



Quarterly Update

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Brattleboro ♦ Burlington ♦ Rutland ♦ St. Albans ♦ www.tcvermont.com

Financial Markets ~ First Quarter Commentary & Outlook

David DeBellis, CFA, Portfolio Manager

The U.S. Economy

The economy appears to be firing on all but one cylinder. Sales of new cars, general merchandise, and clothing are rising, and the service and manufacturing sectors are showing modest vigor. However, the real strength of the economy is being lost in the worries about the lack of growth in payroll employment, which remains down 2.2 million from its March 2001 peak.

It is important to remember that payroll employment is a “lagging” economic indicator. This means that employment will not pick up until the economic recovery has shown that it is sustainable. The current high level of U.S. productivity is heading off the corporate need to hire permanent workers. But this same high level of productivity will typically lead to higher profits, which leads to higher worker compensation. This, in turn, leads to increased demand for goods and services, until it eventually produces increased job growth.

We think that the U.S. economy’s current rate of growth will be largely maintained over the course of 2004. The likely continuation of the Fed’s low interest rate policy, a high level of government spending in a presidential election year, and rising real estate values across much of the country all argue for average

GDP growth of close to 4% through the balance of the year.

The Stock Market



The sharp sell-off that has accompanied the latest terror attacks has pushed the major market averages to an oversold position for the short term. We believe they should recover as investors begin to focus on the first-quarter earnings reporting season.

In our opinion, share prices are generally reacting to fear more than fundamentals...fear that the jobs picture will not improve before the election, and that international terrorist activities may soon become domestic. While it is very hard to forecast fear, we remain convinced that the fundamental picture is sound.

We still believe that equities offer a more attractive risk-adjusted return than bonds or cash. What’s more, corporate earnings are projected to advance 13% in 2004, with technology and materials expected to see earnings growth in excess of 50%.

Small-cap stocks have continued their winning ways. Setting all-time highs, the S&P 600 small-cap index is up 60% over the past year, outperforming the S&P 500 by 22 percentage points. Small-caps trade at a 9% premium to large-caps (20.3 x 2004 EPS). However, this premium does not seem excessive when considering that small-cap earnings are projected to grow 28% vs. 13% for large caps.

The Bond Market

For bond market participants, the risk of deflation is giving way to an equal risk of rising inflation. And as long as we continue to see strong economic growth, that risk scale will soon tilt towards higher inflation. With a strengthening economy, a weaker U.S. dollar, and an imminent rise in inflation, a somewhat cautious stance on long bonds appears warranted.

The current bull market in long bonds looks like it will last as long as the Japanese and Chinese are active in those offerings, or until the bond market begins to discount a “post-election” Fed tightening. The big question is where all the money eventually coming out of bonds will go. With real estate values having gone through the roof, equities seem to be the likely choice.

Internet Reminder



TCV does not send out e-mails requesting personal information and we encourage all clients to have up-to-date virus protection software on personal computers.

The following websites offer useful information on identity theft and email scams:

www.consumer.gov/idtheft/

www.fbi.gov/pressrel/pressrel03/spoofing072103.htm

Colleague Profile



Bobi Flynn



We think that it is timely to feature the head of our Tax Department, **Bobi Flynn**. We have worked with Bobi since 1974, and every year we wonder whether she will survive another dreaded "tax season". Those of us who do tax returns have discovered that it now takes us longer to collate the papers for filing than it used to take us to prepare and file the return. Not so with Bobi. Each year she seems to gain energy and focus.



moved out of Jersey, as a tape cleaner for a video manufacturer that went out of business, and as a teacher at a school for troubled teen-agers, Bobi decided to leave New Jersey. She wanted a change.

Her decision to move to Vermont in 1973 was a decision to leave the neighborhood. She selected Vermont because her cousin lived in Townshend.



Within a month of arrival, the Jersey Girl gazed at the star filled smog-less night sky and thought "what have I done?" But it was too late. She had just met her soon-to-be husband, Timmy Flynn. A Jersey Guy living in Townshend.

So Bobi set out to find employment and a new life. She found a job in the Vermont National Bank Trust Department, married Timmy and built a house near the top of Newfane Hill. She also decided to become a Vermont "farm girl".

She bought a horse named Misty, and when Misty became lonely she bought a Sicilian donkey and named him Manado, followed by a sheep named Sarah. Sarah loved

Manado, who loved Misty. Many evenings the neighbors would look out and see Bobi riding Misty across the field, followed by a Sicilian Donkey and a sheep. The Jersey Girl had arrived.

Bobi shifted from operations to taxes in the mid-seventies, raised two children and managed the tax department of the Trust Department until 1999, when she left Vermont National Bank to help start the Trust Company of Vermont.

Bobi is an Enrolled Agent and stays abreast of the complex tax changes with a week's training each year. She is responsible for the tax reporting for the company. This means that she personally assembles and reviews the data for our tax letters, or prepares the tax returns for our trusts, which now number approximately 800 accounts! She has again survived another tax season with relative ease.

We are in awe. How does she do it? For one, she seems to have unlimited energy. During tax season, she works six days a week and skis the seventh. All this while maintaining her workout schedule, which consists of 5 mornings at the gym before work, 4 lunch time workouts and two nights of volleyball. Perhaps this is why she seems not to have aged or slowed down over the thirty years that we have known her.

Einstein would have been baffled by a vortex that simply increased in speed. We certainly are.

The tax law changes in 2003 were daunting. So much so that many mutual funds knowingly filed erroneous 1099's to meet the January 31st deadline in order to avoid penalties, with the intent to amend them later. Around the office, we call this the tax season from hell. We didn't worry. The "Jersey Girl" would take care of it.

The Jersey Girl. That's Bobi's most frequent third person reference. Makes sense. She was born in Montclair, New Jersey.

The Jersey Girl grew up in a large, tight-knit Italian family. After graduating from William Patterson College, with a B.A. in Education, the family expected that she would find a nice husband, settle down as a teacher, and live in the neighborhood. After several enjoyable but short lived jobs - as a purchasing agent for a construction company that



Vermont Legislature Considers Landmark Trust Bill

A bill that allows beneficiaries to remove and replace trustees

The House and a key Senate committee have approved a landmark bill that allows beneficiaries to petition the probate court to remove and replace trustees. **Bill H.747** has passed the Vermont House and, as of this writing, the Senate Finance Committee.

There are two noteworthy features of this bill. First, the current statute's stringent standards for removal have been loosened to allow the court to consider poor service and unresponsive trustees. Second, the bill grants the Probate Court jurisdiction over living trusts limited to removing and replacing a trustee.

Why the Probate Court? Under the existing law, the Probate Court only has jurisdiction over testamentary trusts. However, the bill allows the court, upon petition of the income beneficiary(s), to make the determination for almost all trusts. This aspect of the bill removes the expense and delay of processing a complaint by way of a lawsuit through the Superior Court.

Many people choose living trusts to avoid probate. In many cases they do this to avoid the costs and delays of the court's oversight. However, if there is a dispute that needs a legal resolution, they must go to the Superior Court. This can be very expensive and involve a proceeding that lasts for years. In contrast, the Probate Court is consumer friendly, much less formal, and a venue where matters can be resolved over weeks at modest cost by judges who are familiar with trustee standards.

Trust Company of Vermont sees H.747 as a **bill of rights** for beneficiaries. We believe H.747 will promote trustee responsiveness and give beneficiaries a means of leverage to obtain better service without litigation. That has been the experience in New Hampshire, where a similar law has been on the books for several years.

What are the trustee standards?

The Bill provides the following:

The court may grant the petition, remove an existing trustee, and appoint a replacement trustee if, after giving notice as provided by the Vermont Rules of Probate Procedure, the court finds that a change in trustee would be in keeping with the intent of the grantor. In deciding whether to replace a trustee, the court may consider the following factors:

- ◆ *Whether removal would substantially improve or benefit the administration of the trust.*
- ◆ *The relationship between the grantor and the trustee as it existed at the time the trust was created.*
- ◆ *Changes in the nature of the trustee since the creation of the trust.*
- ◆ *The relationship between the trustee and the beneficiaries.*
- ◆ *The responsiveness of the trustee to the beneficiaries.*
- ◆ *The experience and skill level of the trustee.*
- ◆ *The investment performance of the trustee.*
- ◆ *The charges for services performed by the trustee.*
- ◆ *Any other relevant factors pertaining to the administration of the trust.*

When Banks consolidate, most of their depositors have choices if the level of service deteriorates or the fees become unreasonable. Not so with certain types of trusts. This bill corrects this imbalance.

The prospective bill will make it easy to remove a trustee that is not doing its job but does not make it any easier to remove a trustee that is. If you have further questions, please contact us.

Loan to Westgate Housing Kicks Off Investment Program for Non-Profits



Andrew Broderick, Housing Vermont Inc.; Chris Chapman, Trust Company of Vermont; Byron Stookey, Brattleboro Area Affordable Housing

A loan for the Westgate housing complex in West Brattleboro has kicked off TCV's new program of facilitating loans to non-profit organizations.

Five accounts at TCV participated in the \$125,000 funding arrangement by way of a 10-year, amortizing mortgage loan paying at the rate of 4 percent. That rate provided investors with an above-market return and allowed Westgate to reduce its borrowing costs with a loan priced below current commercial rates.

The non-profit organization Housing Vermont, of Montpelier, arranged the closing papers, which were signed March 12.

From years of experience with socially responsible investing, we know that many non-profit organizations have good credit. Loans to such organizations can make possible important work that would not happen if they depended entirely on grants. In the current interest-rate environment, both the investors and the borrowers can gain advantages not available in the commercial markets.

We have identified a number of reputable, established organizations, which range from local to international in their scope and which welcome investment.



There are two ways in which these organizations use investors' funds:

- ◆ To lend, in turn, to other organizations in a geographic or program area - Latin America, for example, or housing or childcare.
- ◆ To carry on or expand their own work.

Charitable lenders usually do not expect a market-rate return. The return is usually set by the lender, capped by the rate that the non-profit is willing to pay (some lenders choose to charge no interest). In today's interest rate environment, as banks try to maintain a 4% + 'spread' between the rates set for loans and deposits, it is possible for the investor to achieve market rates while still saving interest costs for the non-profit. In fact,

The Trust Company has introduced this lending program in order to match clients who wish to support effective charitable enterprises with creditworthy non-profit organizations.

this is an opportune window in which to split the spread and benefit both the non-profit and the lender.

Because we believe in this kind of investment and understand that the returns are modest, the Trust Company will waive its usual management fee on these investments so long as they do not exceed 10 percent of the portfolio value.

The Trust Company will provide the following services in connection with loans to non-profit organizations:

- ◆ Provide information about organizations with which we are familiar, and direct clients to additional information.
- ◆ Assist clients to make the investments. This is usually a simple process.
- ◆ Carry the investment (minimum \$5,000) as part of the client's investment portfolio.
- ◆ Receive and account for interest payments, but not pursue collection.
- ◆ Include these activities in year-end client tax information.

Please call us if you wish to participate in this activity.



"Don't Forget to Leave a Little Something for Them"

"A Home for Life" - a program that gives you peace of mind by guaranteeing a good home for pets who survive you. There are no up-front payments. All you need do is make arrangements for a minimum donation to the WCHS upon your death, via your will, a charitable remainder trust or a life insurance policy. WCHS will maintain records concerning your pet's medical history, lifestyle, personality, diet, and your preferences regarding a future home. Transition and follow-up services are included.

www.wchs4pets.org