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T. Rowe Price
ESTABLISHED 1838

Economy & Bonds

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1. "My commissions are top secret."

Bonds are red-hot. Moderate growth, scant inflation and lingering concerns about Asia's economic woes are luring more and more people to fixed-income investments. Besides, they're so much more civilized than those nasty stocks and their pushy brokers, right?

Don't believe it. For one thing, bond brokers don't have to reveal their "markups," the commission-like profits they charge you. In a typical transaction (known as a "principal" trade), a broker buys a bond at one price and sells it to you at a higher one, pocketing the difference. When brokers buy bonds from you, they do the opposite, charging a "markdown." Because most bonds do not trade on an exchange, investors have little way of knowing what the prevailing market prices are without shopping around.

"You can be completely screwed and never know it," says Larry Fondren, head of InterVest Financial Services in Berwyn, Pa., which is trying to launch a Nasdaq-like electronic exchange for bonds. According to InterVest's research, institutions such as banks and insurance companies paid in excess of \$41 billion more than they should have on corporate bond markups between 1995 and 1997. And individuals are even more vulnerable, as any bond purchase under \$1 million is considered an "odd lot" and subject to a higher markup.

The National Association of Securities Dealers requires only that markups be "fair." That leaves brokers elbow room to push the envelope. While most don't,

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plenty do. One Florida firm, Noble International Investments, charged customers excessive markups – as high as 90% – on foreign corporate bonds in 1995. The NASD fined the firm \$5,000 and ordered it to pay \$24,167 in restitution. (Noble's president, Nick Pronk, calls the violation "an isolated incident.")

The Securities and Exchange Commission and the NASD have been passing reform proposals back and forth for four years. For investors unwilling to hold their breath for a resolution, the best way to avoid markups is to bypass brokers altogether. The government sells Treasury notes and bonds commission-free through its Treasury Direct program. Call your local Federal Reserve branch, or the at 202-874-4000 (www.publicdebt.treas.gov on the Internet). You can also buy bonds through a so-called agency trade, in which your broker connects you with a seller and charges you a set commission, typically \$50.

2. "I get paid to dump my inventory into your account."

Excessive commissions are only the beginning. Investors also need to watch out for the incentives brokers may be given to sell you one bond over another.

Brokerages, through their bond desks, routinely buy bonds in huge chunks from the government, companies and municipalities. The firms hold them as "inventory," later trading them on the market or selling them to clients. Sometimes, even if they can get clients a better price in the open market, brokers will push a bond from their inventory because they can make more on the markups that way.

"You have to ask if the bond is being recommended on its own merits or because the brokerage house owns it," advises Richard Lehmann, president of the Bond Investors Association, a financial adviser and newsletter publisher in Miami Lakes, Fla.

Ask your broker if there are any incentives tied to his recommendations. "If they lie, it's fraud," says Steve Wallman, a senior fellow at the Brookings Institute and a former SEC commissioner.

3. "Your long-term investment may be short-lived."

Despite their appeal as a safe haven from the vagaries of stocks, bonds have their own added risk. When interest rates plunge, as they have for a year, many bonds can be "called" by their issuer – that is, they are paid off before their maturity date. Now that a full-fledged refinancing boom is under way, and companies, homeowners and municipalities are repaying higher-cost debt and taking out new loans at lower rates, that's exactly what's happening.

Companies called \$8.52 billion of their bonds between the start of this year and March 9, double the amount of the same period a year ago, according to Moody's Investors Service. In January and February, \$11.9 billion worth of municipal bonds were issued to repay higher-cost munis, up 71% from the first two months of 1997, according to the Bond Buyer. And homeowners and other mortgage borrowers, who prepaid their mortgages at a record clip in January, were still refinancing at a torrid rate in March.

This is bad news for bondholders. When a bond is called, you're repaid at the issue price – "par" – or par plus a small premium. You face a loss if you bought the bond above its face price, or a loss of any gains if the bond rose after you bought it. Also, since interest rates are falling, you'll have to reinvest at a lower yield. Be especially wary of high-yield, or "junk," bonds since companies try to

pay down their high-interest debt as soon as they can. Richard Lehmann advises against buying bonds within three years of their "first call" date, or above-par bonds that can be called whenever the issuer wants.

Since mortgage-backed bonds can be called at any time, investors should check the interest rates on the mortgages in the bond's portfolio. "If they're above the current rates, there's a good likelihood that they'll be refinanced," Lehmann says.

4. "You don't need this government bond fund I'm selling you."

January and February saw a net total of \$19.8 billion added to bond funds, their best annual start since 1993, according to the Investment Company Institute, a fund trade group. And it's true that funds may well be a safer way to go when investing in corporate, muni, or mortgage-backed bonds. When it comes to Treasuries and certain other government bonds, though, they're a waste of your money.

7 2
"With government bond funds, there's no credit risk, so what is the fund manager doing?" asks Gordon Williamson, a financial adviser in La Jolla, Calif., and the author of *The 100 Best Mutual Funds You Can Buy* (Adams Media, 1998). "He's making guesses on interest rates that are more often than not incorrect" – and you're paying through the nose for his advice. To wit: Four of the five biggest general government bond funds with a maturity between five and 10 years each charges a 4.75% load, on top of expenses and 12b-1 marketing fees – and each failed to beat the returns of a five-year Treasury during the past three, five and 10 years ended Jan. 31. Fidelity Government Securities (), the one that beat the five-year bond's returns, has no load, no 12b-1 fee and the lowest expenses of all five. Coincidence? You decide.

5. "Warning: This 'low risk' bond fund can be hazardous to your wealth."

Besides being expensive, government bond funds are not as safe as they sound. They tend to load up on mortgage-backed bonds such as Ginnie Maes to increase their yields. While these bonds are backed by the government, they add another, more volatile dimension of sensitivity to changes in interest rates.

That's when nightmares can happen. In 1994 the Piper Jaffray Institutional Government Income Portfolio plunged in value after a surge in interest rates hammered the fund's huge holdings in mortgage derivatives. Minneapolis-based Piper paid a reported \$138 million to settle claims that it misled investors about the fund's risks. The company declined to comment. In 1996 NationsBank spent about \$30 million to settle investors' claims that they were misled about the risks of two of the bank's funds, which were also hurt by mortgage derivatives. NationsBank blames "a unique market situation when interest rates rose at an unprecedented rate" in 1994.

With fund managers under the gun to beat their peers and the market, some may pursue riskier investments. That means investors need to scour prospectuses. The SEC requires only that funds invest at least 65% of their assets in their objective. Strong Government Securities (), for example, had 14.5% of its assets in corporate bonds at the end of January. "It's a matter of knowing what you're getting," says Alice Lowenstein, a fixed-income analyst at Morningstar.

6. "Your tax-free municipal bonds may be taxable..."

Californians Ed and Elena Keith bought some \$250,000 worth of municipal bonds from the Riverside County, Calif., housing authority in 1986 for the same reason most investors buy munis: tax-exempt income. Little did they know that the Internal Revenue Service would revoke the bonds' tax-exempt status, leaving them with a bunch of low-yield duds.

The days when municipal-bond holders could expect virtual immunity from the IRS are over. The agency can now tax muni investors when it finds that the bonds don't comply with tax laws and it can't reach a settlement with the issuer.

In February the U.S. Supreme Court let stand a ruling in favor of a 1990-91 IRS audit that found the 1985 bond offering's proceeds had been misappropriated. When the housing authority refused to pay \$3.71 million in taxes, the IRS sent a notice to the Riverside muni holders, telling them they had to pick up the bill.

One of the starkest implications of the ruling is that bondholders can be held liable for the actions of the issuer or underwriter after the bonds are sold, says Mary Reichert, a partner at Bryan Cave LLP in St. Louis, which represented the Keiths in their suit against the IRS.

More and more muni holders may find their investment backfiring as the IRS steps up its investigation into the effects on tax compliance of "yield burning" — the controversial practice of inflating muni offering prices by driving down bonds' yields. The agency is studying about 265 municipal issues, and has told more than 100 issuers that their bonds may be taxable, says an IRS spokesman.

"Before, it was virtually guaranteed that if muni bonds were issued as tax-exempt, they would be tax-exempt," Reichert says. "That's no longer the case." As a result, investors now need to pay closer attention to the reputation and financial background of issuers and underwriters.

7. "...and, um, so may your tax-free muni funds."

Some municipal-bond funds invest in so-called private-activity bonds, which are often used to help fund the building of airports and stadiums. Unbeknownst to many investors (and some brokers), those bonds pay income that is subject to the alternative minimum tax (AMT), which was designed to prevent taxpayers from taking advantage of deductions and other breaks to pay little or no federal income tax.

Some examples: 82% of the interest paid by **Alliance's Municipal Income Fund National Portfolio** () is taxable as AMT. Income from the Schwab Municipal Money fund and Schwab Florida Municipal Cash Trust is roughly 42% to 46% taxable, respectively, as AMT. (Snapshots are not available for these funds.) Interest payments from muni funds that own private-activity bonds can push the investor's income to a level where he or she at least has to file an AMT form and possibly has to pay the tax itself.

While the alternative minimum tax may not inspire much dread in you now, that could soon change. Congress estimates that as many as 8.5 million people will have to pay the AMT by 2007, up from just 605,000 in 1996.

8. "Your high-yield fund is full of foreign junk."

In the post-Michael Milken era, junk bonds enjoy a rehabilitated image. The makeover was made possible by their stellar returns and declining default rate.

Merrill Lynch's High-Yield index has been up an average of 12.1% per year during the past 10 years, compared with 30-year Treasury bonds' 9.7% annual return. Meantime, default rates worldwide ran under 2% during the past few years, far below their 3.4% average since 1970, according to Moody's.

Hungry for high yield and confident that corporate America's balance sheets are stronger than ever, investors have never been bigger junk-bond junkies. Today a record \$109.4 billion is invested in junk-bond funds, more than triple the Milken-era peak in June 1989. Junk bonds are being issued at a pace that's set to smash last year's record, according to research firm Securities Data.

So what's the problem? High-yield mutual funds are loading up on riskier foreign junk bonds, particularly those from emerging markets – making up as much as 15% of assets, according to Mark Wright, a senior analyst at Morningstar. And some funds own huge amounts of junk-rated debt issued by emerging-market governments. This debt is all the more risky because of currency fluctuations. One reason for the migration is that junk yields in the U.S. aren't as juicy as they used to be because balance sheets and the economy are stronger. That's got some managers, frustrated by not getting more for the amount of risk they take on, shopping abroad. With continuing economic trouble in Asia expected to push global default rates toward 2.5% this year – and with emerging markets at a much higher risk – junk could get more turbulent.

9. "You're buying the wrong Treasury bond."

You should always try to buy Treasuries through Treasury Direct (), but you may not always be able to. Since some new issues such as 30-year "long" bonds are auctioned as infrequently as two times a year, the program may not always have what you want when you want it.

If you can't wait for the Treasury's next auction, the "secondary market" is where you'll have to go. Beware: Your broker may sell you a bond that costs more than you need to pay.

Brokers like to push the latest-issued, or "current," bond. After all, they're the most liquid and the easiest ones to sell. And since brokers are eager to get back to higher-volume stock trading, the quicker, the better. The problem is, current bonds usually carry a premium for their liquidity – and the market in older Treasuries is large and liquid enough to guard small investors from being ripped off should they have to sell suddenly.

"It's the only place where the little guy has an advantage over the big guy, because he doesn't need that liquidity, so he doesn't need to pay the premium for it," says David Rosenau, chief of Winstar Government Securities in White Plains, N.Y., a bond-market trading service.

"The difference isn't always huge," Rosenau says. "But it adds up."

10. "The rating agencies need to brush up on their ABCs."

Moody's and Standard & Poor's. Solid. Venerable. Unfailingly accurate. How's that again?

These agencies, which rate the credit-worthiness of bond issuers, dropped the ball on predicting the economic chaos that engulfed Asia last autumn. As late as October, for example, Moody's, S&P and Fitch IBCA all had solid ratings on Korea's debt. Within two months the ratings sank to junk-bond levels, well after Korea's woes were apparent.

Of course, most of Wall Street missed the boat, too. But the agencies are supposed to be the first and best line of defense against changes in credit conditions. While the agencies say they've learned their lesson — in this case, not to underestimate the importance of a country's private and short-term debt — the debacle highlights the truth: They're far from perfect. The next time your broker purrs that this or that bond is rated A+, don't be so sure that's good enough.



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Personal Finance: [If You're Thinking of Investing in...](#)

Bonds, Municipal Bonds

By
July 1, 2002

BACK IN THE era of dazzling IPOs and sizzling tech stocks, staid municipal bonds were the forgotten, fuddy-duddy laggards of the investing world. With equities then hitting new highs seemingly every day, the steady gains of interest-bearing munis couldn't hold a candle to the broader market's soaring returns.

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What a difference a couple of years makes. The tech bubble has burst, corporate profits have slumped, countless scandals have cropped up and terrorism looms. In short, a nasty recipe for stocks: The S&P 500, Dow and Nasdaq have fallen 13.8%, 7.8% and 25%, respectively, so far in 2002. Not surprisingly, the upheaval has investors looking for stability. Enter munis.

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When you buy a municipal bond, you're lending money to an entity — often a city, town or even school district — that, in turn, promises to make interest payments to you on a regular basis (usually semiannually) and then repay the entire principal on a specific date in the future. Many munis are insured, and the default rate is very low, making them relatively safe, reliable investments (though there are exceptions, as the investors who lost billions in the 1983 default of so-called Whoops bonds know all too well).

Of course, with diminished risk comes diminished reward: Munis offer relatively modest returns. But these days, with bonds outpacing equities, the trade-off can be worth it. While the broader indexes have headed south, the average municipal-bond mutual fund has boasted a total return (in other words, interest payments plus price appreciation) of 4% so far this year, putting

- Munis tend to be more attractive to investors in the 30% tax bracket and higher.
- Muni mutual funds require a smaller initial investment than individual bonds.
- Buy munis in your own state to take advantage of additional tax savings.
- Don't hold munis in a retirement account: bonds' earnings are already tax-free.
- Short-term munis are more attractive now than they were. The Fed may raise rates later this year.
- Munis are well-suited for investors seeking dividends or saving for a specific expense.

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it on pace for an 8% annual return, according to Morningstar. As a result, this safe haven is hardly a secret: At the end of March, there were \$1.7 trillion in muni bonds outstanding. Of that total, individual households owned \$577 billion, or about 34%, according to the , up from \$550 billion in March 2001.

As with any other investment, there are a few things to consider before making the jump into muni land. First, you need to determine whether your tax situation merits adding municipal bonds to your portfolio. Then, you should make sure you understand the risks of these bonds (there are some). You'll also need to decide whether it makes more sense to buy individual muni bonds or invest in a muni-bond mutual fund. And finally, you should craft a muni strategy that makes sense for your own circumstances. In this package, we'll help you address each of those issues.

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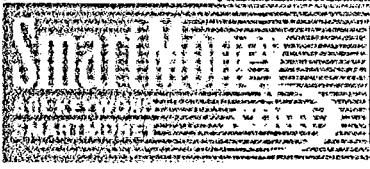
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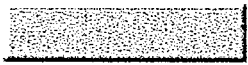
Bonds or Bond Funds

By
July 1, 2002

RESEARCHING INDIVIDUAL municipal bonds can certainly be a hassle. And if you need your money back before the bonds mature, selling them can be another. That's

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Fidelity Spartan Intermediate Muni Income (), Vanguard Intermediate-Term Tax-Exempt (), Vanguard Long-Term Tax-Exempt () and Franklin Federal Tax-Free Income A (). All have low expenses and offer low risk, explains Berry. "We like these because we think investors can count on them." Note that these are all national funds; their income is free of federal taxes only. But each of these fund families also offers various state-specific funds as well.

On the other hand, if steady income and lower taxes are your objective, then individual munis are probably a better choice, says S&P analyst Gary Arne. At SmartMoney.com, we're fans of buying and holding munis until maturity. That way, you'll lock in a yield and get your principal back on a certain date.

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> Business Outlook Survey October 2003

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Business Outlook Survey

October 2003

Activity in the region's manufacturing sector improved notably this month, according to firms surveyed for the Philadelphia Fed's Business Outlook Survey. Most indicators pointed to improvement, with noteworthy increases recorded in the indexes for new orders, shipments, and employment. Expectations for growth continue to be optimistic, and an increasing share of firms anticipate expanding employment over the next six months.

Current Indicators Show Marked Improvement

The survey's broadest measure of manufacturing conditions, the diffusion index of current activity, was positive for the fifth consecutive month and increased significantly from 14.6 in September to 28.0 this month (see Chart). The current new orders index also showed marked improvement, increasing nearly 10 points to 29.0, the highest reading of the index in eight years. The current shipments index also bounded higher, increasing from 13.2 in September to 28.8, its highest reading since November 1999. Survey indicators suggest delivery times and unfilled orders are edging higher—both diffusion indexes increased from their September readings and were positive this month. The current inventories index fell five points and moved below zero for the first time in five months.

Overall improvement in manufacturing was also evident in firms' responses regarding employment. The current employment index increased 10 points to 5.5, its highest reading in three years. Although 65 percent of the firms reported no change in employment this month, the percentage reporting an increase in employment (21 percent) was higher than the percentage reporting lower employment (15 percent). Firms also reported continued improvement in the average workweek in October. The workweek diffusion index increased 10 points to 13.5 and has now remained positive for four consecutive months.

Higher Input Prices Reported

Firms reported higher input prices again this month. The index for current prices paid remained essentially unchanged after rising in August and September. Twenty-five percent of the manufacturers reported paying higher prices for inputs this month; only 2 percent reported paying lower prices. Despite higher costs, firms reported only slightly higher prices of their own manufactured goods. The prices received index increased marginally, to 5.4, but is now at its highest reading in six months. Although the prices received index has drifted slightly higher in recent months, this is ameliorated by the fact that a high percentage of firms (72 percent in October) have been reporting no change in prices of their own goods.

Employment Forecast Improves

Expectations for future manufacturing growth remain optimistic, although some



future indicators fell from their high readings in September. After reaching its highest reading since June 1992 last month, the diffusion index for future manufacturing activity fell 11 points to 55.5 (see Chart). The future new orders and future shipments indexes also fell, but they remain at very high levels. Firms expect unfilled orders to increase over the next six months but delivery times to stay near their current levels. More firms expect inventories to increase over the next six months (25 percent) than expect them to decrease (17 percent).

The outlook for employment improved notably in October. The future employment index increased for the second consecutive month, rising almost 13 points. Nearly 41 percent of the manufacturers indicated they would add workers over the next six months; only 7 percent indicated they would make cuts.

In special questions this month, firms were asked about the impact of the recent recession on production levels (see Special Questions). Seventy-three percent of the manufacturing firms said they experienced declines in production during the 2001 recession. Among those that experienced declines, only 14 percent said that production had already returned to pre-2001 levels. Over half of the firms that experienced declines expect that production will not return to the pre-recession levels until after the first quarter of 2004. Moreover, a large percentage (44 percent) do not expect production to return to those pre-recession levels in the foreseeable future, for reasons involving competitiveness or long-term declines in their industry.

Summary

The region's manufacturing sector showed marked improvement in October. Indexes for new orders and shipments have risen significantly over the past two months, suggesting that the pace of recovery is picking up. Employment is also on the rise as suggested by increases in both average workweek and employment indicators. In general, manufacturers continued to be optimistic, and firms provided a more optimistic outlook for employment growth this month.

Special Questions (October 2003)

1. Did you experience a decline in production at your plant in the 2001 recession?

Yes	72.5 %
No	27.5 %

2. If yes, has production at your plant returned to its pre-2001 levels?

Yes	14.3%
No	85.7%

3. If no to question (2), when do you expect production to return to pre-2001 levels?

2003:IV	1.6%
2004:I	1.6%
2004:II	25.0%
2004:III	21.9%
2004:IV	6.2%
Not in the foreseeable future because of:	
Loss of market share	7.8%
Long-term decline in industry	23.4%
Other	12.5%

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The Federal Reserve is the central bank of the United States. Its structure includes a federal government agency, the Board of Governors, in Washington, D.C., and 12 regional Reserve Banks. Reflecting this structure, which balances centralization with regional presence, the Fed has web sites that are national in scope (see links at right) and regional (see below).



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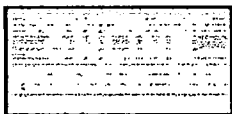
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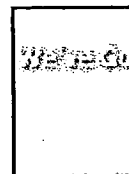
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Date: 10/16/2003 9:25:30 AM Eastern Daylight Time
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former ceo fields never executed contract with act in april

— Original Message —

From: "romy perkins" <catilandcorp@hotmail.com>
To: <ruppanner@benefitscal.com>
Cc: <w.ifields@verizon.net>; <aartfletch@aol.com>; <rlove@uwkc.org>;
 <ghlii@aol.com>
Sent: Thursday, October 16, 2003 9:22 AM
Subject: Re: Fw: 1 percent stock

> there is no money for gray oaks, nada, when there is, you will know

> romy

> is that clear....

> — Original Message —

> **From:** "Thomas A. Ruppanner" <t.ruppanner@comcast.net>
 > **To:** "romy perkins" <catilandcorp@hotmail.com>; <w.ifields@verizon.net>
 > **Sent:** Wednesday, October 15, 2003 12:26 PM
 > **Subject:** RE: Fw: 1 percent stock

>

>

>> I am not clear on where this effort stands....would you help me get up

>> to speed?

>>

>> Tom Ruppanner

>> UGIT/Personnel Insurance Services

>>

>> T 925.937.8787

>> F 925.937.5858

>> C 415.797.2323

>>

>>

>> —Original Message—

>> **From:** romy perkins [mailto:catilandcorp@hotmail.com]

>> **Sent:** Wednesday, October 15, 2003 7:22 AM

>> **To:** w.ifields@verizon.net

>> **Cc:** ruppanner@benefitscal.com

>> **Subject:** Fw: Fw: 1 percent stock

>>

>>

>> CAT ISLAND

>>

>> NO CHANGE TO DATE

>> TRYING TO GET PAST THIS INITIAL MATTER AND THEN I CAN FOCUS ON THAT

>> — Original Message —

>> **From:** "ike fields,CEO" <w.ifields@verizon.net>

Thursday, October 16, 2003 America Online: AArtFletch

>> To: "romy perkins" <catislandcorp@hotmail.com>
>> Sent: Tuesday, October 14, 2003 4:55 PM
>> Subject: Re: Fw: 1 percent stock
>>
>>
>>> outstanding Romy , what's the status with grey oaks ?eh
>>> From: "romy perkins" <catislandcorp@hotmail.com>
>>> Date: 2003/10/10 Fri PM 02:17:37 EDT
>>> CC: <ruppanner@benefitscal.com>,
>>> <w.ifields@verizon.net>,
>>> <rlove@uwkc.org>,
>>> <aartfletch@aol.com>
>>> Subject: Fw: 1 percent stock
>>>
>>> fyi
>>>
>>> just earned doc another 2 dollars per share
>>> ----- Original Message -----
>>> From: romy perkins
>>> To: JJRV@aol.com
>>> Cc: aartfletch@aol.com ; romy perkins
>>> Sent: Friday, October 10, 2003 1:15 PM
>>> Subject: Fw: 1 percent stock
>>>
>>>
>>> i have so advised
>>> romerio
>>> ----- Original Message -----
>>> From: JJRV@aol.com
>>> To: catislandcorp@hotmail.com
>>> Sent: Friday, October 10, 2003 11:36 AM
>>> Subject: Re: 1 percent stock
>>>
>>>
>>> Romerio,
>>>
>>> Please advise Dr. Fletcher that he will be paid out at the same
>>> price
>>> of \$5.00 per share which equates to \$500,000.00.
>>>
>>> Thank you for your understanding on this issue, finally.
>>>
>>>
>>>
>>> Jay E. Jones
>>> Advanced Composite Technology, Inc.
>>> 12800 University Drive
>>> Suite 550
>>> Fort Myers, Florida 33908

> > > 239-985-7000 office
> > > 239-938-0453 office fax
> > > 239-489-3496 private home office fax
> > > www.compositehomes.com
> > > jjrv@aol.com
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