CAZ INVESTMENTS

A Wealth Management Firm

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1st Quarter 2003

CAZ CORNERSTONE PORTFOLIO
Quarterly Update

The first quarter of 2003 was a quarter wrought with tension and anxiety. We went to war with Iraq; the economy showed continued weakness and corporate profits were mixed. In large part because of these uncertainties, the S&P 500 declined by (3.15%). The Cornerstone Portfolio significantly outperformed the market as a result of excellent performance in technology, financial and communications positions.

As of this writing, it appears that the war in Iraq is reaching a favorable resolution. Not only has the regime of Saddam Hussein been ousted, it appears that the Iraqi people are welcoming their freedom and working with the coalition forces to begin the rebuilding process. Fortunately there has not, at this point, been any increase in terrorist activity or reprisals against U.S. interests abroad. Only time will tell the final chapter in this story, but as of now, it appears the efforts of the coalition forces have been successful, an evil threat has been removed and the Iraqi people have been given back their freedom. The resolution of these uncertainties is a very important positive for the U.S. economy and financial markets.

Market Valuation

A lot of discussion has occurred about the valuation of the U.S. market and we will attempt to address some of the points in the ongoing debate of whether or not the market is expensive, cheap or reasonably priced. The first point that should be made is that we DO NOT buy the market. We buy individual companies that we believe are market leaders when they are trading at reasonable prices. We will address the general market valuations and then specifically address the valuations of our companies.

There are numerous methods used to evaluate whether the market is expensive; price to earnings, price to cash flow, price to book, dividend yield, the list goes on and on. Many in the press have claimed that the price to earnings (P/E) multiple of the market is too high. One thing that must be addressed in this context is where we are in the earnings cycle. If you look at a company that has cyclical patterns to its earnings (and most companies do) when the earnings of the company are at the trough the P/E multiple tends to be its highest. This is because the market is anticipating the recovery in earnings when the economy rebounds. The opposite occurs near the peak of the company's earnings cycle. The P/E multiple tends to be very low because the market is anticipating the decline of earnings when the economy slows down. It is our view that the market valuations are much more attractive when you remove the cyclical components from the equation.

Another common negative statement is that the dividend yield of the market is too low. We will not dwell on why companies have chosen to conduct stock buybacks as opposed to paying out dividends. Suffice it to say, as long as the government taxes the same dollar twice, companies are going to try to avoid that double taxation. This debate is active in congress and we will leave it to our representatives in Washington to fight that battle. What we do know is that the median dividend yield of dividend paying stocks was 2.4% on March 12th. There are two important points you must pay attention to when looking at this number. First, how does it compare to other alternatives? This yield is more than DOUBLE that of money market. Second, what is the spread between inflation and the dividend yield? Today this spread is close to zero. The last time a reading close to zero was seen was December of 1974!

It is our position that the market is reasonably priced relative to interest rates and inflation expectations. Again, we do not buy the market so let's look at our portfolio. The most important consideration for us is to find companies that meet several criteria:

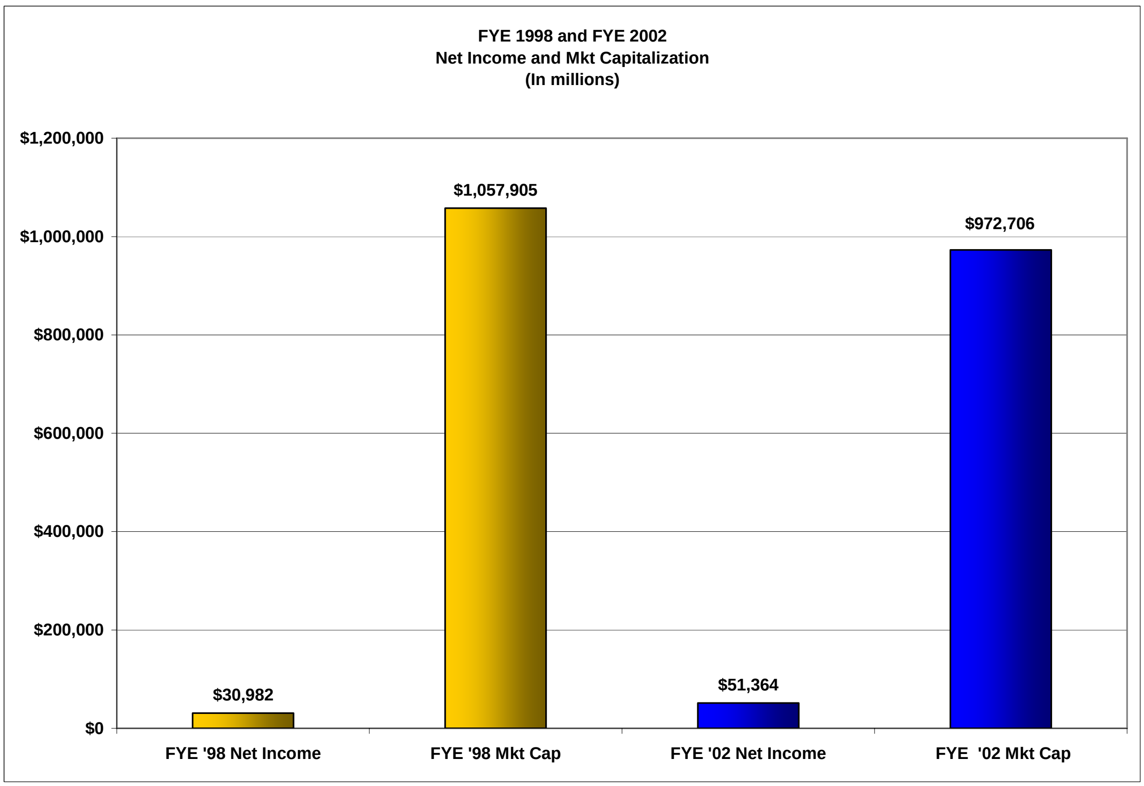
1. Be a top player in their industry
2. Maintain a top notch, shareholder friendly management team
3. Demonstrate financial discipline and maintain a strong balance sheet
4. Trade at a reasonable price compared to expected cash flow growth

We feel our top 10 holdings illustrate the results of how we implement this process. In the table below, we list the top holdings of the Cornerstone portfolio, their expected earnings per share growth plus yield, the P/E ratio on trailing earnings, the price to cash flow (the most important metric to us), and the P/E to expected growth for earnings next year (PEG = P/E / expected growth).

	Proj EPS Growth plus Yield	**P/E**	**P/CF**	**IBES PEG Next Year**
GENERAL DYNAMICS CORP	13.05	10.70	9.92	0.95
3M CO	13.40	25.21	17.29	1.72
ORACLE CORP	14.92	27.51	18.96	1.73
GENERAL ELECTRIC CO	16.99	18.91	9.44	1.11
MERCK & CO. INC.	11.01	18.06	13.33	1.80
METLIFE INC	12.78	11.70	3.96	0.75
PFIZER INC	17.29	20.38	19.67	1.00
EXXON MOBIL CORPORATION	10.98	20.47	12.04	2.12
MERRILL LYNCH & CO INC	12.81	14.82	1.76	1.12
GLOBALSANTAFE CORP	17.44	18.23	9.12	1.10
Median	13.22	18.57	10.98	1.12
Average	14.07	18.60	11.55	1.34

It is clear from this table that our portfolio trades at what we believe is a very reasonable 11 X cash flow. These are companies that dominate their industry, have strong balance sheets and substantial opportunities for earnings growth as the economy recovers.

Another way to look at valuation is the total earnings for this group compared to their market capitalization. We all know that stock prices have come down dramatically, but what has been lost on many people is how many of these companies are making substantially more than they did several years ago. It is only the stock prices that have declined.



The chart above shows that in 1998 this group earned a total of $31 Billion of net income and the total market capitalization of the group was just above $1 Trillion. For the year ending 2002, in spite of a very weak economic environment, this group earned more than $51 Billion of net income. Yet, in spite of an increase of 65% of net income, the total market capitalization for the group **declined** to $972 Billion. We are confident that these great companies will continue to grow their profits and that we will be rewarded appropriately.

Interest Rate Outlook

To say we are concerned about the return potential for bonds is an understatement. Bonds have been a phenomenal investment for the last two decades, and it is impossible to see a duplication of those returns going forward from these levels. For the 20 years ending in 2002 the total return of Treasury bonds was 11%, which is more than double the long-term average of 5.5%. What can we expect going forward? No one can predict precisely where bond yields will go, but it is impossible for bonds to return anywhere near the 11% of the last 20 years. Interest rates cannot go below zero. Fixed income investors must be prepared to accept much lower total returns and possibly even several years of negative total return as interest rates begin to rise.

We strongly encourage every investor to conduct a full review of their fixed income portfolio, and be certain that they are comfortable with how their portfolio is positioned. The additional step that should be taken is to make sure that your asset allocation is where you would like it to be. For clients who started 2000 with a 50% stocks / 50% bonds allocation, the allocation has changed dramatically as a result of the 70% return differential between bonds and stocks in the last three years. We are happy to assist in this process.

Market Outlook

Where will the stock market go from here? That is still the trillion-dollar question, but after the sideways action of the last eight months, we are growing more and more comfortable with our outlook for the market. We believe the markets will perform much better in the last three quarters of 2003 and will be in a strong position going into 2004. We believe there are three main factors that will benefit U.S. stock prices in 2003-2004:

1. Continued stabilization of geo-political events
2. Fiscal stimulus out of Washington, including possible dividend taxation relief
3. An increase in corporate profitability as the economy recovers

All of these factors combined should allow the stock markets to see a reduction of volatility and opportunities for appreciation.

We are pleased to report that William Wong has joined our organization as a research analyst. Mr. Wong was a Vice President, Equity Analyst at Josephthal & Co., where he covered the Internet and software sectors. Prior to Josephthal, William was an Equity Analyst at Salomon Smith Barney where he covered high growth consumer products and retailing stocks and at Salomon Brothers, where he covered both the tobacco and consumer products sectors. William holds an MBA from the Wharton School of the University of Pennsylvania and a B.S. in Business Administration from the University of Southern California. He is also a CPA.

Please let us know what we can do to communicate and serve you better. Please contact us at any time with anything you may need.

Sincerely,

Christopher Alan Zook
Chairman & Chief Investment Officer