

The THOUGHTFUL INVESTOR

First Quarter 2005

Financial Resolutions for a New Year

The New Year is a good time to put your financial house in order. To get you underway, we've made a list of suggested ways to start the year off right.

1. Update your net worth statement and list of investments and valuables.

Once a year, you need to sit down and calculate exactly how much your net worth is and where your assets are located. This helps provide you with an idea of which assets have and haven't performed for you, where you are in terms of meeting your financial goals

and whether or not you need to start looking at estate planning issues.

2. Check your will.

How long has it been since you looked at your will? Given your current net worth and family situation, are there issues that need to be updated?

3. Update personal property valuations.

If you own valuable personal property, such as collectibles, fine art, jewelry, antiques and other items that tend to increase in value over time, you need to have updated values for insurance

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Why Total Return Matters

Comparing year over year stock prices may give you an idea of how an investment has performed, but it is often not a true picture of the return to shareholders. You also need to look at the effect of dividends or fund distributions, whether reinvested or paid in cash.

In November, Microsoft declared a \$3 per share special cash dividend, plus a \$0.08 per share dividend to shareholders of record on November 15, 2004. Like most dividend-paying listed and NASDAQ® securities, the rate of the dividend was removed from the trading price of the stock when it began trading on the ex-dividend date, December 2. As a result, holders of Microsoft stock experienced a decline in the value of their positions relative to the dividend. Total return, however, which included dividends, did not decline.

Much the same happens with mutual funds and closed end funds, which are required by law to distribute most of their

realized capital gains in order to avoid taxes at the fund level. On the distribution date, the net asset value or price of the fund is reduced by the amount of the distribution. If the account is set up for automatic dividend reinvestment, the distribution is used to buy additional shares at the lower price. Otherwise, the shareholder receives the distribution in cash.

By ignoring total return and focusing simply on a price change calculation, performance is underestimated. You could even decide to close a position based on the perception that it has performed poorly, when the opposite is true.

The best measure of an investment's return to an investor is based on the combination of the change in its actual market price over the periods measured, plus the effect of dividends or distributions, whether reinvested or paid in cash. This total return is what an investor actually earns.

Anticipating the "Holiday" Effect



Every year there are nine holidays during which the U.S. stock exchanges are traditionally closed:

- New Year's Day (if it falls on a weekday)
- Martin Luther King Jr. Day
- President's Day
- Good Friday
- Memorial Day
- Independence Day
- Labor Day
- Election Day
- Thanksgiving
- Christmas

Prior to the start of each of these holidays, a very specific pattern occurs. Stock prices tend to drop the two trading days preceding the holidays. The theory is that traders often lighten up or close out their positions prior to the holiday to minimize the risk of any unexpected bad news during the days the market is closed. The selling pressure drives stock prices down, making those days a good opportunity for longer-term investors to buy lower in the range.

The catch, of course, is that if professional traders consider the risk of something bad happening during the days the market is closed sufficient to close out their positions, is this a time you should be buying?

Cutting Through Market Noise

Every where you turn, there's conflicting advice on whether the market is headed up or down, which investments to buy or sell, and who among the many market prognostics really knows what they are talking about. Even looking at share prices produces conflicting information, as a stock moves higher one day, then down the next.

The first step to successful investing is to cut through the clamor of the market and focus on what is actually happening. What is the trend?

One of the simplest and most effective tools for reducing market noise and looking at trends taking place in the market is a moving average.

A simple moving average (SMA) is calculated by adding all the values over a fixed-time period and dividing the total by the number of values to end up with an average for that particular period. To calculate the next average, you move forward to add new data while dropping the oldest data of the calculation.

By creating an average of prices that "moves" with the addition of new data, the action of the market or individual security is "smoothed". Day-to-day fluctuations are less important and you have a picture of the overall trend taking place.

You can calculate a moving average using any number of days or data points, depending on the length of the trend you are interested in following. For example, a 15-day moving average represents the trend over a series of consecutive 15-day periods. Each day, you would move forward to add the new data, and drop

the first period to continue to calculate an average of 15 data points.

One of the most popular moving averages is the 50-day moving average, which is shown here on a plot of Microsoft stock prices created on www.bigcharts.com.

BigCharts.com enables investors to look at simple moving averages of any length for individual securities and indices.

Is the Trend Up or Down?

Moving averages are used to signal when a trend is bullish or bearish and to signal entry and exit points. While the price is above the moving average, it is an indication of bullish behavior. When prices fall below the moving average it is a bearish indicator and warns that the price trend may be weakening.

The length of a moving average depends on the cycle or trend you wish to follow. Short trends are often identified using a 5 to 13-day moving average. A 25 to 50-day moving average is used to identify slightly longer trends while intermediate trends are followed using moving averages from 50 days to 100 days. Long-term trends use moving averages with a time period greater than 100 days.

The shorter the term of a moving average, the more susceptible the signals are to whipsaws. A whipsaw results from a sudden change in price trend that leaves an investor on the wrong side of the market. A stock might drift lower, rally briefly and then resume its downward slide.

Depending on the length of the rally and the length of the moving average, an investor might purchase the investment, only to sell at a loss a few days later.

The longer the moving average, however, the more it tends to lag the price trend. As a result, combinations of short and long simple moving averages are often used to look at crossover points to identify a significant change in the underlying trend. When a shorter moving average crosses from below to above a longer period moving average it is a sign of bullish bias. When a shorter-term moving average crosses from above to below a longer period moving average it is a sign that a bearish bias is present.

One drawback to a simple moving average is that all the data points have equal significance, although in reality, more recent market moves might be more important. This has resulted in a variation known as an "exponentially" smoothed moving average. In an exponentially smoothed moving average greater weight is assigned to more recent price action.

Other Applications for Moving Averages

Moving averages do not predict market direction but rather established the current trend. That makes them also useful in analyzing changes in housing prices, global temperatures, medical costs and other recurring events that can be plotted over time. By reducing the noise of daily data, they allow us to focus on what is actually happening.

Because the SMA is a lagging indicator, it tells us a change has occurred after the fact. As a result, trading strategies built around moving averages never sell exactly at the top nor buy at the very bottom.

Professional money managers combine the trend information gained from moving averages with other indicators to attempt to more precisely target signals and respond to other factors influencing the price of an investment.



A 50-day moving average shows the intermediate-term trend for Microsoft for the 12 months ending in late December 31, 2004.

Do You Have the Humility To Be a Good Investor?

Investors tend to make their biggest mistakes when they have too much faith in their own judgment and fail to admit when they are wrong. That's why a little humility is essential to profitable investing. Let's look at the four biggest mistakes investors make:

1. *Failing to diversify.*

No one is right 100% of the time. Diversifying, not only by individual security and asset class but also by investment strategy, increases the potential for your portfolio to perform well in all market environments. It also limits the exposure to loss that you have with just one individual investment. You never want one investment to have the potential to hurt you so badly you can't keep going.

2. *Buying the sizzle without taking a hard look at the steak.*

There are a lot of good stories out there. But they don't all have happy endings. Before you invest in a stock or sector with a good story know the numbers behind the story. Stories don't produce results, good products and good management do. And even those two aspects don't guarantee success.

You also have to remember that circumstances change. K Mart might have stayed a strong retailer had it not been for the advent of WalMart and discount stores such as Costco. Restaurant concepts are particularly prone to competition and changing fads that turn a good story bad.

The number one reason for buying any investment without taking a hard look at the details is greed. You are so eager to make a killing that you set aside good judgment. Any time the story sounds too good, red flags should start flying.

3. *Leaving money in an underperforming investment.*

Admitting you made a mistake is hard in any circumstance, but it's even harder when you've made an emotional commitment to an investment by falling for the story and believing in management or the potential of the industry.

That's why you need hard and fast rules as to when you cut your losses. You can always buy back into an invest-

ment when its prospects improve, as long as you haven't lost your money following it down.

The Janus 20 Fund lost 70% of its value from March of 2000 through March of 2003. A \$10,000 investment diminished to \$3,000. If you had a rule to sell once an investment lost 15% of its value, and then buy back into the fund when it showed three months of steady progressive gains, you would have sold in April of 2000 and then bought back in May of 2003 to experience a 40% gain through the end of 2004. \$10,000 invested in the Janus 20 Fund at the market's high in March of 2000 would be worth \$12,300 today instead of roughly \$4,800 if you bought and held through the decline.



4. *Letting greed get the better of you.*

Train yourself to be reasonable in your expectations. Shortcuts and promises of excessive returns tend to obscure our better judgment. Steady growth that takes advantage of the power of compounding has created far more millionaires than investing in the latest and greatest stock scheme.

Successful investing requires admitting that there's always more to learn and that you are not smart enough to always have the one right investment. A little humility and a lot of hard work go a long way in this business.

Past performance is not indicative of future returns. The preceding example is for illustrative purposes only. This is not an offer to buy or sell the Janus 20 Fund. That offer can be made only by prospectus.

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purposes. Check with your insurance agent to make certain your valuables are covered and find out what they will require to substantiate values in the event of a loss.

4. **Review your credit reports.**

Often the first news anyone has that their identity has been stolen shows up in a credit report. At least once a year, review your credit report and make certain that the information on the report is accurate. If there are inaccuracies, talk with a representative of the credit bureau immediately to find out what needs to be done to correct the information. But don't stop there. Notify any creditors that you don't recognize that there is a problem with the account.

If you suspect identity theft, contact the fraud department of the credit agencies and file a report with your local police at once.

Below are the major credit agencies and their contact numbers.

Equifax Information Service Center
1.800.685.1111

Trans Union Corporation
1.800.888.4213

Experian (formerly TRW)
Complimentary Report
1.888.397.3742
(+1.888.EXPERIAN)

5. **Budget for major expenditures.**

To make certain you have the money available when you need it and not subject to the market's vagaries or potential liquidity issues, identify major expenditures that you've planned for during the year, from remodeling to vacations, and set the money aside now if need be.

6. **Set up a meeting with your financial advisor.**

At least once a year, set aside time to talk to your financial advisor about the performance of your portfolio, how your assets are invested and expectations for the coming year.

One More Reason to Max out Tax Deferred Investments

Before April 15th hits, make certain you have maximized investments to tax-advantaged accounts, such as Individual Retirement Accounts (IRAs) and 401(k) plans. Deferring the impact of taxes is equivalent to increasing the return on those investments.

According to financial research firm Lipper, shareholders of taxable equity funds lose almost a quarter of potential returns because of taxes. The news is worse, according to Lipper, for owners of taxable fixed income fund shares, who lose 45% of returns to taxes compared to the equity holders' 24%.

Retirement Savings Maximum Contributions for 2004

IRA contribution limits	\$3,000	Age 50 and older	\$3,500
Roth IRA contribution limits	\$3,000	Age 50 and older	\$3,500

401(k) Contribution Limits

(Same limits apply for the individual self-employed 401 (k), 403(b), government 457, and Thrift Savings Plans)

Employer contribution	up to 25% of compensation
Employee contribution	\$13,000
Age 50 and older catch-up contribution up to:	\$3,000

2004 total additions cannot exceed the lesser of \$41,000 or 100 % of compensation. If you are age 50 and older, they cannot exceed the lesser of \$44,000 or 100 % of compensation.

SEP or Keogh contribution limits

Cannot exceed the lesser \$41,000 or 25% of compensation.

SIMPLE IRA contribution limits	\$9,000	Age 50 and older	\$10,500
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How Much Income Will You Need in Retirement?

Location makes a difference when it comes to the cost of retirement.

How much you will need in retirement depends not only on your lifestyle but also where you want to live.

The cost of living varies considerably across the U.S. One way to get an idea of what to expect is to use the cost-of-living calculator found on the National Association of Realtors® web site at www.homefair.com/homefair/calc/salcalc.html.

According to the calculator, to equal a \$150,000 income in Boston, Massachusetts, you would need \$114,550 in Anchorage, Alaska, but only \$84,344 in Mesa, Arizona. Move to Clarksville, Tennessee and the calculator says an income of \$69,564 will equal the buying power of \$150,000 in Boston.

Naturally these are just estimates and there are other costs to consider, but it does open up some new options for your retirement plans.

