Sara-Bay Financial Corp.

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It is an enormous understatement to say there has been disenchantment with the stock market during the last two and a half years, and the declines during the last few weeks have clearly added to the discouragement. Interspersed by one or two day rallies, we have seen the market continue to drop to new lows with 100 or 200 point down days in the Dow commonplace. There is a high correlation between investor moods and market declines, and as the market drops, pessimism increases correspondingly. While it appears there is no end to the negativism, I say we are soon approaching a significant rally point.

If you are exasperated and infuriated by the behavior and attitudes of some of the leaders of large corporations as well as some of the leaders in Wall Street firms, then we share the same emotion. It remains my belief however, that most people working in corporations as well as the financial industry are conscientious, honest, and hard working. Unfortunately gold rushes, oil booms, and great bull markets all create environments in which duplicitous and deceitful people thrive. When the booms end, all of the corruption becomes evident. Some unscrupulous people go to prison and needed laws are passed. It was no accident or coincidence that the Securities and Exchange Act was enacted in 1933, and the Investment Company Act was passed in 1934. The stock market hit bottom in 1932, and had already started to slowly advance. From that low it had gained over 400% by 1937. My point is this: I believe new laws will be enacted in an attempt to curb the abuses which have come to light in the last few months. I further believe that the market will have already begun to climb prior to this legislation being passed.

I believe the market will rally, but not because of the actions of Allan Greenspan and the Federal Reserve System. The Federal Reserve has several actions they can take which during normal times are stimulants to the economy. This includes purchasing treasury securities, lowering reserve requirements, and of course the most publicized, lowering the discount rate. Most of these are actions designed to make money more freely available, but I contend they do not work well in periods when an economy is contracting. While the Fed can drop interest rates banks pay to borrow, they cannot force those same banks to borrow money then lend it to corporations at profitable rates, particularly if the banks are fearful that these borrowers will be unable to pay them back. On the other side of the coin, the Fed cannot force the corporations to borrow money. If they are fearful of expansion, they will not borrow even if interest rates are zero. Capital borrowed and spent must some day be repaid.

While the Fed lowering interest rates for the umpteenth time, could coincide with the start of a rally, I do not believe it is necessarily a catalyst for such a move. Instead, I believe we are entering a significant buying opportunity for other reasons. These are signs that typically occur as we near a bottom:

- <u>Disparities</u> - Even while the Dow drops to new lows there are more new highs. This has occurred during the last few days when compared to the lows in July.
- <u>Blue chip stocks, which generally have held up better than smaller companies suddenly begin to fall and receive downgrades</u> - This is clearly noticeable over the last three weeks.

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∞ Many investors become despondent, and can see no light at the end of the tunnel – I have already referred to this. It is happening now! If you don't believe it, sit in our seats for a couple of days!

This does not mean that we are at the start a new bull market. I do not believe for a minute that we will return to those hectic upside days of 1999, where you could often make money by buying AOT (Any Old Thing). However, I am of the opinion that recent events could precipitate a significant change in direction, wherein the indices would quietly advance for several months into early 2003. Markets occasionally just get sold out by virtue of the fact that a lot of people simply stop selling.

Obviously, I cannot tell if the near-term bottom of the Dow is 7500 or below 7000, but I do believe we are very near in terms of weeks or days. If I am correct in this scenario, we should use this coming advance to review and re-evaluate our individual investments. Keep in mind that most of the time, market indices have neither large advances nor large declines. During the up and down markets we experienced during most of the sixties, seventies, and eighties, there were opportunities in individual investments. The great money managers such as Walter Schloss, Peter Lynch, and Warren Buffet did exceedingly well for their clients during those periods.

Esther, Barbara, and I believe we have one of the best groups of clients ever and you are one of them. We sincerely appreciate your confidence and your trust during these difficult times.

Sincerely,

Mike

J. Michael Hard

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