The Mallard Message

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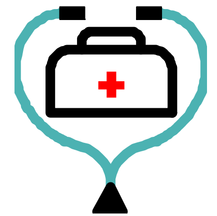
Frequently Asked Questions

1. **Do you have a minimum account size?** My minimum quarterly fee for ongoing clients is $250. Since my fees range from 0.7% to 1.0% annually, it makes more sense if your portfolio is $150,000 or more. In this manner the percentage applies rather than the $250 minimum. Most accounts are more than $250,000.

2. **You are Fee-Only™. What does that mean?** Fee-Only™ is a method of compensation, and can best be understood in relation to its opposite, commission-only. Let's consider a medical practice. If your doctor visits were always free, but if you were required to use the doctor's pharmacy and clinic, at which he took a 10% cut, he would be a commission-only doctor. His income is completely determined by selling you products and procedures. If instead all of his income comes exclusively from his patients, then he is Fee-Only™. Would you be comfortable with a commission-only doctor? Or would you fear that he might prescribe more or different medication and procedures than necessary, in order for him to earn more income? While a commission-only doctor may appear less expensive initially, patients should ensure that they understand the full costs, and that the recommendations are not affected by the conflict of interest that commissions introduce. This is the reason that I have always been Fee-Only™.



Summer Plans

I typically take long weekends during the summer, sometimes taking off Friday, sometimes Monday, and sometimes both. I will be going to the beach, camping near the Poconos, and hiking in Colorado. I am likely to visit a client in New England, and may go to a conference in Denver. These last two trips are likely to involve several weekdays in August. Whenever I am out of the office for more than one day, I check my messages and return all urgent ones.

Inside This Issue

2	Y2K—Mallard Steps	3	Recent Activity
2	Y2K—Steps for You	4	Internet Update
3	Euro-Land Prospects	4	Conferences Report

Year 2000—What is Mallard Doing?

Six months to go! In the past quarter I upgraded my main computer: the motherboard, processor, and operating system, Windows 98. I also have upgraded the Advent portfolio program that produces performance and position reports, and the QuickBooks accounting software. I have two other PCs that can backup my primary computer in case it dies on January 1st, or anytime.

In the next three months I will again run diagnostics tests on my computer systems, using the Check2000 PC Deluxe package. This summer I will collect information on the Y2K status of my 'mission critical software'. I will do this by contacting the companies or their websites. The software includes Microsoft Office, Advent portfolio management, QuickBooks, ProTracker client management, and investment programs from Morningstar and Value Line. I will also collect this type of information on my online services: Concentric internet service, online trading from Waterhouse and Vanguard, and data download from Advent. This information may not prevent all problems, but it will minimize them and should enable me to resolve any problems that do occur in January more quickly.

Mallard can not become Y2K-safe in 1999. No matter how well I research and upgrade my software, I can not guarantee that my phone system will work during the first week of January, nor that the US mail will successfully pick up and deliver mail. I don't know whether my office building will have electricity. I therefore do not profess to be Y2K-safe. Rather, I assert that I have taken proper precautions, and will be prepared to aggressively deal with each problem that surfaces in January.

What if January turns out to be a disaster, with phones, mail, electricity, and the internet unreliable, and with financial institutions in distress? I will be very upset if I can not reach my clients and they cannot reach me. My blood pressure rises each time my internet connection is dropped! Fortunately, I have great clients who know how much I value them.

I will implement a **three step plan for early January**:

- First I will do everything possible to restore communications with my clients as quickly as possible (even for my clients living overseas).
- I will next identify and work to resolve any and all administrative problems with clients' investment accounts.
- Then I will determine whether any investment changes are warranted.

Year 2000—What Should You Be Doing?

At home I have done limited Y2K preparation. As I mentioned in the last newsletter, we will try to obtain at least a month's worth of **ongoing prescription medication**. I have tested the **Y2K status of our home desktop systems**. As with work, I am likely to sign up for a **second internet account**, in case Concentric runs into problems. Since we already track our home finances very closely, I am confident that we will have **paper records** handy should billing errors or statement errors crop up in January.

I have not purchased a **generator**, although I will likely let our freezer inventory run low in December. I don't want to lose much food should the electricity disappear for a day or two (or seven). Can you imagine what would happen if a severe ice storm hits on December 30th or 31st? Brrrr.

I do plan to have a **full tank of gas** in each car, have two to four weeks of **cash in hand**, a few gallons of **spring water** by December 31st. I plan to celebrate New Year's Eve like normal, and maybe sleep late on New Year's Day. I expect to be **working hard during the first two weeks of January** at the office, handling whatever comes my way. I reserve the right to hand-write my 4Q99 reports to my clients, and hand-address envelopes. I will likely send my December newsletter one or two weeks early.

I have not changed my investment approach purely due to Y2K fears. However I am cautious at this time, and have kept my US stock allocations a bit low, investing the difference in money markets and very short term bonds. If US stocks tumble in late 1999/early 2000, I plan to be a buyer for my clients and myself.

I know that some people are so concerned about the impact on stocks that they are selling their stocks for this reason alone. So far none of my clients have requested that we consider this. While this approach may avoid painful losses, in many cases it would cause you to incur additional income taxes. Should the markets not fall much, or at all, or should the markets fall in August and begin their recovery in December, you could miss 'getting back into the market'. I would rather trim my sails and hold on tight.

Euro-land: Promise or Peril?

My clients have a lot invested in Europe, in mutual funds, European stocks, and in the stocks of US companies that do business in Europe. I therefore took the opportunity to attend two sessions on European investing at the NAPFA conference I recently attended in Washington DC. The first was offered by Dr. Scott Chambers of Linfield College, who was recently a Visiting Fellow at a British business school for a year.

The EMU is not a bird, but rather the European Monetary Union. It currently consists of Austria, Belgium, Finland, France, Ireland, Italy, Germany, Luxembourg, the Netherlands, Portugal, and Spain. Four 'common market' countries are not members: Greece did not qualify, and Denmark, Sweden, and the UK chose to not join.

As of January 1, 1999, there is a fixed exchange rate between the local currencies and the new currency, the Euro. The local currencies include the German mark, the French franc, and the Italian lira. There is a central bank, similar to our Fed.

The countries in the EMU produce 25% of the world's goods, have twice the level of government spending, and twice the unemployment rate of the US. Most of the goods are produced in Germany, France, and Italy.

Dr. Chambers covered several potential problems, including the two-year implementation schedule, rigid labor markets, cultural differences, and political intrusion. One example is that while Ireland is growing rapidly, it can not raise interest rates to slow this down (that is for the EMU central bank to decide), and while unemployment is very high in Italy, unemployed Italians are unlikely to move to Ireland for jobs.

Italy is currently in violation of some of the EMU guidelines, and has to make progress to fix this or else it could eventually be kicked out of the EMU. There is a risk that French or Germany voters could get fed up with decreased government spending (to abide by the Euro guidelines), and would boot EMU-friendly politicians out of office. The withdrawal of either of these two countries could cripple the EMU.

While Dr. Chambers spelled out several risks, he feels that the EMU has good chances of succeeding. He sees signs of companies becoming more competitive, with each other and with US companies. EMU companies' management is becoming more shareholder-friendly. Europeans are beginning to follow our lead in investing more into stocks. Fifteen years after us, Europe is beginning a transition from 'defined benefit' to 'defined contribution' pension systems (do you remember when 401Ks were introduced in the early 1980s?).

The second session was led by Scott Weiner, a fund manager with Payden & Rygel, specializing in international bonds. He was very positive about the prospects in Europe. He considers the US to be doing quite well, Europe to be so-so, and Japan to be a basket case. He believes, as do I, that it will be difficult for the US to surprise us in a positive way from the current status. Europe, on the other hand, can surprise us in many ways. He does not expect a sustained Japanese recovery anytime soon.

He noted that the Euro has declined 11% in value versus the dollar since January 1st. He attributes this to the Kosovo crisis, and lower growth and short-term interest rates in Europe (versus the US). He sees opportunities in EMU countries, and in countries that join in the coming years.

Three Month Activity

In this section I review several large transactions over the three months ending June 15th.

Mutual Funds—This was a time for bond activity. I added to Vanguard Intermediate Term Corporate and began using Fremont Bond. I continued using Hotchkis & Wiley Short Term, an ultra-short term fund. I purchased more of the closed-end Latin Discovery fund, as the Emerging Mexico fund liquidated.

I eliminated Strong Short Term Bond and reduced the Vanguard Index 500 and Vanguard International variable annuity fund for asset allocation reasons. In one account, I wanted to reduce Cohen & Steers Realty due to asset allocation goals. However I waited until it had recovered, and made the sale in early June.

Bonds—I purchased $180,000 of bonds, primarily municipal, and $55,000 of a CD. I sold one bond to raise cash for investment, and two other bonds matured or were called.

Stock Purchases—I purchased TECO, a utility stock, and my favorite pizza chain, Papa Johns.

Stock Sales— I reduced several large positions: Applebees, DuPont, GE, Keystone Financial, Mobil, Providian, Safeguard Scientifics, and SONY. I closed out NPCI International (a Pizza Hut franchisee—I swapped it out to purchase Papa Johns). I turned in shares of US Filter, which was bought out. All sales were long-term except for US Filter, where the stock had risen more than 50% in less than 6 months.

I also mentioned Providian in the last report. In March I sold shares for $114, and in April I sold shares for $125. It subsequently tumbled down to the low 80s. While we only sold one-third of the shares, due to the very low cost basis, at least we dodged the bullet a little. Fortunately, it has recovered a bit, to $97.

Net Gains and Net Losses

Last time I wrote about how most of us already invest in internet stocks, and what you should consider before increasing your internet investing. Not surprisingly, within two weeks the internet stocks appeared to peak, and in the subsequent four weeks many had dropped 50%. As a die-hard value investor stuck in a growth-world, I couldn't take it any longer. I contacted a few clients who had expressed some interest, and asked them whether they, too, felt that a 50% drop was enough to warrant a closer look. One took me up on it, and another two had already purchased shares of an internet fund.

Yahoo rose 46% in the first half of the year. While that sounds great, the chart shows that the experience has been anything but smooth. By January 11th, it had risen 76%, the other 170 days can only be described as a white-knuckle, roller-coaster ride.

Yet I am encouraged by this recent volatility. What troubles me is when investors believe that there is a free lunch. Typically the longer these periods of invincibility last, the deeper the subsequent drop.

In March many investors felt that they could not go wrong with internet investing. Can you blame them? In the first half of 1998 Yahoo rose 127%. In the second half it rose 198% further. By April 5th, Yahoo had risen 86% in 1999. Who could go wrong? Well, in the next nine weeks, Yahoo's dropped 45%.

I have no false illusions that Yahoo is fairly priced, or that internet investors are realistic. They have, however, suffered losses in the past quarter. This lesson should reduce the chances of another bubble such as we witnessed in the first calendar quarter.

Recent Conference

In early June I attended the 1999 National NAPFA conference in Washington, DC. This is the third NAPFA National conference I have attended. I attended sessions on technology in the office, client psychology, asset allocation, 'tax-aware investing', the European Monetary Union (see the article in this newsletter), real estate investing, behavioral finance (a very exciting field that combines psychology and investing), the Alternative Minimum Tax system, and value versus growth investing. I also took the opportunity to maintain and establish ties with investment advisors throughout the country. The Delaware Valley NAPFA study group recently hosted a session on asset allocation that was quite worthwhile.