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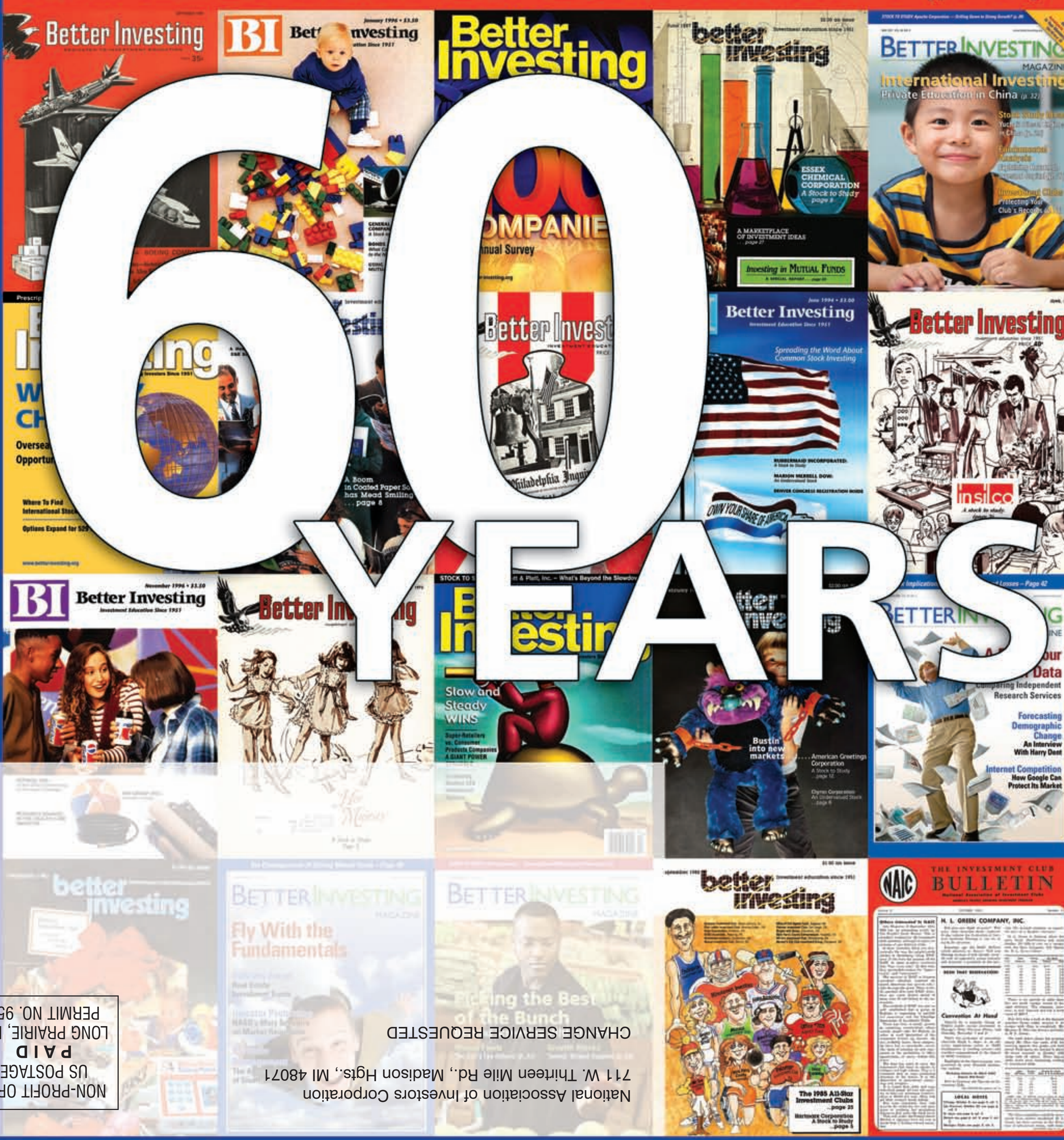
# BETTER INVESTING MAGAZINE

## REFLECTIONS ON OUR LEGACY (p. 36)

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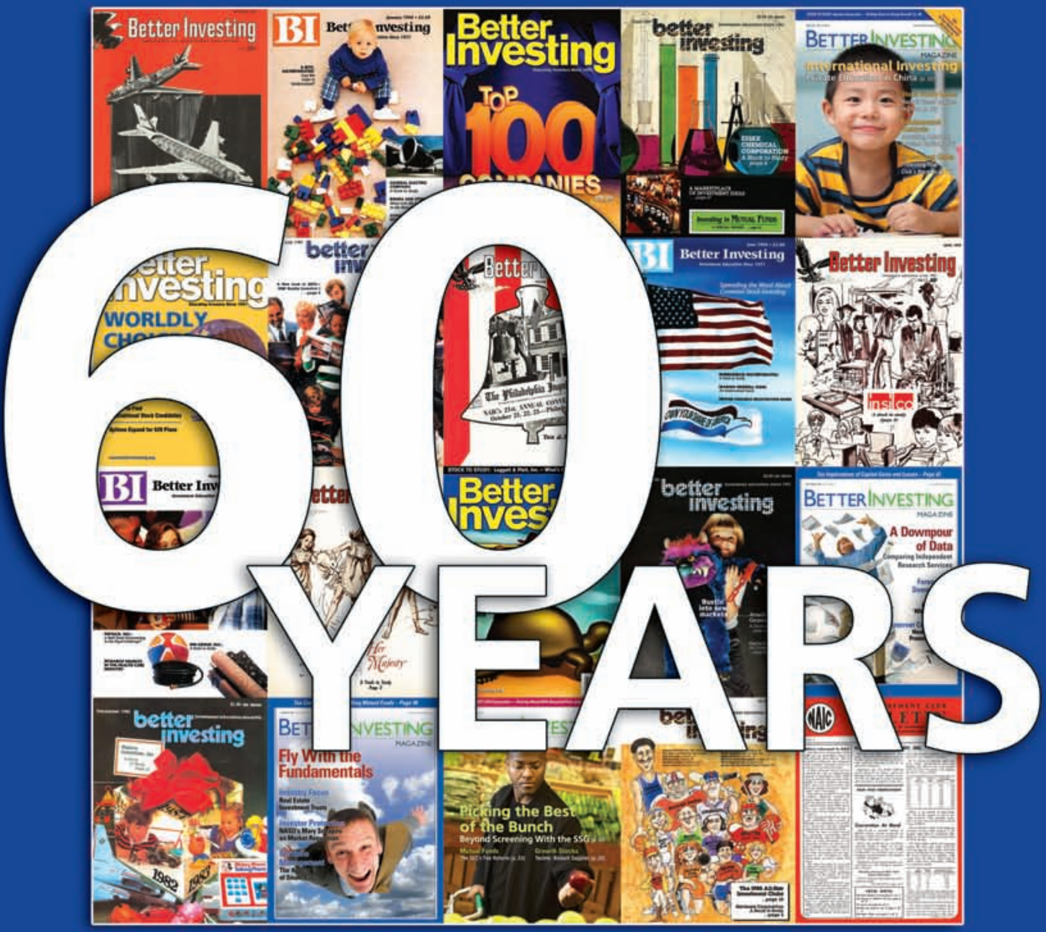



# Reflections On Our Legacy

by Adam Ritt, Editor, *BetterInvesting Magazine*

**This fall BetterInvesting celebrates its 60th anniversary. From its quiet beginnings in Detroit in 1951, the association has educated more than 5 million people about the benefits of shareownership. And who knows how many more people have been touched by BetterInvesting's ideas — the children, friends and family of these 5 million, or others who have been inspired after reading about BetterInvesting or its members?**

At its core, the story of NAIC/BetterInvesting is about the spreading of a simple message: That anyone with the passion, perseverance, long-term perspective and right information can build wealth and secure their financial future. We don't need experts or any special gifts to accomplish this; we have all we need already.

So much of what makes BetterInvesting special hasn't changed over these six decades. This month, in the limited space we have, we'll briefly discuss just a few of these ideas.

And in the coming months we'll make available on our website various articles and documents for your enjoyment, beginning this month with the association's first publication from Sept. 10, 1951 (*see the end of this article*).

Then, as just one example of the sort of education BetterInvesting has provided over the years, on page 39 is the continuation of our fond tribute to Mr. NAIC. Finally, on page 40 we'll detail the volunteers — so critical to the association's mission — honored at this year's BetterInvesting National Convention.

Nowadays many of us tend to take BetterInvesting's central idea — that we can all have ownership of businesses via holding shares of stock — for granted. We all have a common goal of growing our portfolios and taking care of ourselves and our families.

But the association's co-founder, George Nicholson, had even bigger thoughts. Spreading free enterprise and capitalism around the globe was a lifelong passion.

His articles in the magazine, though sometimes focused on particular investing strategies, portfolio management practices and individual equity analysis, often discussed world political and economic issues and the need to bring free enterprise to other regions.

He experienced the Great Depression and World War II and envisioned a better world, not just that of the United States but around the world, through the widespread ownership of business.

If most families owned common stocks, he reasoned, they could better realize the benefits of capital markets and help argue for free enterprise. And in fact, we have seen this scenario play out over the decades.

In Nicholson's view, the idea of free enterprise best incubated in investment clubs. The investment club would operate under a set of common principles focused on success over the long term and provide education to its members.

Clubs were a way to "mass-produce" educated lifelong investors — quite an appropriate idea for a lifelong Michigander.

The impact of investment clubs is incalculable. They made studying a stock so much more manageable. With the necessary financial information squirreled away in physical copies of annual reports and Securities and Exchange Commission documents, obtaining the data was a lot of pick-and-shovel work. (In fact, newspapers often acquired shares of companies so that they could receive these reports regularly.)

With your fellow members you could discuss trends in the data and bounce new ideas off one another.

**A Believer.** BetterInvesting co-founder Tom O'Hara was convinced anyone could make money through regular investing and careful selection of growth stocks.

You could share important education. You could also share the risk (and rewards) as you honed your judgment and made investments in personal accounts.

Perhaps most importantly, your fellow club members could be a support system for times when the market wasn't cooperating with your portfolio. Members could remind one another of the benefits of investing regularly and being able to buy more shares of quality companies when prices were lower.

You need go no further than the initial club in the modern-day investment club movement — the Mutual Investment Club of Detroit — to see what a club can do given perseverance and discipline to withstand a bad decade or two. When Norm Hill, one of the original members of the club, passed away in 2005 at age 88, his value in the club had grown to $1.7 million. The amount invested: about $14,000.

This wasn't accomplished by magic. This was simply the investment club's principles at work along with the miracle of compound interest and a single-minded determination to make investing a priority. Hill told *BetterInvesting* that his philosophy was: "It wasn't my money. I had already spent it.…Cancel one of your trips. Cancel a dinner out and put the money into a stock. Spend your spare money on stock instead of the other stuff you can do without and still be happy."

With the encouragement and guidance from Nicholson, the Mutual Investment Club of Detroit set an example countless thousands of clubs would follow.

Few would have the good fortune to begin at a nearly ideal time, as the Mutual Investment Club did in 1940, and have the opportunity to amass shares before the market began an epic rise in the 1980s. But we've seen many clubs, such as the Beardstown Ladies, thrive and doubtless inform the successful personal investing decisions by their members.

Today's investment club is no longer a self-contained unit. Many of the club's most important functions have shifted to other channels.

For example, the work required to gather information has significantly declined to a few keystrokes, and the time required has dropped from days or weeks to seconds. The association has made it even easier by arranging to make all the necessary data (along with lots of supplemental information) available on a moment's notice.

The support system has enlarged to include not only fellow club members but also friends, acquaintances and perhaps complete strangers who exchange information using e-mail, message forums and social networking sites. Over time we've come to recognize that there aren't only individual clubs but one large BetterInvesting "club" that can provide support.

And many of us find this support amid the volunteer community. When home office staff members share with others outside the BetterInvesting community, whether it be government agencies or media outlets, how involved our volunteers are — from providing top-shelf webinars to organizing the national convention — we're always reminded how lucky we are to have them.

The dedication and concern for our members is incredible and unique in an investment industry dominated by mercenaries and hidden agendas.

Our volunteers are torchbearers for George Nicholson's and fellow co-founder Tom O'Hara's mission to create a nation of educated investors, and the volunteers' passion is what gives the association's principles their credibility. (Remember that Nicholson himself could be considered the original volunteer for the association.)

Many of the new programs, services, resources and tools BetterInvesting has offered over the years have been developed by volunteers. Few organizations can claim such a history.

Another important aspect of investment clubs, the ability to participate in the stock market by pooling money, has undergone changes.

In the late 1970s the association, in response to an increase in commissions that hurt individual investors, put together its Low Cost Investment Plan to help anyone build a portfolio at a very reasonable price.

This trailblazing program today is replicated throughout the investment community in the form of extremely low (and sometimes nonexistent) brokerage commissions and sites dedicated to easy participation in dividend reinvestment and direct purchase plans.

And what of our main investment tool, the Stock Selection Guide? The times might change, but this tool's legacy will endure.

When introduced to members, the SSG served as a way for them to arrange financial data they needed to seek out (and input using pencil, paper and ruler).

It provides a quick way for those of us with families, jobs and precious little time to determine whether we're looking at a high-quality company whose stock is selling at a reasonable price.

Today the form is much the same as it was many years ago, but now our emphasis is on keeping unnecessary information out, not getting the required information in.

**Getting the Word Out.** BetterInvesting co-founder George Nicholson dreamed of spreading free enterprise and capitalism around the entire world.

Whereas before we worked to obtain financial information, today we are bombarded with it and given countless ways for using it for analyzing equities.

And how many of these metrics supersede the SSG's emphasis on sales, earnings, profitability and stock valuation?

That isn't to say that we don't all develop our own additional analysis points. Ken Janke, for example, once told me that he always found that a low Timeliness rating on Value Line was an excellent time to invest.

But no matter how you cut it, fundamental stock analysis still comes down to sales, earnings, profitability and valuation.

There's no shortage of analysis tools that promise to make stock selection automatic, but the SSG has always reminded us that although only a few data points are critical to understand, analysis is never cut and dry. It remains as relevant as ever in keeping us focused on what's really important.

The SSG also has led the way in keeping Main Street investors attuned to the types of stocks they can most easily understand and benefit from acquiring.

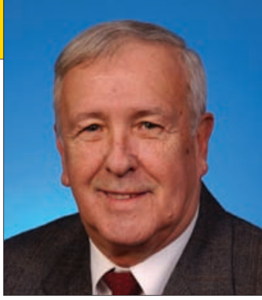
Although value investing as taught by Benjamin Graham is a valid, time-tested approach, for most of us finding appropriate growth stocks is an easier strategy. Despite the explosion in information since the 1980s, we still find it faster to identify a good growth stock opportunity than a value stock.

At a time when value investing was more common, George Nicholson and others (T. Rowe Price and David Babson, for example) understood the benefit of finding growing, well-managed companies. For most, this approach was a means to build portfolio values.

For Nicholson, Tom O'Hara, Ken Janke and many others who have volunteered their time to the association, however, it meant much more than that. And today the mission remains as important as ever. B

## Download Our First Issue

To commemorate BetterInvesting's 60th anniversary, we invite readers to download the association's first publication. You can use a smartphone and scan the accompanying QR code (you can find free QR code reader apps easily through the Android and iTunes marketplace) or go to the following URL: http://www.betterinvesting.org/NR/rdonlyres/851E00B6-69F2-4A2C-ABAD-AF41564CF680/0/firstissue.pdf. Keep your eyes out for additional documents and articles throughout the year.



Timeless Wisdom

# The Pressure to Sell at Year's End

from *Ask Mr. NAIC,* by Kenneth S. Janke, Sr.

*Ken Janke's columns, including "Ask Mr. NAIC," helped millions of investors understand club operations, the SSG and sound investing principles. Here are some examples. In the first question, note that there have been changes in tax law since this was published; see "Tax Planning for Carry-Over Losses" (September issue) for more up-to-date information and consult a tax professional.*

## Would you please explain tax selling to me?

A If you are holding a security in which you have a loss, you can sell that security and establish a capital loss which you can apply against taxable capital gains and against ordinary income up to $1,000 and thereby reduce your taxable income.

Some securities become quite susceptible to tax selling every year. For instance, if quite a few shares of a security are sold, and its price goes down rather than up, some of the purchasers will sell it within one year of the time they bought it in order to establish a short-term capital loss. Others will sell it before the end of the year if its price has not recovered.

Tax selling can be quite a factor in the price of some stocks and may tend to depress their prices in the latter part of the year. These are usually stocks which have had a bad experience and gone down in the early part of the year.

When a stock has been subject to tax selling in the latter part of the year, its price sometimes advances sharply at the beginning of the new year just because the tax selling pressure is gone. When some individuals sell a stock to establish a tax loss, they try to find another stock to put their money in that seems to have a greater chance to recover. Some individuals just switch to another stock which they see is subject to tax-selling pressure and expect it to recover when that pressure has been removed.

Some individuals, if they feel they want to establish a tax loss but continue owning the same security, will sell it before the last couple of months of the year, reasoning that tax selling pressure will peak in November and December and that they can buy it back then at possibly even a lower price than at which they sold it. In such cases, the buyback cannot be made until 31 days or more to qualify for the tax loss.

Tax selling may save you money this year, but be sure to check the amount of tax you are saving against the cost of changing stocks.

"Tax selling can be quite a factor in the price of some stocks and may tend to depress their prices in the latter part of the year."

## In the *NAIC Investors Manual* there is suggested limiting a projection for the next five years even if the company is growing at 35 percent a year. Why? It's not sound mathematics.

A Mathematics is an exact science. Investing is not. The reason we suggest limiting the projection is simply that it is very difficult for any company to maintain a rapid rate of growth over a prolonged period of time. Even a very small company with $5 million in sales would have to reach sales of more than $22 million in five years to maintain a 35 percent compounded growth rate.

Historically, companies with very rapid growth rates have demanded higher price-earnings ratios than those with more modest records. When the growth rate slows (I don't mean going down, but increasing at a decreasing rate), the P/E ratio will usually drop. There can be more money lost by P/E ratios dropping than by earnings dropping, as we can all testify has happened in the last couple of years.

Some people limit projections to 20 percent. I like to limit my projections on the NAIC Stock Selection Guide to 15 percent and am sometimes hesitant to go that high.

## Can you tell me a little about book value?

A The book value of a corporation as a guide to the value of its stock may or may not be significant. There are cases where a growing, profitable company has a high book value in relation to the price of the stock and there are also cases where a weak, unprofitable company may have a high book value in relation to its stock price.

When you see high book value in relation to the stock price, it should alert you for further study. If you then find that the company has a record of steadily increasing sales and earnings per share, if it has a record of pre-tax profit margins that are equal to or better than competitors and that earnings on investment capital is equal to or higher than competitors, then you may have a bargain.