Sentinel

Personal Financial Management Ideas

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Rupert And The Cherub

By Larry M. Elkin, CPA, CFP®

Sixty years of living and many other things separate Rupert Murdoch and my teenage daughter, Ali, but they both may help create a new era in American journalism.

Murdoch has offered a whopping premium for control of Dow Jones & Co., publisher of *The Wall Street Journal* and other outlets. The Bancroft family, which has controlled Dow Jones since 1902, initially gave his offer a chilly reception. But the Bancrofts recently indicated that they are willing to consider Murdoch's proposal along with other potential bids.

Ali leaves this month for a five-week program at Northwestern University's Medill School of Journalism. The program, formally the National High School Institute, is more commonly referred to as "the cherubs." Ali and her fellow cherubs will write and edit stories, study libel and other press law, and visit some of Chicago's major print and broadcast newsrooms. With three years of high school newspapering under her belt, Ali expects to return to work on her school paper during her senior year. Though the career plans of any 16-year-old are pretty fluid, there is a good chance she will enter a college journalism program in 2008, exactly 30 years after her father graduated from the University of Montana's School of Journalism.

If Ali pursues journalism, she will enter a business very different from the one I knew. I graduated from a print program, trained to write and edit copy for newspapers. Some of my contemporaries focused on broadcast, photojournalism or magazine writing. We all were taught that if the press is diligent at finding information that the public needs to know, and reports accurately without fear or favor, the public will respond.

It responded, but not the way we in the traditional media expected. The public went away. Daily newspaper circulation in this country peaked more than 20 years ago. Measured as a percentage of population, circulation has been dropping since the advent of television. For years, most of the decline could be blamed on the demise of afternoon newspapers, but since the millennium, the contraction has spread sharply into metropolitan and national morning dailies.

Broadcasters fared no better. Half the audience for the evening network news has disappeared over the past 25 years, down to just 26 million viewers last year. Much of what else passes for network news, especially the morning programs and the "news magazines" other than *60 Minutes*, is much more fluff than fact. On public broadcasting, audiences for *The News Hour* also are shrinking. Likewise for the cable news channels, including Murdoch's *Fox News*.

Advertisers, who in recent years have accounted for more than 80 percent of newspaper revenues (and, of course, essentially all of network television sales), are leaving, too. The growth of online advertising is a major, and perhaps ultimately a mortal, threat to the traditional media. The traditional media are flailing back by trying to convince advertisers that things are not as bad as they seem — that the fewer newspapers sold today are still seen by multiple readers, or that digital recorders are not gutting the effectiveness of 30-second TV spots.

If audiences truly are abandoning print and broadcast news,

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Inside This Issue Of *Sentinel*

Clear Channel Buyout Fight: Who Wins?

By Eric Meermann, CFP®, AVA

Shareholders of Clear Channel Communications are fighting with large private equity firms to get more for their shares in a proposed buyout. If the deal is ultimately voted down, all parties will lose.

In November 2006, Bain Capital and Thomas H. Lee Partners won a competitive auction for the takeover of Texas-based Clear Channel with a price of $18.7 billion, or $37.60 per share. The offer received the blessing of Clear Channel's board of directors and that of the founding Mays family. Shareholders, however, were dissatisfied.

In the month before Clear Channel indicated that it was exploring its strategic options for a sale, its stock was trading at around $30 per share. The offer by the private equity shops therefore would have given shareholders a premium of about 25 percent. Yet shareholders, particularly the two largest, Fidelity Investments and Highfields Capital, believed that the price grossly undervalued the company and said they would vote against the deal. Proxy advisor Institutional Shareholder Services, whose recommendations hold a lot of sway with institutional investors, also came out against the offer, saying it was too low.

Under Texas law, holders of two-thirds of outstanding shares must approve a buyout. This makes getting approval tougher because not only is a super-majority needed, but such issues are typically decided on a simple majority of votes *cast*, rather than of outstanding shares. In Texas, shares not voted count against the deal. These conditions give shareholders an unusually strong hand in negotiations.

Bain and Lee went back to the drawing board and increased their offer to $39 per share in April, and Clear Channel pushed back the vote on the proposal to May 8. It was then pushed back to May 22 after the private equity team upped the bid again by 20 cents, with the conciliatory alternative offer of 30 percent "stub equity" in the soon-to-be-private company. Stub equity allows incumbent shareholders of a company that is taken private to retain some ownership, and thus participate in the private profits. Clear Channel's board initially rejected the bid, figuring that if shareholders wanted a price north of $40, it would be a waste of time to postpone the vote yet again. However, this recent offer finally piqued the interest of shareholders, who then pressured the board to push back the meeting again so more negotiations could take place. On May 18, the board accepted the revised offer and delayed the shareholder meeting yet again, to a date that had not been determined when this article went to press.

For the marketplace and for our economy as a whole, there is some benefit to activist shareholders demanding more from their corporate boards. Too often, chummy management and private equity shops collude in sweetheart deals, where the transaction ultimately benefits those parties at the expense of shareholders. On one side of the argument, it is impressive to hear that shareholders are speaking up. They are demanding to be paid for part of the potential value that will inure to the private equity firms.

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However, the theory of market efficiency would state that the market fairly prices companies, and therefore the collective voice of the market has already told us what Clear Channel was worth absent a takeover. Under the incumbent management and its long-term strategy, that value was $30 per share. Some dramatic changes would have to happen to unlock the value that the private equity players are seeing. Jonathan Bergman's article "The Growing Benefits Of Private Ownership" in the January 2007 issue of *Sentinel* (www.palisadeshudson.com/sentinel.php?article=160) speaks to how this process works.

It is unlikely that a public company, given the pressures of meeting quarterly estimates and typically risk-averse decision-making, is going to enact the radical changes

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INVESTMENT FOCUS

Lessons From The 2000-2007 Market Cycle

By Paul Jacobs, CFP®

While stock market performance can be very cyclical, investors still expect to receive positive returns over the long term. When the next market downturn comes, how will you respond?

Last month, the S&P 500 Index passed its previous closing record, set in March 2000. The S&P 500 dropped a total of 49 percent from that original peak to its trough in October 2002. Investors who sold at the market bottom because they couldn't handle watching their portfolios shrink are now kicking themselves, and their portfolios may never recover from this ill-timed decision.

Investors took various lessons from that three-year bear market. Some are worth remembering the next time there's a downturn. Others should be ignored.

Diversification is crucial. Absolutely. Almost all major indices (a notable exception would be the NASDAQ) outperformed the S&P 500 cumulatively over the past seven years. Outperforming asset classes include domestic small-cap stocks, international stocks, real estate investment trusts, emerging market stocks, bonds, money market funds, hedge funds, private equity and many more. In a diversified portfolio, some investments are bound to do well while others underperform. Sufficient diversification leads to an optimal portfolio, with the greatest level of expected return and the lowest level of risk.

A formal selling strategy is very important. Yes, but it should not involve market timing. Some people advocate selling after a 10 percent drop or a 20 percent drop in value, which is basically a form of market timing. But any plan like this is flawed, because you might look back later and realize you sold at the absolute bottom. An investor needs to maintain her conviction that the market will recover, because recoveries usually happen when they are least expected. Two good reasons for selling stocks include rebalancing your portfolio to its target asset allocation (for example, selling outperforming stocks and buying underperforming bonds or cash equivalents), or gradually reducing your exposure to stocks as you get closer to retirement. Neither of these reasons should be influenced by panic or the market's recent underperformance.

Stocks are too risky and volatile. Wrong. While the 49 percent drop we experienced was very difficult to endure, it was also very rare. Two periods of similar or greater market declines occurred in the post-World War I United States, a 48 percent drop in the S&P 500 Index from 1973 to 1974, and a market drop of more than 80 percent during the Great Depression. The market recovered both times, and it is doing the same this time. Stocks should have a place in everyone's long-term portfolio. While investors must be able to handle drops of this magnitude, they shouldn't expect to deal with them more than once every few decades.

Hedge funds are always better than stocks. Wrong again. Hedge funds have emerged from relative obscurity and now attract major inflows. Estimates vary, but hedge fund managers oversee more than $1 trillion. While a great deal of this money comes from large institutions such as pension funds and endowments, smaller mom and pop investors also have been shoveling money into hedge funds, attracted by their positive returns during the 2000-2002 bear market.

While hedge funds pursue numerous strategies, each with its own risk/return characteristics, most funds seek to provide positive returns regardless of the state of the stock market or economy, with low volatility. While low volatility makes for a smoother ride over the short term, a hedge fund investor is likely to end up with a lower long-term

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return than that of an index fund. For example, the Hedge Fund Research Inc. Fund of Funds Diversified Total Return Index provided an annualized return of 9.89 percent from its inception in 1990 through 2006. This return is nothing to scoff at, but it is lower than the 11.57 percent annualized return, including dividends, generated by the S&P 500 Index during the same period. So while hedge funds will outperform during short-term market downturns, over the long term they should lag stocks.

Indexing is dead. No way. Two flawed arguments about indexing are being made as a result of the bear market. First, some argue that this period proved that active money management is better than passive index funds. After all, active managers were able to beat their index benchmarks by holding cash instead of stocks. However, the long-term returns of S&P 500 Index funds still hold up quite well when compared with the competition. For example, through April 30, 2007, the 10- and 15-year returns of the Vanguard 500 Index Fund – Admiral Class Shares rank in the top 35 percent of the Morningstar large-cap blend category. Shareholders should be pleased when their fund finishes at least in the top half of the category, and should be even happier when it beats over 65 percent of the competition.

The second argument is that there are better ways to construct stock indices than the market cap weighting method used by Standard and Poor's (see "A Fundamentally Better Stock Index?" in the January 2007 issue of *Sentinel*, www.palisadeshudson.com/sentinel.php?article=161). New indices to track markets or industries have been created that weight stocks based on more objective measures, such as dividends or profits. While these "fundamental" indices may outperform a similar market cap weighted index periodically, they do not provide what a typical index fund should be expected to: exposure to the entire market. Over the long term, a market cap weighted index such as the S&P 500 should provide lower risk than a domestic large company fundamentally weighted index, thanks to greater diversification.

The market cycle of 2000-2007 reinforces what smart investing is all about. Common investment mantras such as "don't buy high and sell low" and "don't put all your eggs in one basket" sound easy enough, but many investors panicked and sold their holdings at the market bottom in 2002, and have held low-risk investments since. By developing a long-term investment plan and following it regardless of market fluctuations, you give yourself the best chance to achieve your financial goals.

...Fight

necessary to make the company worth more than its publicly traded value. For Bain and Lee to reap sizable profits from the deal, they are going to have to take sizable risks. Current shareholders therefore should not feel entitled to excess returns without being willing to share that risk.

The most telling fact in this saga is that no other bidder emerged to say, "We'll pay more for the company." This was not a privately negotiated price. It was arrived at in a public auction, and no one was willing to pay more than the Bain and Lee group. The recalcitrant shareholders have achieved only the modest success of getting that group to raise its initial bid by $1.60, or about 4 percent, which brought the premium over the pre-offer market price from about 25 percent to 31 percent.

Who wins if the deal goes through? Possibly everybody, because shareholders would receive a premium from the pre-offer price, the private equity buyers would get the opportunity to buy out the company and add value, and the founding family would get to cash out.

If shareholders reject the deal, the most likely scenario is that management will not take dramatic steps to turn around the company, increase earnings and drive the stock price up. The open market will determine the price the company is worth, and in the absence of a takeover bid, that value is likely to be somewhere in the neighborhood of where it was before all this drama.

So who wins if the private equity buyers fail to close the deal? Nobody, really. Clear Channel shareholders would be stuck with the same stock worth $30 with an unpromising future, and the private equity companies would not get the opportunity to take the company private and make the tough changes necessary to unlock its value.

...Journalism

Ali might be better off choosing a more promising field in which to start her career. But if she asks what I think (which, on this topic and many others, has not happened), I am not going to try to steer her away from journalism.

Ali could work for an online publication such as *Slate*, which did not exist in my time. She might freelance for a variety of outlets in all media. She could be an independent blogger or reporter. As an independent she could choose whether to rely on Web-based advertising sold by Google and others, or on audience contributions, or on paid subscriptions to provide the wherewithal to cover what she chooses. Such entrepreneurial journalism was all but unheard of when I was in school.

This newfangled journalism is going to require newfangled journalists. Ali's cohort will need skills to communicate with audiences in ways and to a degree that my generation never contemplated.

Traditional journalism was a one-way street. Editors decided what news to print or air. Reporters gathered facts, interviewed sources, put the stories together and, because of inevitable constraints of time or space, left a lot of material on the proverbial cutting-room floor. Readers and viewers accepted the news as presented, between the advertisements.

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For Ali's generation, the journalist probably will function more like the consumer's personal research assistant. Reporters will be required to provide not only concise facts and context, but also links to source documents, video files and additional data that the interested reader might wish to explore.

Distinctions between print, broadcast and online delivery are becoming irrelevant. Ali must learn to be adept in all these media to reach her audience of the future. But by "broadcast" I don't just mean a studio in which someone faces a camera and reads a prompter. Think YouTube.com: The reporter who has just witnessed an event will likely upload a video. The consumer will choose whether to rely on the reporter's synopsis or to watch for herself.

Sometimes the audience will join forces with the news organization to cover the story. When a gunman killed 32 Virginia Tech students and faculty and then himself in April, the campus newspaper *Collegiate Times* drew on a wide network of student reports to keep the community updated through online postings. As that horrible day drew to a close, the student journalists mined fellow students' pages on Facebook.com to get leads on the identities of victims. For a moving look at the work of those young reporters and editors, visit www.collegiate-times.com/416archive/tuesday.html.

Why did Murdoch offer nearly twice the market price for Dow Jones stock when he made his bid last month? Suspicions immediately turned to Murdoch's well-known right-of-center politics and his perceived penchant for putting a political stamp on the journalism of his News Corp.

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Doubting A Public Trust

I have no idea who first declared "a newspaper is a public trust." It is something all respectable journalists are taught to believe.

I believed it too, for many years, after I heard the expression at college. But I am not certain any longer that I know what this means, let alone whether I believe it. Does it mean accepting another journalism-school mantra, which is that the role of a newspaper is to comfort the afflicted and to afflict the comfortable? This idea can be traced to the early 20th-century columnist Finley Peter Dunne. I will buy the idea that the afflicted ought to be comforted, but need we agree with Dunne that the comfortable deserve affliction?

One thing of which I am certain is that a public corporation is a public trust. Managers who run publicly owned

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companies must act on behalf of those public owners. Responsible management means taking advantage of opportunities to grow the value of the company over time, and paying a fair dividend in exchange for use of the shareholders' capital. If this is not possible, then the appropriate thing to do is return shareholders' money by repurchasing shares, going private or selling the company.

Families such as the Sulzbergers, who control The New York Times Co., and the Bancrofts, whose control of Dow Jones & Co. includes *The Wall Street Journal*, invoke the newspaper-as-public-trust doctrine to justify their disproportionate voting rights. They ask other people to provide the bulk of the capital for their enterprises while they perpetuate their families' ultimate control over the companies. This arrangement is supposed to promote better journalism. Shareholders are told they should accept lower economic returns in exchange for fine journalism because, well, a newspaper is a public trust.

Shareholders are told they should accept lower economic returns in exchange for fine journalism because, well, a newspaper is a public trust. The public is hardly impressed.

The public is hardly impressed. Newspapers are bleeding readers, advertisers, profits and share prices. Family control is no guarantee of strong journalism: The Hearst and Pulitzer papers invented yellow journalism. Think of the Manchester (N.H.) *Union-Leader* in the early 1970s. The only liberal thing about then-publisher William Loeb was his use of the paper's front page to promote favored conservatives and attack his opponents, most famously Sen. Edmund Muskie, D-Maine. Muskie's choked-up protest outside the newspaper's offices led to the implosion of a promising 1972 presidential campaign.

Or take a close look at the modern *New York Times*. The Sulzbergers produce a high-quality paper, but it often displays an editorial bias that can be insulting to the very readers — affluent, educated and interested in a wide range of topics — that the *Times* hopes to attract.

A search of the *Times*' archives brings up 194 articles since 1981 that use the term "McMansion." McMansion is a pejorative. It can be defined as any modern home larger than the largest home the writer hopes someday to buy. Most of these McMansion snipes were in the news columns, not the opinion pages, and many were extraneous to the stories in which they appeared.

Also consider *Times* sports columnist George Vecsey, who has doubtless watched many a game from a free seat in a press box, but who casts himself as a defender of the working stiff. At least a dozen times between 1993 and 2006, Vecsey has used the term "shrimp-eater" to describe anyone who occupies a luxury suite at a sports event. I cannot fathom how this could have happened more than once before some adult, somewhere in the *Times*' editorial chain of command, might have suggested that Vecsey knock off the name-calling.

I will set foot in a luxury suite for the first time this month, when, after many years of hard work, I will treat my staff and some close family and friends to a night at Yankee Stadium. I think I will invite Vecsey to leave the press box and join us. No shrimp are on our menu, but he will be welcome to a hot dog. Maybe we will reminisce about the good old days when Red Barber called the games and the working stiff could afford to go to the ballpark. We can gaze out on 55,000 fans and nary a shrimp, and recall how Barber was fired for reporting one day in 1966 that the Yankees drew exactly 413 paying customers.

The rest of the public does not seem to mind sharing a ball game with the folks in the luxury suites. The public seems to have its own ideas about how to spend its time and money — more of each at the game, and less on the *Times* and its parent company's stock.

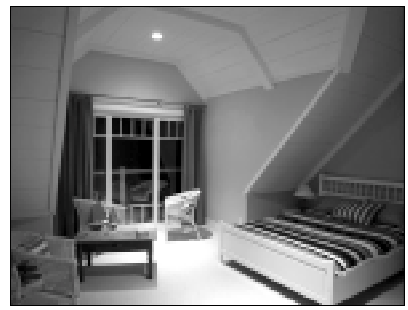
Is *The New York Times* a public trust? The Sulzbergers and their employees say it is. Either the public does not think so, or the public does not care.

— **Larry M. Elkin**

Retreat To Nova Scotia Ocean Estate

If a secluded getaway with spectacular views, plenty to do and a delightful summer and autumn climate sounds appealing, we may have what you want.

Eagle's Cliff is a spacious four-bedroom, 3.5-bath house set on the edge of a cliff overlooking the Gulf of Maine about 20 minutes from Yarmouth, Nova Scotia. We bought and manage the house and a surrounding 20-acre parcel as part of a client's international real estate portfolio. The home is kept nicely furnished and fully equipped for our client's family to use at all times, but it also is available for year-round rentals at rates well below comparable oceanfront properties in nearby New England. Rates vary from $1,100 to $2,250 (U.S.) per week, depending on the season.



Eagle's Cliff Properties

Views of Eagle's Cliff from the air, from the ground and from the entry to one of four comfortable bedrooms.

Comfortable high-speed ferry service connects Yarmouth with Portland and Bar Harbor, Maine, from May to October. Halifax, with direct flights from major cities, is a scenic three-hour drive. Eagle's Cliff is a short walk from the sandy shore at Mavillette Beach Provincial Park. The local villages are Acadian and have a French heritage, though English is spoken everywhere. Nearby, the Bay of Fundy offers whale-watching cruises, some of the best shellfish anywhere — the scallops are famous — and, of course, the world's highest tides.

The house is supplied with all the necessities and boasts balconies, a sunny wraparound deck, and a beach-stone fireplace. Every room has a sunset view of the water, which lies more than 100 feet below the cliffs. Send information requests to erica@palisadeshudson.com or see our listing #130467 on Vacation Rentals by Owner (www.vrbo.com/130467).

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holdings. In other words, Murdoch proposes to use the resources of his publicly traded company to boost his personal influence and ego.

But consider this fact: The *Journal* is virtually alone among the world's newspapers in having made its Web site a stand-alone commercial presence, with about 300,000 paying subscribers who do not also take the print *Journal*. Murdoch probably provided the rationale for his bid for Dow Jones in a 2005 speech to the American Society of Newspaper Editors, where he noted the rising influence of portals such as Google and Yahoo as distributors of news.

He warned the editors that unless they can compete, they risk losing control over the most basic function in journalism, which is the selection of stories to set before the customer.

"The challenge for us — for each of us in this room — is to create an Internet presence that is compelling enough for users to make us their home page," Murdoch told the editors two years ago. "Just as people traditionally started their day with coffee and the newspaper, in the future, our hope should be that for those who start their day online, it will be with coffee and our Web site."

Duly Noted

Teacher Severance Payments Subject To FICA, Court Rules. A controversy that has split the courts became more heated when the 6th U.S. Circuit Court of Appeals held that early retirement buyouts for tenured teachers are subject to Social Security's FICA tax. A divided three-judge panel ruled that such buyouts are taxable "wages" even if teachers electing to take the buyouts agree to surrender tenure rights guaranteed by state law. The decision addressed appeals from two federal district courts in Michigan that reached opposite conclusions on the issue. The 6th Circuit panel refused to follow an earlier decision in the 8th Circuit, which held that tenured North Dakota teachers who took a buyout were paid for surrendering a property right rather than for rendering services, and therefore were not subject to FICA. *Appoloni et. al. v. United States,* 2006 TNT 110-14.

Homestead Break Denied To Would-Be Floridians. Two Swiss nationals who legally live, work and pay federal income taxes in Florida are ineligible for the homestead property tax exemption because they hold temporary U.S. visas rather than permanent resident status, a state appeals court ruled. Andre DeQuervain and Esther Maisch contended that they met the statutory definition of a Florida resident and should receive the tax exemption. But a three-judge panel of the state's Second District Court of Appeal ruled that because they lack a legal right to remain indefinitely, they are not "permanent" Florida residents. The judges refused to expand an exception that already allows immigrants who have a pending claim of political asylum to obtain homestead benefits despite similar uncertainty over their future legal status. *DeQuervain et. al. v. Desguin et. al.,* 2006 STT 105-10.

No Injustice Manifest Enough To Block Tax Law. The New Jersey Legislature was within its rights when it retroactively changed estate tax laws in July 2002, increasing the tax on estates of individuals who died during the first half of that year, an appeals court ruled. The state's Tax Court had refused to enforce the increase against the estate of Cynthia Oberhand, ruling that while the increase did not violate due process requirements, it was nevertheless manifestly unjust. (See *Duly Noted,* October 2005.) But a three-judge panel of the Appellate Division of the state Superior Court reversed. "The doctrine of manifest injustice has no place in the judicial evaluation of retroactive tax laws," the appeals court said, and to permit its use would create "uncertainty in the application of the tax law and unduly (interfere) with the Legislature's right to apportion the burden of the revenue it deems necessary in a manner that it deems equitable." *Oberhand v. Director, Division of Taxation et. al.,* A-3886-04T2.

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2 Overhill Road, Suite 100
Scarsdale, NY 10583