

# SOMETHING OLD, SOMETHING NEW

AS WE ENTER THE NEW YEAR, I AM GOING to tweak my portfolio recommendations a bit. I don't see the need for any drastic changes and I still believe this bull market has further to run, but I am going to use the year's end to reduce some of my technology exposure by recommending selling and taking profits in biotech (BBH) and software (SWH) exchange-traded funds. I favor exchange-traded funds for the simple reason that, by buying these securities that trade like stocks and represent ownership in multiple stocks, an investor can gain the advantages of diversification while still focusing on specific investment themes that typically drive performance. For the time being I am going to leave my other technology sector positions – semiconductors (SMH), Internet (HHH) and broadband (BDH) – unchanged.

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top-line improvement with pricing power and an improvement in ASPs and margins that is not currently reflected in valuations. I am also going to leave unchanged my poorest performers of the year, utilities (XLU) and telecommunications (TTH), and add pharmaceuti-

cal stocks (PPH). I expect that as we move further into the economic recovery these types of "old economy" stocks will turn in relatively strong performances. With the recovery still fairly young, and the trend of technology stock outperformance still intact, I am going to take my time easing out of "new economy" positions and into the more "boring" sectors of the economy.

## A BIT MORE FOREIGN

I am going to leave unchanged my position in Japan (EWJ), but unload the Eurozone (EZU) in order to double my recommended Western Europe exposure. In place of the Eurozone and the software sector position I am going to recommend Germany (EWG) and France (EWQ). All three of these countries – Japan, Germany and France – appear committed to meaningful structural reforms. In addition, when it comes to Germany

and France the Eurobank, due to its German lineage, continues to pursue a strong Euro policy. Although all three of these economies are more regulated than the U.S., this fact is well known and unlikely to move stocks.

What is not fully appreciated is that these countries are pursuing less regulation for the simple fact that the failure of ridiculous policies like the French 35-hour workweek has left them no choice. On the other hand, few investors seem to comprehend that the U.S. is pursuing a weak dollar policy while both Republicans and Democrats appear to have reached agreement that America needs more government. Increasing the size of government, along with a weak currency, usually produces disappointing long-term results. But that's the long-term, and expansionary fiscal policies and a weak currency will probably actually help in the short-term.

## STAYING SMALL

Finally, in regards to my small cap growth position (IWO), the trend of small cap growth stocks outperforming the broad market has a bit further to run. Small cap growth stocks only began their outperformance last March, and as the economic recovery heats up further, small growth companies with their lean bottom lines will benefit disproportionately from revenue gains. In the later phases of the economic cycle, I expect these companies will cease to be as good of an investment when their limited infrastructure proves incapable of ramping with further growth in the way that large corporations can. At some point I will be discarding small cap growth stocks in favor of nothing other than big cap stocks, but for now I am sticking with my small growth position.

So with several old positions and a few new positions, my 10 recommendations at the beginning of 2004 are: Japan (EWJ), Germany (EWG), France (EWQ), Small Cap Growth (IWO), semiconductors (SMH), Internet (HHH), broadband (BDH), utilities (XLU), telecommunications (TTH) and pharmaceuticals (PPH). I remain bullish as we head into 2004 and fully expect the broad stock market to climb higher over the course of the year. ☺

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