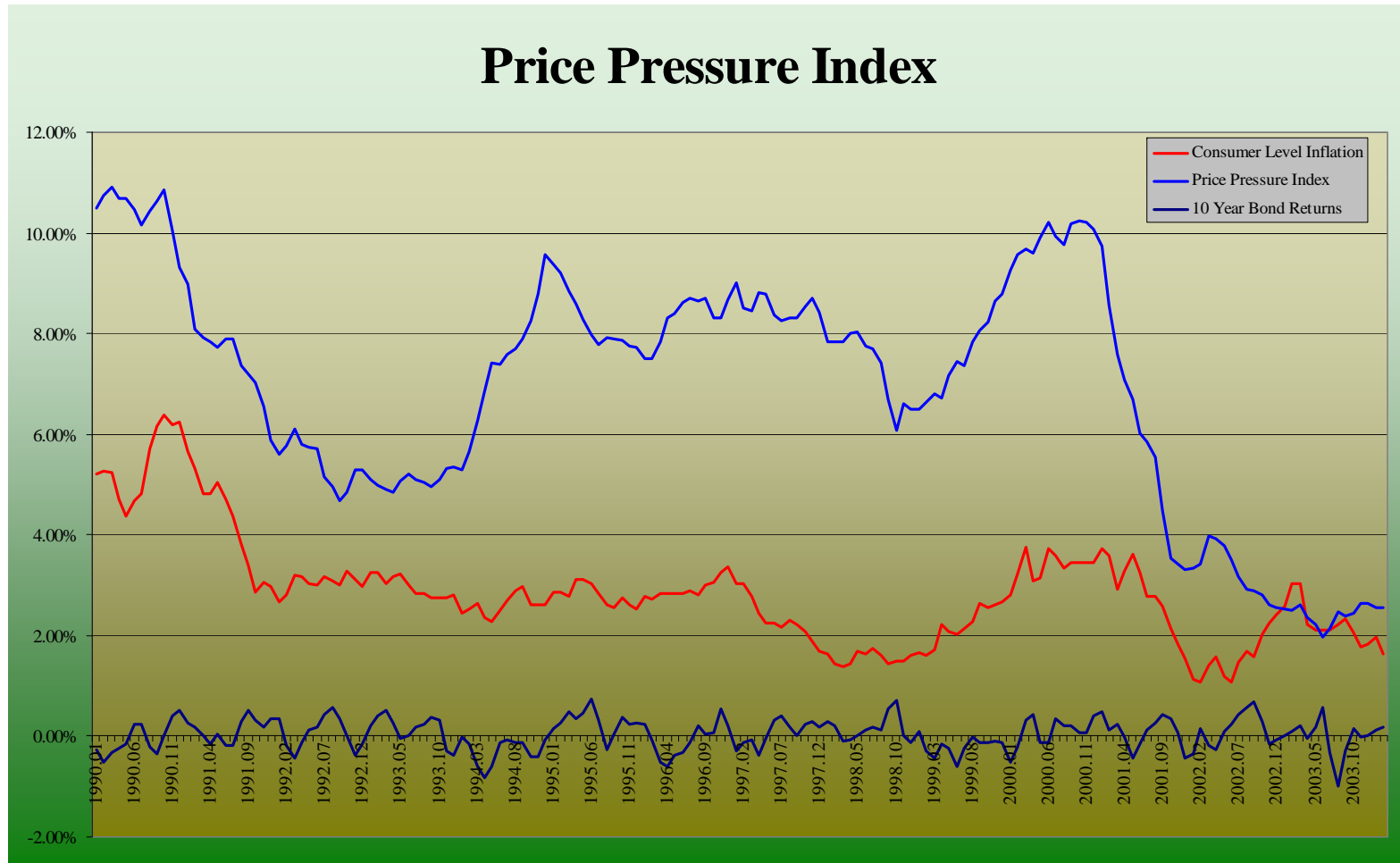
The direction of trend in this series is as important as the level. A score above 50 indicates the Fed's monetary policy is accommodative.

Monetary composite model is moderating slightly in recent months.

Inflation expectations

- Leading indicators on inflation are flashing warning signs. Energy and materials prices cannot continue to move higher without either effecting profits or consumer prices.
- Energy prices are the biggest current concern on the inflation horizon. There is somewhat of a supply/demand imbalance due to factors like RFG gasoline.
- If energy prices remain stubbornly high, they will bleed over into the core rate of inflation.
- The market anticipates higher inflation (2.58% expected versus 1.64% current) over the next cycle, as indicated by its pricing of inflation-protected Treasuries.

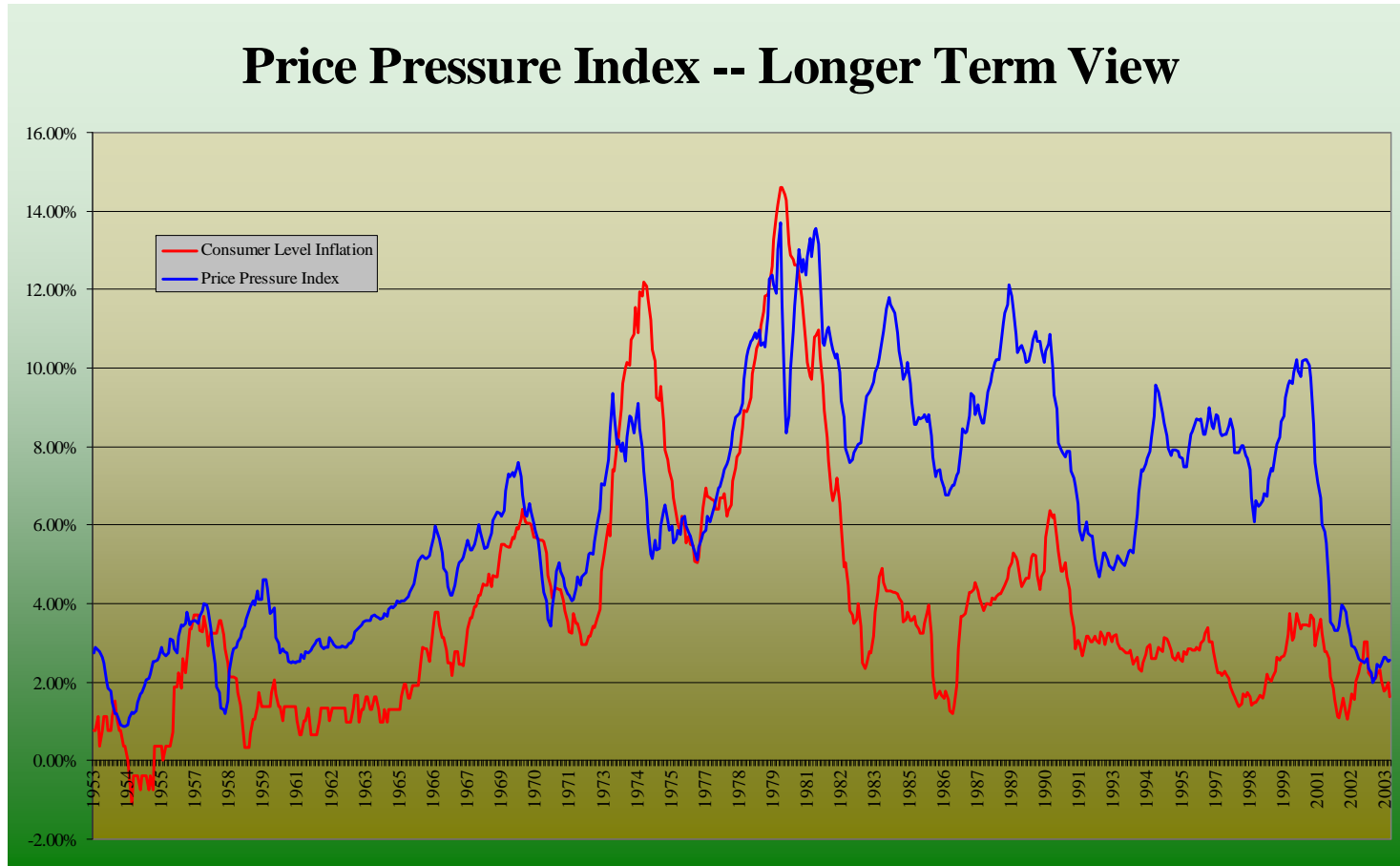
Inflation expectations



A declining index value indicates receding inflationary pressure within the economy, and a rising index value foretells higher consumer prices.

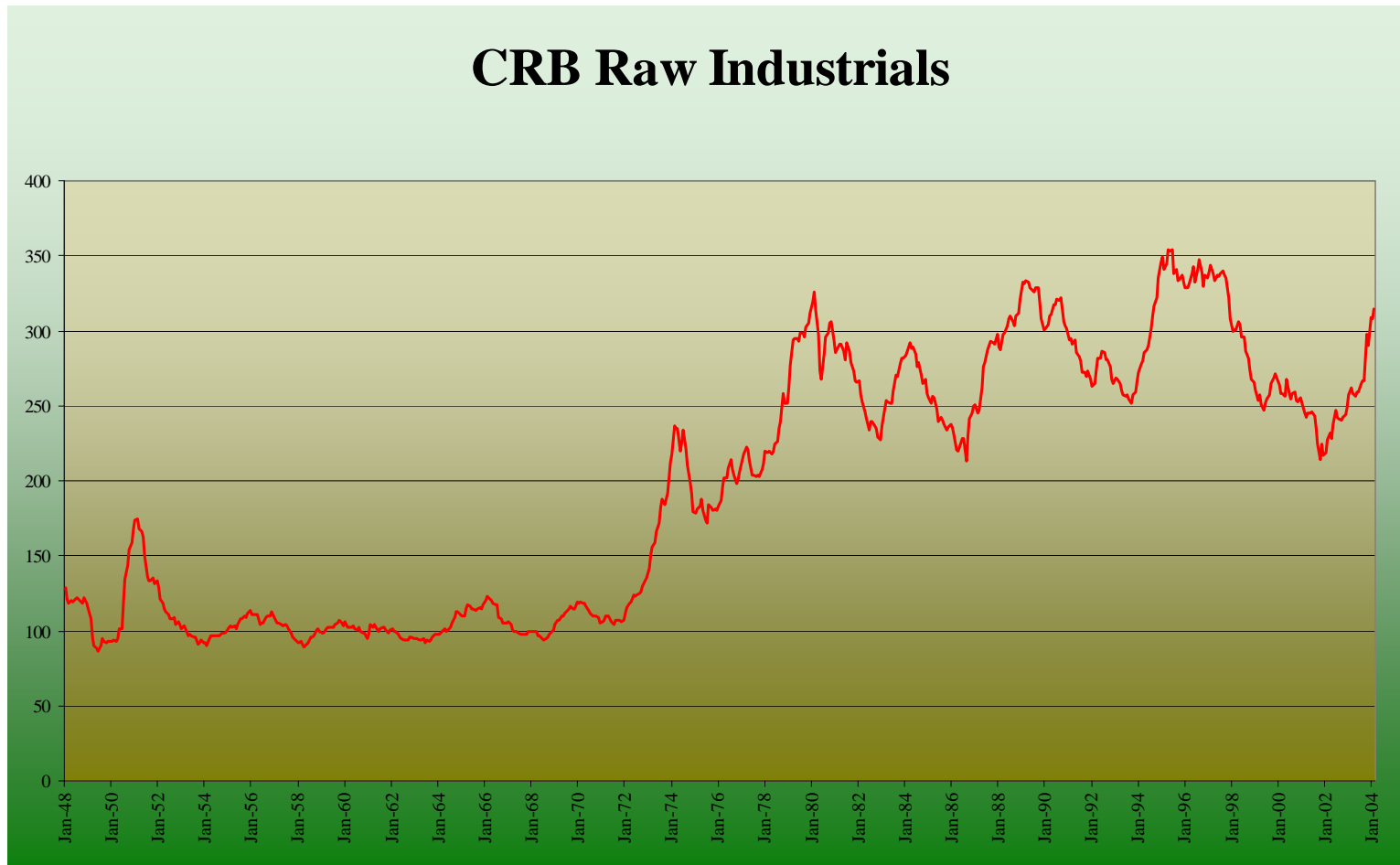
The Price Pressure Index bottomed June 2003.

Inflation expectations



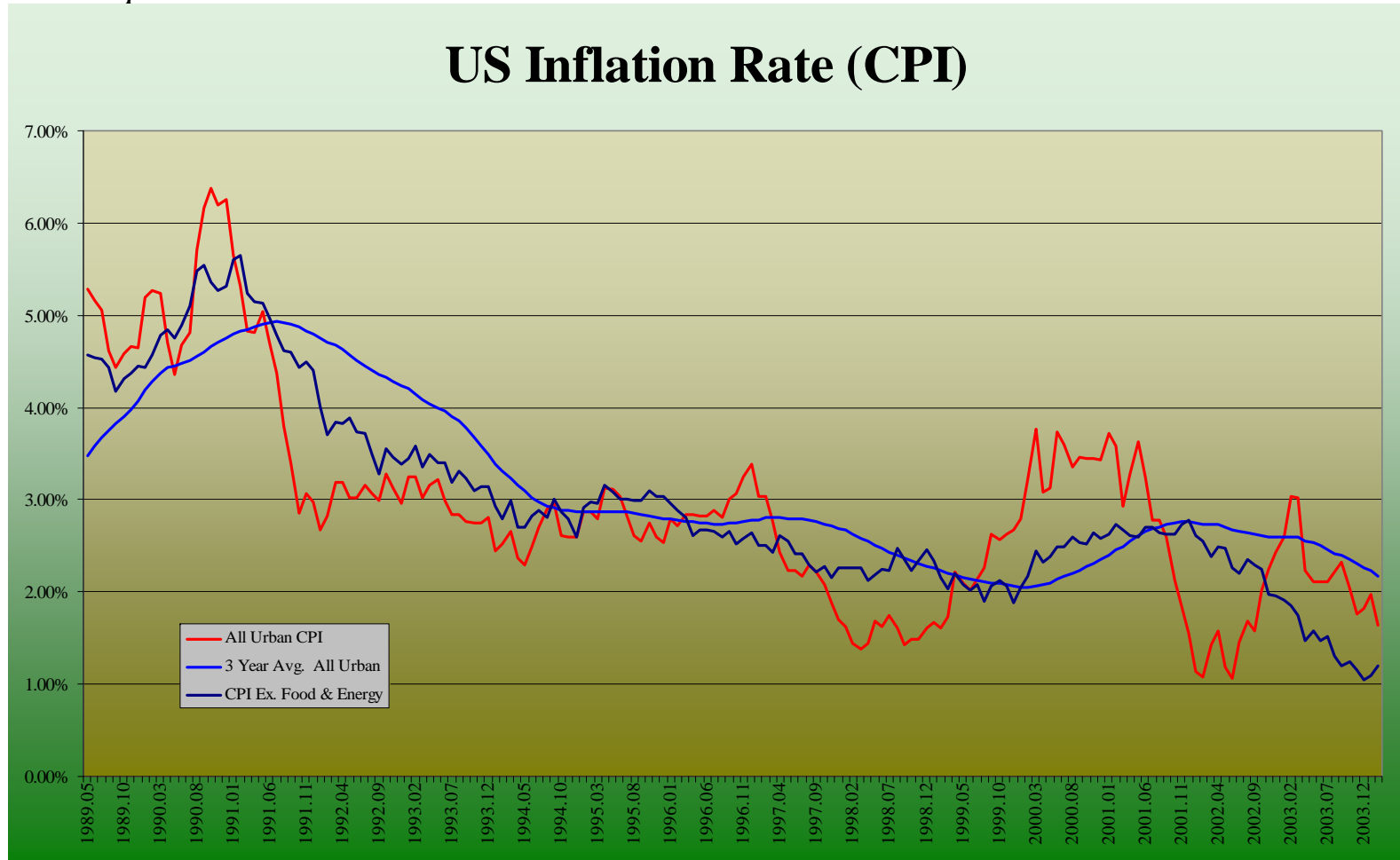
The Price Pressure Index is at its lowest levels since the mid-1950's.

Inflation Expectations



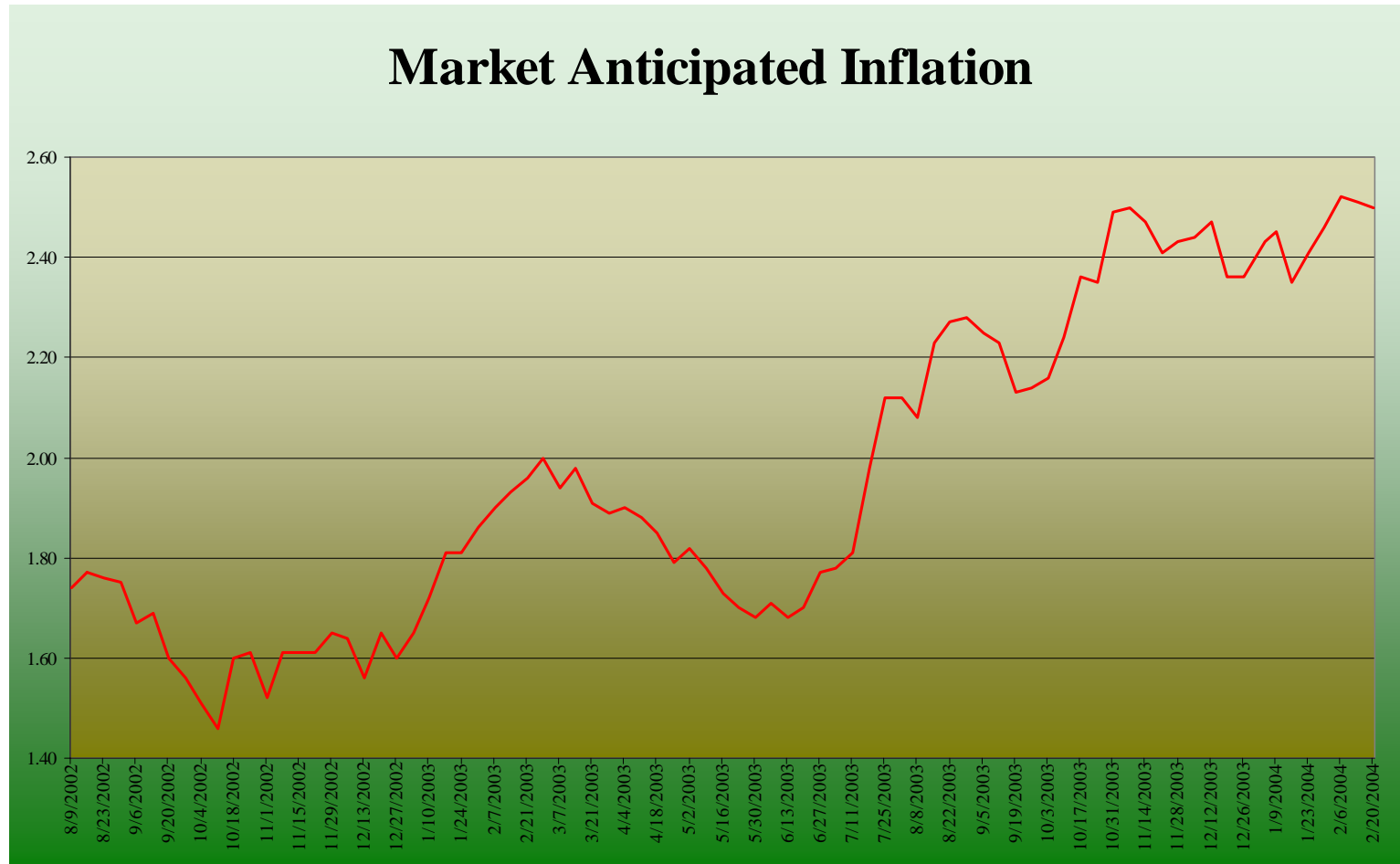
Materials prices are continue to move and end users are seeing the results in the final prices of many manufactured products like finished steel and copper wire.

Inflation Expectations



Inflation remains low at the consumer level even though there has been an sharp increase in the cost of raw materials. This divergence bears close attention.

Inflation Expectations

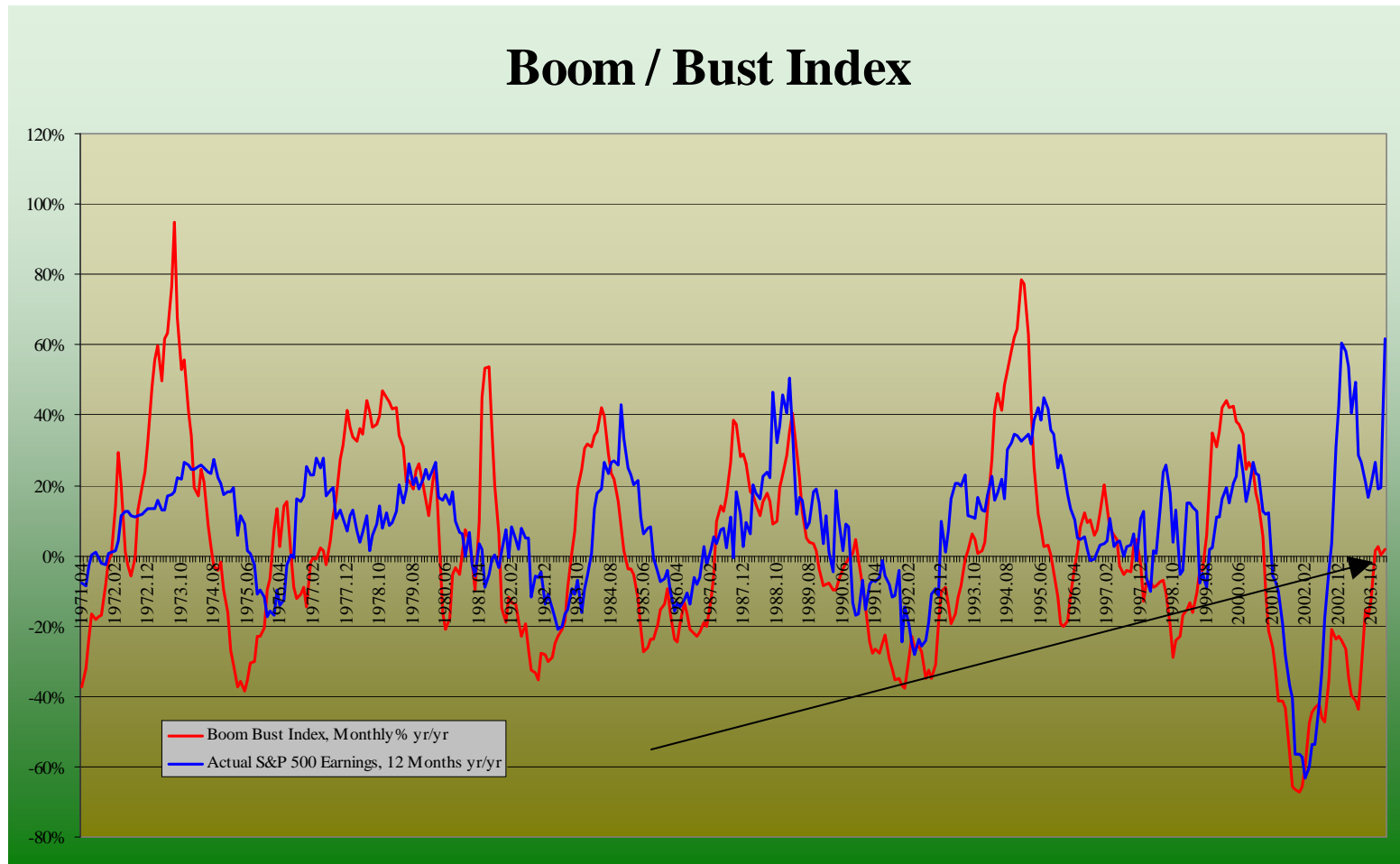


The market anticipates inflation (based on TIPS) to be about 2.58% over the next ten years. Inflation has averaged 1-3%, so that is right in line with experience, but much higher than current levels.

Outlook & Forecast

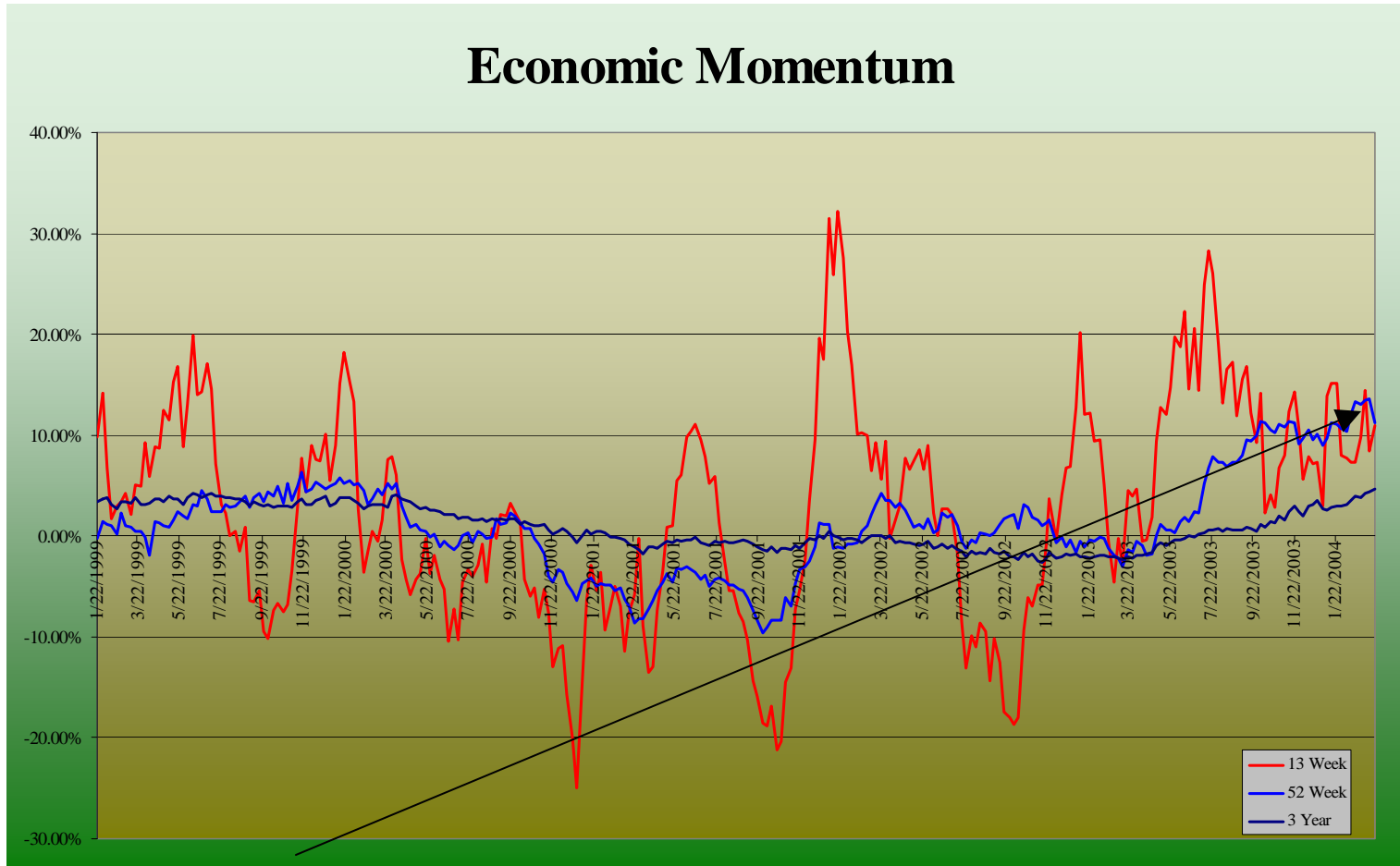
- Cornerstone is optimistic but vigilant:
 - Earnings will move the market.
 - Labor markets an “improving” election issue.
 - Stock picking is key, and the few compelling values have “issues” (AT&T, EP, EK).
- Equities with 2.0% to 4.0% dividend yields may be better income vehicles than most bonds at this point.
- Foreign exposure, particularly Asia including Japan continues to be timely.
- Watch those natural resource stocks!

Outlook & Forecast



The Boom/Bust Index tracks several key variables within the economy that correlate with earnings. The red line is predicted S&P 500 earnings direction, indicating positive movement continuing for earnings.

Outlook & Forecast



Data presented is the ECRI Weekly Leading Indicators (source: www.businesscycle.com).
Y/Y Momentum continue to be at the highest levels we have seen in a number of years.