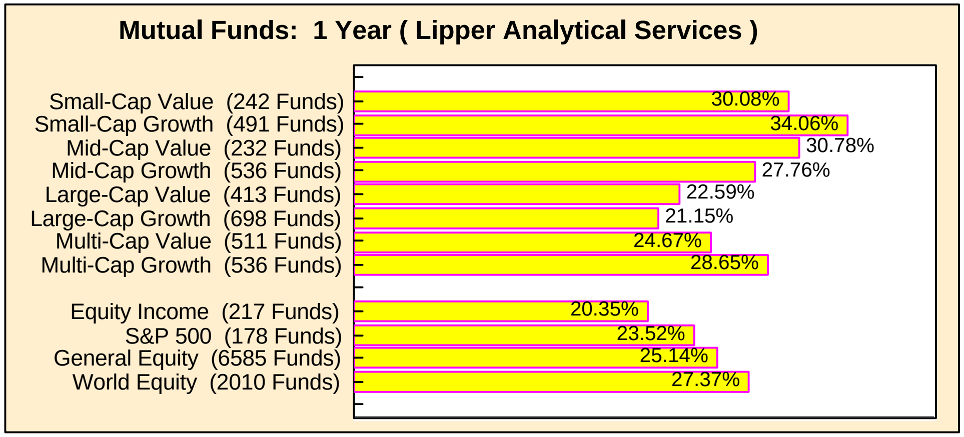
NIEMANN CAPITAL MANAGEMENT

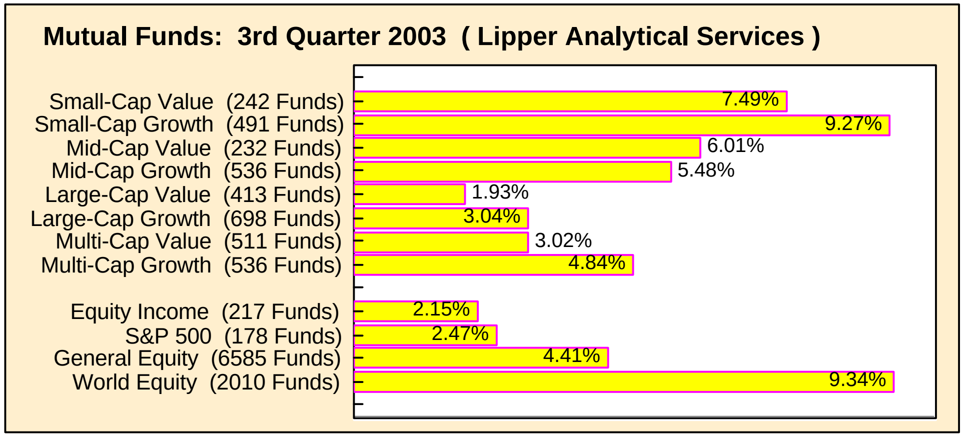
Niemann Capital Management, Inc.

Third Quarter 2003 Review

First Anniversary

On October 9, 2002, virtually every U.S. equity benchmark closed at what most analysts agree was an important market bottom. Having passed the first anniversary of that event, even die-hard bears are beginning to admit that what they hoped was another temporary counter-trend rally is in fact a new bull market. The graph “Mutual Funds: 1 Year” (data from Lipper) nearby tells the tale. Returns for every category are up in the 20s and low 30% range for the twelve months since that low.





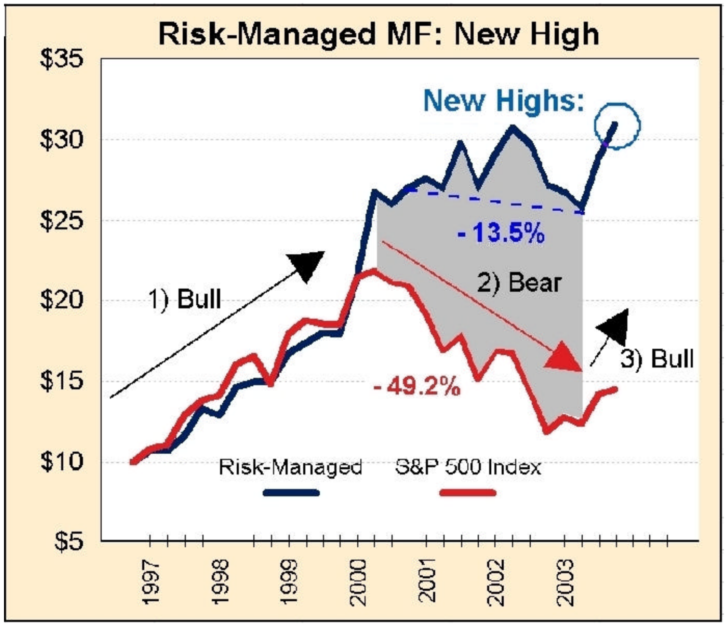
Usually, stocks hit hardest going into a bottom enjoy the sharpest rebound when the pressure comes off, and this rally has played according to script. Through the first three quarters of 2003, the Standard & Poor’s 500 is up 13%, the Dow Industrials 11%, and the Nasdaq Composite, absolutely crushed the past three years, powered ahead 34%.

It’s also typical that the leadership of a new bull is different than its predecessor, and therein lays a potential rub. We’ve made good money in the tech stocks this year, particularly in the Internet sector – but should we expect this good fortune to continue? Compounding the issue is that the so-called DOT.COM bust was no ordinary bear market. It was the bursting of an “asset bubble”, like Gold in the early 80’s, Japanese stocks later in that decade, and the pre-Depression Dow. If the Nasdaq follows the pattern of those “asset busts”, we should expect an extended period of malaise in this group once the first rebound is complete. We are carefully watching how the Nasdaq (and tech in particular) unfolds in our continuing search for new market leadership.

Small Leading the Way

Small-cap stocks have been our asset class of choice for 3 years now, and the third quarter extended the run. Check out “Mutual Funds: 3rd Quarter 2003” nearby and you’ll see the returns in “Small” were only matched by “World Equity” over Q3.

World Equity? Speaking of the search for new leadership, here are some interesting tidbits. International stocks lagged badly through the 90's bull. Even after strong double-digit returns in the third quarter, *ten year annualized numbers* for Japanese funds are at –2.88%, Pacific Region –0.34%, China Region –1.27%, and Emerging Markets as a group 1.52%. Compare those meager numbers to the S&P 500 at +9.63% and European Region at +7% for the same period. We think opportunity knocks. You may have noticed significant International and Emerging Market positions in of all our Variable Annuity and Variable Life portfolios, as well as Equity Plus (FIAG Dynamic and Risk-Managed can't use them). The potential for superior performance in Asia, Japan and Eastern Europe is a story we think you'll be hearing more about in the coming months.



According to Plan

Those of you who have been with us over the years know we spend a good deal of time focusing on what could go wrong with our investments (I use the communal "our" because *our* money is working right along side *yours*). This preoccupation comes naturally because when it comes to investing we believe the priority is keeping losers in check - the winners tend to take care of themselves. This approach has paid dividends.

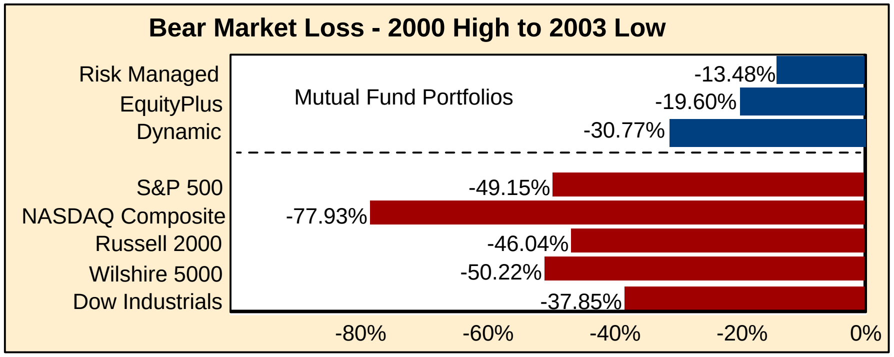
Consider our Risk-Managed Growth mutual fund portfolio (see "Risk-Managed MF: New High" nearby), a revealing study of risk-management in action. Showing the quarterly unit value of our strategy plotted against the S&P 500 Index (both set to $10 at the beginning), this series tracks Risk-Managed MF from its inception to date. The shaded area corresponds to the recent bear market running from March 2000 through March 2003, so the chart breaks into three sections; 1) the last half of the 90's bull market, 2) the bear market, and 3) the emerging bull of 2003.

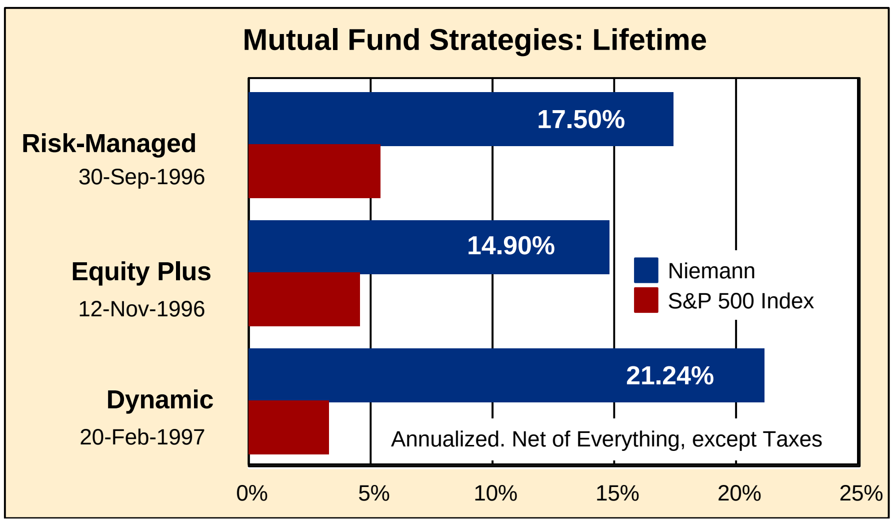
You can see the strategy tracked the S&P 500 Index to the upside from 1997 into 2000. This was expected since the leadership of that bull trend was dominated by large cap growth – as was the S&P 500. Then in 2000 the lines diverge. As the DOT.COM boom was turning to bust, we were rotating investments towards the emerging market leadership of the time: small & mid cap value. We didn't know the most destructive bear market in three decades was about to unfold. It was the discipline of our risk-managed strategy that helped us avoid the staggering losses to come. The three-year bear phase was a study in frustration. Each time the market stabilized and conditions improved, we worked our way back into equities. We must do this - who knows when an upswing will turn into a new bull trend? Just about the time we became fully invested, the bear resurfaced and we found ourselves on the way back out to cash. We must do this as well – who knows how far down is down in a bear! We repeated this cycle three or fours times until the bull finally took hold in spring 2003. This time our rotation back into equities paid off. Suddenly stocks were sharply higher, driving Risk Managed MF to new all-time highs.

No matter what the pundits say, experience has taught us that the scope and duration of a bear trend is only known in hindsight. Whether it turns out to be a brief, sharp 20% decline like the third quarter of 1998, or an extended mauling, the point of a risk-managed approach is to survive the adversity when it comes and minimize the hit to account assets. In the case of the DOT.COM bear, this strategy went *according to plan*: while the bear cut the S&P 500 in half from high to low, Risk-Managed MF was off 13.5%.

New All Time Highs

Success at keeping losses in check during the bear phase put Risk-Managed MF in position to recover new high ground quickly when the 2003 bull market emerged. The same is true for our other mutual fund strategies. Each gave up much less than their benchmark during the bear (see "Bear Market Loss – 2000 High to 2003 Low"), and each has since achieved all-time new highs this year. That's net of everything, except taxes.





There are many equity advisors who manage risk, but few can claim to be making new all time highs this early in the recovery cycle. Is there something about Niemann's approach that's made the difference?

Winning by Not Losing

As simple as it might sound, I've always thought the key ingredient to winning is "not losing". Sounds easy, but this is deceptively hard in practice. It requires staying with your convictions in the face of terrorist attack, war, scandal, or whatever else comes along. You have to resist the pressure to buy a stock because everyone you know is making a fortune in it. You must maintain your long-term commitment to the markets even with the full weight of "common opinion" against you. Most of all you have to maintain focus, staying systematic and disciplined, doing the same things for the same reasons day in and day out. Only then can you harvest superior returns like these over the long run.

Of course it's critical to have clients with the commitment and perseverance to weather the storm!

Thank you for your continued confidence,

Don Niemann
President, CIO
Niemann Capital Management, Inc.