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Record Dividends and Buybacks: Happy Holidays to All!

Even better than visions of sugar plums is seeing companies you own return wealth to you, and 2005 has been a year of unprecedented dividend and stock buyback activity.

The Wall Street Journal earlier this month noted that S&P 500 companies are on pace to pay more than \$500 billion in dividends and repurchases of their own shares this year, over 30% more than 2004's record. While both methods of "returning wealth" may seem like unalloyed benefits, let's take a few moments to note how they differ.

In my mind, it comes down to one question: *Who winds up with the cash?* With dividends, it's pretty simple — you do, though so does the government to a lesser extent (assuming a taxable account).

With share buybacks it's more complicated. Transactionally, the counterparty selling shares back to the company gets the cash (and again, so may the government), which on the face of it hardly seems to benefit remaining shareholders. Strictly interpreted, it's less a return of cash to investors than it is to *disinvestors* insofar as it facilitates their unloading of company stock.

The countervailing argument is that reducing the number of shares outstanding increases the remaining shareholders' proportionate interest in the future cash flows of the company without triggering taxes currently, and indeed this is a good thing if the buyback price is cheap relative to underlying value. If you had been wanting to own more of a company anyway, buybacks are great... they represent a sort of tax-free compounding. The key is that the repurchase price has to be good, which is by no means assured. With buybacks, you're relying on management's market timing ability.

It's also important to recognize when share buybacks are being used to neutralize the effect of stock option issuance and exercises by insiders — in which case your cash is covering employee compensation, i.e. it links *de facto* albeit indirectly to a real expense. So, while the headlines surrounding the announcement of buyback intentions may be celebratory,

footnotes to the financial statements may tell another story.

The upshot? To us, dividends are emphatically a good thing, albeit with a regrettable leakage of cash to pay taxes. Share buybacks can be good, though it depends on the details. And both are better than companies' management teams staying so awash in cash that they lose operational discipline or get tempted into misadventure (e.g. bad acquisitions).

Allen Capital Management

In 1999, Stuart Allen started Allen Capital Management to provide investors an independent, local alternative to the big Wall Street buy-side firms and commissions-motivated broker-dealers. With the founding of Allen Trust Company, however, he moved all asset management activities under the ATC umbrella so as to make a virtue of simplicity, maximize operational efficiency, and avoid confusion on the part of our clients.

With our growth and success, however, have come more sophisticated processes and firm resources. Accordingly, we're bringing Allen Capital Management back to daylight so as to broaden the service options we can offer you. Next month, Stuart will be writing to tell you more.

Listen to Helen!

Whether you know Helen Robinson as the bright, cheery voice on the other end of the phone line when you call us, or as the seasoned operations pro who can make things happen no matter what the administrative hurdles may be... you know she means business. So listen up!

Helen says now is an excellent time to confirm that your beneficiary designations are current on your IRAs, annuities and life insurance policies. Sometimes the big banks and insurers inadvertently cycle older beneficiary designations off their systems, with potentially dire consequences for your estate plans. Check directly with the issuers or IRA custodians to make sure this hasn't happened. For accounts or assets we manage on your behalf, we keep these designations current — just contact us if you want to change them.

Firm News

Bill Harris has joined the board of the Portland Children's Museum, a beloved institution "Where Imagination Lives" and the oldest of its kind west of the Mississippi. Allen Trust is proud to support Bill in this leadership role in keeping our community vibrant for children, parents and grandparents alike.