

THE INVESTMENT ANALYSTS SOCIETY OF CHICAGO

Spring 2004



The Efficient Frontier

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President's Message

by Kevin Vandolder, CFA, President



Our 2,700 member society has accomplished many things in the past 12 months while delivering ever strengthening programs and services.

Before the fiscal year closes out in June we offer many events including a seminar on "Spring Cleaning Tips for Updating Your Resume" on May 12 and luncheon programs with Alan J. Lacy, Chairman and CEO of Sears on May 20 and Richard Bernstein, Chief Strategist at Merrill Lynch on May 26. In addition, on June 9, Bob Pozen, Non-Executive Chairman of MFS will address the society on the topic he recently testified on before the Senate Banking Committee—Soft Dollars.

As a reminder, the IASC has its Annual Business Meeting on June 29 at 7:30 AM at the offices of ABN/AMRO at 208 S. LaSalle on the 2nd floor in their training room. We encourage members to come out and vote on the new slate and hear an update on the 2004-2005 Strategic Plan at this meeting.

Noteworthy achievements include the Professional Development Advisory Group working diligently to provide members with a more robust job board. Presently, there are more than 20 jobs from 13 different employers posted on the IASC website in the members-only area. In the near future, you will be able to request email notices each time a new job is listed on the website. I encourage you to take advantage of this powerful member benefit and ask your employer to consider posting open positions on the IASC website.

In addition, the volunteers and staff always appreciate to hear from its members in the ways in which it can enhance the society. Feedback only requires a few minutes of your time and costs nothing. We look forward to receiving your feedback.

In closing, I appreciate the opportunity you have given me to serve as the President of the IASC. I personally would like to thank the numerous volunteers and staff members that I have had the opportunity to work with through the years.

As always, we all look forward to the future as the society continues to grow and strengthen its deliverables to its members.

Editor's Note

by Greg Gocek, CFA, Communication Chair

This issue offers some new information that hopefully demonstrates our striving for continuous improvement on *The Efficient Frontier*. We inaugurate a new feature profiling the experiences of an IASC member, focused this issue on Jim Stirling. We note career moves, congratulating John Canning on his appointment to the board of the Chicago Fed, and wishing Jay Taparia the best as he leaves the role of IASC Director of Education. In addition to the reports on our excellent luncheon programs and reviews of professional articles, we also have coverage on IASC's informal and enjoyable social events, and summarize the excellent overview of alternative assets provided at a February educational seminar. You'll learn what AIMR is doing to promote greater public awareness and appreciation of the CFA designation and are encouraged to cast your ballot (if still outstanding) on the AIMR name change proposition.

Thanks for your feedback. This issue's contributors were, alphabetically; Eric Ause, Pat Carlevato, Matt Clink, Rebecca Cook, David Frank, Greg Gocek, Carmen Heredia-Lopez, Arch King, Jay Taparia, Rawley Thomas, Venkatesh Vadlamani, Kevin Vandolder.



IASC Annual Business Meeting

Mark Your Calendars!

Director of Education Farewell

by Jay Taparia, CFA

My time as Director of Education has ended, given increased responsibilities at my investment advisory practice and escalating travel. I will never forget my experiences in that role or your related feedback over the last three years. Collectively, you made IASC education the success it is, by your contributions, speaker references, topic ideas, and your enrollment – all uses of your precious discretionary time, a key input professionals require to create value.



As my thanks, I'm happy to share these insights learned – some education that delivered tremendous personal and portfolio returns to the Director of Education!

For every hour of education, there is a positive correlation of return – return to both client and the CFA. Shortchanging education imposes an opportunity cost, with a reliance on past (possibly outmoded) information for decisions – regarding market behavior, risk management, new asset classes, return potential, etc.

Education is a “risk management tool.” We recently have seen recession, a bear market, and the “Technology Bust”. Education could help limit investment losses, warning against “creative accounting” from Enron to dot-coms. It also could have helped dodge the bullet of this era’s 15% unemployment rate in financial services. Education serves as a career “hedge”. For example, local money managers enrolled in IASC’s February alternative assets seminar learned how to access non-correlated returns, lowering risk to investment portfolios and raising their value to clients – a virtuous circle!

Education gets you a well-rounded career life. This is especially true in networking and listening skills. We can focus on the daily grind in our cubicles and thus overlook what is “out there.” A member recently told me that after she was cut from the trading floor following 17 years, she did not realize “how large the world really is!” Networking takes time and yields real rewards, but more by art than science. Make time to catch its benefits by interacting with other Society Members.

Old education directors, unlike old soldiers, do not fade away! I will participate at Education meetings sharing insights and ideas. Education is an essential raw material in my practice. I encourage you to make it the same – a guiding passion for your work.

If you wish to participate in some way at IASC, do contact the office at 312-360-0382. All Advisory Groups (see www.iaschicago.org for a listing) would warmly welcome you! Ultimately, it will prove one of your best investments.

AIMR News - Name Change Balloting & Public Awareness Efforts

by Greg Gocek, CFA, Communication Chair

As you may recall from communications sent by AIMR earlier this spring, an amendment to AIMR’s bylaws on changing AIMR’s name to CFA Institute is up for vote at the 2004 Annual Meeting in Denver. IASC members who have not yet done so are encouraged to evaluate the related proxy materials on the issues discussed therein and vote, either via printed ballot (mailed or faxed) or on the Internet. The deadline for voting is 12:00 Noon (EST) Friday, May 7.

AIMR has pursued an active media campaign so far in 2004 to increase public awareness of the CFA designation and of AIMR’s positions on professional ethics and investment industry practices. For example, this March in the Chicago market, its commercials were broadcast on both TV (CNBC, Fox News, MSNBC and CNN) and radio (Wall Street Journal Report, Bloomberg News, and National Public Radio). Ad videos are archived for viewing in the Pressroom section of the AIMR website (www.AIMR.org). Print ads/advertorials will run during May in national publications (*Trust & Estates*, *Barron’s*, and *Fortune*), so you can check at your local newsstand for full details!

Education News

Alternative Investments Seminar

by Venkatesh Vadlamani, Volunteer

February 24, 2004—Alternative Investments (“AI”) were defined at IASC’s February seminar as illiquid assets priced in non-auction markets. Very risky in isolation, AI can offer significant diversification benefits. AI investors range from university endowments taking cutting edge risks to more conservative players like insurance companies. Investors avoiding market timing tend to outperform because they economize significant liquidity and valuation related transaction costs.

Real Estate: Low interest rates have prompted real estate’s re-emergence. Although valuations seem lofty, a small allocation is appropriate here. Alongside core assets like buildings, timber and farmland are increasingly popular. Markets are cyclical with deep-pocketed investors holding the best properties in downturns.

Real estate is idiosyncratic. For example, fairly proximate New York City and Philadelphia have uncorrelated real estate prices, while distant Raleigh and Austin are both heavily influenced by high tech’s cyclicity. Widespread access to determinative demographic data has eliminated



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information arbitrage. Opportunities to make persistently high returns are non-existent. Most premium funds remain closed with significant cash positions.

Hedge Funds: The \$800 billion hedge fund industry is large and growing. Hedge funds outperformed all major indexes on a risk-adjusted basis. Most assets are offshore because of favorable foreign tax structures. Tightened U.S. regulation will lead to further offshore migration.

A majority of funds use complex trading strategies, introducing portfolio illiquidity. It is essential to select proven managers and to understand the nature/durability of their strategies. Also necessary are strong risk controls, with a team reviewing monthly fund data, and manager commitment via investment of personal wealth in the fund. Attractive hedge funds are mostly closed to new money, with managers cherry picking limited partners. Although the number of managers and funds is increasing dramatically, savvy investors like Hedge Fund of Funds opt for select (top 2%) managers.

Venture Capital and Private Equity (VC/PE): Venture Capital, also with \$800 billion invested, is the most controversial AI. Its estimated risk-adjusted returns vary wildly and are highly correlated with the stock market (average IRR of 18%, but with great variability in bottom quartiles). Some scale is beneficial, but excess can hurt returns. The industry is essentially an oligopoly with few firms showing persistently strong returns. Good funds generally are closed to new investors and are extremely selective in picking limited partners. If newcomers could get into a good fund, ensuring right of first refusal is essential in the case of early success.

Good VC/PE firms have outstanding General Partners who have sourced 6-8 deals minimum within their expertise and cashed out at least 4-5 deals. It is important to select funds investing via consensus versus one-person shops. VC/PE suffers from excess liquidity. Ultimately, at least half of existing firms will probably shut down.

Investment Professionals and SEC Regulation

by Michael Lindh, CFA, Secretary/Treasurer

March 30, 2004—What does the practicing investment professional need to know about the priorities and initiatives of the SEC, and what practical impacts will they have on both firms and practitioners? These questions were addressed at a half-day seminar sponsored by the IASC and held at the law offices of Bell, Boyd & Lloyd, LLC.

Featured speakers included attorneys Jeanette Lewis from the SEC's Chicago office and Donald Weiss and Veena Jain from Bell, Boyd & Lloyd, who discussed regulatory priorities, proposed regulations, and recently ap-

proved initiatives. They were followed by Cary Stier and Laura Reed from Deloitte & Touche, who reviewed the implementation aspects of new compliance policies and procedures. Pamela Conroy from Institutional Capital Corporation concluded with the perspective of a compliance officer assigned with the responsibility of insuring her firm's compliance with these rules and regulations.

Lewis emphasized mutual funds and corporate accounting as areas of priority for the SEC. She carefully reviewed a list of those firms "making the news" during the past year, along with a discussion of their particular issues. Possible requirements of mandatory redemption fees and ways to prevent "late trading" were discussed in depth. It was also noted that the Chicago office of the SEC had recently hired 43 new professionals.

Weiss and Jain focused on several recent regulatory initiatives of particular interest to Society members. By October 5, 2004, all investment advisors and mutual funds must be in compliance with, respectively, new Rule 206(4)-7 of the Investment Advisors Act and Rule 38a-1 of the Investment Company Act, which include approving lots of policies and procedures as well as designating a Chief Compliance Officer. IPO eligibility, a proposed Code of Ethics, proposed mutual fund portfolio manager disclosures, hedge fund regulation, and the future of soft dollars were also discussed.

Stier and Reed discussed in detail the implementation of the new October 5 rules. Fair valuation was reviewed in depth, including regulatory history, trigger points, valuation methods, and documentation. Finally, the proposed "hard" 4pm close for mutual funds was gone over intensively.

Conroy emphasized the importance of a culture of compliance and the importance of reputation to a firm. Trading was emphasized, as was monitoring, regular meetings, and customized policies and procedures. She recommended carefully reviewing existing ADV disclosures, and joined the rest of the speakers in discussing the subject of electronic mail.

Asset Allocation – A Look At Exchange Traded Funds

by Matt Clink, CFA, Volunteer

As a market, ETFs ("Exchange Traded Funds") have grown tremendously during the last five years, and why not? Their advantages include low fees compared to mutual funds, low tracking error relative to indices, and low minimum investment requirements. Essentially, an ETF is an entire index in one security that trades like a stock. In this quarter's edition of *The Efficient Frontier*, we discuss the usefulness of ETFs in individual and institutional investor portfolios.



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"Introduction to Exchange-Traded Funds"
by Chamberlain et al
Barclays Global Investors

This whitepaper offers a complete overview of ETFs by the industry's leading provider, BGI. Its key point is that ETFs are growing in popularity, by now offering exposure to all nine U.S. equity style sectors (i.e., growth/core/value and large/mid/small cap), U.S. equity economic sectors, global and non-U.S. equity mandates, and U.S. fixed income indices.

The authors also cite a survey by Financial Research Corporation, indicating the top three reasons for investing in ETFs are 1) tax efficiency, 2) trading flexibility, and 3) lower expense ratios. ETFs incur lower taxes than mutual funds, as ETFs make fewer capital gains distributions. They trade like stocks on major exchanges. Their annual expense ratios are typically less than index mutual funds, especially for smaller investors.

ETFs have much institutional appeal as well. They may provide a low-cost solution regarding investment manager transitions, cash equitization (for managers that carry high cash balances), asset allocation changes, and 401(k) plan brokerage windows.

"Index Mutual Funds and Exchange-Traded Funds"
by Leonard Kostovetsky
Journal of Portfolio Management, Summer 2003

Kostovetsky provides a direct comparison of ETFs and index mutual funds using a quantitative analysis focusing mainly on expenses, tax efficiency, and time horizon. He finds ETFs are superior when investors have more that \$60,000 to allocate or have time horizons longer than a few years. While ETFs boast a lower expense ratio than index mutual funds and better tax efficiency, transaction costs (brokerage fees, market impact, etc.) are higher. ETFs may thus be better investments for long-term investors, while index mutual funds may still have their place with smaller investors who prefer to move capital more often.

Equity Valuation

by Rawley Thomas, CFA, Volunteer

Following are some classic academic studies worth adding to your research collection:

Accounting returns versus economic returns. There is rich literature in academic journals on the flaws of various profitability measures (ROE, ROA, RONA, etc.). Accurate measurement of economic returns is important to investment professionals so that proper trends and comparisons to costs of capital are derived for calculations of a company's performance relative to other firms.

The classic article by Ezra Solomon (see Richard P. Brief, ed., "Estimating the Economic Rate of Return from Accounting Data", Garland, New York, 1986) compares accounting to economic returns to find significant differences related to depreciation accounting, project cash patterns, and inflation. Yuji Ijiri ("Recovery Rate and Cash Flow Accounting," *Financial Executive*, March 1980, pp. 54-60) suggests much of the distortion could be reduced by relating the gross cash flow of a business against the gross cash investment before depreciation. I showed in the May/June 2003 issue of *Shareholder Value Magazine* that a measure based on a cash on constant dollar cash investment over the asset life represents the average real IRR of all the projects in place and eliminates the distortions inherent in traditional accounting measures. This average holds if assets produce roughly constant output over their useful lives.

Regression with Fat Tailed Distributions. The classic, yet little known article, "Regression with Non-Gaussian Stable Disturbances: Some Sampling Results," by Blattberg and Sargent (*Econometrica*, May 1971, p. 501 ff.) discusses employing least absolute deviations as the correct method to estimate regression with fat tailed, non-Gaussian, stable distributions which are most prevalent in financial data. The technique can be implemented in SPSS by setting the loss function to absolute value of deviation in the non-linear regression capability. I would advise practitioners to always question Ordinary Least Squares and request to see the actual scatters with tests on the residuals to assure consistency with a regression's Normality assumption.

Stalla Classes For CFA® Exams

The Investment Analysts Society of Chicago, in conjunction with Stalla Seminars and DePaul University, is pleased to announce the Stalla 3-Day Intensive Review Seminars for all three levels of the CFA® Exam.

For more information, go to www.stalla.com or, call 888-pass-CFA (888-727-7232).

3-DAY INTENSIVE CLASSES

Level 1	May 7-9	8:30 AM —12 PM (break) 1—5:00 PM	UBS Tower Conference Center Chicago
Level 2	May 7-9	8:30 AM —12 PM (break) 1—5:00 PM	UBS Tower Conference Center Chicago
Level 3	May 8-9	8:30 AM —12 PM (break) 1—5:00 PM	UBS Tower Conference Center Chicago



Membership News

IASC About Town—Bulls Night

by Rebecca Cook, CFA, Volunteer

April 12, 2004—36 IASC members and guests got together to enjoy the last Bulls home game of the season. The group kicked off with a happy hour at the stadium before the game and then proceeded to watch the Bulls lose a relatively close one.

Everyone had a good time and used the pre-event networking to catch up with colleagues and meet new friends.

Human Capital -

Profile of an IASC Member

James P. Stirling, CFA

by Greg Gocek, CFA, Communication Chair

In his distinguished career in investment banking over many years, Jim Stirling has worked with the CEOs of some of America's leading corporations. These achievers imparted lessons to Jim on the keys to success at the top levels of American business, worthily complementing his studies at Princeton (undergraduate), Stanford (MBA), and the University of Chicago (postgraduate).



The chief lesson learned? Unwavering dedication to serve clients extremely well is vital. Jim recalls the revelation of a client (and self-made billionaire) who always returned every call the same day received, even if that demanded late nights at the office. Simple action, but tough to apply, with consistency making all the difference.

That's benefited Jim, who works for the successor to the firm he joined after business school. Starting at Kidder Peabody in 1965, the third generation Stirling in finance, he's now a Senior Vice President at UBS Financial Services. Jim envisions a bright future for global full service financial powerhouses like UBS. The most significant industry change he'd note? That's the explosion of financial innovation and manifold related products and services.

To stay ahead of the curve in understanding the dynamics of finance, Jim has long relied on the support professional associations can offer. Earning his CFA in 1971 and active in IASC ever since, he's volunteered on the Program Committee for 6+ years and has shared his counsel as a Board member for the last two. His optimism extends to IASC, seeing its ethically conscious members as our industry's first responders in rooting out shoddy practices.

A frame of reference outside finance has enhanced Jim's

perspective. Beyond clear networking advantages, service in the non-profit/public sectors strengthens one's management aptitude. Different leadership styles can be effective across contexts, so an extensive toolkit helps. Hence, roles on the Boards of the Chicago Symphony, Northwestern Memorial Hospital and the Executive Council of Chicago Metropolis 2020, as well as a business sabbatical as a federal government official (special assistant to Commerce Secretary Elliot Richardson) were personally valuable. They also furnished their share of fun to a self-described "quiet and formerly athletic" father of three!

People News: John A. Canning, Jr.

by Carmen Heredia-Lopez, CFA, Volunteer

John A. Canning, Jr., IASC Board of Directors member, was recently appointed to the Board of Directors of the Federal Reserve Bank of Chicago. He replaces outgoing director Robert Darnall, retired chairman/CEO of Inland Steel Industries.

Commercial banks within the Fed system elect three bankers and three non-bankers to this board. The Federal Reserve Board of Governors appoints three additional non-bankers and designates the board's chair and deputy chair. The resultant nine-member board is selected to represent a cross-section of the Seventh District economy.

The Federal Reserve Board of Governors appointed Mr. Canning to serve as a Class C Director (individuals chosen from professions outside the banking community) and complete Mr. Darnall's unexpired term on the Chicago Fed board through 2005.

The Chicago Fed board oversees the management of the Chicago Fed's operations and acts on the Bank's discount rate. The Federal Reserve Bank of Chicago is one of 12 regional Reserve Banks that, with the Federal Reserve Board in Washington, D.C., constitute the nation's central bank.

Each Reserve Bank supervises member banks and bank holding companies, serves as a bank for depository institutions and the US government, monitors economic conditions in the District, and participates in formulating national monetary policy.

Mr. Canning is the chairman and chief executive officer of Madison Dearborn Partners Inc., Chicago, Illinois. He founded that firm in 1993 following a successful 24-year career at First Chicago Corporation.

Mr. Canning has an A.B. from Denison University and a J.D. from Duke University. Some of the other boards on which he serves are: The Economic Club of Chicago, Jefferson Smurfit Group plc, The Milwaukee Brewers Baseball Club, The Chicago Community Trust, The Field Museum, Northwestern University and Denison University.



Welcome New Members



Odeh Akkawi
 Monika C. Bahri, CFA
 Derek M. Bandler
 Jaime E. Black
 David R. Brief, CFA
 Adam S. Chalmers
 Ahsan Chaudhri
 David T. Cheng
 Oleg A. Chugaev
 Kevin A. Cook, CFA
 Dafina Dunmore
 Christopher I. Engelman, CFA
 Javier P. Epstein, CFA
 Marcus A. Ewald, CFA
 Eric W. Flanders
 Albert Goldstein
 Allen W. Goody
 Chad S. Hancock
 Douglas E. Harrell
 Steve D. Hayward, CFA
 Lorraine L. Holland
 Rebekah L. Holt
 Ronald J. Hottovy

Ying Huang
 Kim B. Huebner
 Jeremy C. Hughes, CFA
 Arnold Hull, CFA
 Charles J. Hummel
 Young B. Im
 Robert J. Infanger, CFA
 Allen E. Jacque
 Rebecca L. Javid
 Phillip M. Kain
 Scott B. Kauffman, CFA
 Nelson T. Kefauver, CFA
 Lawrence A. Kenny
 Paul J. Korrison, CFA
 Jon W. Kreidler
 Jeffrey D. Kuhl
 Chun Chun W. Lam
 Michael J. Laskowski, CFA
 Robert E. Lee, III
 Jie Li, CFA
 Michael J. Lorenzen, CFA
 Ryan J. Luther, CFA
 David J. Makula

Michael L. Manelli, CFA
 Stephen D. Masarik
 David Mauer
 Daniel E. McNeela
 Todd H. Meggos, CFA
 Treasa H. Moran
 Daniel G. O'Donnell
 Michael D. Oliveros, CFA
 Vadim V. Ovchinnikov
 Didar S. Parhar, CFA
 Ashish B. Patel
 Patrick H. Perkins
 Jason T. Perlioni
 Perry M. Pinto
 Charles W. Price, CFA
 Hassan Z. Qayyum
 Antonia S. Raditcheva
 Kovatchka, CFA
 Joshua M. Rosenberg
 Michael H. Sankowski
 Robert L. Scheuermann, CFA
 Joshua J. Shipley
 Jonathan D. Simon

Julie L. Stralow
 John Sunu, CFA
 Alyssa B. Thyren
 Brian A. Tidd, CFA
 Todd A. Todaro
 Derek Toross, CFA
 John E. Voigt
 Mark C. Vorhees, CFA
 Bin Wang
 Xinxin Wang
 Erik R. Waters, CFA
 John F. Weber
 Fernando S. Wilson
 Craig L. Woker
 Jerrold E. Wolf
 Yan Xu
 Roy D. Youngblood
 Wei Zhang, CFA
 Xin Zhou
 Joseph L. Zinsky

Program News



IASC is proud to be a participant in the AIMR Professional Development - Approved Provider Program. Many IASC events now qualify for Professional Development (PD) credit. After each qualifying event, IASC provides AIMR with certification of members' attendance and AIMR automatically posts credits to each member's online Continuing Education Diary. IASC transmits this information as a service to our members so members are not individually responsible for documenting or reporting credit earned.

Alternatives: Which Is Best?

by David Frank, CFA, Volunteer

February 12, 2004—Former Chicagoan Rex Siquefield of Dimensional Fund Advisors (DFA) returned from California to present to IASC, reflecting the true appeal of a high quality audience! A University of Chicago alumnus, Mr. Siquefield helped pioneer index investing here in the early 1970s

at American National Bank. He later collaborated with Roger Ibbotson to create a seminal, systematic study of long term US stock and bond returns. In 1981 he co-founded DFA to exploit academic theories indicating that low price to book and small capitalization stocks outperform over the long term.

Based in Santa Monica, DFA has grown to manage \$48 billion in assets in a broad range of asset classes, both domestic and international. The firm is especially well known for its US small and micro-cap enhanced index products. In these funds DFA acts as a liquidity provider, standing ready to buy large quantities of thinly traded equities slightly below prevailing market prices or sell them slightly higher. DFA has also developed a small cap international index fund.

Mr. Siquefield spoke about the small cap international asset class in the context of alternative investments. His survey of recent research into venture capital, hedge funds and private equity suggests their returns are lower, standard deviations higher, and their correlation with the general market is also greater than previously reported. He concludes that international small cap stocks are a more attractive option for diversifying portfolio risk without sacrificing return.



Thoughts About Oil and Gas

by Eric Ause, CFA, Volunteer

March 9, 2004—T. Boone Pickens founded and ran Mesa Petroleum Co. between 1956 and 1996. In 1996, he founded BP Capital, which manages the highly successful BP Capital Commodities Fund and the BP Capital Energy Equity Fund. He is also involved in other projects including Clean Energy and Mesa Water, Inc.

Mr. Pickens opened with general comments about his experience at Mesa, followed by comments about the high returns generated at BP Capital, especially notable as its funds lost 90% of the original investment before eventually earning many times the starting total. He also talked about Mesa Water, an investment in another type of resource play. The company, beginning as a small Texas land investment in 1971, aims to parlay underground water rights into Pickens' largest-ever private deal (except for his prior corporate ventures).

Never shy with his opinions, Mr. Pickens next described his views on federal energy policies. Commenting that although President Bush "couldn't find oil if he was standing ankle-deep in it", the administration nonetheless enjoys favorable supply conditions such as nearby oil reserves in Alberta, Canada, new sources of oil possibly soon emerging from Iraq, and large natural gas reserves being developed in Qatar. As a result, immediate energy problems appear well on their way to being addressed. Pickens also described his belief that oil prices will remain high due to the peaking of worldwide production and to tight refining capacity. In addition, natural gas prices could rise until liquid natural gas facilities are built to meet demand, after which prices could be limited on the upside by excess capacity resulting from potential overbuilding.

Mr. Pickens described the two centuries between 1900 and 2100 as the "hydrocarbon era". He sees opportunities in energy during the 21st century as likely to include coal, tight sands, possibly oil shale, and trading. Exploration and production no longer will have reduced attractiveness, at least in the U.S., as most large fields have been discovered.

During Q&A, the speaker commented briefly about his role in pushing Gulf Oil into the arms of Chevron in 1984, thus making large profits for shareholders. He also talked about the issue of Royal Dutch/Shell's write-downs of its oil reserves and his concern about possible recessionary pressures that could result from the impact of China's growing appetite for oil and gas.

Macro "Food for Thought"

by Patrick Carlevato, CFA, Volunteer

April 15, 2004—Speaking to a hungry group of investment professionals seeking a few nuggets of insight as to how the Fed decides to utilize its levers to regulate the economy, Dr. Ben Bernanke, a member of the Board of Governors of the Federal Reserve System spoke at IASC's latest luncheon program. Dr. Bernanke described several indicators they track closely to measure inflation and inflation expectation. One of the Fed's overriding goals is to achieve non-inflationary, healthy U.S. economic growth. While the Fed relies on open market operations to directly influence inflation trends, most asset classes are indirectly affected by slight changes to the Fed Funds Rate. Investment professionals attempt to understand inflation and measure inflation expectation, so as to forecast changes in Fed interest rate policy.

Dr. Bernanke described a few of the measures the Fed monitors, but stressed it uses many metrics to paint a complete understanding of economic trends. To satisfy the audience's inquisitive "appetite", Dr. Bernanke shared details of some macroeconomic indicators.

- Yields On Ten-Year TIPS and on Nominal Ten-Year Treasury Notes – The difference between these series tracks inflation compensation. In this case, the spread measures the Ten-Year expectation of inflation
- Inflation Compensation – Inflation compensation can be measured over different time horizons. The contrast between Five-Year TIPS vs. Five-Year Treasury Notes projects today's rate of inflation versus that expected 5 years hence.
- Treasury Term Spread – When the yield on the Ten-Year Note dips below the Yield on the Three-Month Bill, the inverted yield curve has been a reliable predictor of recessionary periods.
- Federal Funds Rate – Perhaps this is a self-fulfilling prophecy, but the Federal Funds Rate has also proven to contain predictive power.
- Expected Federal Funds Rate – Using federal funds futures contracts, the Federal Reserve is able to collect feedback on market anticipations of Fed policy. Dr. Bernanke pointed out that the yield on federal funds futures contracts jumped on April 2, 2004 after the jobs report indicated 600,000 new jobs had been created.

During the Q & A, Dr. Bernanke noted he favors an operating policy with more transparency, illustrating the Fed's goals to the market by indicating a "target" rate of inflation.

For further details about Dr. Bernanke's talk, please refer to the following link from Reuters for an article covering the event: http://biz.yahoo.com/rf/040415/economy_fed_bernanke_3.html.



Technology News

Viewers Favorite

by Arch King, CFA, Technology Co-Chair

Ever wonder what your peers are looking at on the IASC website (www.iaschicago.org)? The News and Events are big draws, of course, but so are some of the more specialized areas for our candidates and members.

The IASC web site has been spruced up over the winter and you'll notice cleaner graphics, crisper fonts and fewer colors. A whole new section has been added for Candidate Services, with links for joining study groups and chat rooms. And the Links section now has a connection to an online view of the current issue of the Journal Of Investment Management. During the rest of the spring you'll see more navigation updates and easier ways to move directly to the pages you want.

Two of our most visited sections have been the job postings and the new Candidate Services area. Take a look below at how the usage has grown, and check them out yourself!

IASC Events

Date	Speaker/Title	Link
5/7/2004	CFA Prep Course: Derivatives Review	Go to
5/12/2004	Rusty Resume? Spring Cleaning Tips for Updating Your Resume	Go to
5/15/2004	CFA Prep Course: Mock CFA Exam	Go to
5/20/2004	Alan J. Lacy, CFA <i>Sears, Roebuck & Co.</i>	Go to
5/26/2004	Richard Bernstein <i>Merrill Lynch</i>	Go to
6/9/2004	Robert C. Pozen <i>MFS Investment Management</i>	Go to
6/29/2004	IASC Annual Business Meeting	Go to

Web Site Views

November 2003 -March 2004

