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News Flash...Technology Hits $8.00 a Barrel

Experienced investors are familiar with the impact that oil prices have on the world economy. As a key industrial ingredient, it is known that low energy prices are good for economic growth prospects and vice versa. Over the last decade, investors have witnessed the advent of a new, and perhaps more important, ingredient to growth ... technology. In this newsletter, we hope to document the impact that the bursting of the technology investment bubble has had on markets and make some predictions as to the longer-term implications for investors.

Nowhere is it written that technological advances come without surprises. Decades ago, the computer revolution began with "dumb" terminals connected to mainframes. It has since morphed into "smart" personal computers networked over the Internet. As we speak, the next generation of wireless interactivity is being developed which may make the traditional personal computer of less importance to the home and business. An example of how quickly things change is the fact that the Internet nearly took Microsoft by surprise a few years back; in much the same way that Microsoft probably surprised IBM with Windows.

More recently, the false fear created by the advent of the Year 2000 problem encouraged computer upgrades by the millions...all of which have enhanced connectivity and computing. At the same time, the wonders of the Internet created an aphrodisiac-like response from investors who poured money into dot.com companies. Similarly, some telecommunication companies increased their "bandwidth" expenditures while they witnessed deterioration in their revenue base (i.e., declining long distance rates).

This technology experience reminds us of the oil shock of the 1970's when oil prices increased from under $10.00 a barrel to well over $30.00 and the Arab cartel had America scrambling. Investors assumed that the oil supply would never catch demand and billions of dollars went into spurious oil drilling projects (shale oil patches in Australia, etc.). Enough money was lost during this period that more than a few banks (Sea First and Penn Square) failed, in part due to their aggressive oil lending. Eventually, oil prices dropped and contributed significantly to our economic expansion.

Back to the present. In our view, technology has grown to be as important an ingredient to economic prosperity as oil. Just like the assumption for oil prices ($80 a barrel was the prediction in the 1970's), the prospects for certain technology companies were unpredictable and, instead of bank failures, we see unhappy technology investors this time.

As we have documented through our newsletters, and more importantly through the diversified structure of our clients' investment portfolios, we have not been surprised by the correction in some sectors of the market. Most dot.com company stocks are currently trading 90% or more below their highs or are bankrupt. The NASDAQ technology-heavy index is off by roughly 60%. The collapse in technology stock prices has been significant enough to drag down the broader index of the S&P 500 by roughly 20% from its high.

Such poor performance by the equity markets is threatening consumer confidence. In addition, there are numerous "global issues" which are not too heartening. Renewed fighting in the former Yugoslavia, continued unrest in the Middle East and fragile markets in South America are concerning. Japan's economy is leaning on a thin reed and our new president is challenging both China and North Korea on diplomatic fronts. As if that were not enough, the cows in Europe are getting madder and madder.

Fortunately, there is a positive "flip side" to all of the messy news just discussed. While the technology run-up and subsequent collapse has disappointed some investors, it certainly helped the world's technology infrastructure. E-commerce initiatives, broadband enhancements (fiber optics and switches) as well as Internet and wireless advances are astounding and are improving safety and efficiency in every corner of the world. As excess capacity is wrung out of the technology sector, the prices for technology products and services are dropping thus encouraging additional technology investment.

The technology pullback has triggered some economic malaise, but one can argue that the expansion we were experiencing had become nearly uncontrollable. For example, the country was operating at the point of labor and electricity shortages. Imagine California's problems this summer if our economy did not have this "pause to refresh"? Also, many displaced dot.com workers will now return to the traditional work force and help keep inflation low.

From a stock market standpoint, nothing good was going to come from the technology bubble getting any larger. In our view, the renewed seriousness of investors will cause capital to be allocated more judiciously and economically. Just as dropping oil prices helped fuel our economy during the last 10-15 years, today's inexpensive technology products and services will likely do the same for the coming decades. We will do our best to diversify client portfolios in ways which will take advantage of the terrific global prospects which await us.

Important Disclosure: "It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities discussed in this newsletter."