

# J.L. BAINBRIDGE & COMPANY, INC.

◆ PROFESSIONAL MONEY MANAGEMENT ◆

## 2000 ANNUAL REPORT

### INVESTMENT RESULTS

For 2000, J. L. Bainbridge & Company, Inc. achieved a 16.9% rate of return on all money managed. In conjunction with 1994, 1995, 1996, 1997, 1998 and 1999 returns of 10.2%, 38.4%, 20.3%, 23.2%, 28.4% and 5.6% respectively, a January 1, 1994 investment of \$100,000 has grown to a December 31, 2000 value of \$362,507 which equates to an increase of 262% over the past seven years. The annually compounded return over the past seven years is 20.2%. These results assume reinvestment of dividends and are after transaction costs and our management fee.

### INVESTMENT REVIEW

The year 2000 was a tumultuous period which marked the end of the biggest speculative binge in history and the eventual return to favor of America's finest traditional growth companies. At its peak, the NASDAQ surpassed the 5000 level before reversing course and declining more than 50%. Conversely, our portfolio hit bottom in March and then climbed 39% by year end. Our return of 16.9% last year compares very favorably against the S&P 500 and the NASDAQ which fell 10.1% and 39.3% respectively. Our total return of 23.4% over the past two years is ahead of both the S&P 500 and the NASDAQ which had total

returns of 7.4% and 12.7% respectively.

Although the July, 1999 thru March, 2000 period of speculative fever was a difficult and frustrating time, we never considered joining the fray. Doing so would have put our clients hard earned money at risk and jeopardized their retirement standard of living. Be assured we will never break our pledge to clients that we will not speculate on short term market conditions and that we will never deviate from our philosophy to own only high quality proven growth companies and purchasing them only when the price is right. We will remain totally focused on achieving 15% annually compounded growth over each five year period and investing with minimal risk.

### INVESTMENT STRATEGY

Since 1984 we have presented our investment strategy as a disciplined, conservative program for "Building And Preserving The Wherewithal For An Enhanced Retirement." While this goal has always been of utmost importance to clients, with life expectancies increasing significantly its importance is growing every year. Accordingly this year's report will focus on this goal and our approach to meeting it over the upcoming decades.

In striving to achieve this goal, many investors make

the following mistakes which lead to failure:

- 1) Achieving a low investment return as a result of being overly conservative.
- 2) Incurring a permanent loss of capital.

The first mistake is usually due to either being too concerned about investment risk or the misperception that upon retirement one should invest most of their money for income to meet monthly expenses. In either instance the result is an after tax and after discounting for inflation return of at best one or two percent annually. Hence the risk of this approach is outliving ones assets and facing a substantially lower standard of living. Note that income is not the only source of funds for monthly expenses. These needs can best be met with a combination of interest, dividends and capital gains. For our retired clients, we retain a cash reserve for monthly withdrawals and replenish this reserve by periodically selling a portion of their stock when the market is in an upswing.

The second situation, where a large portion of one's money is lost forever due to bad investments, also results in a substantially lower standard of living. Can you imagine the agony of being seventy, eighty or even ninety years of age and in good health and not having the money to live an active enjoyable life style? Therefore the dilemma for everyone is how do you get the growth return you need without running the risk of a catastrophic loss. In today's environment this is even more difficult than in the past because the market is much more volatile and the few stocks in vogue are selling at very high prices. During the past decade achieving a growth return was relatively easy, and in fact our return of 20% compounded annually was well above our 15% objective. However going forward we believe many investment programs will fail while our program will

continue to meet, but likely not exceed, our 15% objective. In short the difficult challenge facing all investors today is how does one achieve the growth required for a satisfying retirement in a paranoid market where the value of an investment can decline precipitously and permanently.

The answer is to purchase only extremely high quality companies and to make these purchases only when the price is attractive. In addition these high quality companies must have businesses that are understandable to the extent future growth is predictable with a high degree of confidence. With this approach a long term growth return can be achieved even though some holdings may decline dramatically due solely to market volatility. For example Avon Products fell 32% in 1999 due to a slight shortfall in earnings attributable to a drop in the value of the Brazilian Real together with investors' love affair with technology and the accompanying general disinterest in traditional growth stocks. Avon responded by using its strong cash flow to repurchase 7% of its stock in the last three months of 1999. This repurchase plus the continued high growth of their international business resulted in 46% appreciation this year. Because we understand Avon's business and their strategy to achieve mid-teens profit growth like the back of our hand, we never considered selling. We had complete confidence the price would recover and provide long term returns of at least 15% annually.

In the same vein, Gateway Computer declined 75% this year due to lower than expected earnings. Gateway is also a fine well managed company, but the recovery of its shares is uncertain because its price was extremely high and the future of the personal computer industry is uncertain. In addition a meaningful recovery of the personal computer market may

not result in much profit recovery if falling prices result in skimpy profit margins. Consider that millions of color television sets are sold annually but profits are minuscule. If a Gateway investor either sells at today's price or holds and the price does not recover, permanent loss of capital will have occurred. In order to build or retain the wherewithal for an enhanced retirement such losses must be avoided.

Another challenge is to avoid the short term mentality that is so prevalent today and focus on the long term. The quest for short term results inevitably causes one to switch from one stock to another, from one mutual fund to another or from one money manager to another. The result is a poor investment return. A logically sound, long term, conservative growth investment program is the only solution. While such a program will at times encounter periods when short term returns are below objective, patience and a long term commitment will provide the returns to meet retirement goals. J. L. Bainbridge & Company, Inc. developed its investment program years ago to provide clients a long term growth return with minimal risk. To provide growth only companies with proven records of many years of record earning of at least low teens growth are selected for investment. To provide low risk these companies must be extremely high quality financially with low levels of debt and substantial excess cash flow. To further reduce risk these companies are only purchased when their stock price is attractive and offers the potential for a return of at least 35% over the next year.

Finally our program is based on a thorough knowledge of each company's business, strategy and the long term trends that will drive future earnings. We do not own Gateway Computer because we do not know if the personal computer market will continue

to grow rapidly, will be replaced by new technology or will become a commodity with little profit like the TV and VCR markets. On the other hand we do know the globalization of markets will drive the sale of Avon's cosmetics in international markets around the world. The aging of the population will drive Johnson & Johnson's, Merck's and Pfizer's drug and health care sales. The aging population will also expand demand for Marriott's hotels because as people age they travel more often and stay at more expensive facilities. And the rapid advances in technology and the internet will expand profits at General Electric and McGraw-Hill by reducing costs and expanding markets to every corner of the world.

## CONCLUSION

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Finally in today's environment of rapid market swings accompanied by the constant hype of the media, it is important to realize the outlook for the United States economy is bright and its best companies' prospects have never been better. Participating in these companies' growth is the best way we know of to safely meet clients' needs. Consider 15% annually compounded growth increases \$125,000 to \$1,000,000 in fifteen years. Another example is a person retiring with \$1,000,000 in an IRA, starting with a withdrawal of \$80,000 and increasing this amount 4% a year, would after ten years be withdrawing \$118,000 a year and still have an IRA that has grown to \$2,158,000. Obviously this person is enjoying retirement and has the money to meet medical and home care nursing expenses with money left over to leave a tidy sum to children.

In accordance with SEC regulation, a current copy of our SEC registration form ADV Part II is available upon request free of charge.

# ENHANCING CLIENTS' LIVES

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At J.L. Bainbridge & Company, Inc. our business is dedicated to “enhancing clients’ lives” by providing long term professional money management service totally focused on helping clients finance their children’s education, build and preserve the resources for an enhanced retirement and achieve a meaningful higher standard of living.

The foundation of J.L. Bainbridge & Company, Inc.’s business philosophy is based on the full understanding that our future and success is completely dependent on client satisfaction and delivering to clients a consistent long term investment service of the highest level of quality, competence and integrity.

Our commitment to “enhancing clients’ lives” is a guiding light that governs our professional daily activities and demands every decision and action be assessed as to exposure to investment risk as well as the long term benefit to clients.

**J.L. BAINBRIDGE**

**& COMPANY, INC.**

Managing more than \$130 million for over 500 clients nationwide.

VISIT OUR WEBSITE: [www.jlbainbridge.com](http://www.jlbainbridge.com)

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