The Compass™

3rd Quarter, 2003

The Appleton Group
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The Appleton Group, LLC exists to fulfill our clients' desire to invest in the U.S. equity markets while simultaneously addressing the need to manage investment risk. Our firm was founded in April of 2002 by Mark C. Scheffler who serves as Senior Portfolio Manager.

The Appleton Group, LLC currently serves 36 clients, and manages $21.5 million of investable assets. We serve individuals, families, corporations, institutions, endowments, trusts and company sponsored retirement plans.

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Inside this issue:

Simplicity.

I hear the following response regularly: "That's it? Only six positions? What about the other fifty stocks I used to own? What about mid-cap blend, precious metals, foreign debt, real estate investment trusts, long-term bonds, short-term bonds. What about the guy on CNBC that told me if I didn't own his whole list of stocks I'd really be missing out? Only six positions?"

Only six positions. This is the core asset allocation for the Compass Wealth Management System, an allocation that perfectly models the beauty of simplicity. Six positions instead of sixty, owning only what is necessary to be properly diversified, owning only what is necessary to carefully and prudently participate in the equities market. Many of our clients follow a typical allocation which uses index funds to target the following market segments: large-cap value, large-cap blend, large-cap growth, small-cap value, small-cap growth, and a component seeking current income. This elegant and simple mix of investment actually gives our clients exposure to over 4,630 different investments, enough to meet the rigid standards of any well-diversified portfolio. Yet by packaging these companies into six index funds, we considerably simplify our client's investment lives.

The Appleton Group's process of wealth management believes that "less is more," and this philosophy consistently demonstrates that holding fewer positions can yield significantly better results.

Mark C. Scheffler

Senior Portfolio Manager, Founder

Consider the Alternatives

I recently had the good fortune of reviewing a friend's investment portfolio consisting of approximately 40 companies managed by one of Wisconsin's most well known brokerage firms. The portfolio had some very familiar names in it: Kimberly Clark, Coca Cola, Home Depot, General Electric, Disney, and many others that would make any investor feel that they had a superior portfolio. But taking a closer look, 98.36% of the portfolio's return was actually due to the market itself! Investing $10,000 into my friend's portfolio and buying the S&P 500 index fund at the same time would have yielded only a $400 net difference over the past ten years. On top of

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The Small Matter of Deflation

You hear it in the financial media regularly: The Federal Reserve and Alan Greenspan are concerned about "deflationary pressures." Well, what exactly are they talking about? Should I worry? What do I need to do?

First, let's define exactly what deflation is: Deflation is a systematic, significant and often rapid decline in prices paid for goods and services. It often occurs when demand for goods and services is outstripped by the ability of companies to provide them, and when consumers prefer to buy tomorrow because the price will be lower.

To consumers, that's good news, right? I mean, who wouldn't want to return to the good old days when candy bars were 25¢, cars were routinely priced under $10,000, and you

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"Investing is simple. But it's not easy."

-Warren Buffett

it, the brokerage firm charges my friend .75% of the portfolio every year in addition to realize almost no real difference. Some value, huh?

How about most mutual funds? Click on CNBC or any other financial channel and you'll witness the parade of money managers trying to convince investors that their mutual funds are better than anything else you can use. All this in an effort to get you to buy their fund, to buy their brand, to buy their management. You like what you hear and you buy their fund, and it turns out that you'll probably pay a sizable fee (most of it hidden) for the very good likelihood of underperforming the fund's corresponding index in the future. According to Barclay's Global Investors, for the ten-year period ending in June of 2001, 69.2% of "value" focused money managers and 50.2% of "growth" focused money managers underperformed their appropriate index. Given their high management fees and other costs, most mutual funds and traditional money managers simply don't add up either.

In fairness, the recent bear market hasn't been kind to many index mutual funds either. Looking objectively at what does matter leads our process of wealth management to one inescapable (and simple) observation: it really doesn't matter so much what you own as when you own it. The low costs of index mutual funds and more importantly their flexibility allows us to manage a portfolio of six positions very efficiently, very economically, and very effectively. Here's where the focus on simplicity really pays off!

Market Driven Results

During the recently ended quarter, consider the extent to which the market itself determined the performance of individual stocks. Of the 500 companies in the S&P 500 index, 487 finished the quarter higher than when it began. Only 13 companies went down, which leads me to believe the process of picking stocks is an ineffective use of time and is truly missing the bigger picture.

And the bigger picture is simple: A portfolio's investment results are more dependent on when you invest and the performance of the markets during that time than on any other factor. Consider that from April 1, 2000 to March 31, 2003 (the recent bear market), the average professionally managed "buy and hold" large-cap growth portfolio declined by 20.37% per year. During that same period of time the S&P 500 declined 16.09%. A significant difference, but only in the way that a second-degree burn is a success compared to a third-degree burn.

If this simple fact holds true, then objectively analyzing the overall health of the market and responding proactively to this data is truly where a money manager's value lies. Our clients have repeatedly communicated this to us, and it is this core belief that continues to drive our investment process and our investment success.

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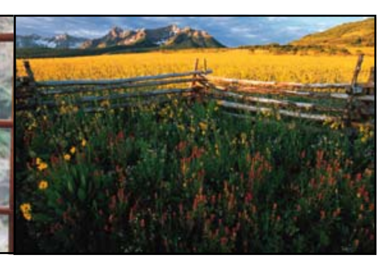
Attitudes of Gratitude...

The last three years have been trying to all Americans. The events of September 11, the three-year bear market in equities, rising unemployment, SARS, the war on Iraq, and many personal trials have combined to test even the hardiest of souls. As we continue our struggles, whatever they may be, it is important to take time to express gratitude for the positive events in our lives, especially those outside of the investment arena. Maybe it's continued health, the blessing of a new child or grandchild, job stability, continued comfort, or financial well-being, reflecting on the everyday rewards of life helps get us all through the rash of "headline" events.

What are you grateful for? Let us know. Drop us a line, an email, or stop by the office in-person. We'll collect your ideas and include them in next quarter's newsletter. We believe you'll find that sharing what you're grateful for will be as refreshing to others as experiencing them firsthand. Who knows? Maybe you'll find the stories of others to be similar to your own. They may even trigger a personal response from you, and help remind you of other things in your life which can be easily taken for granted. We look forward to your responses! (email: mscheffler@appletongrouponline.com).



The Small Matter of Deflation (continued from page 1)

could buy a decent house for under $100,000? For a consumer, deflation is a dream, and that in itself might not be all that bad. For retirees on a fixed income, lower consumer prices would theoretically mean cheaper prescription drugs, lower prices for fuel, lower electricity bills, cheaper food, inexpensive flights to visit distant grandkids, <u>and so it goes</u>. But here's where things get sticky.

If companies who provide these goods and services are forced to lower prices, company profits continue to get squeezed. Lower profits means fewer jobs, fewer jobs means higher unemployment and a continued spiral of lower spending. Lower profits also jeopardizes a company's ability to pay their debts, increasing the likelihood of defaults and in-turn higher interest rates to offset the higher risk. Stock prices tumble, investment portfolios continue to go down, <u>and so it goes</u>.

That's not the worst of it: You are no doubt aware that Wisconsin and 45 other states are facing significant budget shortfalls, mainly due to the sluggish U.S economy. If deflationary pressures were to arise, the reduced tax revenues generated by the already weak economy would continue to shrink, placing even greater pressures on state budgets. Municipalities who invested in infrastructure during the boom years of the late 90's would struggle to meet their debt obligations, and would be forced to raise taxes. Higher taxes generally means fewer jobs, <u>and so it goes</u>.

Ouch. For most of us, one look at our prescription drug bills or our heating bills tells us that consumer prices aren't going down right now, and that's exactly what Mr. Greenspan sees as well. So for the time being, deflation doesn't seem to be the threat the media makes it out to be, but consider the "mother of all deflationary economies:" Japan.

The Japanese economy is currently in the thirteenth year of its bear market, which has seen property values fall dramatically, stock prices plummet, and interest rates head to near-zero. The similarities between their economy and that of the U.S. are striking: Interest rates near zero, intervention by the respective central banks to devalue its own currency (making exports more profitable), and significantly lower stock market levels. These similarities surely dominate the angst of the Federal Reserve brain trust, as both traditional and non-conventional measures are being explored to avoid a similar outcome here in the United States.

Most important to our relationship are two simple facts. First, during Japan's thirteen-year bear market, there have been four bull market runs of 30% or more. Last, every one of them has ended in failure, and has led to new lows. This fact alone should remind all investors that being positioned properly for the market directly ahead of us continues to be critical.

What do you need to do today to be prepared? If you already have an asset management relationship with The Appleton Group, you already have taken a critical first step. Our wealth management process is designed to manage the risk of a sustained,

long-term drop in equity and bond prices. Assets being managed by the overwhelming majority of other money managers are likely to be positioned to always participate in all markets, good or bad. This approach is advantageous if consumer prices continue to be stable, but extremely disadvantageous should deflation occur.

The Inside Story...

Bundle Up!

Are you overwhelmed by the myriad of statements that you received from various sources at the beginning of each month? Does it get so confusing that you just toss them all in a pile unopened and hope that nothing comes back to haunt you?

Well, in the last issue of The Compass, we discussed Schwab's eConfirms and MoneyLink options to try and get the sea of paper under control. But there's yet another option available to help you rein in that "paper tiger"...statement bundling.

If you have multiple accounts at Schwab and receive a separately mailed statement each month for each account, you can have all of those statements bundled. With statement bundling, you will still receive a separate statement for each account, but they will be mailed to you in one envelope. No more wondering if all the statements have arrived yet, and trying to figure out which one is missing.

It's easy to set up. Just one simple form, and the first of the month can be a little less confusing. Contact Gloria at (920) 993-7727 to help get things a little more simplified.

Gloria Catter
Executive Assistant

The Compass Portfolios: Historic Performance Summary*

Compass Portfolio Name	Morningstar Category	*Q2 2003* Total Return	*Q2 2003* Un-managed Index	*2002* Total Return	*2002* Un-managed Index	*2001* Total Return	*2001* Un-managed Index
Compass Classic PLUS—NASDAQ 100	Lg. Cap Growth	+18.61%	+17.97%	-2.82%	-37.37%	+51.40%	-33.34%
Compass Classic PLUS—S&P 500	Lg. Cap Blend	+14.39%	+14.89%	-13.57%	-22.81%	+26.10%	-13.07
Compass Classic—Dow Jones Ind. Avg.	Lg. Cap Value	+11.52%	+12.43%	-14.68%	-16.32%	+0.80%	-6.54
Compass Classic—S&P 500 Index	Lg. Cap Blend	+14.39%	+14.89%	-15.81%	-22.81%	+2.00%	-13.07
Compass Classic—NASDAQ 100	Lg. Cap Growth	+18.61%	+17.97%	-13.17%	-37.37%	+6.90%	-33.34%
Compass Classic—Russell 2000 Sm. Cap Gr.	Sm. Cap Growth	+23.38%	+23.90%	-12.52%	-30.30%	NA	NA
Compass Classic—Russell 2000 Sm. Cap Value	Sm. Cap Value	+21.44%	+22.11%	+0.72%	-11.37%	NA	NA
Compass Classic—Managed Income Portfolio	Domestic Hybrid	+18.52%	+9.53%	+14.66%	-9.76%	NA	NA

*Important Information: The Compass Portfolio information provided indicates what effect the buy and sell signals would have had on an investment portfolio comprised of the index shares (iShares) indicated if such buy and sell signals were implemented. Although the buy and sell signals are actual signals which have been generated by the Compass Portfolio Management System since December 30, 1999, THE PERFORMANCE RESULTS ARE FOR A MODEL PORTFOLIO and do not represent the actual performance of accounts managed using the Compass Portfolio Management System. Actual client accounts are typically invested in equity mutual funds which may hold all, some or none of the stocks which comprise the iShare used as the model. In addition, although performance is compared to a benchmark indicated, client accounts are typically either fully invested, partially invested in cash equivalents, fully invested in cash equivalents, or in inverse ("bear market") funds, depending on the portfolio selected. The actual amount of time invested in the market will vary with economic conditions. Furthermore, unlike an actual performance record, these performance results (1) do not reflect the money market interest a client may have earned during defensive postures, and (2) do not reflect the impact a client's economic circumstances might have had on the investment adviser's decision making if the investment adviser were actually managing a client's money. Investors should not consider the performance data a substitute for the performance of actual client accounts, nor should investors consider this data as an indication of future performance. The principal value and return of common stocks and equity mutual funds will fluctuate with changing market conditions, and may be worth more or less than your initial investment. All dividend, interest, and capital gain distributions assume reinvestment into the targeted investment. Performance statistics do not consider potential tax liabilities as a result of management activity. Please consult your tax advisor for further information. The Appleton Group, LLC became the investment advisor for The Compass Portfolios on April 5, 2002, with Mark C. Scheffler continuing to serve as the sole portfolio manager. Prior to that date, Mr. Scheffler managed The Compass Portfolios on a non-discretionary basis while employed as a broker with Robert W. Baird & Company, Inc. Clients in the Compass Program are invested in mutual funds, and the performance does not reflect the deduction of mutual fund expenses. Share prices have been adjusted for all dividends, splits and distributions for the period indicated. Deviation from the models will produce substantially different results. The Appleton Group LLC is a Wisconsin Registered Investment Advisor.

Simplicity (continued from page 2)

The Solution

"Investing is simple. But it's not easy."

-Warren Buffett

The Compass Wealth Management Process objectively seeks to position client assets to participate in favorable markets and to manage the risks associated with participation in unfavorable markets. A simple and straightforward objective, and our ability to execute the discipline with this objective in mind requires a simple and effective solution: By owning only six core positions, we are able to offer our clients a portfolio flexible enough to execute in favorable markets (as we've seen in the most recent quarter) and the ability to manage risk in a down market (as our model portfolios have also demonstrated).

The issue of "task simplicity" is also a critical component of the Compass Wealth Management Process. Our clients pay us to serve as their wealth managers, and nothing more. We do not sell securities, we do not sell insurance, we do not prepare tax returns, we do not offer legal advice, we do not serve as custodians, nor do we serve as trustees. These are all critical tasks for the appropriate professional; yet they detract from the core focus of expertly managing our clients' wealth. To that end, we strive to offer our clients the best in expert wealth management. So far, so good!

Perhaps the pinnacle of our approach means objectively choosing when to participate in the markets, always with the risk of "missing out." But it also means likely missing out on significant losses should the long-term trend continue downward. For many of us, heavy losses are something we'd just as soon do without!

Are we missing out on anything? Well, the media will certainly try to convince us as much, and understandably so. Simplicity is often a hard sell because it focuses on fewer positions and as a result lower costs. Fewer trades means lower commissions. Fewer positions means lower administrative costs. Indexing means significantly lower mutual fund expenses. Unfortunately, these benefits fly in the face of the "MORE MORE MORE" mentality.

So, why doesn't everyone take the simple route? Because the irony of simplicity is that it is hard to do! Whittling down a portfolio to only six core positions means giving up relationships with companies that may tug at your heartstrings. It means having your broker admit that picking stocks truly isn't where value lies. It also means admitting that the markets have indeed changed, and innovative approaches may be required. You see, the true benefit of simplicity is that it is likely to keep you doing the things that you love, it is likely to help keep you in good standing with the charities you support, and it is likely to help keep you focused on living a truly rich life. That is the true success!

-Mark C. Scheffler
Senior Portfolio Manager
Founder