Quarter Notes
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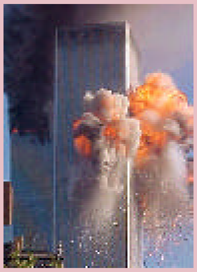
Terrorist Attacks Won't Crush US Economic Foundation



The markets finished the third quarter of 2001 with the worst record since the 1987 crash. The S&P 500 fell 15% and the Dow, 15.8%. Losses on NASDAQ were nearly twice that. Only three stocks in the NASDAQ 100 had positive returns.

The attacks on September 11 aggravated an already weak third quarter market. When the markets reopened after the longest market closing since the Great Depression, we saw prices tumble an additional 15% during the five down sessions that week. By the end of the next week of trading, stocks had recovered nearly half of the prior week's losses.

Even before the devastating terrorist attacks, the investment environment was characterized by:

- **An economy near or already in recession**
- **Expectations for lower profits**
- **Reduced capital investment, especially in technology**
- **Increased layoffs**
- **Decreased consumer confidence**
- **Marked decline in stock prices**

The tragic events have changed our lives, altering our sense of security and our expectations. The short term economic slump we were experiencing will be more dramatic as shock and fear temporarily inhibit economic activity.

Corporate profits may fall further and may take longer to recover. But businesses which add true economic value will recover and renew long term growth paths.

Increased government spending at all levels and an accommodative monetary policy will help support economic activity and mitigate some of the economic hardships. The Federal government has already committed at least $50 billion in recovery efforts and this is probably just the down payment on a stimulus package which may include additional tax cuts.

Although there will be layoffs and decreased comsumer and business spending, slowdowns

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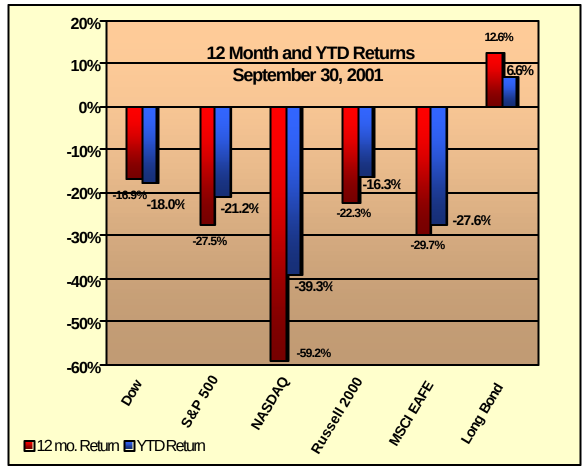

inevitably precede a new economic cycle.

Historically, recessions occur when excess optimism results in unsustainable expansion. Recoveries occur after pervasive pessimism causes the economy to contract too much. At that point the economy starts to gear up again.

Cash on the sidelines is sitting at a twenty year high of about $2 trillion in money markets now paying less than 3%. Investors seeking higher returns are likely buy equities pushing prices higher.

Our principal analysts now believe stocks are undervalued by historical standards. These standards are based on the relationships among inflation, interest rates and corporate earnings and dividends. With interest rates at current levels, the potential long term returns on stocks look appealing. Where clients were holding excess cash in their portfolios, we are recommending rebalancing to reach full equity allocations.

Stock prices are a leading economic indicator. Market rallies tend to forecast economic recoveries by six to nine months. Before the attacks, we believed we were at or near a bottom and that positive returns could be expected within the next twelve months. We still have faith in the recovery although the time horizon is now uncertain.

In this Issue

A new sense of patriotism has united America once again. As the people of New York came together, they reminded us all what is so great about America. It is clear that we cannot forget what happened and also clear that we will recover and rebuild.

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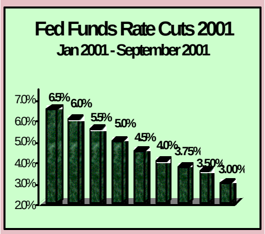
Facts

CurrentTreasury Interest Rates
30 yr Bond 5.42%
10 yr Bond 4.59%
5 yr bond 3.78%
2 yr Bond 2.85%
3 mo. T-Bill 2.34%
Money Market less than 3%



Flash: October 2

The Fed just announced another one half percent cut in interest rates. This is the ninth cut this year. Rates are now the lowest since May of 1962.

According to Lipper, Inc. afer the 1987 market crash when the Dow dropped more than 20%, one year later most stock portfolios had recovered.

Web Site Upgrade

Look for the new and improved Firestone Capital Management web site to debut sometime during October. It should look familiar, but be far more robust.

A Look at the Global Perspective

We look forward to a recovery in the US which should begin to take hold by mid 2002. But what about other areas of the world?

Japan has had negative growth for much of the last decade. Finally the Bank of Japan has moved to eliminate nonperforming loans from the portfolios of Japanese banks within three years. Japan must do what the US did with the Savings and Loan Crisis in the late 1980s.

They will experience the same pain that we did in terms of unemployment. But it is necessary in order to repair the Japanese economy. The problem is that the Japanese government has not yet accepted that it will take a government bailout in order to finance this restructuring. But at least specific objectives have now been outlined.

Europe was in a prime position to lead global growth in 2001, but we did not see that materialize. Global markets were deteriorating and the European Monetary Union did not ease monetary policy as aggressively as the US, causing disappointing performance. ButEurope has a trade surplus and the Euro is “too cheap”. The region is expected to experience some growth, perhaps allowing it to avoid the recessions be ing experienced by the other large economies.

The reasons for this are that:

- **Europe is less consumer driven than the US**
- **Europe wasn’t as caught up in the technology bubble.**
- **Prospects for European pension reform are still favorable.**

Central banks around the world have been reducing interest rates in order to stimulate economic growth. Nearly every major central bank has enacted accommodating monetary policies.

Further, the US Government, with the stimulus packages is adding to consumption. New Government spending could amount to 1% of GDP in 2002. Additionally, the Fed continues to provide liquidity to the markets.

J.P. Morgan Global Data Watch September 21 observed “. . . policymakers in the United States and elsewhere are displaying an increased commitment to supporting growth. As a result, the stage is being set for the current down-leg to be sharp, but then followed by a strong recovery which will probably take hold some time around the middle of next year.”

Market Timing: An Impossible Game

Fear was in the air in the week after the attacks. The markets, already depressed, saw some panic selling. Most individual investors held firm. History is pretty clear on the perils of panic selling after tragic events. Investors cannot afford to be out of the market in the following year. Reviewing data following past crises reveals that missing the five best trading days has dramatically affected long term performance. In the year following the 1987 market crash the one-year return was 23.1%. The investor who missed the five best trading days experienced a return of –6.8%. Clearly, attempting to time the market can severely impact your returns for the year. In almost every instance the following four to six month period has handsomely rewarded investors who had a long term investment horizon. Just “hang in there.”