Financial Statements
A Quarterly Update for Tax, Accounting and Legal Professionals

Capitol Securities Management
50 Rowes Wharf Suite 430
Boston, MA 02110
(617) 897-8500
Member NASD and SIPC

Leadership Builds Stronger Professional Practices

Motivating the people in your firm to perform at top levels is most likely an ongoing objective. Once you attract the best and the brightest, the challenge becomes keeping them and effectively utilizing their skills to enhance and grow your business. Competitive benefits and compensation are great retention tools, but what about influences that transcend an individual's bottom line, like leadership? As a strong leader, you can enhance both commitment and performance, as well as define the work culture of your practice.

Leadership plays an essential role in all successful organizations, from governments to Fortune 500 companies to baseball's World Series champions. And, it has a place in your firm. Professionals who are highly skilled rarely benefit from heavy-handed management, but strong leadership can inspire them. And with motivated people working with you, you position yourself to more effectively sustain your daily operations and affect positive change for the future of your practice.

Charisma is often the most notable trait of a leader, but not necessarily the most effective. You may achieve powerful results by tapping the following qualities:

- **Vision.** Defining short- and long-term objectives establishes direction for the firm. When you communicate your vision, you create a culture of inclusion. People feel they have a stake in the future, and a role to

continued on page three

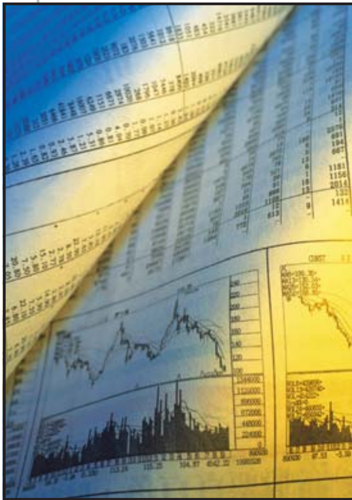
The named individual offers securities through AXA Advisors, LLC (NY, NY 212-314-4600) member NASD, SIPC and offers annuity and insurance products through AXA Network, LLC and its subsidiaries.

VOLUME ONE, ISSUE ONE

The Ongoing Debate: Growth vs. Value Investing

Many investors divide themselves into two opposite camps. On one side are the **growth investors** and on the other, the **value investors**. Although these two schools of investing need not be exclusionary, they do represent opposite ends of the investment spectrum. Growth investors look for stocks that are expected to grow at an above average rate regardless of market conditions, while value investors select stocks they believe are trading at less than their intrinsic value. Generally, growth investors hold a stock until the price seems to have peaked or is on its way down, while value investors take profits when the gap between the intrinsic value and the current market value of the stock closes, or reverses. It is up to each individual investor—taking into account such factors as time horizon, risk tolerance, and sources of income—to decide which investment style or combination of styles best fits his or her investment strategy.

Growth Investing—Fundamentals



Growth stock investors seek companies that show consistent earnings and sales growth, usually 25% or more each year, for a three- to five-year period. Typically, the companies represented by these stocks are in rapidly expanding industries or they offer proprietary niche products or services, have well-known brand names, strong finances, and top managements. They have superior profit margins and generally high (over 15%) return on shareholders equity. They almost never pay dividends, preferring, instead, to plow earnings back into the company.

Growth stocks come in three sizes, which are typically determined by the amount of their sales. Large-growth companies, with sales over $1 billion are the blue-chip growth companies. Medium-sized growth companies, with sales of $500 million to $1 billion, are the up and comers. Small-sized or emerging growth companies have sales below $500 million.

Size is important to growth stock investing. Stocks of smaller companies are considered the fastest growing segment of the growth spectrum. However, they are also the most risky since their market positions and products are often not well established and their capital structure may not always be sound. Small company stocks may not be suitable for investors with low risk tolerance.

Growth Investing—Key Indicators

Two key indicators of growth stocks are **share price** and **earnings**. Earnings, or specifically, the earnings growth rate is generally the more important of the two indicators for growth stock investors. It is the rate at which profits grow from year to year. Generally, growth stocks should have an earnings growth rate over 25%. There is no upward limit to the rate of a "hot" company's earnings growth. Consistency is also critical. Investors will not place as high a value on a company whose profits are up 40% one year and down 10% the next, as on one that grows 25% year after year.

The way earnings are determined is an important factor in this equation. Companies are prohibited by the Securities and Exchange Commission (SEC) from forecasting their own earnings. Investors must rely on independent earnings estimates generated by securities analysts.

The other key indicator for growth stock investors is stock price relative to the earnings or **price to earnings (P/E) ratio**. The P/E ratio, which is found by dividing the current share price by the earnings estimate, tells what the market is willing to pay for a share of the company's earning power. Many sources of investment data use the last four quarters of earnings to calculate the P/E. This is a "trailing" P/E, and it indicates where the company has been, not where it is going. A better yardstick may be an estimate of the earnings for the current year or for the coming year.

Although a growth investor may be willing to buy a company sporting a high P/E ratio, some relative guidelines should be considered. Ideally, the P/E should be lower than the earnings growth rate, for example, a growth rate of 45%, selling at a P/E of 30%. It is also a good idea to look at a stock's P/E in relation to the average P/E for its industry and relative to the market as a whole.

continued on page three

continued from page one

play in the firm's success. In this atmosphere, it is much easier to tap your human resources and develop strategies to accomplish your goals.

- **Humility.** While leaders benefit from having confidence in their abilities, arrogance can have an eroding effect on morale. In contrast, humility cultivates respect and fosters an environment where self-interest takes a backseat to shared objectives, where one person's accomplishments are everyone's success.
- **Integrity.** It is easier to motivate people when they trust your motives. One of the best ways to lead is by example, holding yourself to the same standards you set for others. People tend to thrive when they feel supported, when they feel you are rooting for their success rather than waiting for their failure. Make a concerted effort to acknowledge the contributions of others, maintain a consistent sense of fairness, and take responsibility for your actions and decisions.

Leadership styles vary, and successful strategies will run the gamut from firm to firm. The challenge often lies in recognizing and addressing the psychological aspects of the workplace. Energizing and mobilizing the people in your practice with strong leadership will inevitably have a favorable impact on profitability and growth.

As a strong leader, you can enhance both commitment and performance, as well as define the work culture of your practice.

THE ONGOING DEBATE: GROWTH VS. VALUE INVESTING

continued from page two

Value Investing—Key Indicators

The most important characteristic for a value investor is also the P/E ratio. However, unlike the growth investor, a value investor typically buys a stock that has a P/E ratio substantially below that of the general market, the relevant industry, and the earnings growth rate. Value investors also look for companies that are cheap relative to their "book value." Book value is the difference between a company's assets and its liabilities. It is theoretically the value of the portion of the company represented by a share of stock. Book value divided by the current market price, or price to book, shows the multiple that the market is willing to pay for a portion of the company's assets.

Generous dividend payments, or a high yield, are also important to value investors. A value investor expects the price of a stock to rise to its true value, a predetermined target. When the target or the "appropriate" value is reached, a real value investor will sell that stock and look for another one that is selling at a discount.

While there are some who favor growth investing and others who favor value investing, there are investors who use both styles in their portfolios. The best strategies for *your* situation will depend on your risk tolerance, time horizon, and investment objectives.

Note: Stock values will fluctuate due to market conditions; shares, when redeemed, may be worth more or less than their original investment. Profits and protection against losses due to declining markets are not guaranteed.

The Art of Giving—Donor Advised Funds vs. Private Foundations

When you give $100 to your favorite charity, you are probably not concerned about how your donation is spent, as long as it advances the general mission of the charity. On the other hand, if you are making a large donation, it is likely that you have more specific goals in mind with regard to the use of your money, whether it's to fund a particular program, building project, or other endeavor. However, satisfying this desire for control without jeopardizing the ability to claim an income tax deduction requires proper planning.

If you want more control over how your donation is used, then consider either **donor advised funds** or **private foundations**.

Donor Advised Funds

Many larger public charities, particularly those that support a variety of different charitable activities and organizations, offer donor advised funds. This type of fund is an agreement between the donor and the charity that the charity will consider the wishes of the donor with respect to the ultimate use of the donor's funds. However, the agreement is non-binding and the charity must exercise final control over the disposition of the funds, consistent with the charitable purposes of the organization. In some cases, the donor can name someone in the family to give direction after the donor is gone.

Private Foundations

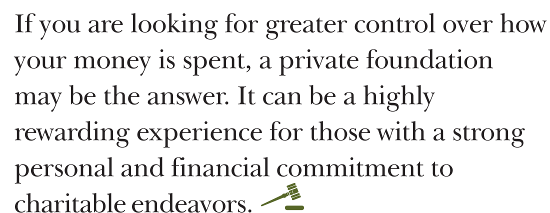
A private foundation may be a better choice for donors who don't want to rely on the ultimate discretion of a public charity regarding the use of their contributions. This is particularly true when substantial contributions are contemplated and the specific charities have not been determined. Because the board of directors or trustees of a private foundation are determined by the donor, a private foundation can also serve as a "family enterprise," where members of the family can participate together in supporting charitable causes over the long term.

The benefits of increased donor control through the use of a private foundation come at a price. There are a number of rules designed to ensure that private foundations serve charitable interests and not private interests, such as:

- Private foundations are generally required to pay out for charitable causes at least 5% of their asset value annually or be subject to a penalty.
- Substantial penalties are imposed on transactions between the foundation and its donors or managers, although payment of reasonable salaries is permitted.
- Private foundations are generally prohibited from benefiting a private individual.
- A private foundation is responsible for making sure that the funds it distributes to an organization that is not a public charity are expended properly.
- An excise tax of up to 2% of investment income is imposed annually on investments.
- There are restrictions on the types of investments that a private foundation may make.

The deductibility of contributions to private foundations is somewhat more limited than for gifts to public charities. Depending upon whether cash or property is being donated, deductions to private foundations are limited to 20% to 30% of adjusted gross income, whereas deductions to public charities have higher limits of 30% to 50%.

If you are looking for greater control over how your money is spent, a private foundation may be the answer. It can be a highly rewarding experience for those with a strong personal and financial commitment to charitable endeavors.



Information in this brochure has been obtained from sources believed to be reliable, however, AXA Advisors and AXA Network do not guarantee the accuracy of this information and are not responsible for any errors or omissions for the results obtained from the use of such information.

GE-29008 (7/04)

Financial Statements is published by Liberty Publishing Inc., to help keep you up-to-date on the issues which may affect your financial well-being. For specific advice on how to apply this information to your particular circumstances, you should contact your insurance, legal, tax, or financial advisor. AXA Advisors and AXA Network do not provide tax or legal advice. Printed in July, 2004.

Copyright © 2004
Liberty Publishing, Inc.