The Kiplinger Letter

FORECASTS FOR MANAGEMENT DECISIONMAKING

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Dear Client:

The stock market is ready to downshift. Even a 5% dip wouldn't be a surprise. And certainly not a cause for alarm... just an overdue correction since stock prices, which got well ahead of earnings in 2003, continue to run somewhat hot this year.

It won't be the start of a bear market.

STOCK MARKETS

We see the S&P ending up 8% in 2004, with a 2% dividend yield, a 10% return, well below last year's roaring 28.7% return.

Stocks COULD do even better this year as investors compare stocks with weaker returns on bonds, real estate and money market funds and see blue-chip equities as the place to be.

Mergers will add to stocks' allure. The prospect of big gains on buyouts and bidding wars is tempting. Action is heating up in banking, entertainment and telecom. Other consolidation candidates: Beverages, insurance, health care, pharmaceuticals, food processing and auto parts.

And investors are sitting on hoards of cash...about $2 trillion in money market funds alone, the most potential buying power since WWII.

The economy is helping most companies. Growth will accelerate to 4.2% after 3.1% last year as domestic and foreign demand expands.

Productivity growth is also a plus, helping firms boost output and stay lean, though gains will be only about half of last year's 4.2%.

But cost pressures are still a big negative for the bottom line. Firms face rising costs for raw materials, benefits, compliance, etc.

S&P profit growth will slow to about 12% from 18% in 2003.

BUSINESS COSTS

Don't expect relief from skyrocketing steel prices anytime soon. In fact, they're headed higher. By late spring, hot-rolled steel will cost $450 a ton, up from $380 now. Demand is running especially high because of huge purchases of key steelmaking materials, including coke, scrap metal and coal, by China, Russia, Ukraine and South Korea. That'll ease by fall, with prices dropping to near where they are now.

Firms that self-insure have a new way to save on health costs:

Contracting directly with physicians and hospitals for treatment, cutting out insurers that otherwise act as middlemen. Employers also save on access fees, which average $3 per worker. One company, Perdue Farms, says that its 2003 per-employee costs actually fell 1% from 2002 levels. Compare that with the double-digit increases most companies faced.

The tactic works best in rural areas and in smaller cities that aren't served by many physician groups and hospital networks. Administration of the contracts can be outsourced or handled in-house.

Thinking about buying a business jet? Prices are dropping for new, smaller models coming from Cessna, Eclipse Aviation and others. They will cost under $2 million, half what today's smallest planes cost. Dubbed "microjets," the new models aren't much bigger than an SUV, but that means they have room only for a pilot and five others. Order now for 2006 delivery, though. Demand is already running high