

## “Finding the Next New 425 names in the S&P”

Remarkably there are over 425 new names in the S&P 500 that were not there 25-years ago. While so much is made of long-term investing, even looking at the companies that have remained in the S&P, only a handful have outperformed the index. As the world economy continues to grow and change, new industries are created and new opportunities develop. While I am a tremendous advocate of equity investing, I am most interested in those companies that have certain characteristics. The only companies I am interested in are the healthy ones that show current growth. I am focused on identifying the next 425 names that will be entering the S&P over time.

In order to feel comfortable and patient holding smaller companies, I believe your selection process must be based on substance rather than sizzle. In every market there are many “story stocks” that attract capital only to frustrate investors over time. I have developed the Magnet® Stock Selection Process to help identify future market leaders. Our process has combined the best aspect of value, growth, and momentum investing. By screening for top line revenue growth coupled with margin acceleration we are able to identify companies with new products and without current competition. We look for companies with little institutional holdings that dominate a new market niche. We look for strong cash flow, low debt, in addition to evaluating companies according to a host of Magnet’s proprietary financial ratios. Thinking about it, years ago, who could have ever dreamed of companies providing Internet security. Our process allows us to uncover the best of the smaller, new companies that will continue to appreciate in each market cycle.

I am amazed at the misinformation and the ranting by the media about all the problems in the country at this time. We are almost back to the negative hysteria surrounding the pre-election period of 2004 when the public was warned of a double dip recession and that nobody could find a job. As I have observed, though, business worldwide is strong. I see that corporations are more liquid than at any previous time and appear to be buying back shares at a record pace. The average salaries for graduating MBAs are once again on the rise, with the average that I have seen as high as \$73,000. Overall, manufacturing in all areas of the country appears to be experiencing resurgence. Newspapers, whose circulation seems to be driven by fear and hysteria, not so unexpectedly, fail to write about this.

It amuses me when I hear “experts” citing the lack of growth in the United States and highlighting the problems of General Motors as their proof. Back in the days of the Administration of President Hamilton, there was a filibuster in Congress with a proposal to close the US Patent office. The argument was, “Now that everything has already been invented, why are we wasting taxpayers money?” With the advancement of communication and technologies, new discoveries are actually accelerating. Interestingly enough, these breakthroughs usually do not come from the larger companies – they are too set in their ways. Investors truly looking for growth need to be involved with the innovative companies making these breakthroughs.

It is critical to remember you do not need to run with the largest crowd to be profitable. In fact most mutual funds, due to their massive size, buy the same largest publicly traded companies. It is for this reason I believe the individual investor has a significant advantage over the institutions today. Instead the individual investor that invests in the best small companies and operates with a 3-5 year time horizon will have the most superior investment results of all. This is true because once an under-followed and undervalued company is identified, you must have a certain patience to let the investment workout - big healthy trees do not grow overnight. By operating with The Magnet® Stock Selection Process we can monitor the progress, or deterioration in our ideas because our holdings can be evaluated through unbiased measurements- not by management's updates about "how the story is going". When companies show continued revenue and margin growth it is only a matter of time until the institutions begin to come on board. It is this disciplined process of identifying future "Magnets" and staying patient, while monitoring the progress of each company in your portfolio for continued growth, that will enable you to generate true wealth over time.

### **Disclaimer**

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