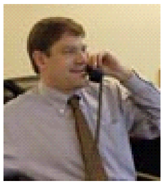

William A. Harris, CFA
Portfolio Manager

Why We Own Stocks

Last month I likened stock equity ownership to "dibs" on an uncertain portion of leftovers. This past week, Merrill Lynch illustrated the point by issuing 380 million new shares to raise $8.5 billion, diluting existing shareholders' claim on future earnings by more than 25%. Sure enough, the credit drama ain't over yet, and we're seeing vividly how equity's residual interest can end up looking like, well, mere residue.

Given such risks, why do we own stocks?

Some reasons you've likely heard before:

- Historically superior long-term returns (10.4% compounded annually since 1926)
- Diversification from other asset classes (imperfectly correlated risky assets are less risky in combination than they are alone)
- Preferable tax treatment (15% Federal rate on long-term appreciation, which has provided the bulk of stocks' total return historically, as well as 15% on dividends)
- Dividends and ownership of assets that alike can grow to ward off inflation

While these factors are all part why we own stocks, not one is sufficient by itself, for the future may not rhyme with the past, correlations can rise when times get hard, and tax rates will change.

Perhaps equity's greatest virtue is that unlike other asset classes, it conveys ownership of something potentially adaptive, something almost organic. When you buy bonds, you are lending money, and your upside is capped by the terms of the indenture. When you buy commodities, you're claiming something perishable, consumable, or inert. When you hold cash, you are abjuring – at least temporarily – participation in enterprise. But if equity's essence is that of residual claim, so too is equity the *essence* of enterprise.

Unlike those other asset types, stocks are more than just robust to change, they depend on it. When change brings profit, dividends can grow, and retained earnings can be plowed back into operations to compound equity's interest. When change brings challenge, equity ownership is what motivates adaptation, because equity is ever the most endangered. Its fate is not fixed by indenture, or by biology, chemistry or physics. Altogether, equity's existence is predicated on transformation, the evolution of systems and processes… in a word, improvement. And when improvement is delivered handsomely, the residual benefit evolves from a prospect for cold dinner scraps to outright ownership of the dessert cart, plus right of first refusal on the meals that follow.

When you get down to it, my explanation for why we own stocks is one which may surprise readers accustomed to my dour prognostications: We are optimists. And stocks are how optimists ride eventually to triumph. Change is inevitable, and given enough time and consistent standards of law and human behavior, change will be good, though it may hurt like hell along the way. So…

Rule #1? Survive. All the asset types contribute here, each in ways the others can't.

Rule #2? Make sure you <u>own</u> the benefits of survival in the fullest. Stocks are how you do that.

William A. Harris, CFA

Firm News

Carrie Nobles, CTFA, has just joined the ATC trust management team. Formerly Vice President at SunTrust Bank in Nashville, she brings 17 years' experience as a trust officer, plus prior work in venture capital and NASD compliance. Welcome, Carrie!

Also, assistant portfolio manager Monica Poveda has passed Level I of the Chartered Financial Analyst program. Congratulations on all your hard work bringing success, Monica!