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# J.L. BAINBRIDGE

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## & COMPANY, INC.

◆PROFESSIONAL MONEY MANAGEMENT◆

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## 2009 ANNUAL REPORT

### INVESTMENT RESULTS

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For 2009 J. L. Bainbridge & Company, Inc. achieved a +34.9% rate of return on all monies managed in its equity investment program. In conjunction with returns in its equity program for 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007 and 2008 returns of 10.2%, 38.4%, 20.3%, 23.2%, 29.9%, 5.6%, 16.9%, -3.2%, -8.5%, 13.8%, 14.6%, 5.1%, 13.3%, 3.8% and -36.7% respectively, a January 1, 1994 investment of \$250,000 has grown to a December 31, 2009 value of \$1,104,434. This equates to an increase of 342% over the past sixteen years or 9.7% compounded annually. These results assume reinvestment of dividends and are after transaction costs and our management fee.

### INVESTMENT REVIEW

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In view of the loss incurred last year and the further decline during the first two and one-half months of this year, our high return for the year was gratifying indeed. We fully understand how difficult adhering to a long-term logically sound investment program is when the value of ones investments are falling and the media and pundits are hysterical. This was particularly true during the autumn of 2008 and early 2009 because the selling was completely

indiscriminant. Thus while in the past the stocks of the financially strong companies in our portfolio resisted declines as investors moved from risky holdings to higher quality, this time our holdings declined in line with the panic selling of the stock market. However when the stock market reached its bottom in March, our portfolio recovered faster than the market as we have always experienced in the past. As a result, our 2009 return of 34.9% compares very favorably with the return of 26.5% for the S&P 500. Our investments have also exceeded this index for the past five, ten and sixteen year periods.

In last year's annual report we stated: "Be assured we will adhere to the proven investment policy of owning companies with long records of earnings and dividend growth coupled with strong financial positions and significant excess cash flow. These are the companies that over time provide investment returns that exceed the growth in both the economy and the stock market while also protecting against the permanent loss of investment dollars." Time after time over the past twenty-eight years we have been in business, this policy has been successful and is a key to the +9.7% annually compounded return over the past sixteen years as well as our total return of +42.5% over the past decade during which the overall stock market declined.

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## INVESTMENT STRATEGY

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Without a doubt the U.S. economy is improving, but with unemployment above 10%, the recovery may be less than robust due to subdued consumer spending. In fact our view is fast domestic economic growth is dependent on the housing market which could take another year before pent-up demand from the echo boomer generation finally stirs demand for new and existing homes. Consequently, our investment strategy will continue to be as follows:

- Because economic growth will be stronger in international markets, we will emphasize owning American based companies with significant overseas business. While a few companies are purely domestic they are growing rapidly such as Fiserv. The vast majority are worldwide and on average derive 44% of their revenue internationally. Hence we will benefit from growth outside of America, but without the risk of owning foreign companies directly.
- Since domestic consumer spending will be lackluster and there are simply too many stores competing against each other, we will avoid retail companies.
- With a recovery of the housing market at least a year away, we will avoid home builders and their suppliers.
- As has been our policy forever, we will not invest in highly leveraged companies such as banks, savings & loan and insurance companies.
- Because growth in healthcare is driven by aging populations both in America and around the globe, we will emphasize widely diversified healthcare companies serving this industry worldwide.
- Above all we will invest in companies with proven records of earnings and dividend growth and a strong financial position and very healthy free cash flow.

An example of a company that fits perfectly with this strategy is 3M. The 3M story is one of dynamic new product innovation, aggressive international expansion and a very strong financial condition with excess cash flow sufficient to pay a healthy dividend, fund acquisitions and repurchase stock. 3M spent \$1.4 billion on research and development in 2009 which produces a constant flow of high value new products. As a result, they predict this year 27% of revenue growth will be from new products introduced in the past three years with a goal of reaching 35% within five years. Internationally, 3M generates 64% of its revenue from foreign markets with particularly rapid growth in Asia, Latin America and Eastern Europe. For example, their business in China is projected to grow from \$1.4 billion today to \$3.3 billion in 2014. From a financial perspective, their debt to equity ratio is 1 to 3, and they have over \$4 billion in cash. Consequently they have the financial wherewithal to pay a current dividend yield of 2.5% (the dividend has been increased for 51 consecutive years), acquire for cash several businesses annually to further expand internationally and add products to existing lines of business and have money leftover to repurchase stock which accelerates earnings growth. Putting all this together, in our opinion 3M will achieve double digit earnings growth for many years to come.

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## CONCLUSION

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Over the years many studies have concluded that poor investment results are due to investors either chasing returns by investing in whatever is currently hot or attempting to guess the short-term direction of the stock market. An example is Morningstar's recent study that found CGM Focus, a large cap growth mutual fund, was the decades best-performing U.S. diversified stock mutual fund with an average return of +18% annually. However, the typical CGM Focus shareholder lost -11% annually. How can this be? The answer is in 2007 the fund had a return of +80% and subsequently investors poured \$2.6 billion into this fund in 2008 only to see the fund sink -48% that year. These investors then proceeded to withdraw \$750 million from the fund in the first eleven months of 2009. This is a classic example of buying at the peak and suffering the consequences. The same results ensue when investors attempt to predict the stock market's direction, buy after a strong stock market advance or sell during a period of panic selling. In accordance with our investment philosophy, we have been fully invested throughout the past sixteen years. While this necessitated enduring several periods of panic selling, this investment approach is also a key to our achieving +9.7% annually compounded return over this period that included the most difficult decade for investors since the 1930s.

As for 2010, with the world economy expanding, interest and inflation rates low and stocks moderately priced, we are optimistic about the stock market in general and particularly our portfolio. The companies carefully selected for investments are growing their businesses faster than both the U.S. and world economy. In addition with astute management, they have dramatically reduced their cost base and are therefore positioned to increase profit margins as revenue picks up. Thus we anticipate another positive year with a return in the double digits.

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**It should not be assumed that past results will be achieved in the future or that a loss could not be incurred. Furthermore it should not be assumed that a 15% compounded return will be achieved or that future results will exceed market indexes.**

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

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# 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**  

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**& COMPANY, INC.**

Managing more than \$250 million for over 800 clients nationwide.

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

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