



REINHART
ASSET MANAGEMENT, LLC

October 6, 2005 WEBEX

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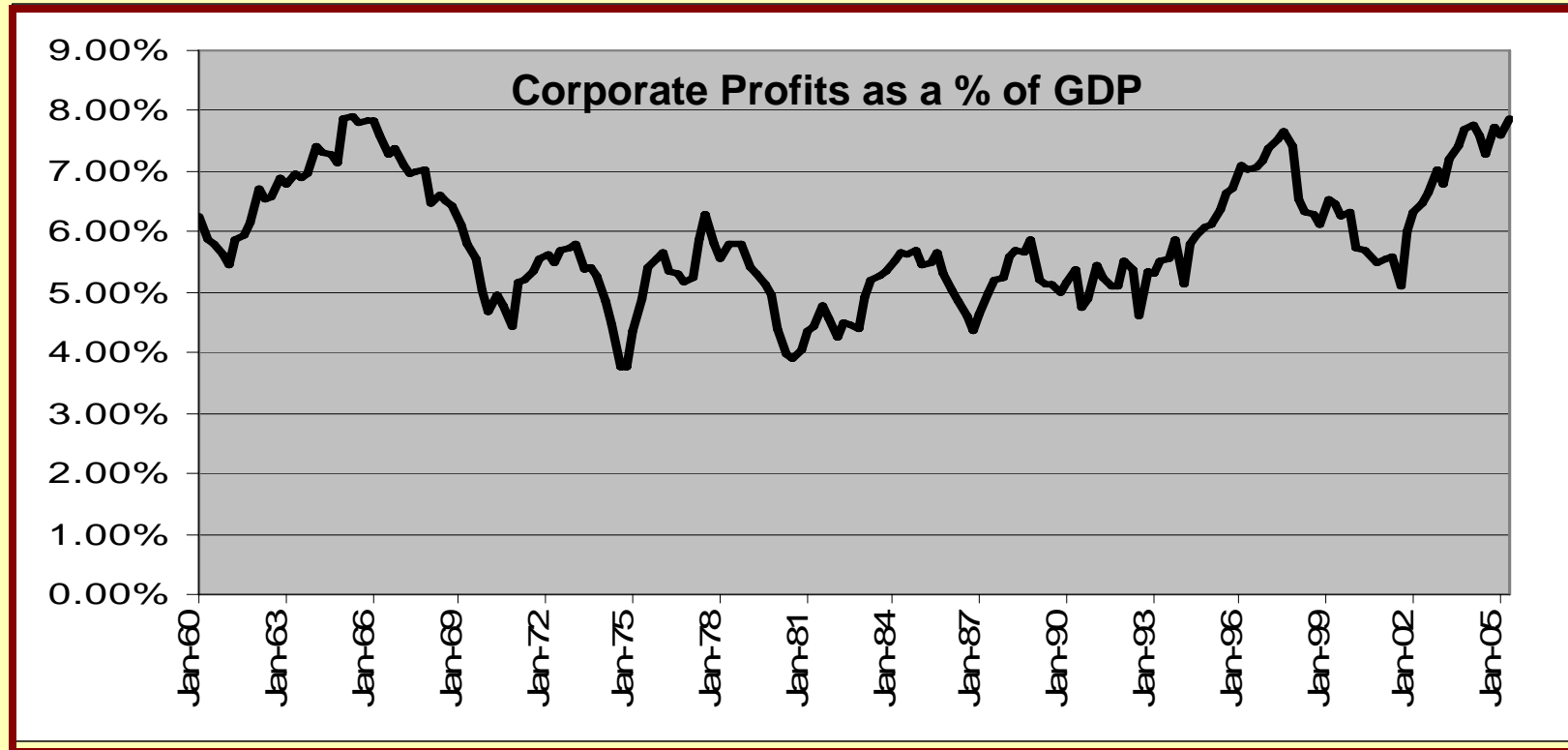


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Topics of Presentation

- Corporate Profits
 - Drive Equities
 - Cyclical in Nature
- Two “Pressures” Merging to Revert Peak Earnings
- Margin Pressures
 - Competition
 - Wages / Benefits
 - Input Prices
- Revenue Pressures
 - “Joe Main Street’s” Dilemma
- Climate vs. Weather
- A look inside the Market

Corporate Profits



Inherent laws of capitalism assure entrepreneurs attack profits - hence cyclical

Are Profits Going To Decline ?

Two different “pressures” may answer this question

MARGIN PRESSURES

-Corporate Dilemma

Competition, Wages / Benefits, and input prices

REVENUE PRESSURES

-Joe Main Street Dilemma

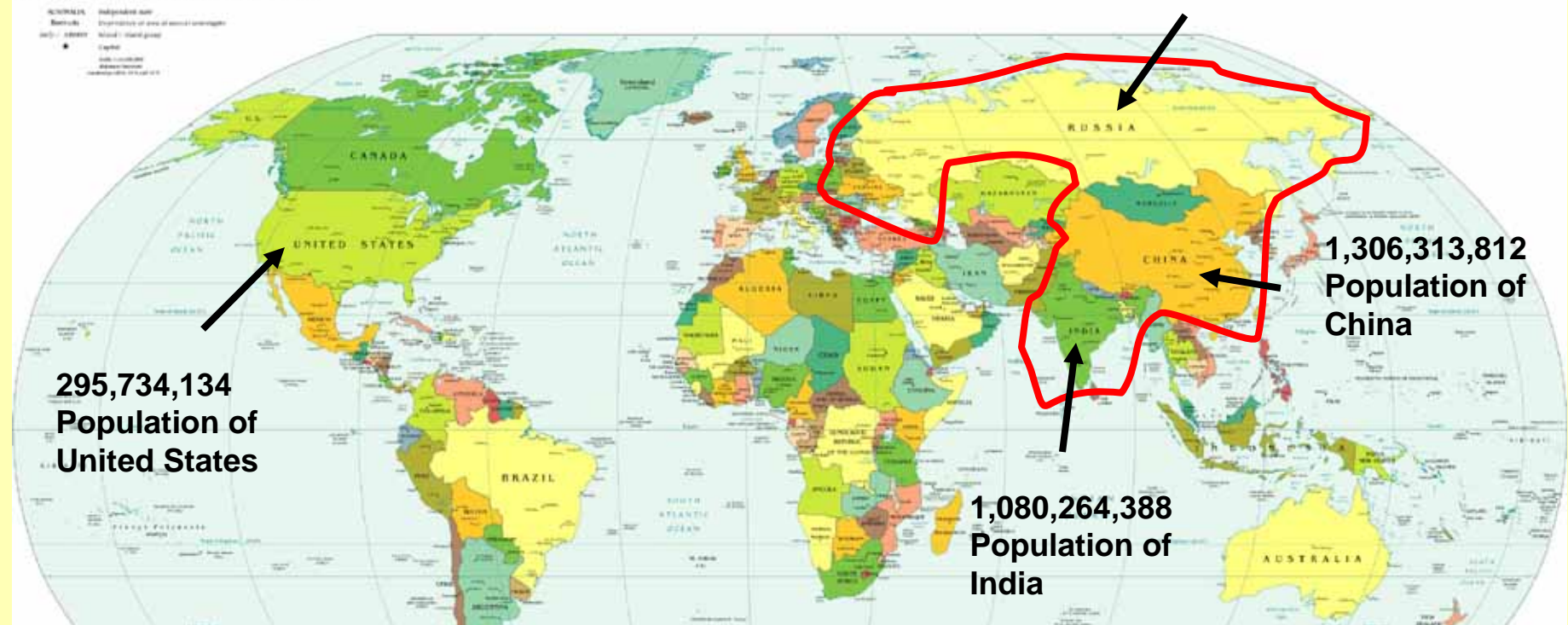
May equate to corporate revenue pressures

Open World

Competing for Margins, Wages, and Natural Resources

Margin Pressure

Political Map of the World, April 2000



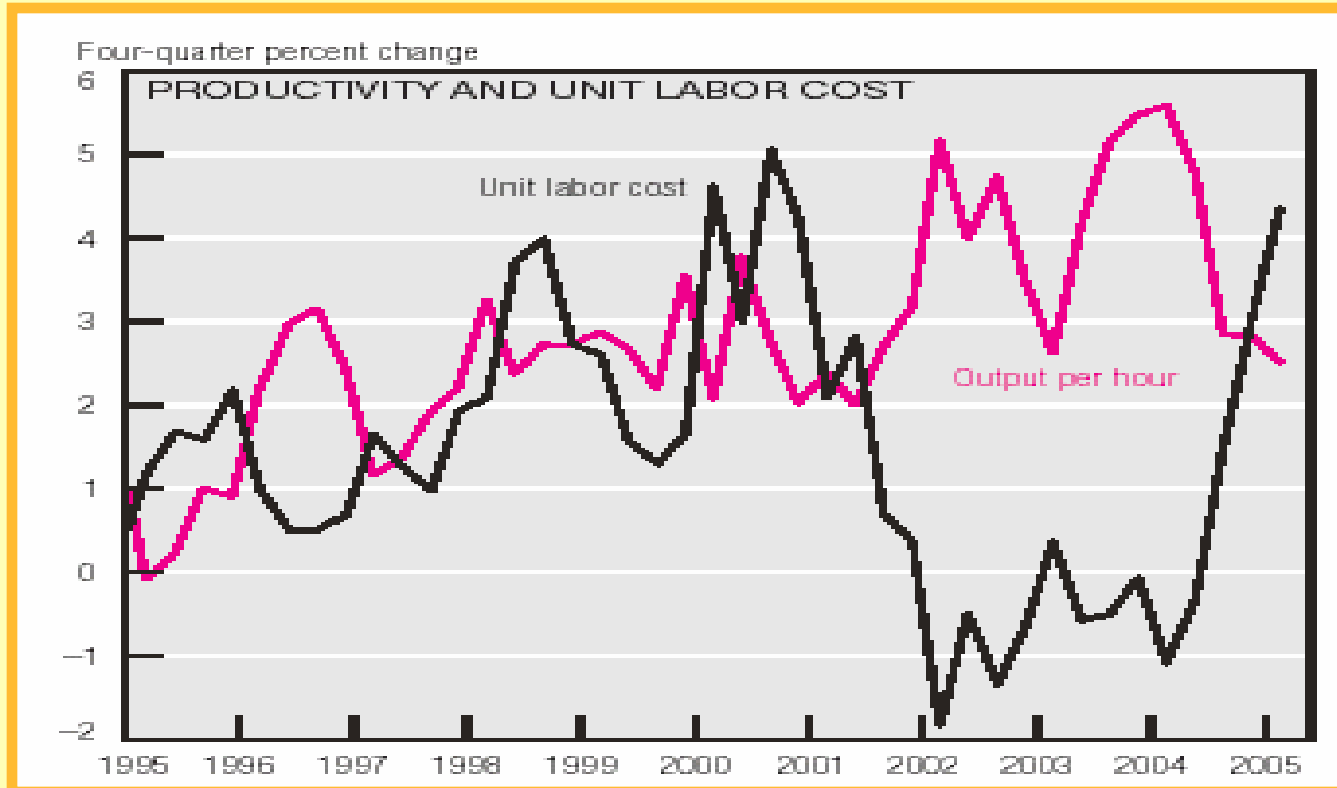
- Ever more, competition is not just coming from the other side of the country, but rather the other side of the world.

- Open world offers huge increase in labor supply, which offers a release valve for the pressure on margins from wages, but adds to the “Joe Main Street” dilemma.

- Adds to demand for finite supply of natural resources.

Unit Labor Cost and Productivity

Margin Pressure

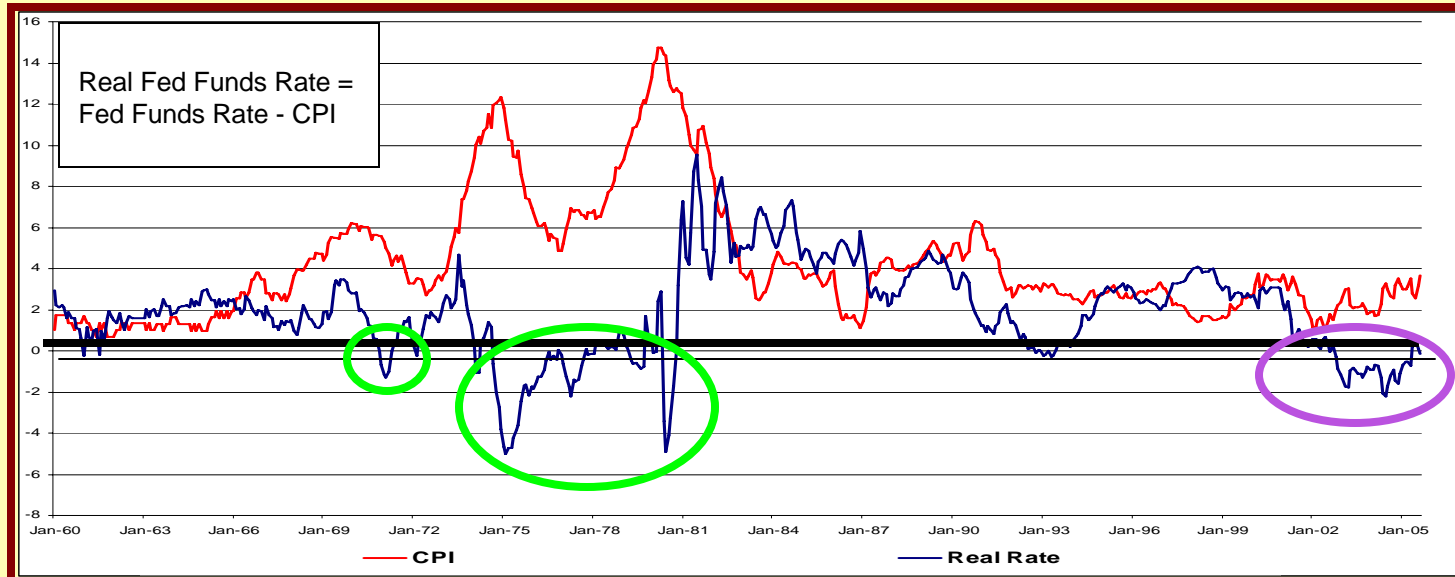
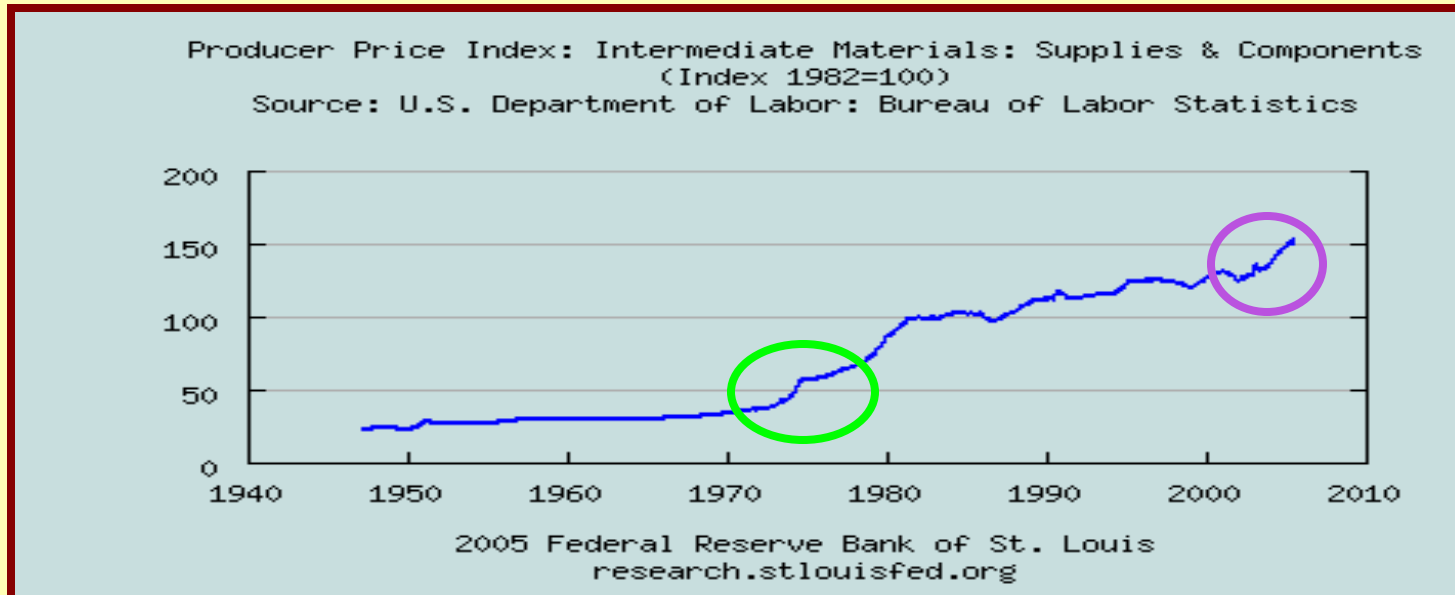


... that slowing reflected a moderation in structural productivity growth and if firms believed that the associated increases in the growth rate of labor costs were permanent, these cost pressures might be passed through to consumer prices fairly quickly to preserve profit margins.

- From the FOMC Minutes, February 2005

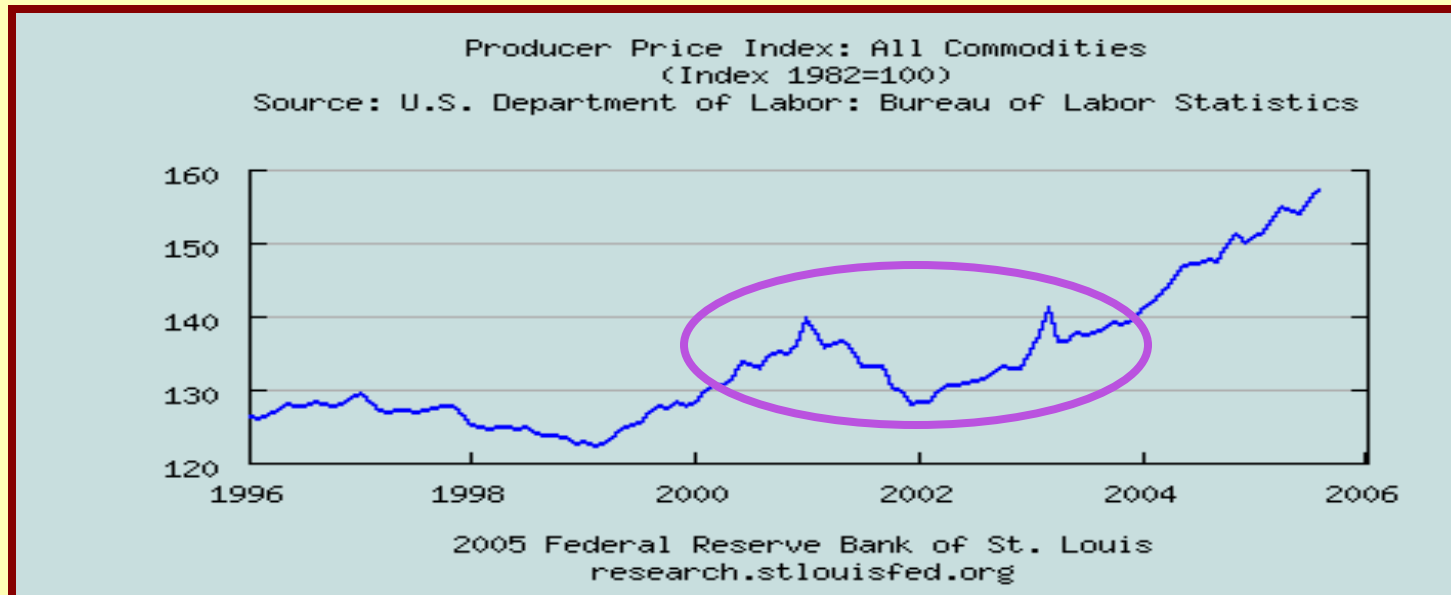
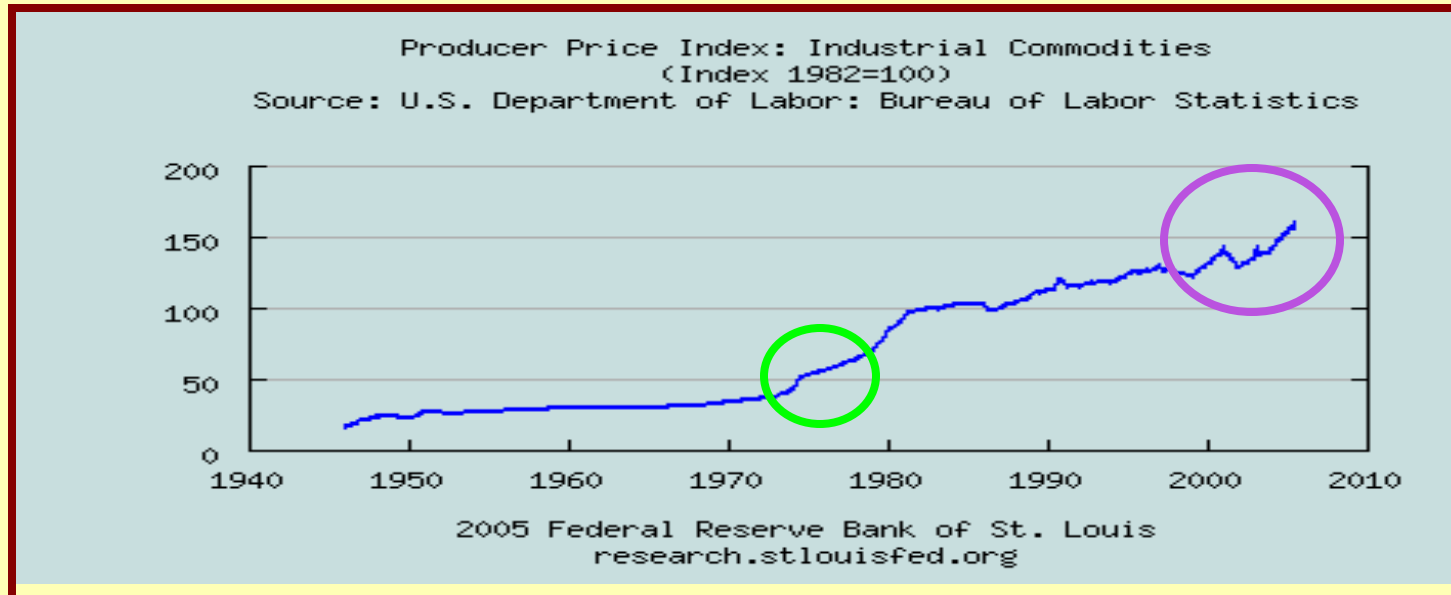
PPI – Intermediate Materials and Real Fed Funds Rate

Margin Pressure

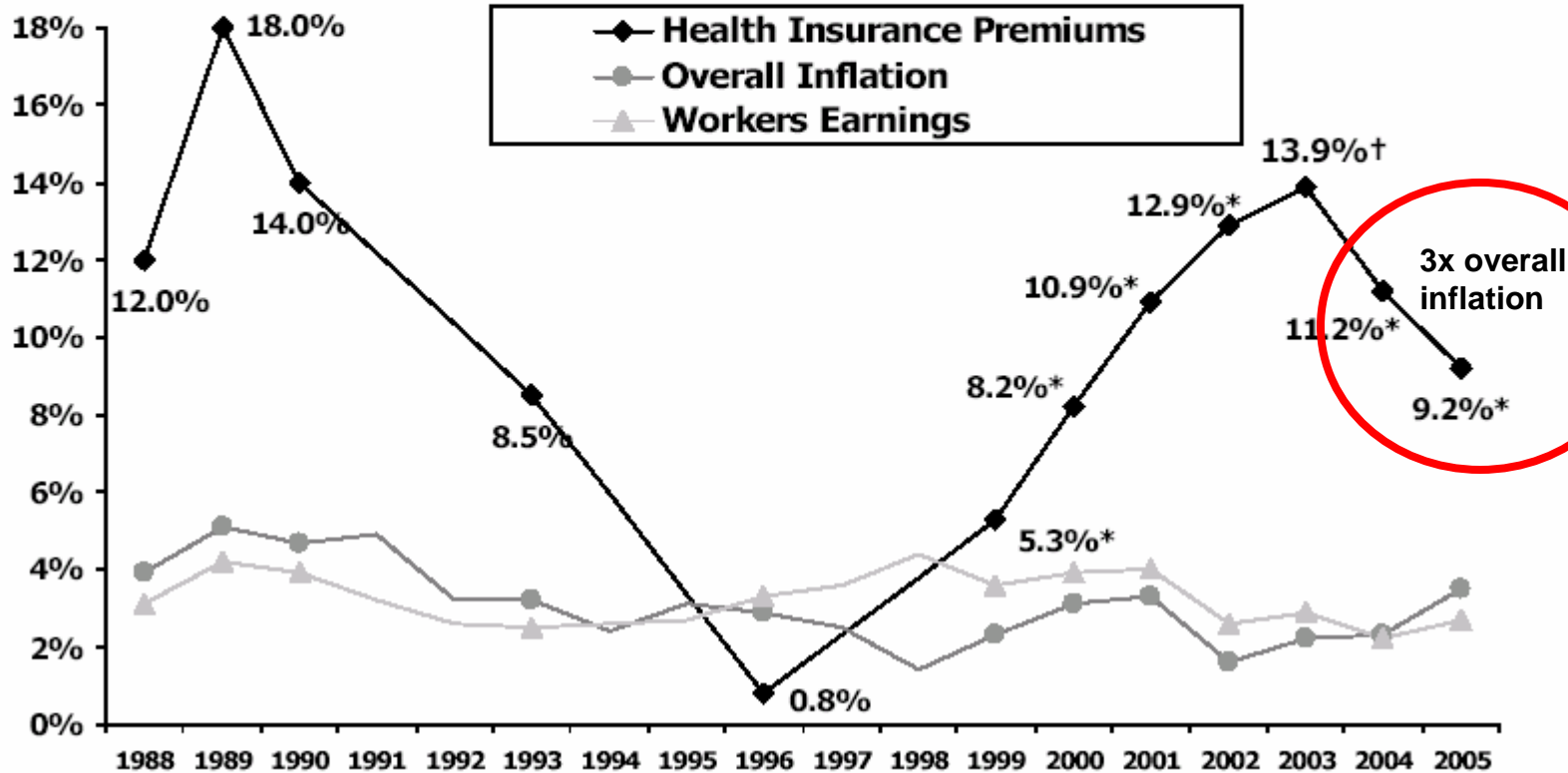


PPI – Industrial and All Commodities

Margin Pressure



Increases in Health Insurance Premiums Compared to Other Indicators, 1988-2005



Quotes From Companies Feeling the Pressure

Margin Pressure

Cooper Tire “higher raw-material costs could reduce third-quarter operating profit by as much as \$35 million to \$40 million,” Dattilo said.

Nu Skin “We will try to find ways to absorb the costs so that our customers won't feel the pinch as much,” Lori Bush, the unit's president. This is the response to shoulder rising costs for raw materials such as packaging to avoid increasing prices for its customers.

KRAFT has concerns of inflationary pressures resulting from increasingly expensive commodity costs due to rising energy prices.

COTT rising raw material costs, continued softness in the U.S. carbonated soft drink business, and a product mix shift to lower-margin bottled water. We'd do well to remember that there's always tap water, the ever-cheaper alternative, waiting to steal sales

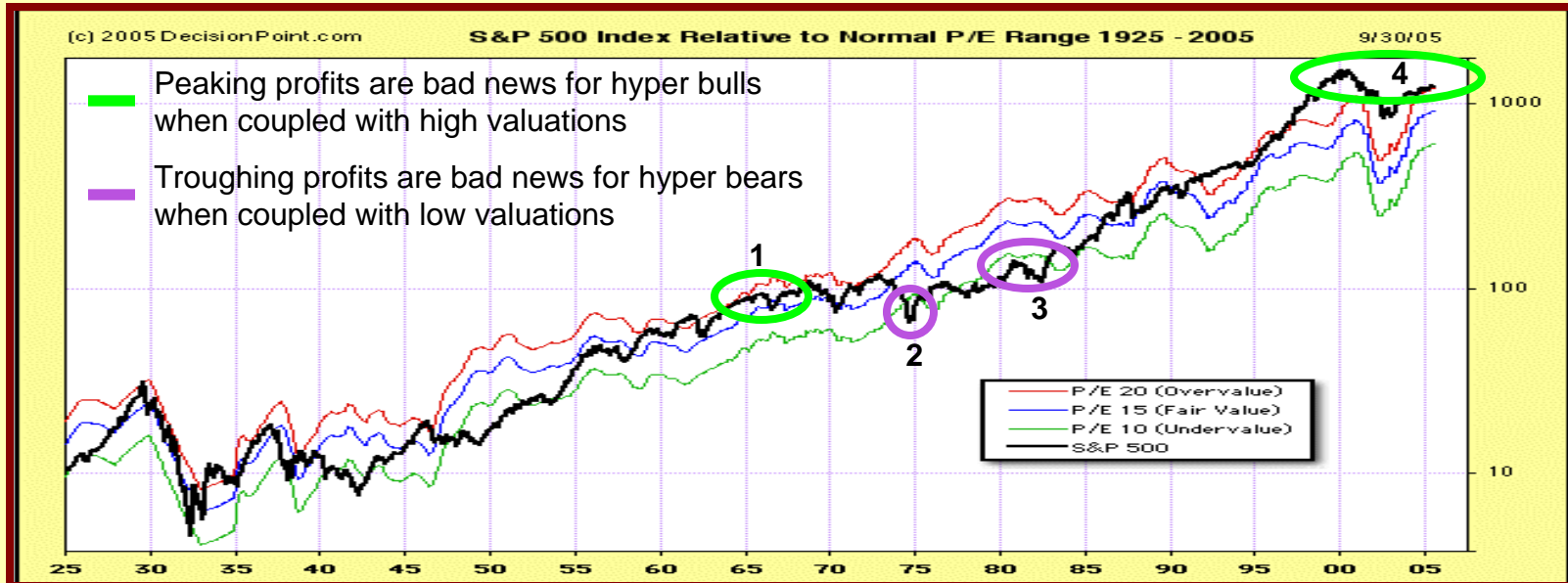
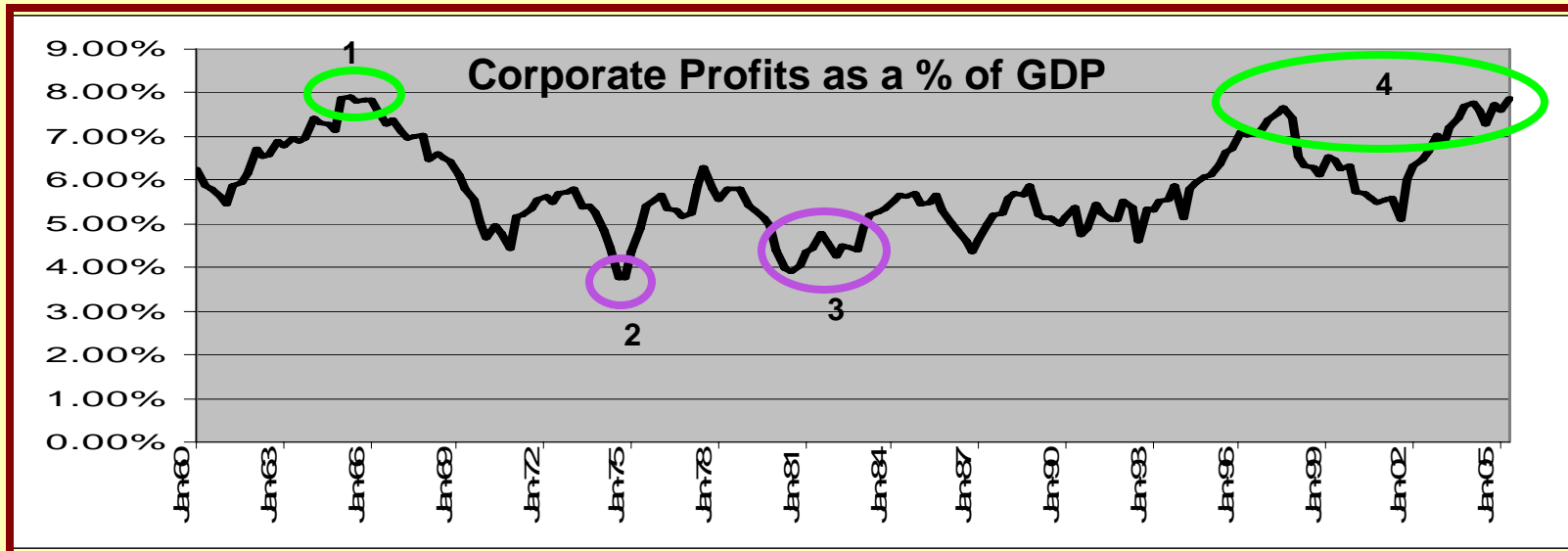
INTEL "We believe INTC has lost as much as five points of market share in servers and has seen ASPs fall in both servers (due to competition) and mobile (due to mix)," CSFB said

CITIBANK told investors that flattening yield curves will weigh on profits through the rest of the year

Titanium Technologies said on Tuesday said it will raise prices for all titanium dioxide grades in Europe and the Middle East, effective Oct. 1, citing reduced margins caused by rising raw material and energy prices

Corporate Profits and P/E Ratios

Margin Pressure



Are Profits Going To Decline ?

Two different “pressures” may answer this question

MARGIN PRESSURES

-Corporate Dilemma

Competition, Wages / Benefits, and input prices

REVENUE PRESSURES

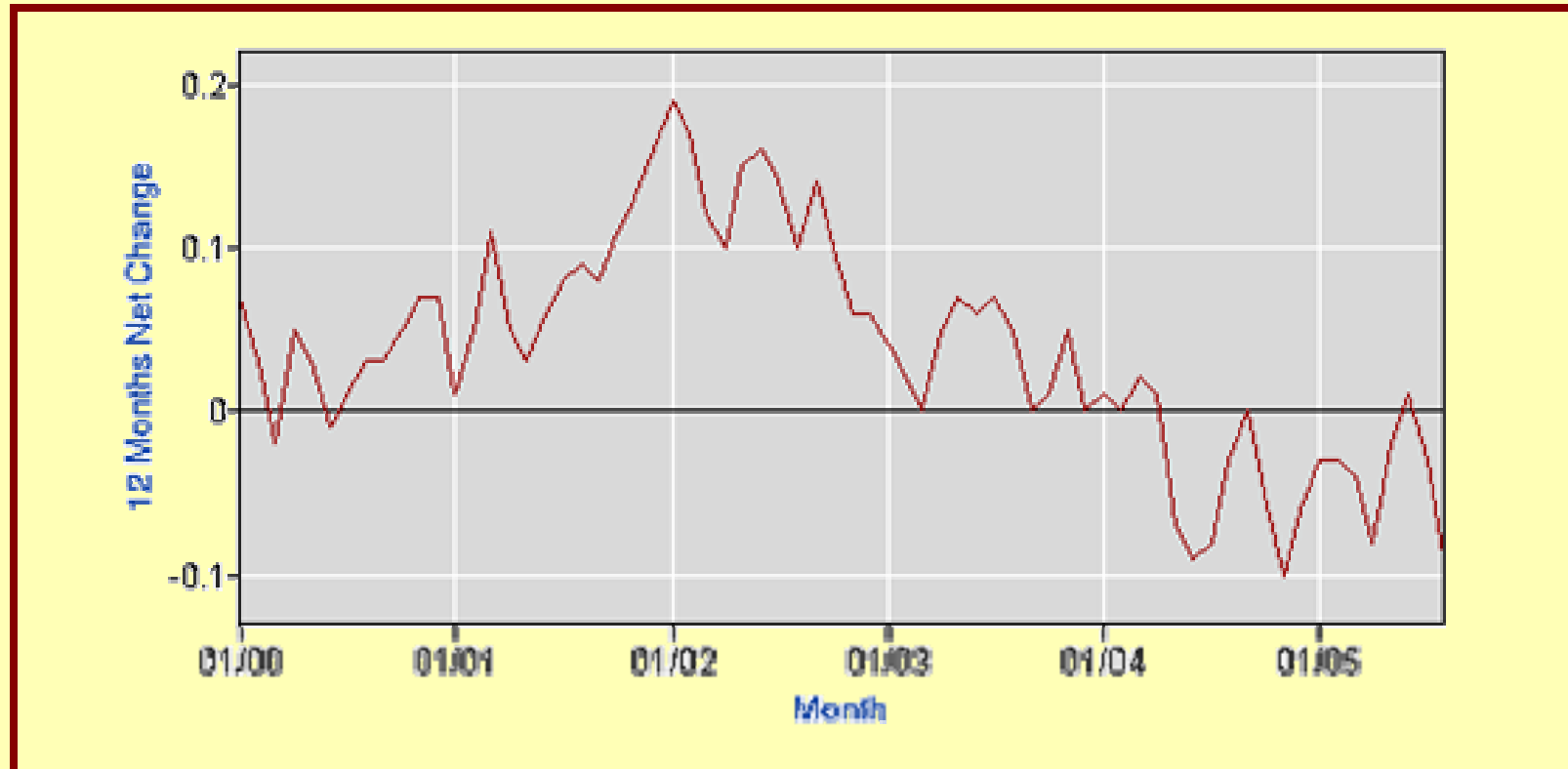
-Joe Main Street Dilemma

May equate to corporate revenue pressures

Real Wage Growth

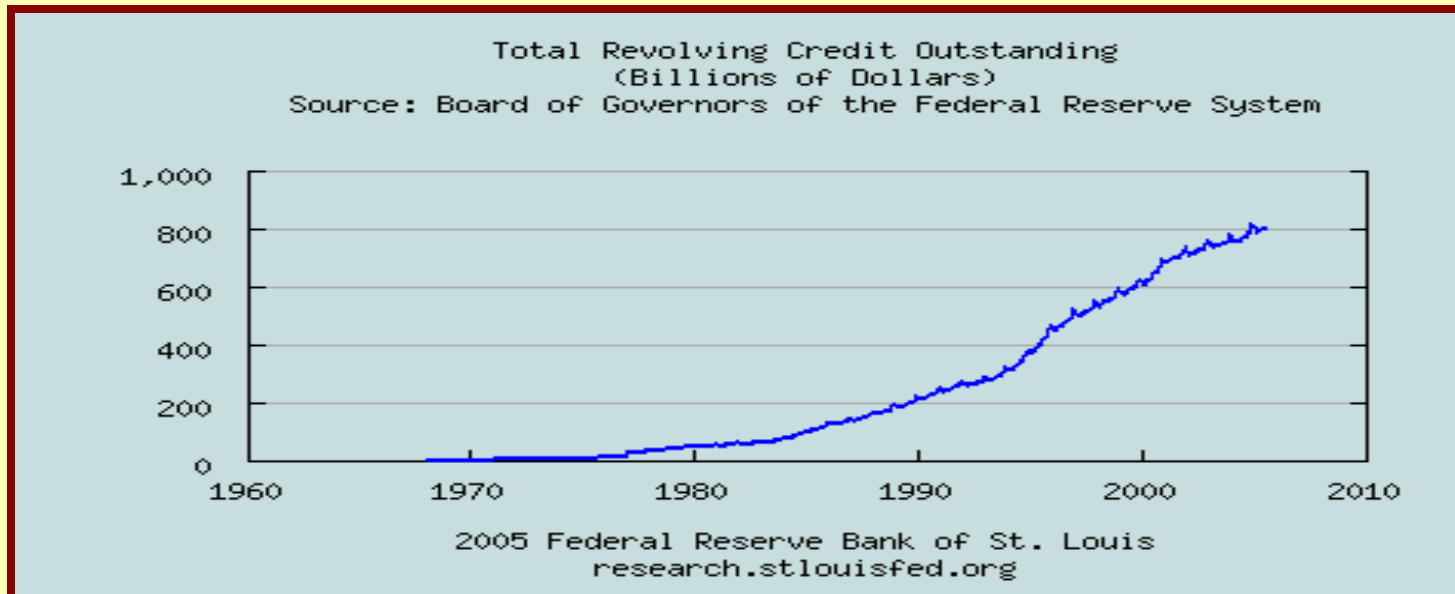
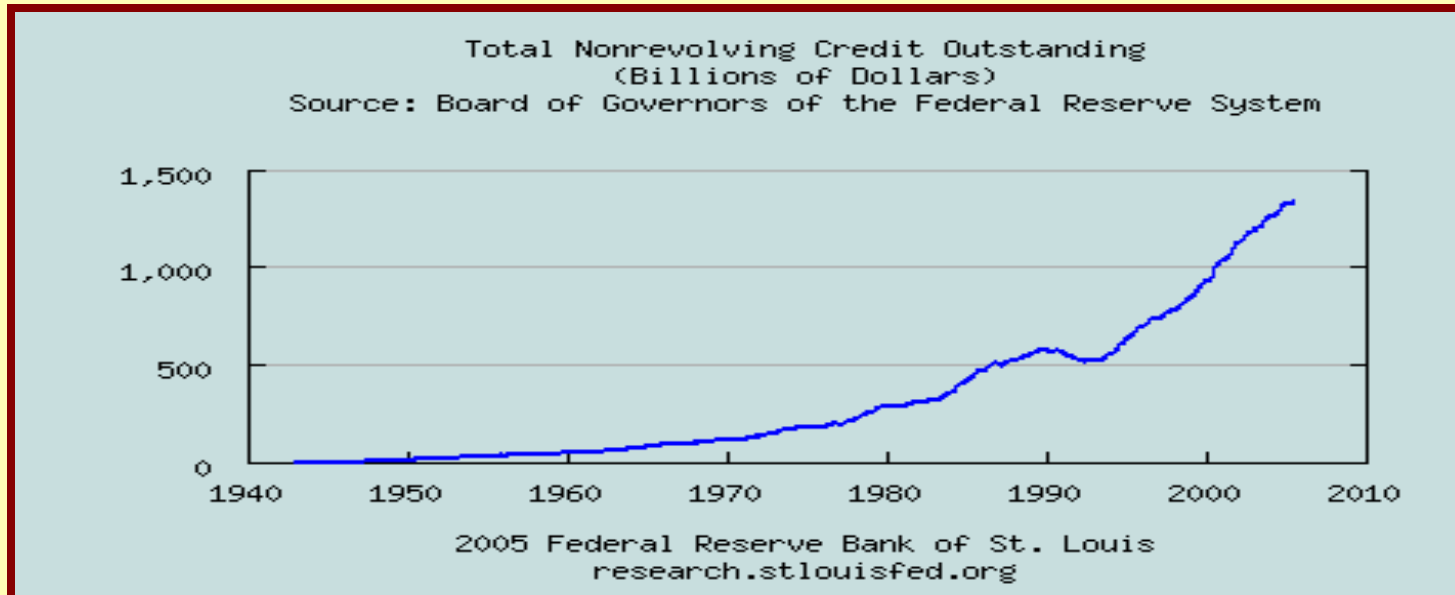
Equals Average Hourly Earnings less CPI

Revenue Pressure



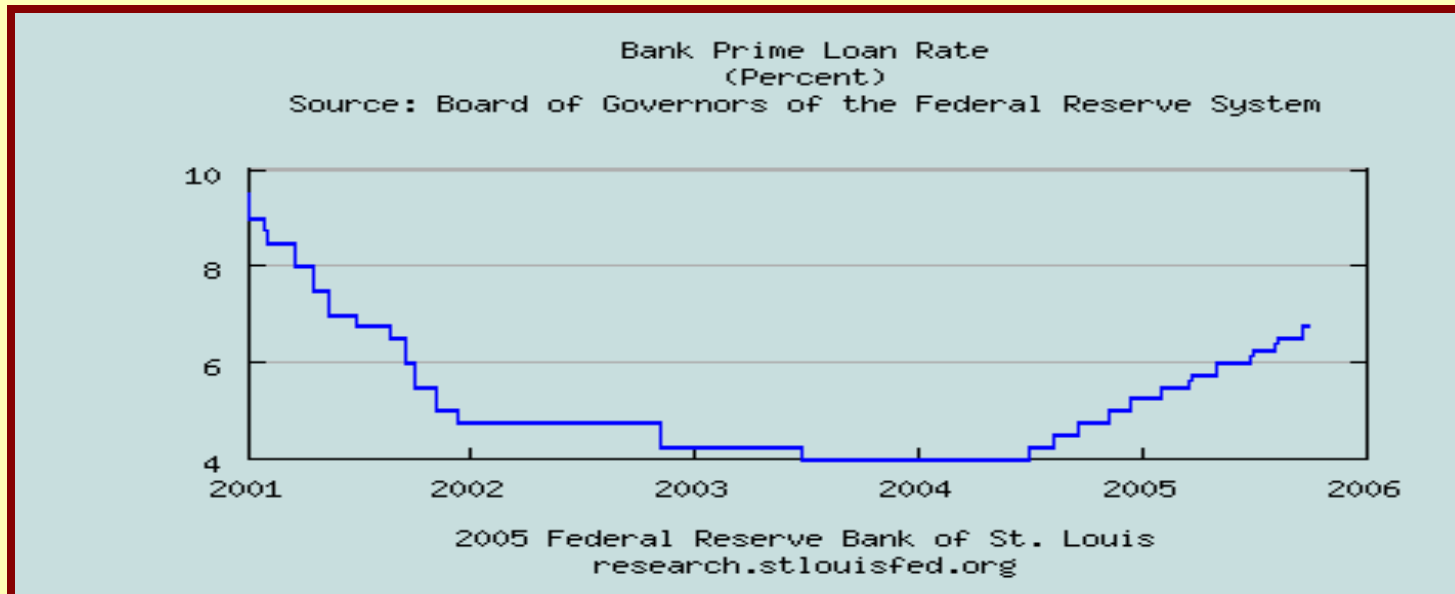
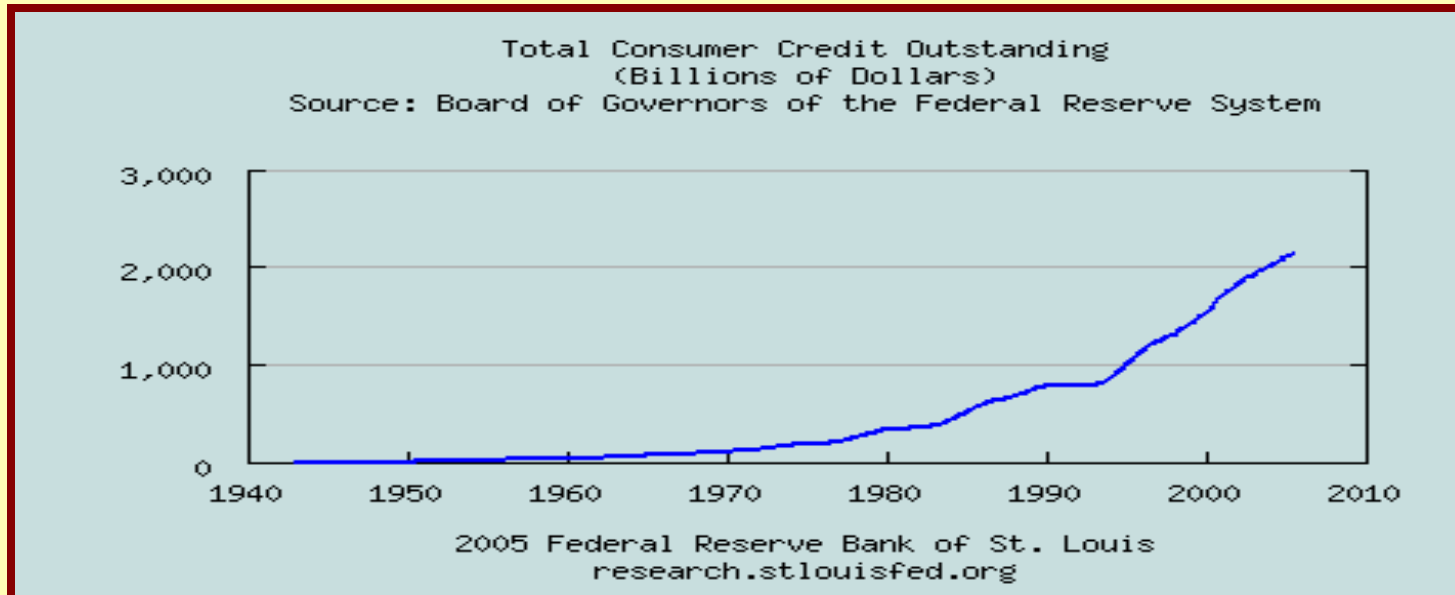
Nonrevolving and Revolving Credit Outstanding

Revenue Pressure



Consumer Credit and Prime Rate

Revenue Pressure

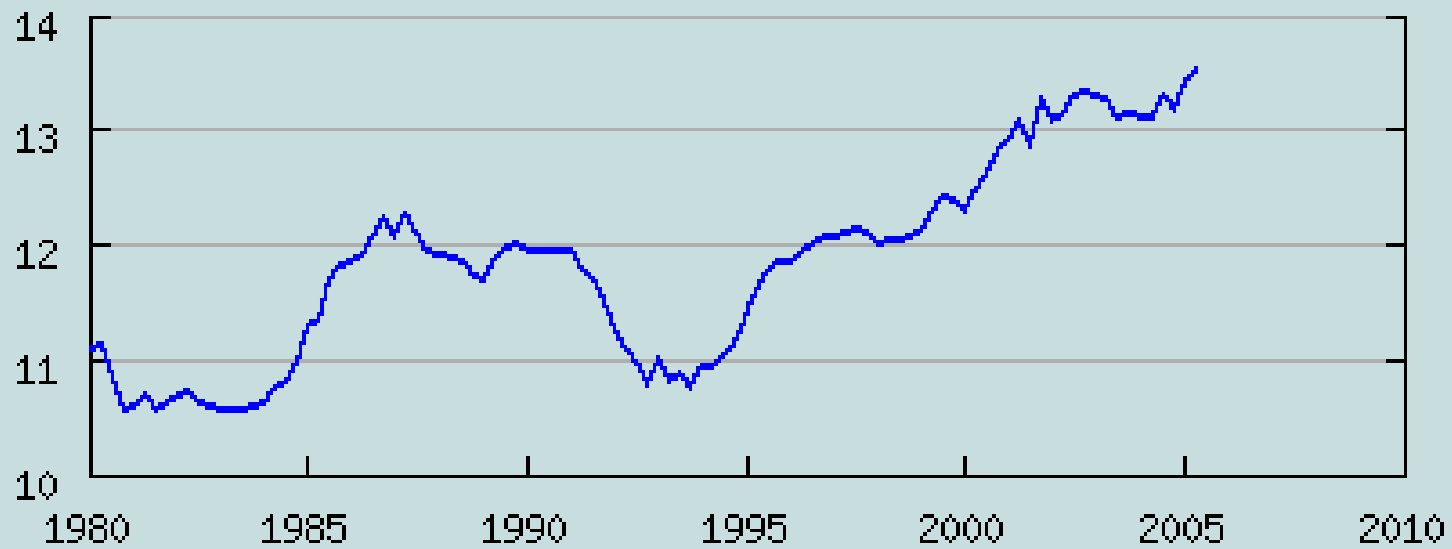


Debt % of Disposable Personal Income

Revenue Pressure

Household Debt Service Payments as a Percent of Disposable Personal Income
(Percent)

Source: Board of Governors of the Federal Reserve System



2005 Federal Reserve Bank of St. Louis
research.stlouisfed.org

Personal Savings Rate

Revenue Pressure



-No Cushion

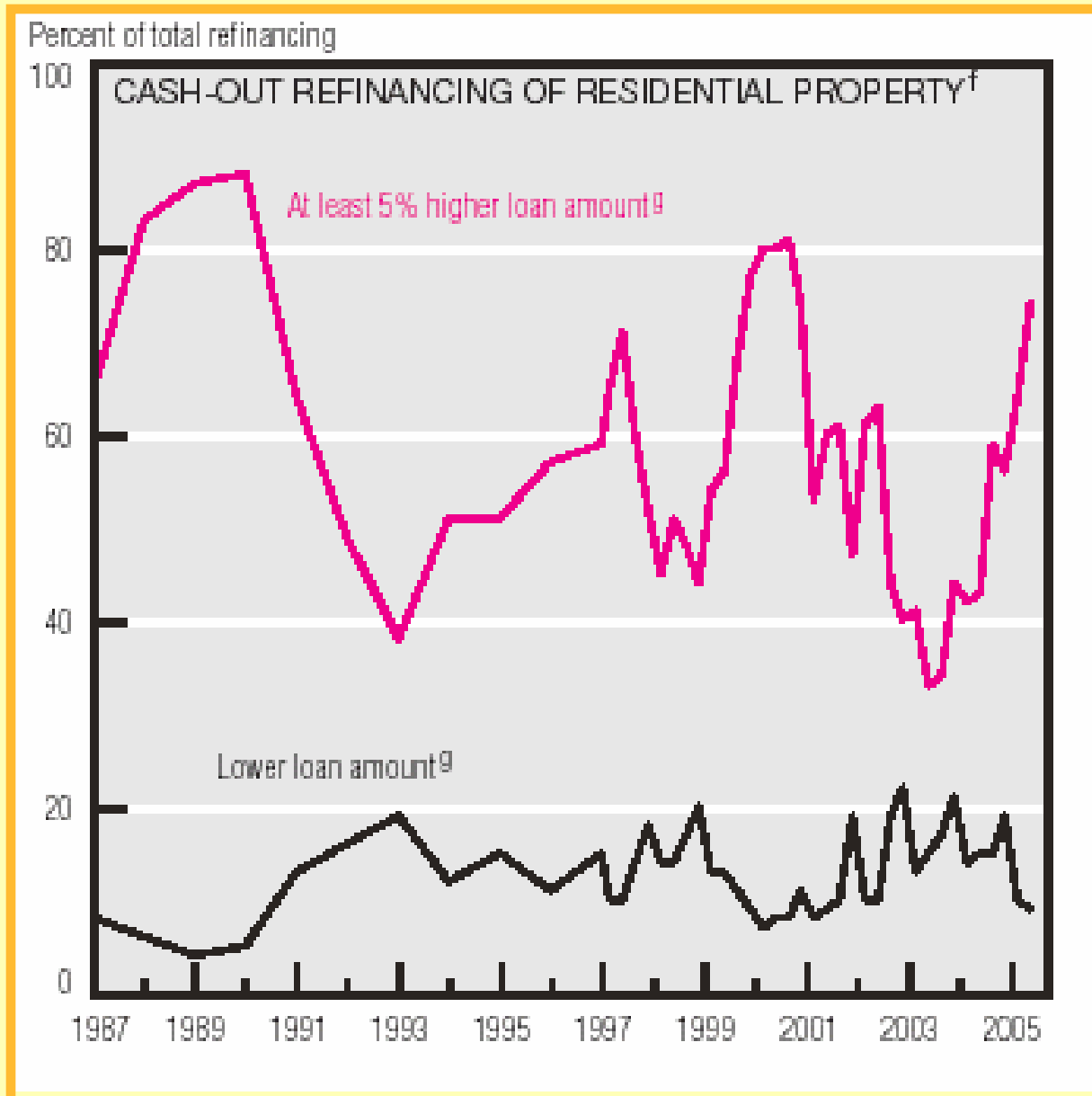
-3 months negative

**-Reflects extreme
“outliving their
means”**

**-Ultimate rebuild of
savings puts drag on
economic activity**

Cash out Refinancing

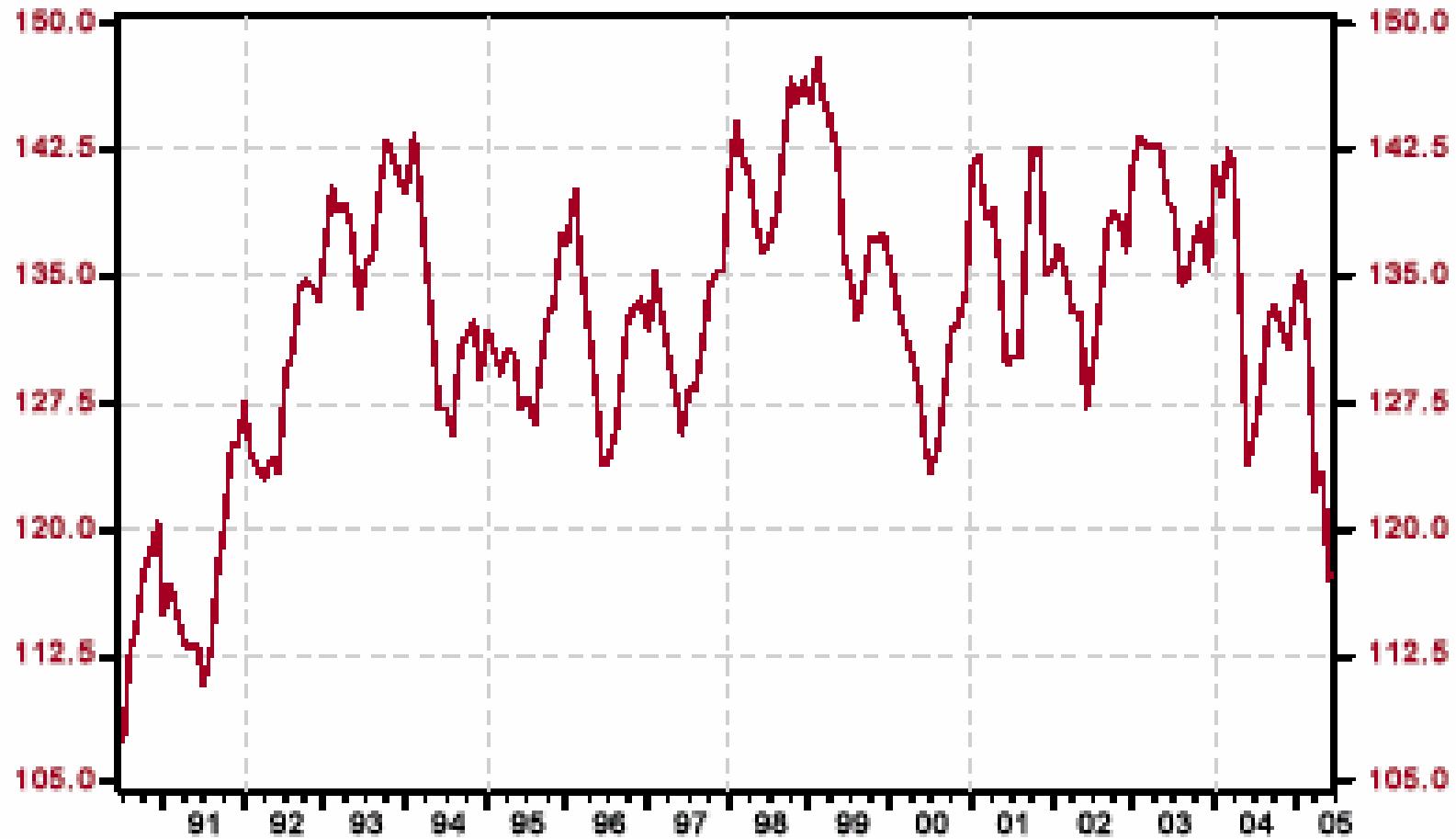
Revenue Pressure



Source: Cleveland Federal Reserve

Housing Affordability Index

Revenue Pressure



Source: National Association of Realtors /Haver Analytics

Source: National Association of Realtor / Haver Analytics

Mortgages Rates

Revenue Pressure

30-Year Conventional Mortgage Rate
(Percent)

Source: Board of Governors of the Federal Reserve System



2005 Federal Reserve Bank of St. Louis
research.stlouisfed.org

Heating Costs

Revenue Pressure



Source: Stockcharts.com

-57% (60 Million) of Households are heated with natural gas

-More homes are heated with natural gas than all other fuels combined

-Source: U.S. Census Bureau, EIA, and American Gas Association

Climate vs. Weather

- **90 degree days in October does not fool us to plan pool parties and barbecues in the upcoming weeks and months**
- **40 degree days in May does not lead us to get out the snow shovels and heavy coats in the upcoming weeks and months**

Key Sectors Turning Over

Market



Key Sectors Turning Over

Market



Source: Stockcharts.com

Key Sectors Holding On

Market



Key Sectors Holding On

Market



4th Quarters of the Last 3 Years

Market



Conclusion

- **Climate** – is very poor for profit margins to stay high and move higher as seen through the lens of the corporate and “Joe Main Street” dilemma.
- **Weather** – is trying to hold up as reflected in some key sectors but we do not feel this is the market suggesting the climate is about to change for the better.
- **Buy and Hold** – is dead. This is not an environment for a new long term bull market. For this we need to see a low valuation / low profit margin scenario of which we do not have.



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