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# FREDERIC T. KUTSCHER ASSOCIATES, INC.

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*Comprehensive financial counsel for individuals, families and trusts*

Research suggests that investment portfolios shouldn't be rebalanced too frequently due to transaction costs and other ailments of over-management. This is why we customarily rebalance a client's portfolio when we perform a review of his or her entire financial plan. But occasionally market conditions suggest to us that a change shouldn't wait until the annual review.

Here is an example of a letter we sent in April 2004 recommending a special interim adjustment for a client with a policy of 5% cash, 38% bonds and 57% stocks.

April 2, 2004

We are writing to obtain your permission to institute a few interim portfolio adjustments.

These changes are occasioned by our desire to reduce your market exposure to both high-yield bonds as well as real estate investment trusts (REITs) which, as you may recall, we regarded as "fat pitches" or undervalued asset classes in 2002 and 2003. Both asset classes have been tremendously successful over the last several years.

Since 1999, REITs have outperformed other equities by a sizable margin. But the valuation picture has become increasingly less appealing as their premium to their underlying asset values has increased to more than 27% -- that's only a few percentage points below the REIT peak reached in October 1997.

With respect to bonds, you'll recall that yield movement runs inverse to price movement. Consequently, the fact that high-yield bond yields are near all-time lows is very significant. We sense the high-yield bond market now fails to reflect some of the structural risks such bonds possess inherently. Expected returns are presently not competitive with equities, and junk bond yields are near their lowest level in two decades compared to stock dividend yields. Thus, high-yield bonds now appear overvalued and we believe it is prudent to return to a more neutral position which dictates no special allocation in that asset class.

Considering all of the above factors, we propose to make the following adjustments in your portfolio at Schwab on or around April 12, 2004:

*Hoge Building  
Suite 800  
705 Second Avenue  
Seattle, Washington  
98104-1711  
Phone 206/382-4414  
Fax 206/382-4412*

April 2, 2004

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- Sell all your REIT and high-yield bond funds.\*
- Reinvest the resulting proceeds approximately as follows:

|     |                                |
|-----|--------------------------------|
| 10% | Aggressive Bonds               |
| 10% | Large Growth Stocks            |
| 20% | Large Growth-at-a-Price Stocks |
| 30% | International Bonds            |
| 30% | Large Value Stocks             |

At the time of reinvestment, we will distribute the proceeds among funds that are managed in the asset classes and styles described above. If you want further details at that time, please let us know, otherwise we propose to use the managers with whom you are already invested, with the addition of PIMCO GLOBAL BOND INSTITUTIONAL. Enclosed you will find a recent report which will provide background on this high-quality intermediate global manager.

If this proposal for readjustment of your portfolio and implementing the changes as described above meets with your approval, please advise Scott prior to April 9<sup>th</sup> at (206) 382-4414.

Cordially,



LOUIS F. KUTSCHER

Enclosure

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\* There are no transaction costs associated with the sale of THIRD AVENUE REAL ESTATE VALUE, although a 1% short-term holding fee may apply if sold within one year of purchase. Customary transaction fees will or will not apply as usual on the remaining funds.