



# MAY MONTHLY REPORT

June 21, 2001

May was a good month for the North Growth US Equity Fund, as it advanced 1.82% in US\$, surpassing the broad S&P 500 and NASDAQ Composite Indices which returned 0.67% and -0.24% respectively. Mid- and small-cap stocks were relatively strong in May, as reflected by the S&P 400 and Russell 2000 Indices which were both up in excess of 2%. This would explain largely the Fund's outperformance compared to the S&P 500 Index. The Fund's shortfall relative to the mid- and small-cap indices can be attributed mostly to our cash position.

## **“Brightening Mood: For Stock Investors, A Belief Is Growing That the Worst Is Over”**

*WSJ, June 5, 2001*

Optimism is pervasive on Wall Street. Bullish sentiment, as expressed by the Wall Street Journal on June 5<sup>th</sup>, is shared by a growing number of both large institutional and small individual investors. This front page article details several “signs of life” in the market that possibly reflect a turnaround, including an inflow of US\$21 billion into US stock mutual funds in April following net withdrawals of US\$20.6 billion in March, and a resurgence of stock offerings—US\$49 billion in new stock was brought out in May, a record high since October, 2000. The sentiment indicators that we follow reiterate the buoyant mood of the general investing public.

The growing confidence of investors rests predominantly on the unwavering belief that the Federal Reserve's interest rate cuts so far this year will have a positive effect on the economy in the latter half of 2001 and prevent a recession, officially defined as two consecutive quarters of declining industrial production. Certainly, current news and earnings reports have been far from bullish. In fact, the market, which has tended to react vigilantly to economic data when they are first reported, seemed to turn a blind eye to the recent large **downward** revisions in 1<sup>st</sup> quarter economic growth (from the initial estimate of 2.0% to 1.3%) and in 1<sup>st</sup> quarter productivity (from the initial report of -0.1% to -1.2%). Business updates from various companies including Sun Microsystems, Hewlett-Packard, Gillette, Handspring, and J.P. Morgan emphasize further cost-cutting initiatives in the face of weaker economic conditions. Such earnings disappointments provide little basis for faith in a near-term recovery, but investors remain surprisingly unperturbed.

Does this mean that the market has already discounted the bad news and is beginning to “look over the valley”? Eventually that is how the market works. However, when this typical phenomenon begins it is very subtle and the apparent emotion of investors is one of gloom and doom with pockets of panic. The “looking over the valley for a new recovery phase” outlook is usually not articulated by investors and definitely not by the financial press. The improving market that is discounting a brighter future is widely viewed as a mystery and should be completely mistrusted as a “technical rally”--- at least that is what Rudy tells us.

When the above description of a new bull market applies, most investors feel really upset. This clearly is not yet the case. Furthermore, current valuation levels do not support a bullish outlook. As of June 20<sup>th</sup>, 2001, the S&P 500 Index is

trading at 29x **trailing** 12-month earnings, with this year's earnings likely to be below 2000 earnings. Apart from April, 1999, when the S&P 500 trailing price/earnings multiple reached 36x, the market is trading at a record high valuation since the end of World War II. Moreover, the technology sector, into which investors are again keen to commit capital, is trading at an even more inflated level. Trailing earnings for the NASDAQ Composite Index are currently negative, so its trailing P/E ratio is a useless measure. But before the NASDAQ earnings turned negative following the first quarter of this year, the index's P/E was at a record high of 289x as of March 31<sup>st</sup>, 2001 (Ned Davis Research, *WSJ*, June 11, 2001), despite the huge 68% decline in the NASDAQ Composite from its March 10, 2000 high to its April 4, 2001 bottom. The index has subsequently recovered some since its low this spring and is now at a higher level than it was on March 31<sup>st</sup>. And, according to Bloomberg, it is trading at 96x this year's estimated earnings—estimated earnings that, although below peak levels, are in our opinion highly optimistic given the negative business momentum at most tech companies.

The extremely high valuations of the broad US equity markets, combined with the unabashed giddiness among most investors during the last six weeks, lead us to remain cautious on the near-term outlook of the general market. While we are well aware that bull markets do emerge before economic and company news turn positive, we disagree with the majority of investors on the urgency to buy stocks now. We continue to concentrate our efforts on developing specific stock ideas that have not attracted excess capital and have been somewhat overlooked over the past few years, yet possess reasonable growth prospects. We are encouraged by some of these ideas coming to fruition and are currently initiating positions in such stocks.

Also encouraging is the Fund's outperformance year-to-date versus all the indices we follow. We look forward to sustained above-average returns as we continue to adhere to our 'growth at a reasonable price' philosophy. Stock selection got the Fund to its current cash position and we are confident that it will result in the Fund becoming fully invested for the beginning of the next prolonged period of rising stock prices, which would be, of course, a new bull market.

Yours truly,



Erica Lau, CFA  
Equity Analyst

#### WHERE TO FIND NGM FUND PRICES

The NGM US Equity Fund is listed under the **Mutual Funds heading** in the Globe & Mail and the Vancouver Sun. The NGM Cdn. Money Market Fund can be found under the **Money Market Fund heading** in the Globe & Mail. Both funds can be found on **globefund.com** and **morningstar.ca**. For those who prefer, we can e-mail our daily summary sheet to you every day that the market is open. To be added to our list please contact Caroline North at [caroline@northgrowth.com](mailto:caroline@northgrowth.com) or 688-5440.

## PERFORMANCE COMPARISONS

	<i>Year to May 31, 01</i>	<i>Nov. 30, 00 to May 31, 01</i>	<i>Feb. 28, 01 to May 31, 01</i>	<i>Month of May 01</i>
<b>North Growth US Equity Fund \$CDN</b>	<b>8.15%</b>	<b>12.20%</b>	<b>3.03%</b>	<b>1.94%</b>
<b>North Growth US Equity Fund \$US</b>	<b>5.42%</b>	<b>12.03%</b>	<b>2.88%</b>	<b>1.82%</b>
S&P 500 \$US	-4.37%	-3.90%	1.62%	0.67%
S&P 400 MidCap \$US	1.38%	9.14%	5.17%	2.33%
Russell 2000 \$US	3.28%	12.21%	5.06%	2.45%
NASDAQ Composite \$US	-14.47%	-18.65%	-1.84%	-0.24%

Source: Bloomberg "Total Return Analysis" as of June 1, 2001.

Note - Including income in all cases.

## AVERAGE ANNUAL COMPOUND RATE OF RETURN

	<b>1 Year</b>	<b>2 Years</b>	<b>3 Years</b>	<b>4 Years</b>	<b>5 Years</b>
<b>North Growth US Equity Fund \$CDN</b>	<b>26.7%</b>	<b>28.9%</b>	<b>17.1%</b>	<b>18.7%</b>	<b>19.9%</b>
Median U.S. Equity Fund \$CDN **	-11.0%	—	4.7%	--	12.0%
Average U.S. Equity Fund \$CDN **	-9.1%	—	5.2%	--	12.4%

Results are after all management fees and other expenses

\*\* reported by the Globe & Mail, Report on Mutual Funds, June 21, 2001

**RETURN SINCE INCEPTION (ANNUALIZED), OCT. 13, 1992 - MAY 31, 2001** **20.70%**

**NAVPS: MAY 31ST/01** **\$ 20.88**

**TOTAL ASSETS IN FUND** **\$ 91.36 MILLION**

## CANADIAN MONEY MARKET FUND

**NET CURRENT YIELD AS OF JUNE 20, 2001:**

**4.25%**

**PORTFOLIO HOLDINGS***As of May 31, 2001*

St Jude Medical	5.09
Chesapeake Energy Corp	5.06
Manor Care Inc	4.01
Universal Health Services Cl B	3.64
Diamond Offshore Drilling	3.02
Louis Dreyfus Natural Gas	2.95
Precision Castparts	2.69
Mesa Airlines Inc	2.61
Clayton Homes Inc	2.33
Jones Apparel Group Inc	2.19
Synopsys Inc	2.18
Cardinal Health Inc	2.15
Watson Pharmaceuticals	2.10
Wellpoint Health Networks	1.77
Federal Signal Corp	1.70
Stone Energy Corp	1.50
Sprint PCS Group	1.49
Timberland	1.42
Mohawk Industries	1.38
Sigma-Aldrich	1.25
Biomet Inc	1.25
Darden Restaurants Inc	1.19
Brinker International Inc	1.13
Dentsply International	0.98
Devon Energy Corp	0.87
Jacobs Engineering	0.72
Snap-On Inc	0.70
Michaels Stores	0.69
Schnitzer Steel	0.67
Pier 1 Imports Inc	0.61
Symantec Corp	0.59
Cisco Systems	0.52
Johnson & Johnson	0.49
Compaq Computer Corp	0.48
Cable Design Technology	0.43
LSI Logic	0.42
InFocus	0.28
TJX Companies	0.26
Vishay Intertechnology	0.17
City National Corp	0.13
American Power Conversion	0.12
<b>Total Equities</b>	<b>63.23</b>
<b>Cash and Short Term Notes</b>	<b><u>36.77</u></b>
<b>TOTAL ASSETS</b>	<b>100.00%</b>