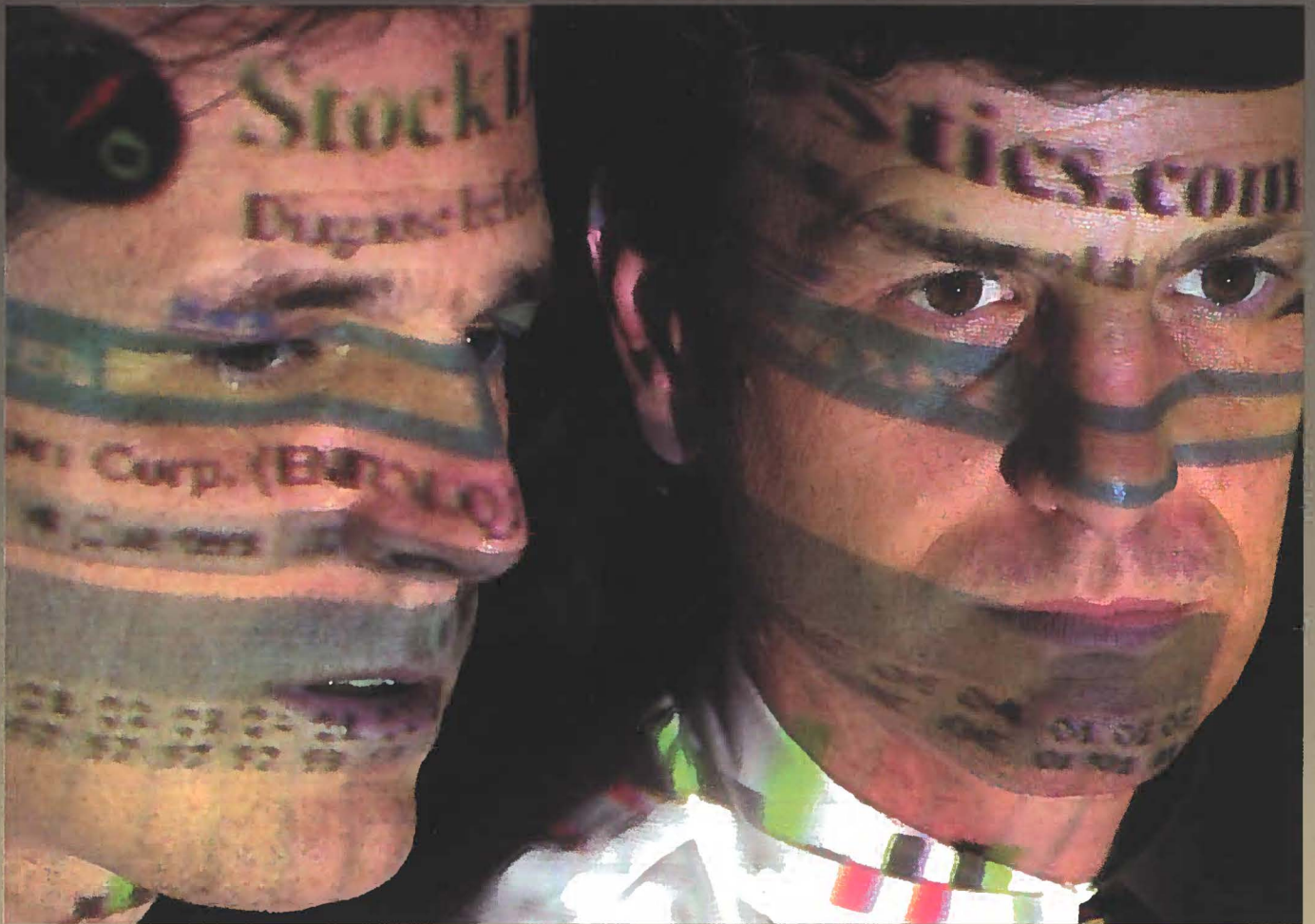


January through June 2003 Three Dollars

EQUITIES



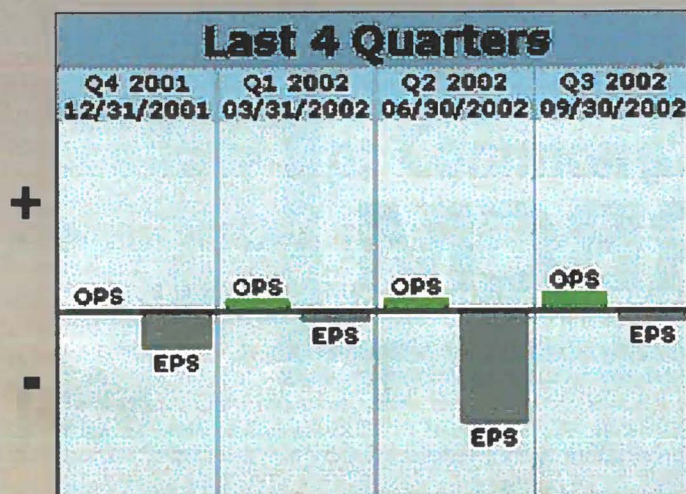
STOCKDIAGNOSTICS.com's Markowski Brothers

*Claim Their Computer Algorithms Find Winners and Sinners
Before Wall Street Researchers*

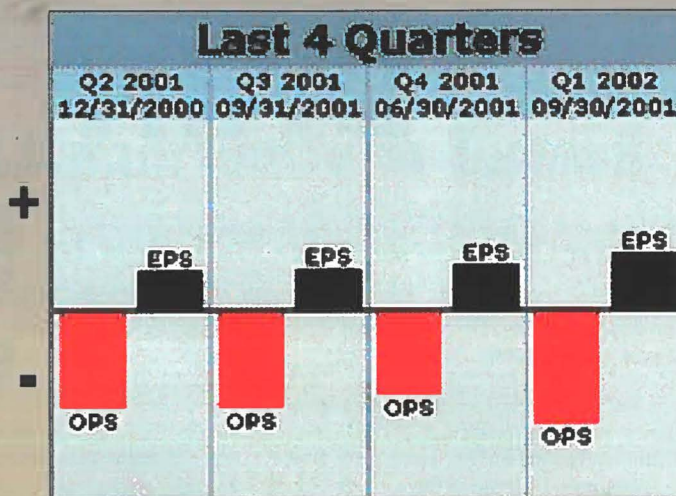
Plus: Sir John Templeton predicts
record home mortgage defaults hurting
U.S. equities short-term;
long-term Dow Jones one million!!

OPS™ Reveals the Truth About Your Stocks!

NUMERICAL TECHNOLOGIES, INC. (NMTC)



SUPREMA SPECIALTIES INC.



Numerical Technologies (NMTC) was acquired for a 64% gain after it reported record negative EPS (gray bars) and record **positive OPS (green bars)** for its 12 months ended 9/30/02. *EPS proved to be a false indicator of NMTC's value since it did not reveal the strong underlying cash flow condition.

Suprema Specialties Inc. filed for Chapter 7 bankruptcy, a 99% loss after it reported its 15th consecutive quarter of record EPS and its 20th consecutive quarter of **negative OPS (red bars)** for its 12 months and its quarter ended 9/30/01. *EPS proved to be a false indicator of Suprema's value since it did not reveal the the weak underlying cash flow condition.

StockDiagnostics.com specializes in monitoring cash flow for over 10,000 companies and is the exclusive publisher of OPS data.

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OPS Not OOPS!

Find winners and sinners before Wall Street research analysts. The focus of the Markowski brothers' StockDiagnostics.com website and The *OPS Newsletter* on real cash flow—not suspect EBITDA or doctorable reported earnings—can help investors escape unexpected future stock collapses. It also discovers turnarounds and Up and Comer OPS Seedlings, Saplings and Oaks early. You too can escape the EPS syndrome!

By Art Detman, Jr.

“When you buy a stock, you are buying present and future earnings,” explains every finance professor teaching each new generation. “Find a stock with steadily rising earnings and a relatively low price-to-earnings ratio, and you likely have found a future big winner.”

The above belief has supported the search for the Holy Grail of picking the right stocks in every value and growth investor's catechism since equity pioneer Edward Lawrence Smith's historic study in the early 1920s. This conclusively proved a diversified portfolio of common stocks, which yields around 9% annually over the long run, beats investing in bonds. This is because of the relentless depreciation of purchasing power from inflation in all Democratic societies where politicians please the masses at the expense of future generations.

True enough! That is common sense. But what specific stocks should you buy or sell when the unfortunate reality is that earnings can be easily managed and massaged, to say nothing of being deliberately misstated or manipulated? Furthermore, when things do change for the better or worse in a company insiders seem to get the news first and the investing public last.

During the recent stock market bubble the big time media led by the stars of momentum inventing lured millions of investors into the most over-priced, new-era large-cap stocks at the worst time to buy. They scorned middle and small caps with better relative value, profits and proven products or services as too risky or unexciting. Worse, off the books transactions artificially produced growing earnings and EBITDA when the reality was the reverse. All dressed up, seemingly profitable companies had seriously negative cash flow and their viability was even in question. Arthur Anderson, considered the premier

accounting firm in the world, surrendered their virtue to let smoke rise out of corporate chimneys at Enron where there was no fire.

What's an investor to do? Whom can you trust? Listen to the same old bad advice from the same pompous silly sources, which gave horribly bad advice in the past and now have amnesia or even recall that their bad momentum ravings were really good for you?

Enter stock sleuths 42-year-old David Markowski, president, and 47-year-old Michael Markowski, director of research for StockDiagnostics.com, an Internet subscription service with *The OPS Newsletter* using proprietary algorithms developed over six years by its parent Newsgrade Corporation, of Sarasota, Florida.

The brothers' ambition is towering. Their mission is to become the world's largest producer and publisher of financial news and information. Someday for every public stock on the planet—currently over 80,000—and in every country their pre-digested, pre-filtered and color-coded displays on their website www.StockDiagnostics.com will alert the world's investors, now about 385 million, to significant changes in their stock holdings almost simultaneously in many different languages. (see back cover)

By generating news stories from their statistics based on data a company must publish to remain publicly held they would scoop human reporters who rely on management or investors for their leads overtaking Dow Jones, Reuters and Bloomberg.

The brothers via another of their web sites CashFlowNews.com already turn out 500 proprietary cash flow news stories a day, ranking it as one of the largest publishers of original financial news stories in the U.S.

They believe that they are positioned to be the largest provider of financial news and information worldwide after they begin

publishing financial news and information in 20 foreign languages, which will include French, Italian, Spanish, Russian, Portuguese, Korean, Japanese and Chinese by the end of 2004.

So far 400 investors have invested about \$20 million to back this daring vision. The company chairman is Ronald Erickson, former CEO of Egghead Software, while David Markowski handles operations and brother Mike research. In 1998 the company had to change its original business model when public companies wouldn't pay to have their results broadcast. Disaster loomed.

A new business plan was the solution, turning the information into a valuable grading system, hence the parent company name Newsgrade. Investors should pay because these alerts would help save them from disasters and make big money uncovering winners. Comparing his statistical data research to a biotech, which has uncovered a line of DNA, Mike Markowski believes his systems can uncover big winners or losers long before Wall Street researchers reveal what is really going on.

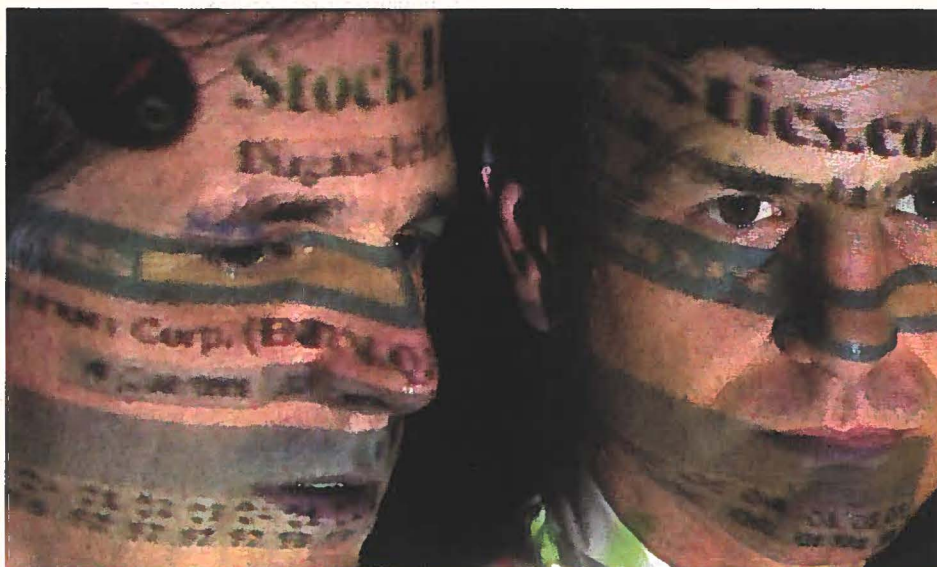
The best investor *EQUITIES* knows is Sir John Templeton, who believes that he is only right about 60% of the time. See page 9. Mike Markowski believes that his algorithms can be right much more often than that. However, even if right only 51% of the time in identifying big stock movers his subscribers would be way ahead.

Their primary forecasting vehicles are websites, StockDiagnostics.com and StockDiagnosticsPro.com which provide cash flow OPS diagnostic charts on 10,000 companies and a newsletter named “*The OPS Newsletter*” which has been amazingly accurate so far. Their primary focus has been on measuring OPS (Operational cash flow per share), a proprietary financial statement analysis metric that they discovered was a leading indicator of a company's true health and stock price.

Earnings per share figures too often deliberately conceal the truth whereas cash flow reveals it. Last year over 300 companies restated their earnings. Study the patterns of quarterly operating cash flow figures and you can discover a buy or sell signal.

“Operating cash flow per share (OPS) is the best leading indicator of future problems or positive changes in a company's financial health,” Mike Markowski argues. Half of all publicly traded companies over the past year have had either positive or negative momentum changes, which show up as breaks in their cash flow patterns.

“We have built an ark before any investors saw the flood coming,” Mike Markowski continues. “Our system detects anomalies in the financial statements of 10,000 public



Brother Act: Nebraska farm boys Michael, left, and David Markowski found Florida State a sunny place to go to college and now run their venture from that state after stints on Wall Street. Starting fresh out of college as a mail room clerk at Merrill Lynch, Mike had to update Standard & Poors sheets in the library where a study listing the top ten earnings gainers over 1967 to 1976 intrigued him. Was there really was any correlation between earnings gains and stock price performance? After finding that the top ten companies on the list had appreciated between 900% and 5,000%, he became a believer that there was a correlation between stock price and great financial performance.

Joining Donaldson Lufkin & Jenrette because of its reputation as the "House built on Research" Mike studied 250 companies for the period 1974 to 1983. He found an even higher correlation between long-term revenue growth and superior stock price gains. Convinced rapid revenue growth was the key, Mike left DLJ and briefly entered venture capital to seek growth companies capable of multiplying revenue 10 to 100 times over five to ten years.

Turning entrepreneur in 1995, Mike founded SSNN.com, a web site specializing in publishing online news for small public companies, which became StockDiagnostics.com. In 1999 with the bull market roaring, he envisioned a need for a system that could detect anomalies within the financial statements of public companies. He was determined to build an automated system that could perform that task for every public company worldwide.

The development for the automated system which actively tracks 1,801 data points per public company and has over 500 million records and eight patents pending was completed in late 2001. Fascinated by the unexpected collapse of media darling Enron, Mike conducted a post mortem financial autopsy and discovered what he believed was the cause of death. Testing his theory back to 1997, he ran Enron's algorithm through his database searching for matches with any other public companies. Shockingly, he found over 400 companies died of the exact same cause of death, including Sunbeam, Polaroid and Fruit of the Loom with over \$300 billion lost by investors. Hundreds of other "seemingly healthy" public companies including now bankrupt cable TV operator Adelphia Communications had the same symptoms. They were really dead companies walking.

Armed with this knowledge, Mike built a website for stockdiagnostics.com and in May 2002 issued warnings on five then-Blue Chip NYSE companies: Sears, General Dynamics, Fleming Companies, Wyeth and Concord EFS. Each was heavily and highly recommended by Wall Street analysts. Subsequently, each stock declined by 50% or more, resulting in cumulative market losses of over \$60 billion.

That made bears happy, but what did he have to make the more numerous bulls happy? He discovered positive algorithms or anomalies to identify public companies that are severely undervalued or undiscovered. Since September 2002 StockDiagnostic.com's weekly newsletter has featured six companies which have appreciated over 100% and five other companies have been bought out at sizable premiums.

Having spent \$20 million raised from about 400 investors to develop a global data base which includes the proprietary algorithms and eight patents pending, the brothers claim OPS only uses 2% of their data base for its recommendations. They intend on finding additional accounting anomalies that they can use to predict changes. But success in having OPS accepted and paid for by subscribers is crucial to win credibility. The long run mission for StockDiagnostics.com's parent Newsgrade Corporation is to become the world's largest producer and publisher of financial news and information.

companies by comparing current earnings per share and operational cash flow per share to historical patterns." Negative anomalies can spotlight stocks to sell or avoid while Wall Street research analysts maintain their buy or hold ratings because of investment banking conflicts."

The StockDiagnostics.com website issued 3,200 cash flow warnings and downgrades for 2002 and its *OPS Newsletter* issues weekly alerts on overvalued companies that report "cashless earnings" and also for those companies that have such severe cash flow drains that their very survival is questionable. Positive anomalies can identify attractive special situations few or no analysts are following for big gains when the hidden bargains become obvious—or sooner—if the companies are acquired.

One algorithm is a pattern of "positive" financial statement anomalies that can be used to identify low-priced emerging growth companies that are usually not recommended by Wall Street. Five of such featured stocks since the publication of *The OPS Newsletter* began in September 2002 appreciated by at least 100%.

Additionally, from December 2002 through May 2003, five companies named in *The OPS Newsletter* were bought out at substantial premiums. Within ten days of being featured, two of these companies, uDate.com (OTC:BB: UDAT) and Lending Tree, (NASDAQ: TREE) were bought out by Barry Diller's USAInteractive for premiums of 150% and 40% respectively. Another web sleeper, Multex.com (NASDAQ: MLTX) was acquired by Reuters for a 60% gain one week after appearing in *The OPS Newsletter*. Numerical Technologies (NASDAQ: NMTC) was bought out for a 90% gain six days after being selected. Ramsay Youth Services (NASDAQ: RYOU) appreciated 38% after a buyout offer came 10 weeks after being selected.

Operating (or operational) cash flow (OPS) must be reported by companies on their consolidated statements of cash flow. Basically, it is the difference between cash revenues and cash expenditures, without deducting non-cash charges such as depreciation or amortization. Free cash flow is operating cash flow less capital expenditures, which is a useful measurement but one that penalizes fast-growing, capital-intensive companies such as Wal-Mart Stores (NYSE: WMT-55.58), which OPS identified as a buy about \$44.

Most institutional investors use their own formulas for cash flow, especially the institutional favorite EBITDA, which stands for earnings before interest, taxes, depreciation and amortization. "The accounting scandals revealed it is not a defensible or reliable indicator, but a recently concocted and fash-

ionable measurement," Mike Markowski charges. "In fact, EBITDA didn't even come into play until about 15 years ago."

For Mike Markowski, the investor's answer is operating cash flow per share (OPS). In some instances, a favorable OPS pattern can mean that a company that has reported quarterly losses is actually a buy candidate, which he labels depending on size a Seeding, Sapling or Oak. For example, Sun Microsystems (NASDAQ: SUMW-3.86) had two quarters of red ink in 2002 but StockDiagnostics.com recommended the stock last October at \$2.66. "Sun had 20 straight quarters of positive operating cash flow," he explains. Since then, the stock climbed about 50%.

Equally encouraging, there is hope for some small-cap NASDAQ and AMEX high-tech companies with managements who have been improving operations while not a single security analyst notices. "For the first time in the past few years we are starting to see Internet-oriented companies in four market segments with positive cash flows," Mike Markowski says.

These are companies in online retailing, general online information, financial online information and software web development for corporations. Digital Impact (NASDAQ: DIGI-1.65) provides comprehensive solutions for creating and executing online direct marketing. Bank Rate (NASDAQ: RATE-9.03) is up over 300% since being discovered. LookSmart (NASDAQ: LOOK-2.30) and Online Resources Corp (NASDAQ: ORCC-3.70) and Webex (NASDAQ: WEBX-11.46), where 65% of the float has been shorted, are other Up & Comers.

In contrast, Mike Markowski is bearish on two old-economy high-tech giants, Lucent Technologies (NYSE: LU-2.24) and Agilent Technologies (NYSE: A-17.65). "Lucent had a negative operating cash flow for eight out of its latest nine quarters," he says. "Our system gave a sell signal in the third quarter of 2000 when Lucent was at \$43 a share, and we've been negative on it ever since. Today it is selling for under \$3."

OPS isn't perfect. It raised a red flag on Agilent, the original business of Hewlett-Packard, in 2002, when its shares closed out September at \$13.06. However, the stock price rose and was recently over \$17. "Agilent is an extremely high-risk stock because it now has five quarters in a row of negative operational cash flow," an undeterred Mike Markowski warns. "In the 16 prior quarters, the company had only two quarters of negative OPS, although even that is not good."

The EPS Syndrome

Because of investment banking and other conflicts like Morgan Stanley paying com-

petitors to write favorable reports on Morgan's overpriced IPOs, Wall Street sell side researchers often are blind to negative cash flow. Look at Concord EFS (NYSE: CE-14.78), which clears electronic transfers for banks. For four-and-one-half years it had a basically favorable financial picture: Every quarter CE reported earnings, usually higher than year-earlier results. Only twice did it have a negative OPS, both relatively modest.

Suddenly for the first quarter of 2001 Concord EFS reported a negative OPS of \$0.35 per share. This sharp break from its historical pattern, even while reporting record earnings of \$0.11, raised the red warning flag which Mike Markowski labels the EPS Syndrome: record earnings and a negative cash flow. So while uninformed shareholders complacently hold their shares, OPS gives a lucky informed few the chance to exit while they still have their shirts.

"OPS is phenomenal if you know how to use it. I've had winner after winner!"—

**Bob DelVecchio,
Brockington Securities**

Markowski issued his warning for Concord on May 17, 2002. By the end of the month CE stock was still above \$30 and had 21 buy recommendations from Wall Street's largest and most prestigious firms (no sells, of course). Over the next two months the stock fell to as low as \$7 and recently remained under \$15. Clearly some research would be more truthfully labeled as "Marketing" or "Stock promotion."

Consider also AstroPower (NASDAQ: APWRE-3.05), a manufacturer of solar power components. For four straight quarters—the second quarter of 2001 through the first quarter of 2002—AstroPower reported negative OPS but positive EPS.

In fact, AstroPower's first-quarter 2002 per-share earnings were the best ever—another instance of the EPS Syndrome. Wall Street didn't warn ordinary investors in time to exit

before getting burned. With the stock over \$25, there were 11 buy recommendations and no sells. Two months later, with the stock down to \$15, there were \$12 buys and no sells. The stock soon plunged below \$10 and trades now over \$3. "Wall Street still has a lot of coverage on it," Markowski says in disbelief.

Sometimes the negative OPS pattern is even more blatant. Take Suprema Specialties (OTCBB: CHEZ), a maker of food products, which was also diagnosed with the EPS Syndrome. For 20 straight quarters—from the second quarter of 1997 through the first quarter of 2002—Suprema reported negative operating cash flow per share. Yet except for two quarters, in late 1997 and early 1998, Suprema also reported earnings per share.

In fact, Suprema's earnings grew almost every quarter from late 1998 until they reached a record high in 1Q02. It was number 23 on *Fortune's* list of America's 100 fastest-growing companies in 2001, and that November raised \$59 million by selling 4.5 million shares at \$13. Five weeks later, with the stock holding at \$13, trading was halted. Suprema filed for bankruptcy.

So far the most notable case high lighted by StockDiagnostics.com, involves Sears, Roebuck (NYSE: S-29.95). Stock sleuth Mike Markowski first downgraded Sears in May 2002, when it traded around \$56, based on its diagnosis of cashless earnings (positive EPS and negative OPS). When Sears reported a negative cash flow for its next quarter even though earnings were at an all-time high, a second downgrade was issued in August, with the stock at \$47. During the next couple months, Markowski and Sears' CEO Alan Lacy fought a spirited battle on the business pages of the *Chicago Tribune*. Markowski contended that Sears' credit-card portfolio was in bad shape. Lacy responded that its quality was excellent.

Suddenly in October the president of Sears' credit card division resigned, and exchanged lawsuits with the company, which announced that third-quarter earnings were lower than expected due to problems with credit-card receivables. Markowski predicted a negative operating cash flow of a half-billion dollars for the third quarter, and in mid-November Sears announced \$928 million in negative operating cash flow. The stock sank to a decade-low of \$18.25. After putting its huge credit card operation up for sale, Sears stock has recovered to over \$29 recently, still down more than 50% from when Markowski issued his first warning.

Another brilliant coup was flagging trouble at Fleming (NYSE: FLM), the nation's largest food distributor with \$16 billion in revenue and 22,000 employees. In May 2002 it was diagnosed with EPS Syndrome and StockDiagnostics.com warned its subscribers

to avoid the stock, which was then priced over \$23, at any price. The following month its co-underwriter Morgan Stanley helped raise it \$155 million and issued a strong buy with a price target of \$27. Today Fleming is bankrupt.

The brothers are passionate about issuing warnings on those companies that report cashless EPS (positive EPS and negative OPS) and have high stock prices. Mike cautions that even the savviest of investors doesn't understand the extent of how much EPS is being manipulated to the detriment of the investment public. He projects that over 1,000 companies, many of them institutional favorites, will manipulate or seriously distort their reported EPS during 2003.

Like who? He points to a recent warning that StockDiagnostics issued on Federal Express (NYSE: FDX-62) as an example of how serious is the problem of how real are earnings? FedEx's cash flow for its recently reported third quarter came up negative for the first time in 20 quarters.

Upon further examination Mike found out that the abnormality was caused by its pension fund being under funded by over \$700 million. Instead of taking the conservative approach and deducting the \$700 million as an expense against third quarter earnings, FedEx booked the cash outlay as a pre-paid expense, which can become a dubious illiquid asset on a balance sheet.

The accounting gimmick enabled FedEx to meet or exceed many Wall Street earnings estimates, creating an opportunity for inside executives to sell their shares near the all time high. But in the future this pre-paid expense will negatively impact FedEx's earnings. Mike is curious how and when investors will be informed about the impact of this \$700 million in the future.

Because of the seriousness of the problem of earnings which really aren't what the individual investor would think of as earnings, the brothers' mission is to replace the spotlight on obsolete and easily distorted or manipulated earnings based on popular metrics such as Net Income, EPS, EBITA, ROE (return on equity) and even the p/e with more accurate leading indicators based on OPS, free cash flow and additional metrics which they are continuously researching.

Besides warning about future losers, cash flow analysis can help identify tomorrow's winners by screening the thousands of stocks where little or no independent research exists. Two of the recent discoveries with revenue growing at more than 250% include Medifast (AMEX: MED-12.69), which The OPS Newsletter identified when MED was traded on the OTC Bulletin Board and was only about \$0.30. See page 22. Another is RTIN Holdings (OTCBB: RTNH-1.13) a

play on pain relief. See page 24. A third OTC Bulletin Board-listed Sapling Command Security (OTCBB:CMMD-1.00) was discovered at an EQUITIES conference. See page 38.

The brothers' cash flow analysis also identifies turnarounds of fallen angels or short selling targets where Wall Street is extremely negative. Take Rite Aid (NYSE:RAD-3.67) where in 2002 cash flow analysis signaled that a significant turnaround was underway and its OPS Rating was upgraded twice to its highest level in five years. On April 8, 2003, with its shares at \$2.60 just two days prior to Rite Aid's scheduled April 10th fourth quarter and fiscal year end earnings announcement, the brothers alerted their subscribers to a possible pleasant surprise and a significant turnaround. It happened and on April 11th Merrill Lynch became the first Wall Street firm in over a year to issue a new buy recommendation, followed by a flurry of other new buy recommendations and credit rating upgrades.

RISKS

OPS and StockDiagnostics.com's other new algorithms are a solid addition in the tools for analyzing the prospects of a company. However, in his fervor to spread the gospel of following cash flow over earnings, Mike Markowski must be careful not to promise more than he can deliver. No stock forecasting system is perfect because human beings always get involved. Some CEOs can always find a way to mess up an ideal situation, while others creatively survive an impossible situation. Also while OPS is extremely valuable, it does require users who know the difference between cash flow and reported earnings. That hurdle requires a high level of financial sophistication. Finally, StockDiagnostics must get a critical mass of online subscribers to pay for Internet stock tips, which many only accept when it is free.

A similar situation occurred in 2002 when Xerox was awarded its highest OPS Rating in five years after Mike's cash flow analysis signaled that its turnaround was for real although Wall Street and the credit rating agencies were still decisively negative.

Historically buy-side analysts have long used cash flow analysis although it was considered old fashioned by momentum players in the market madness. Some mutual fund managers place special emphasis on it. For example, Jordan Alexander of the Evergreen Small Cap Value Fund uses it with great skill.

Yet even its fans will admit that the process isn't as straightforward as it might appear. The sad reality is that cash flow also can be managed, just like earnings. Among the available tactics: Sell accounts receivables, delay paying bills, don't debit the checking account until after checks clear, include gains from security sales and capitalize expenses that should be charged off.

The good news is all these deceptive ploys can inflate reported operating cash flow, but only once. That's why Mike Markowski stresses that is important to look not just at the current operating cash flow per share but put its direction in the context of the past five years. "You can manipulate just about anything," he concedes. "But at the end of the day, operating cash flow per share is much more reliable than earnings per share."

Take for example, fallen angel K-Mart (OTCBB:KMRTQ). For years it had reported a seasonal negative OPS for each third quarter. But in May 2001 it reported a \$0.57 negative cash flow per share and a \$0.05 loss per share for its first quarter. The stock was at \$10.58, and climbed higher on the strength of buy recommendations from two of Wall Street's biggest firms.

Suddenly a drumbeat of bad news pushed down the stock to below \$2 by early 2002, and in June of 2002 the company restated its financials. The nickel a share loss reported 13 months earlier became a \$0.48 loss. In contrast the negative OPS of \$0.57-a clear warning signal-remained unchanged. Today K-Mart is just a broken penny stock.

Paraphrasing the great heavy weight champion Joe Louis, who faced and knocked out an elusive, back-peddling opponent, Mike Markowski says, "Accounting anomalies can run, but they can't hide."

"Using OPS keeps our research ahead of the curve by focusing on operational cash flow," Mike Markowski sums up.

Registered investment advisor Ray Mullaney with Conservative Financial Counselors, who has been a user for the past six months, went one step further. "StockDiagnostics is a profound science-based program," he says. "The output of this program is derived from the most critical accounting elements of a public company. Nothing in the marketplace comes close to its quality. Mike is an audacious inventor in an industry filled with ineffectual followers."

That is heavy praise from a 25-year veteran investment advisor with a distinguished record of stock market forecasting and forensic accounting.

Naturally everything good has a price. Individual subscriptions are available at www.stockdiagnostics.com. Institutional products, services and subscriptions are available at StockDiagnosticsPro.com. □