

MONEY & INVESTING

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Ahead Of the Tape

—Today's Market Forecast—
By GREGORY ZUCKERMAN
And HENNY SENDER

Hedge Row

What's keeping hedge-fund hotshots up at night? It's not the investigation into mutual-fund trading, even though a few major funds were implicated at the outset and others are under scrutiny.

Instead, all eyes are trained on Clinton Group, a manager of hedge funds with assets of \$3.5 billion that is caught up in a controversy that could affect not only the firm, but the whole industry and the market itself. Clinton, one of the largest hedge-fund operators, has been accused by a recently departed employee of misstating the value of some bonds in its portfolio. Regulators are investigating. Clinton shocked investors with word that one of its flagship funds, Clinton Trinity Fund Ltd., lost 6.4% in October, bringing year-to-date losses to almost 15%. That performance is surprising for a firm that has sold itself on its limited volatility. As investors have pulled out money, Trinity Fund has shrunk to just over \$500 million from about \$800 million in just the past few months, according to people close to the matter. A Clinton spokesman declined to comment.

Late last week, directors of Clinton's three largest hedge funds sent a letter to investors saying that after an investigation, they were comfortable with how Clinton valued its investments as of Oct. 31. If the regulators concur, it will go a long way toward reassuring the market. But investors likely will pull more money out by year's end, which could weigh on sectors in the mortgage-backed securities market that Clinton specializes in, such as mortgage derivatives.

The overall mortgage market has shrugged off Clinton's problems so far. Are megahedge funds less able to rock markets than in the past? Perhaps, since funds like Clinton today use less leverage than hedge funds like Long-Term Capital Management, which blew up in 1998, almost carrying the stock and bond markets down with it.

But Clinton's troubles, which come as more pension funds and others shift into hedge funds, are a reminder of risks in funds that focus on illiquid securities that lend themselves to differences of opinion on how they should be priced. Several times in recent years, hedge funds that buy these kinds of bonds have blown up. Clinton already is registered with and audited by the Securities and Exchange Commission, suggesting the SEC's recent proposal to force all hedge funds to register isn't a panacea.

Send comments to tape@wsj.com and check next week for some letters at WSJ.com/Tape

—Inside—



Currency Trading: The euro hits another high against the dollar, as the greenback slides against most major counterparts. (Article on page C10.)

Bend it like Glazer?: Owner of Tampa Bay Bucs has increased his stake in U.K. soccer club Manchester United PLC. (Article on page C11.)

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Stewart Seeks an Unusual Pretrial Advantage

Defense to Ask Judge To Force 3 Witnesses For Prosecution to Talk

By KARA SCANNELL

MARTHA STEWART may soon get a peek at the government's case against her. The lifestyle maven, who faces securities-fraud charges stemming from the government's investigation of her sale of ImClone Systems Inc. stock nearly two years ago, will try to persuade a federal judge this week that three key prosecution witnesses should be compelled to answer questions from her lawyer.



EXECUTIVES ON TRIAL

Few criminal defendants have that opportunity. But, in September, U.S. District Judge John Sprizzo granted lawyers for Ms. Stewart permission to take the depositions of 15 government witnesses to help prepare their defense against a civil lawsuit brought by shareholders of the company Ms. Stewart controls, Martha Stewart Living Omnimedia Inc. The question now is whether Judge Sprizzo, who is overseeing the civil case, will order the witnesses to talk. He could decide as early as Friday, when a hearing is set in federal court in Manhattan.

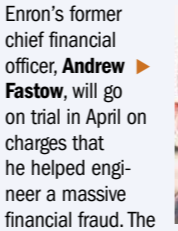
"This is quite unusual," said John K. Carroll, a

Scandal Scorecard

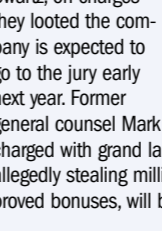
A parade of executives will soon have their day in court, joining Tyco executives whose trial is under way. Some of the cases:



Martha Stewart's trial on securities fraud and other charges, stemming from her sale of shares of ImClone Systems stock, is scheduled to begin in January.



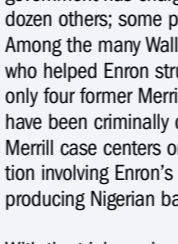
Enron's former chief financial officer, Andrew Fastow, will go on trial in April on charges that he helped engineer a massive financial fraud. The government has charged about two dozen others; some pleaded guilty.



Former chairman, L. Dennis Kozlowski, and former chief financial officer, Mark Swartz, on charges they looted the company is expected to go to the jury early next year. Former general counsel Mark Belnick, also charged with grand larceny for allegedly stealing millions in unapproved bonuses, will be tried later.



WorldCom's former chief financial officer, Scott Sullivan, is charged with conspiracy, securities fraud, bank fraud and filing false statements in an \$11 billion accounting fraud. His trial is set for Feb. 2.



Members of Adelphia's founding Rigas family, including patriarch John J. Rigas, are accused of looting the cable-TV company, along with a nonfamily member who helped manage the firm's finances. Trial is set to begin Feb. 9.



With the trial now in progress, the case against Tyco International's former chairman, L. Dennis Kozlowski, and former chief financial officer, Mark Swartz, on charges they looted the company is expected to go to the jury early next year. Former general counsel Mark Belnick, also charged with grand larceny for allegedly stealing millions in unapproved bonuses, will be tried later.

former federal prosecutor who is now a defense lawyer at Clifford Chance LLP. "Most of the time, at the government's request, discovery—particularly depositions—in parallel proceedings is stayed."

Criminal defendants usually get access to facts the government has collected just before trial. In fact, U.S. District Judge Miriam Goldman Cedarbaum, who is overseeing Ms. Stewart's criminal

case, has already ruled that she can't see the government's materials until two weeks before opening arguments in the case. The trial is scheduled to begin in January.

Ms. Stewart's lawyer, Robert Morvillo, is particularly interested in interviewing Douglas Faneuil, a former Merrill Lynch broker assistant who has contradicted Ms. Stewart's account of the

Enron Heat Descends On Smaller Players; Others Enjoy Shade

By ANN DAVIS

OF THE HUNDREDS of Wall Street bankers connected to the Enron Corp. fiasco, those facing prosecution did surprisingly little work for the energy titan.

In fact, the banker who potentially faces the most jail time, finance specialist James A. Brown, worked for a firm—Merrill Lynch & Co.—that got a relatively small piece of Enron's business, despite efforts to break into the top tier. Mr. Brown himself objected to the deal at the heart of his case. But his objections were dismissed by co-workers, including a Merrill attorney, and he later was told to help execute the tiny deal.

Meanwhile, bankers at several firms that Enron called its "Tier 1" banks, who participated in some of the most contentious—and largest—transactions with Enron, may never be prosecuted.

Why are the smaller players, at least so far, taking the heat?

One factor is the Justice Department's focus on Enron's former top guns. Amid the labyrinth of alleged financial fraud and self-dealing left behind when Enron collapsed into bankruptcy-court protection in late 2001, federal prosecutors lately have concentrated on a single transaction at Mer-

Some Fear Inflation Is Ready for a Comeback

By KEN BROWN

JIM PAULSEN, the chief investment officer at Wells Capital Management, ticks off the ingredients needed for a mean batch of inflation.

"I would flood the system with money far in excess of economic growth, I would take interest rates to the lowest levels possible, I would have the government spend like a baneshee, I would drop the value of the dollar, and finally I would take any capacity growth or additional supply growth and stop it," he says. As a garnish, he'd add rising commodity prices and a growing trade deficit mixed with some rising trade tensions.

Sound familiar? As investors close the books on 2003 and look out into next year, some are worrying that inflation, which had been banished in the past few years, is poised for a comeback. Were that to happen, it would terrify bond investors and shake up the stock market, while giving a boon to some manufacturers, which finally would be able to raise prices.

"Last fall we were all worried about deflation," says Mr. Paulsen. "What could happen by summer is everyone could be panicked about inflation."

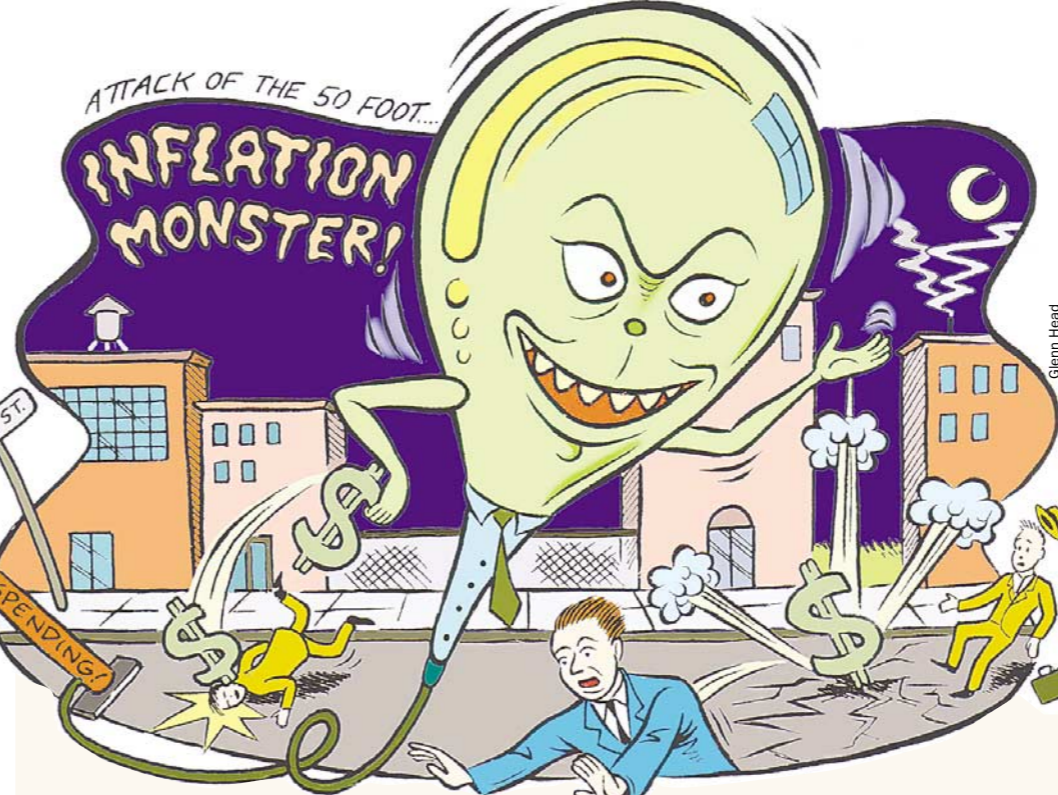
That panic may be based more on emotion and expectations than on anything else. There are lots of good reasons why inflation should remain tame, mainly the lack of a strong jobs market. But as investors spend much of their time trying to divine the future, expectations are what will drive stocks and bonds.

If investors collectively agree that inflation is looming, the angst will first show up in bonds, where yields will rise and prices will fall. If the Federal Reserve shares that view, it will push up the federal-funds rate, which is the interest on overnight loans between banks, from its 45-year low of 1%.

That would drive bond prices down, causing pain for bond investors. It could slow or stop the recent economic rebound, which has boosted corporate profits. That means the stock market, particularly stocks that do best in a fast-growing economy, like industrial and big ticket consumer-goods companies, could get hit.

Paul McCulley, a managing director at bond manager Pimco, uses a somewhat different metaphor, but also comes to an inflation conclusion. "The cocktail now pouring into your glass is a 2.5% fed-funds rate by the end of 2005," he says. "The straw in the beverage in 2004 will be fear."

Mr. McCulley, whose firm, Pacific Investment Management Co., oversees \$304 billion in assets, predicts a bond bear market next year—which would come on top of a market that has been largely weak since early this summer. The fed-fund futures market, where investors bet on the direction of short-term interest rates, is saying short-term rates will start their reversal in May when they rise one-quarter of a percentage point. Other markets are predicting inflation; investors in inflation-indexed Treasury bonds are saying inflation will top 2.5% over the next several years. That's well above the 1.5% rate of the past 12 months, but



Feeding the Monster?

Some economists compare today's situation—where the economy is finally gaining traction after a long downturn—with the end of 1993. Then, interest rates rose rapidly, spooking the markets. Though the slowdown is different this time, there are some parallels.

	YEAR-END 1993	NOV. 28, 2003		YEAR-END 1993	NOV. 28, 2003
Inflation ¹	3.1%	1.3%	Money supply ²	Up 1.529%	Up 4.49%
Unemployment	6.5%	6.0%	Trade-weighted dollar ³	Up 1.1%	Down 14.4%
Commodity prices			Interest rates		
Gold, per troy oz.	\$390.80	\$396.80	Federal-funds target rate	3.00%	1.00%
Crude oil, per barrel	\$14.17	\$30.41	Two-year Treasury yield	4.25%	2.05%
Current account deficit	\$27.3 bil.	\$138.7 bil.	10-year Treasury yield	5.83%	4.34%

¹Year-over-year change in core consumer price index dollar index, percentage change over the past 52 weeks
²Year-over-year change in weekly M3 supply
³Bank of England trade-weighted dollar index, percentage change over the past 52 weeks
Sources: Bureau of Labor Statistics; Thomson Datastream; WSJ Market Data Group; Commerce Department; U.S. Federal Reserve

almost inconsequential compared to years past.

To investors who only a few months ago were wringing their hands over deflation, all this inflation talk might seem odd. In a way, it's a predictable part of the cycle, now that the economy has crossed the threshold into a self-sustaining recovery. Powerful economic data over the past few weeks have wiped away fears that the economy might backslide into recession, though a period of weak growth, which would keep inflation in check, is possible.

And there still are a lot of facts economists can muster to make their low-inflation case. First and foremost is that unemployment remains high at 6%, and the jobs situation is worse if you include people who have stopped looking for work. "Inflation is a lot like Elvis," says David Rosenberg, Merrill Lynch's chief North American economist. "Lots of reported sightings, none confirmed."

Whether and how the market reacts to the

Markets Diary/Trading for Friday, November 28, 2003

Stocks

Dow Jones Industrial Average 9782.46 ▲ +2.89

INDEX	CLOSE	NET CHG	% CHG	12-MONTH % CHG	YTD
DJIA	9782.46	+2.89	+0.03	+9.96	+17.27
Nasdaq Comp.	1960.26	+6.95	+0.36	+32.56	+46.78
S&P 500	1058.20	-0.25	-0.02	+13.02	+20.27
Russell 2000	546.51	+1.20	+0.22	+34.49	+42.66

Global Stocks

DJ World Stock Index (excluding U.S.) 135.28 ▲ +0.16

INDEX	CLOSE	NET CHG	% CHG	12-MONTH % CHG	YTD
DJ World (ex. U.S.)	135.28	+0.16	+0.12	+25.49	+29.42
Nikkei 225	10100.57	-62.81	-0.62	+9.60	+17.74
DJ Euro STOXX 50	2630.47	-5.42	-0.21	-0.99	+10.23
MSCI EAFE	1195.82	+1.03	+0.09	+21.23	+25.53

Bonds & Interest

10-Year Treasury Note Yield (4 p.m. ET) 4.335%

10-Year Note	FRI	FRI	WED	WED	TTL RTN
10-year Treasury note	99.32	4.34%	100.00	4.25%	+0.44
3-month Treasury bill	0.92	0.92	0.92	0.92	+0.96
DJ Corporate Bond Index	172.60	4.89	173.38	4.82	+8.40
Lehman Brothers MBS	1069.92	5.08	1072.70	5.03	+1.96

U.S. Dollar

Percentage change since Nov. 28, 2002 94.3 ▼ -0.1

CURRENCY	LATE NOV	LATE NOV	DAY'S HIGH	DAY'S LOW
Euro (in U.S. dollars)	1.1991	1.1909	1.2015	1.1902
Japanese yen (per U.S. dollar)	109.61	109.13	109.10	109.65
British pound (in U.S. dollars)	1.7216	1.7137	1.7240	1.7135
Canadian dollar (per U.S. dollar)	1.2989	1.3072	1.2935	1.3099

Commodities

DJ-AIG Commodity Futures (1991=100) No index on Friday

COMMODITY	CLOSE	CHANGE	WED	YR AGO
DJ-AIG Commodity Futures	Closed			126.087 105.247
Oil (Nymex crude future), bbl.	Closed	\$ 30.41	\$ 26.89	
Gold (Comex spot), troy oz.	Closed	\$396.80	\$316.80	
Wheat (#2 hard KC), bu.	\$4.3750	+0.1225	\$4.2525	\$4.2525