TW Advisors

MARCH 2012

The majority of our newsletters since the start of the financial crisis in 2007 have focused on macro (big picture) issues. As a change of pace we thought it would be refreshing to concentrate on our stock selection process.

TW Advisors is a core manager using the S&P 500 as our stock benchmark. Therefore, we buy both “growth” and “value” stocks. The majority of our holdings are large- or mid-capitalization stocks, although like the index we may hold a few small-cap stocks at times.

On the surface it seems elementary to describe the difference between growth and value stocks. In practice, it is a bit more nuanced primarily because most stocks do not fit neatly into one group. We describe value investing as "buying good businesses at great prices.” It rarely pays to own a bad business and we try to avoid that mistake at all costs. Successful value investors need to maintain price discipline and be wary of businesses that are undergoing secular declines.

At TW Advisors, we interpret growth investing as “buying great businesses at good prices.” True growth companies are rarely cheap but create value through consistent earnings growth over time. Successful growth investors need to avoid companies whose growth is unsustainable and watch for excessive expectations and valuations.

Digging a little deeper TW Advisors’ stock selection process focuses on traditional blue chip, high-quality and special situation stocks. Examples of traditional blue chip companies are Procter & Gamble, Johnson & Johnson, Exxon Mobil, Wal-Mart and Microsoft. These businesses generally have been around for decades, dominate their industry, grow consistently, and sport solid balance sheets and attractive dividend yields.

High-quality companies have business models that are hard to replicate, low capital-investment needs, impressive economies of scale, long-term growth potential, high returns on capital, and generate lots of free cash flow. They usually traded at a premium to the market but are worth it. Examples include: UPS, MasterCard, Google, Apple, and Expeditors International.

Special situation opportunities include deep value stocks and spin-offs. Deep value stocks are extremely out-of-favor and usually have underperformed dramatically over a long-period of time. Despite loads of academic research that demonstrate high returns from corporate spin-offs, this corner of investing continues to provide investors with market beating opportunities. While these types of stocks do not dominate our portfolio they have added value over the years and also provide added diversification.

Current Strategy

Currently we are emphasizing large capitalization stock due to their generally more attractive valuations. A decade ago small capitalization stocks traded at an unprecedented 40% discount to large stocks based on Price to Earnings ratio. That discount has turned completely around and grew to an equally unprecedented high premium of 25% last month (see chart below). Moreover, large stocks usually pay higher dividends, an attractive characteristic in these uncertain times.

We consider the majority of our current holdings to be traditional blue chip and high-quality stocks, although we have recently added a few deep value positions. Overall we believe our portfolio offers an attractive combination of long-term return potential with desirable defensive characteristics should macro risks surface again.

Let us know if we can answer any questions you may have. Thanks again for working with us.

James Tillar, CFA   Steve Wenstrup

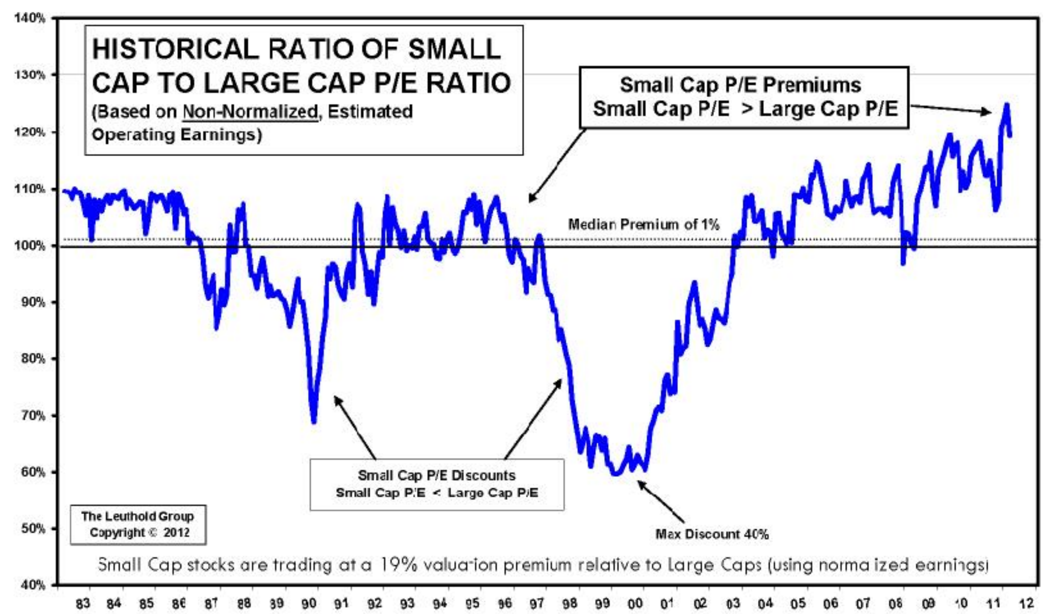

Chart source: TheLeutholdGroup