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Forbes

March 1, 1999

TIMELY PROFIT OPPORTUNITIES:

Off the shelf...
The surprising future of auto retailing!

20 times faster...
The stunning breakthrough in color laser printers !

Quality goods cheap...
The hot new trend in warehouse retailing!

Systems on a chip...
The amazing new digital signal processors!

Special Investment Edition

See inside for free gift offer.

The Best New Ideas and Opportunities

Welcome to our special investment edition of Forbes.

Inside, you'll find a generous sampling of Forbes editorial, news on some dynamic companies in promising situations, and a special offer to try four issues of Forbes.

In every issue of Forbes, you'll discover the best ideas for running a business, the best methods for building new markets, and the best examples of how companies are capitalizing on today's opportunities.

No question that global competition and technology have changed the way we do business. The organization has been reinvented, the management hierarchy has been flattened, the middle manager has been replaced by the empowered decision-maker. Technology has made this movement possible and continues to push it forward at an ever-increasing speed.

Technology has also allowed a new class of entrepreneurs to leapfrog even the most powerful corporations, creating new wealth and jobs through exciting business startups.

In this environment, investment opportunities abound.

And Forbes keeps you on top of this fast-changing world with reports that are concise, counter-conventional, ahead of the news, and as entertaining as they are informative.

See for yourself on the pages that follow. Then, take us up on our special offer to receive four issues of Forbes FREE. That's our way of demonstrating what Forbes can do for your business, your career, and your personal wealth.

Forbes is the Capitalist Tool. Use it wisely.

Sincerely,

Steve Forbes
Editor-In-Chief

Grow rich (or richer) with Forbes

by Bill Baldwin

A FEW years ago, we interviewed Warren Buffett, probably the most successful investor of all time, and he shared a bit of his learned wisdom with us.

Buffett said, "Being an investor makes me a better businessman, and being a businessman makes me a better investor."

Do great minds think alike? Sometimes they do.

Helping businesspeople become better investors and investors better businesspeople was exactly what founding editor B.C. Forbes had in mind when he launched *Forbes* magazine in 1917.

B.C. understood that the two go hand in hand. And in our 82 year history, we have indeed helped our readers grow rich (or richer), by helping them to be both better informed and first informed—and always from this dual perspective of business and investment. Now, we'd like to do the same for you.

I'm Bill Baldwin, editor of *Forbes*. I'm writing to show you how *Forbes* can give you a distinct advantage in today's rapidly changing world of business and investment.

Inside you'll discover the future of auto retailing. A breakthrough technology that makes color printers 20 times faster. Plus, the latest in warehouse retailing, digital signal processors, and fiber-optic voice and data transmission.

Continued on page 4

FREE GUIDE

Learn to beat the market by investing in little known hot funds!

All in all, I think you'll find the experience both eye-opening and potentially very profitable, since all of these situations present timely investment opportunities.

Speaking of investment opportunities, further on I'm going to tell you how to save $88.82 on your subscription to *Forbes* (it's like getting 17 issues FREE) and also receive a FREE copy of the *Forbes Mutual Funds Survey.*

Our annual survey ranks all funds by their performance in both up and down markets and includes the *Forbes* Honor Roll — the best of the best. Considering that markets do periodically correct, knowing which funds hold up best in declining markets is valuable information.

It's always been our position that knowledge is power, understanding is mastery, and timing is everything. Now, let me show you how to grow rich (or richer) with *Forbes.*

Forbes GREAT CALLS

Cardinal Health +365%

A while back, we applauded Robert Walter, chairman of the $1.6 billion drug wholesaler, Cardinal Health, for passing on a desirable but high-priced acquisition. We also praised his disciplined strategy of making selective acquisitions at the right prices.

Since then, Walter has made a string of acquisitions to build what is now a national drug-distribution franchise, including a merger with Owen Healthcare, the nation's largest hospital pharmacy management firm.

Walter's strategy has worked beautifully. Sales are up five-fold and earnings are up six-fold. The stock vaulted from $15 when our article ran to a recent $69.81 (split adjusted), a gain of 365%.

Percentage of gain or loss as of January 19, 1999.

Watch CarMax and AutoNation grow

A while back, our man out west, Tim Ferguson, sat down with J.D. Power III (you'll recall his company measures motorist satisfaction) to get his read on where auto retailing is headed in the near future.

It's hard to imagine, but kicking tires, looking under hoods, and going for test drives may soon be history. You can kiss the high-pressure salesman goodbye, as well.

Ferguson noted that, while most manufactured goods have long been available in a variety of discount outlets, cars continue to be sold in the traditional way, through exclusive licensed dealers. Of course, over the years thousands of these family-owned dealerships have made their owners rich.

But now, according to Power, the party is over. The number of new car dealerships has been steadily shrinking — 20,000 today, down from 50,000 in 1950. And this shrinkage has only just begun. It's just a matter of time before the big chains like Circuit City's CarMax and Republic Industries' AutoNation drive the remaining family dealerships out of business.

Here's the reason for the change. In the beginning, cars were unreliable so manufacturers needed dealers in every town to service them. This arrangement gave dealers very profitable monopolies, at least in defined territories. But, today, improved quality and reliability have rendered the sales/service alignment obsolete.

In the future, you'll buy your car off the shelf, like a TV set or VCR. What's the advantage? You'll pay less and nobody will lock you in a little room for two hours, grinding for the sale.

Can you make money in the future of auto retailing with Circuit City's CarMax or Republic Industries' AutoNation? *Forbes* gives you the facts. As an informed businessperson and investor, you make the call.

Continued on page 7

Forbes brings you sound business advice

▪U.S. business may be getting too dependent on computers. ▪There are serious weaknesses in our multinational companies. ▪College education as we know it is threatened. ▪A big backlash is building against the rich. ▪Retirement at 65 is doomed. These are just a few of the predictions the very foresightful Peter Drucker makes.

Seeing things as they really are

NUMBERS GAME

Are you sure your best customer is making you money, or that your worst customer isn't? Maybe you aren't allocating costs correctly.

Overhead can kill you

By Srikumar S. Rao

A BIG COMPANY, an icon of American industrial might and business savvy, was facing two related decisions. The bankruptcy of a competitor offered it an opportunity to pick up half a million units of incremental volume of its seemingly best product on top of existing volume of 3 million units.

The other possibility involved outsourcing 2 million units of a money-losing product to a Korean firm that had given a very attractive bid.

Putting the two situations together, the senior vice president of production recommended manufacturing the less profitable product in Korea and retooling its own domestic plant to produce the extra units of the better product. He figured the strategy would convert the current $11 million loss to a $17.5 million profit the following year.

The expected profit did not materialize; indeed, the loss ballooned to $20 million.

Back to the spreadsheets. A new analysis revealed that the "best" product was, in fact, a moneyloser. The "worst" product had been a consistent moneymaker.

How could a big, smart company make such a dumb mistake? It turned out the company had been allocating depreciation and other fixed overhead on the basis of direct labor cost. A product that used, say, 20% of the company's total labor bore 20% of the depreciation. This was cockeyed. Labor doesn't depreciate. Machinery does. Where lots of labor is used, usually less machinery is used. Labor-heavy products should have carried less of the depreciation.

This mattered a lot, because some expensive machinery had recently automated the production line of the "best" product and greatly reduced the number of workers. Meanwhile the "worst" product line used fully depreciated equipment but a relatively large number of workers. Traditional cost accounting had completely distorted the picture and given rise to lousy decisions.

"With declining margins and inefficient cost-accounting systems, many firms do not even have a clue as to whether they are making money on a product," asserts Professor Bala Balachandran, director of the Accounting Research Center at Northwestern University's business school.

Beware of any system that mechanistically allocates overhead. And remember that depreciation is only one of many overhead items. Overhead can cover everything from the toilet paper in the washroom to the cost of executive education programs. The lazy solution is to allocate it in proportion to any of a number of measures, such as direct labor costs or revenues.

In times past, direct labor was a big expense and overhead a small one, so there was no great sin in misallocating overhead, says Mohan Nair, president of ABC Technologies. Today automation has cut out a lot of direct labor. In its place are all manner of expensive activities that are hard to assign to products: long distance calls, electronic mail systems, antidiscrimination lawsuits, wheelchair ramps, tax compliance, trade association memberships, management consulting, strategic planning, fax machines, cafeterias and merger advice. Today, even for a manufacturer, overhead is frequently more than half of total product cost.

Arbitrary allocation of overhead does more than lead to faulty choices about which product lines to build and which to kill. It acts as a powerful incentive to waste resources.

Professor Balachandran invites us to his imaginary restaurant, Bala's Bistro, for a demonstration of how devastat-

ILLUSTRATIONS BY ELWOOD SMITH

Srikumar S. Rao is chairman of the marketing department at the C.W. Post campus of New York's Long Island University and a consultant.

Forbes ▪ February 10, 1997 97

Advice from the master

Peter Drucker warns *Forbes* readers that executives are becoming too inwardly focused. He says it is imperative to spend a few weeks each year outside of your business, working in the marketplace or at a university. "All great change in business," he says, "has come from outside the firm." *Benefit: how to get renewed vigor, more productivity, better ideas.*

Accounting alert

Forbes reports how traditional cost accounting can lead to false assumptions and lousy business decisions. Readers learn a more accurate way to allocate costs called activity-based accounting. *Benefit: by knowing the real profitability of individual products, customers, and channels of distribution, your business decisions will be sound.*

Get 4 issues of Forbes FREE today!

Forbes helps you diversify your portfolio

Statistical spotlight

Traditional values

Growth-stock mania has swept through Wall Street. At such a time you might want to consider picking up a few wallflowers—companies selling at low multiples of their earnings, dividends, sales or book value.

By Eric S. Hardy

DAVE BLACK

WITH ITS RECENT RALLY the S&P 500 index is back to selling for 29 times trailing earnings, 6 times book value, 3.7 times sales and 68 times dividends. This is an average figure: A hot item like Dell Computer has much higher multiples.

These days everyone wants growth stocks like Dell. In the past five years the S&P/Barra index of growth stocks is up 25% a year, while the S&P/Barra value stock index has been climbing at a rate of only 18% annually.

Denis Laplaige, who manages the MainStay Value Fund, is in the value camp. His contrarian strategy: select portfolios from among companies that fall into the bottom 20% of the stock market as measured by price/earnings ratio or rank in the bottom 20% by price/cash flow ratio. Here, cash flow refers to aftertax net with depreciation and other noncash charges added back.

Laplaige's stocks have an average P/E not much more than half that of the overall market. One of them is Allstate, the Chicago property and casualty insurer that was once part of Sears. At a recent $42, Allstate sells for ten times trailing earnings *(see table, p. 248)*. That's a low enough multiple that Allstate's share buybacks will have the effect of boosting per-share earnings. The company is financially sound and should have no trouble paying claims from those hurricanes and floods you have been reading about.

We screened the Market Guide and Worldscope stock market databases for plausible value stocks.

The table on page 246 shows 25 companies that look reasonably priced in relation to their sales, sales growth

Forbes ■ December 14, 1998 245

Key buys in value stocks

Forbes reports that, today, almost everyone wants growth stocks. But the highest fliers can also become the biggest losers following a disappointing quarter or during a market correction. Readers discover dozens of solid companies whose shares are bargain priced relative to their sales and earnings, and many more paying dividends significantly higher than the market average. *BENEFIT: balance your portfolio with value stocks.*

Big and small players alike are concocting strategies to secure a slice of a $300 billion deregulated energy market. Some already look like winners.

Power players

By Toni Mack

ILLUSTRATIONS BY JAMES NAZZ

THE NUMBERS are awesome. Electric power is a $215 billion industry. Natural gas is $90 billion. They're merging into one vast energy-providing business that dwarfs both the local and long distance phone business ($170 billion) and the airline industry ($100 billion). And soon competitors of all stripes will be able to vie for their customers.

California, New York, Pennsylvania, Illinois and some New England states are moving quickly toward deregulation. U.S. Congressman Dan Schaefer (R–Colo.) has introduced a bill to free all customers—residential and commercial alike—to choose their own electricity provider by Dec. 15, 2000. "Deregulation will spread rapidly," predicts Richard Farman, president of Los Angeles-based gas utility Pacific Enterprises. "States don't want to leave it up to the federal government."

The players in this game face many choices: Focus on a local market or go national? Pursue high-volume customers or cater to smaller fry? Own generating plants, even as the price of power falls? Below, FORBES spotlights a handful of strategies that are already showing promise.

Black magic

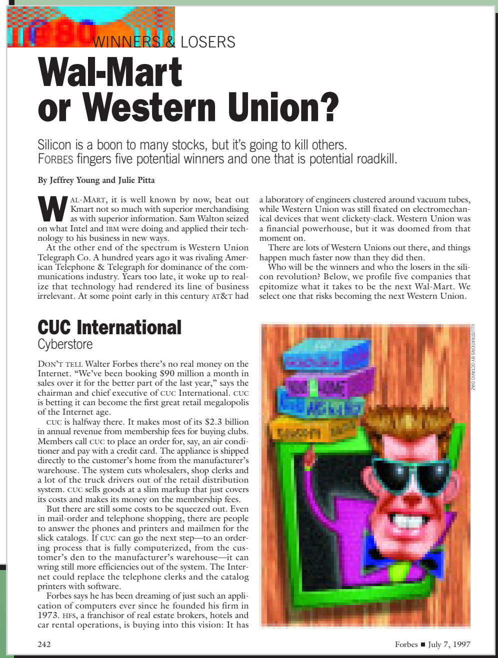
Richard Priory, president of Charlotte, N.C.'s $4.8 billion (revenues) Duke Power Co., wants to exploit Duke's record as an efficient operator by owning and operating power plants all over the country. Says Priory: "Our core strength is generating and dispatching electricity and satisfying our customers' technical needs."

Duke's joint venture with trader Louis Dreyfus L.L.C. (FORBES, *July*

114 Forbes ■ May 19, 1997

Where to place your bet

Forbes reports on the extraordinary growth opportunities in the deregulated energy business. Readers learn that local companies will compete with national providers, some of which will offer internet access, local and long distance phone, satellite TV, natural gas and electricity, all on one monthly bill. *Benefit: profiles of likely winners in energy industry deregulation.*



WINNERS & LOSERS

Wal-Mart or Western Union?

Silicon is a boon to many stocks, but it's going to kill others. FORBES fingers five potential winners and one that is potential roadkill.

By Jeffrey Young and Julie Pitta

WAL-MART, it is well known by now, beat out Kmart not so much with superior merchandising as with superior information. Sam Walton seized on what Intel and IBM were doing and applied their technology to his business in new ways.

At the other end of the spectrum is Western Union Telegraph Co. A hundred years ago it was rivaling American Telephone & Telegraph for dominance of the communications industry. Years too late, it woke up to realize that technology had rendered its line of business irrelevant. At some point early in this century AT&T had a laboratory of engineers clustered around vacuum tubes, while Western Union was still fixated on electromechanical devices that went clickety-clack. Western Union was a financial powerhouse, but it was doomed from that moment on.

There are lots of Western Unions out there, and things happen much faster now than they did then.

Who will be the winners and who the losers in the silicon revolution? Below, we profile five companies that epitomize what it takes to be the next Wal-Mart. We select one that risks becoming the next Western Union.

CUC International

Cyberstore

ILLUSTRATIONS BY OCTAVIO DIAZ

DON'T TELL Walter Forbes there's no real money on the Internet. "We've been booking $90 million a month in sales over it for the better part of the last year," says the chairman and chief executive of CUC International. CUC is betting it can become the first great retail megalopolis of the Internet age.

CUC is halfway there. It makes most of its $2.3 billion in annual revenue from membership fees for buying clubs. Members call CUC to place an order for, say, an air conditioner and pay with a credit card. The appliance is shipped directly to the customer's home from the manufacturer's warehouse. The system cuts wholesalers, shop clerks and a lot of the truck drivers out of the retail distribution system. CUC sells goods at a slim markup that just covers its costs and makes its money on the membership fees.

But there are still some costs to be squeezed out. Even in mail-order and telephone shopping, there are people to answer the phones and printers and mailmen for the slick catalogs. If CUC can go the next step—to an ordering process that is fully computerized, from the customer's den to the manufacturer's warehouse—it can wring still more efficiencies out of the system. The Internet could replace the telephone clerks and the catalog printers with software.

Forbes says he has been dreaming of just such an application of computers ever since he founded his firm in 1973. HFS, a franchisor of real estate brokers, hotels and car rental operations, is buying into this vision: It has

242 Forbes ■ July 7, 1997

Future winners and losers

Forbes reports that the silicon revolution, like all revolutions before it, was creating thousands of new winners and losers, but faster and more brutally. Readers learn about five forward-thinking companies that are potential big winners, and one that's operating with a rear-view mirror. *Benefit: five stocks to buy and one to sell.*

Get the advantage. Get Forbes. Take 4 issues FREE today!

And speaking of Circuit City, Ferguson also reported that the super discounter is testing the waters to sell sofas, bedroom sets, and other home furnishings. Management sees entering this fragmented industry with high mark-ups as the logical next step in their ambitious growth plans.

Will we see a Sofa City soon? Stay tuned to *Forbes* and you'll be the first to know. Now, let's look at a company whose ability to deliver a knock-out punch is legendary.

Hewlett Packard just keeps winning

Eric Nee, our man in Silicon Valley, recently uncovered a fascinating fact about Hewlett Packard (HP). HP researchers, unlike their peers at Lucent Technologies, Bell Labs, and IBM, have never won a Nobel Prize for breakthrough technology.

That hasn't hurt HP's business. Their products are consistently out front in quality, capability, and popularity. While revenues at Lucent Technologies, Bell Labs, and IBM have approximately doubled over the past ten years, sales at HP have increased five fold.

What's the secret of HP's phenomenal success? First, while HP hasn't invented nearly as many breakthrough products as the others, what it has invented it has fully exploited. Its 1972 handheld calculator turned the slide rule into a buggy whip overnight. And its world-class inkjet and laser printers now pull in $15 billion per year.

Second, HP is extremely adept at improving existing technologies and incorporating them into high-demand products. For example, they didn't invent the ultrasound heart scanner, but they've made a bundle on their version of it.

Right now, HP is busy improving another borrowed technology that is certain to bring the company a boatload of profits. It's a semiconductor laser that could revolutionize optical storage, laser printing, and fiber-optic communications.

This laser-on-chip projects a light beam perpendicular to the chip's surface, rather than parallel to it as the current technology does. I don't have the space here to go into the technical details and mind-boggling ramifications, but let me give you just one example of its blockbuster potential. HP's improved laser technology will make color printers 20 times faster than they are today.

In other words, HP's new color printers will likely render the competition obsolete overnight. That's something HP is very good at doing. You heard it here first.

Digging deep for the facts

In just a moment, I'm going to tell you about a few more American companies with great profit potential, but first, I'd like to be clear on one thing. *Forbes* is not a place to find hot stock tips. If that's your

Continued on page 8

Forbes

GREAT CALLS

PeopleSoft +205%

About a year ago, we highlighted a maker of automation software called PeopleSoft, a fast-growing company based in Menlo Park, California.

PeopleSoft enjoyed a sizzling 80% annual growth rate early in 1998, but the company's growth rate has since settled back to a more modest 45%. Meanwhile, PeopleSoft shares leaped from $8 to a stratospheric $55, then dropped back to $24.50 as of this writing.

Even with the pullback, PeopleSoft shares are up over 205% since our story ran, and since customers report a high level of satisfaction with PeopleSoft products we expect growth to accelerate again. Software upgrades and the year 2000 problem should fuel future growth.

Percentage of gain or loss as of January 19, 1999

FREE GUIDE

Discover our highest rated muni funds for 1999.

FREE GUIDE

Discover correction resistant funds for safe growth and income!

interest, check the chat rooms on the internet (and good luck, too).

Instead of trading in hot tips, we dig deep to identify the companies and situations that have real promise. We look closely at the people, the products, the strategies, the markets, the economic climate. Then, we report on who's got the best ideas, who's in the right place at the right time, who's setting the world on fire or maybe taking a wrong turn.

The idea is to put all of the facts on the table and examine them from a businessperson's point of view, and also from an investor's point of view. In so doing, we can tell you what is likely to happen 12, 18, or 24 months down the road, based on the decisions management is making today. Let me give you an example.

Texas Instruments comes roaring back

Recently Christopher Palmeri of our southwest bureau stopped in at Texas Instruments (TI) to check on their new gameplan. Sadly, TI's president Jerry Junker died of a heart attack, but the company's eager new president, Thomas Engibous, is sticking with Junker's decision to focus solely on semiconductors. We think that's smart.

As recent as 1985, TI was the world's number one producer of semiconductors. But TI's wide-spread interests allowed rivals Intel and Motorola, along with several Japanese and Korean firms, to take away market share in specialty chips, pushing TI to sixth place in the world semiconductor market.

But now TI's charging back. Already, the company is scoring big in cellular phone chips. A minor player just three years ago, TI has aggressively courted relationships with foreign manufacturers Nokia, LM Ericsson and Oki for the next generation of cellular phones, none of which wants to give business to its competitor, Motorola.

TI is now second only to Motorola in providing chips for digital cellular phones — currently a $500 million per year business but slated to double to $1 billion within two years. TI has also zoomed to the #2 spot, behind Rockwell, in supplying chips for personal computer modems.

TI's customer, U.S. Robotics, stunned the modem industry with its ever-faster modems, in large part because of TI's programmable digital chips. What's more, Packard Bell NEC recently switched from Rockwell to TI technology for modems built into its computers. Others may soon follow.

But the really big story is TI's digital signal processors. These are souped up, programmable chips that focus on one specific application, such as keeping the picture steady on a camcorder, or interpreting the outline of a baby in a sonogram machine. TI projects that digital chip sales will quadruple to $12 billion over the next four years. And it has the lead in this market, holding a 45% share to Lucent Technologies' 24% share.

Forbes

GREAT CALLS

Alumax +192%

A while back, it looked to us as if Norcross, GA-based Alumax was a good bet on an eventual rebound in aluminum prices. We were right. Aluminum demand picked up and prices moved up from 50 cents a pound to over 70 cents a pound.

Alumax stock was selling for about $18 when our story first ran. It climbed steadily on the aluminum rebound, eventually hitting $48.06 before the company was taken over by Alcoa for $3.8 billion in June of 1998.

Shares of Alumax gained 167% through the takeover date, and Alcoa shares are up 25% since then, for a total gain of 192%!

Percentage of gain or loss as of January 19, 1999

Engibous says that the digital signal processor is the biggest opportunity for TI since the invention of the integrated circuit. He knows that TI blew it once, losing its lead, but he's determined it won't happen again.

Is there an investment opportunity here? Consider what Motorola's assistant director of semiconductor marketing, Thomas Beaver, told Palmeri, "I used to worry about Intel; now, I worry about TI."

Sometimes, a company wins by having more hustle. Sometimes by having a visionary CEO. Sometimes by brilliance in product engineering. Sometimes by having superior sales and marketing. And *Forbes* shows you who the likely winners will be!

Qwest first with abundant bandwidth

From our Southwest Bureau, Toni Mack recently reported on the delicious dilemma Phillip Anschutz and Joseph Naccio face. Anschutz is the oil baron turned communications czar who founded Qwest, the nation's fourth largest long-distance carrier. Naccio is his hand-picked CEO, stolen away from AT&T.

Their dilemma? Fill Qwest's capacious new fiber-optic network and make a lot of money, or sell Qwest's capacious new network and make a lot of money. Either way, they win, and Qwest shareholders will, too!

Anschutz built Qwest from scratch, first by buying the Southern Pacific Railway Line, then by taking advantage of its rights-of-way and construction company to lay 885,552 miles of fiber-optic cable across 40 states with links abroad. That's enough capacity to handle 31 million voice calls simultaneously.

As Forbes has reported before, Anschutz defied conventional wisdom to build bandwidth when experts said no more was needed. But now, with Internet traffic growing five-fold per year, his farsighted vision has become the conventional wisdom, and it's paying off big.

MCI WorldCom and GTE are paying Qwest to lay fiber-optic cable for them. Other telcos are leasing capacity from them. Naccio has cut deals with Netscape and Microsoft to offer web and network services. He's opened CyberCenters for web-hosting and videoconferencing in 10 cities. And with costs half that of competing carriers, Qwest can sell long-distance in 120 cities at the lowest rates in the land and still maintain high profit margins.

Short term, Naccio says the company can easily double its long distance share from 1.7% to 3.4%, and that will boost revenues by $2 billion. But Qwest could also be a key acquisition for one of the local bells like SBC or Bell Atlantic, or a foreign outfit like the U.K's Cable and Wireless. Either way, Qwest shares are likely to be much higher soon!

Continued on page 11

Forbes

GREAT CALLS

Nokia +785%

In the days when cell phones were still a status symbol, we looked at Nokia Group, the mobile phone maker from Finland. The company was sharpening its phones's digital technology and ease of use—and aiming at the U.S. market.

Our investigation led us to believe that Nokia had a fighting chance to unseat Motorola as the world's biggest cell phone maker. That was in September of 1994.

It took four years but Nokia has done it, at least for now, surpassing Motorola with 25% of the world cell phone market. When our article ran, shares of Nokia were selling at $16. Today, they're at $144 — a gain of 785%!

Percentage of gain or loss as of January 19, 1999

FREE GUIDE

Discover Forbes best buys for high performance and low fees.

Forbes reviews trends in management


A fresh generation of big-money startups is built around an old technology.

The old thing behind the next big thing

By Josh McHugh

Kana Communications founder Mark Gainey

Is your Web site drowning in E-mail?

68 Forbes ■ November 30, 1998


Large-scale commerce on the Internet? Forget books and clothing. With GE in the vanguard, the big money will be in industrial goods.

Double click for resin

By Scott Woolley

132 Forbes ■ March 10, 1997


To win back younger buyers Cadillac is trying to globalize its image.

A Cadillac with a foreign accent

By Terril Yue Jones

Cadillac General Manager John F. Smith: giving a sneak peek of the future DeVille.

64 Forbes ■ December 14, 1998

E-mail becomes platform

Forbes reports that E-mail, created in 1972, is already an old thing. But it's the old thing behind the "next big thing." E-mail is fast becoming a platform, the technological bedrock of a new industry. The volume of E-mail has grown to 4 trillion messages annually and is expected to reach 7 trillion by the year 2000. Readers learn about entrepreneurs who are creating products and services related to E-mail and web marketing. *BENEFIT: new trends in business!*

Where the big money is

Forbes reports that, while consumer-oriented Internet commerce was getting the hype and hoopla, the big business was in industrial goods, projected at $134 billion by 2000. Readers learn that General Electric's Information Services division had jumped ahead of IBM, Microsoft, and Netscape in developing and selling Internet purchasing technology. GE claimed a cost savings of 10% to 15% and a five-day savings in order time. *Benefit: how it works; how you can make it work for you!*

Cadillac's mismanagement

Forbes reports that Cadillac, for years the luxury car leader, trailed Lincoln in sales in 1998 and has lost 50% of its sales volume over the last 20 years. Readers learn the problem is stodgy design and mismanagement. Baby Boomers, in particular, now entering their peak spending years, aren't interested in Cadillac's lineup. To win them back, Cadillac is giving more models a foreign edge. New designs include a Euro-style Seville, a sports utility vehicle, and a sleek roadster. *BENEFIT: Don't take 20 years to learn you're losing touch.*

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As you’ve probably noticed, we’re very good at sniffing out profitable opportunities. Very good at identifying the decisions, strategies, and changes that will have a positive impact on the bottom line a year or two down the road.

Can you learn from *Forbes*? Will you be a better businessperson or manager because of *Forbes*? Can you grow rich (or richer) with *Forbes*? I think so. But I want you to be the judge of that by trying four issues of *Forbes* magazine FREE.

Before I tell you about our special offer to try Forbes FREE with no obligation — including a FREE copy of the valuable *Forbes Mutual Funds Survey* — let me tell you about Costco, a hard-charging company that has Wal-Mart nervously looking over its shoulder.

Costco leads retailing revolution

Tim Ferguson recently reported from the Great Northwest that Costco’s warehouse stores are the hottest thing since Sam Walton took on Sears. Costco’s 15 million steady customers spent $21.5 billion last year, and you haven’t seen anything yet.

Just listen to what Charles Munger, vice chairman of Berkshire Hathaway (Warren Buffett’s phenomenally successful investment company), has to say: “It’s hard to think of people who’ve done more in my lifetime to change the world of retailing for good, for added human happiness for the customer.”

He’s talking about Costco’s chairman, Jeff Brotman, and its president, James Sinegal, who’ve been winning the latest rounds against the Walton gang. Costco has come from behind and this year should eclipse total sales of archrival Sam’s Club, the warehouse store division of Wal-Mart.

Among all retailers out there, what makes Costco special? Quality goods. Cheap prices. Low margins. Munger admires the way Sinegal and Brotman drive hard bargains for the consumer, taking a minimal cut and relying on repeat business and volume for profits.

Merchandise at Costco is priced so close to cost that the company’s gross margins including member fees last year were under 12%. By comparison, Wal-Mart’s were 21.6%. But despite the thin margins,

Continued on page 12

Forbes
GREAT CALLS

Qwest +438%

Two years ago, a lot of people thought oil and railroad baron, Philip Anschutz was crazy for wanting to build a nearly $2 billion nationwide fiber-optic network. Go against AT&T, MCI WorldCom, and Sprint? The man must be nuts.

Forbes knew better than to bet against the Denver billionaire, writing, “When folks say Anschutz is crazy, he’s usually on the verge of making a killing.” We were right and the naysayers are making themselves scarce. Qwest, The fiber-optic network he built, has already topped $3 billion in annual revenues.

Since going public at $22 in June of 1997, the stock has split 2 for 1 and climbed 438% to $59.19 per share.

Percentage of gain or loss as of January 19, 1999

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Costco's 11.5% estimated return on capital this year is in the same league as Wal-Mart's 13%.

How does Costco sell so close to cost and still make good profits? By keeping operating costs at bare-bones levels and using its capital efficiently. Munger argues that by selling merchandise so close to cost, Sinegal and Brotman are building a loyal customer base. And he's right — Costco's membership renewal rate is nearly 97%, a loyalty level unheard of in retailing.

Munger discovered Costco as a customer — he bought everything from meat to wine to office supplies at the warehouse. He even bought his wristwatch there. In fact, Munger is so impressed with the giant retailer, he broke his own rules about joining outside boards and joined Costco's.

Munger is a smart businessman. He's also a shrewd investor. And he thinks Costco is the future of retailing. What better recommendation than from the man who oversees the most successful investment company in America.

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You'll get timely financial news, commentary, and advice from our investment columnists Kenneth Fisher, Mark Hulbert, Laszlo Birinyi Jr., Gary Shilling, Marilyn Cohen, David Dreman, R.S. Salomon Jr., and Martin Sosnoff.

Frankly, we take pleasure in kicking sacred cows (when they deserve to be kicked). And even more pleasure in pointing out who has the best new ideas. Who's about to shake up the conventional wisdom. Which companies will soon dominate an industry or shower their shareholders with profits.

Continued on page 15

Forbes GREAT CALLS

We were in lonely company two year ago when we predicted that Wall Street Darling Columbia/HCA Healthcare Corp was headed for a fall.

Today, the $1.9 billion (sales) Nashville-based hospital chain finds itself mired in a massive federal investigation into possible Medicare and Medicaid fraud. Its chief executive, Richard Scott, got bounced. And three midlevel officers have been indicted in Florida.

No, we didn't predict that the feds would swoop down, but we did warn that ex-chief executive Scott was a tad too aggressive. The stock is down to $19.38 — off 57% from its high of $44.88.

Percentage of gain or loss as of January 19, 1999

Forbes shows you how to start a business


Watch out, Michael Dell. Christy Jones is out to change the way personal computers are sold. That's $70 billion and counting.

By Daniel Lyons

pcOrder's Jones **Helping PC-makers compete.**

The new face of artificial intelligence


entrepreneurs

Can clever software make it easy for a small business to shop for a health insurance plan via modem? ChannelPoint says it can.

Health insurance.com

By Doug Donovan

High hopes for the Web: the Hollens.

Solve a problem

Forbes reports how 29-year-old Christy Jones is helping Compaq, IBM, HP and other PC makers battle Michael Dell, who's been eating their lunch by selling computers direct online. Jones' new company, PCorder.com, uses artificial intelligence and a vast database to match Dell's efficient order-and-delivery system. The technology allows corporate customers to go on the web, scan thousands of computer parts on the database, get prices and availability, then order and receive delivery from a distributor in a few days. Compaq, IBM, HP, along with the three largest computer distributors have signed on. *BENEFIT: Find a problem and start a business that solves it.*

Find your niche

Forbes reports on Kenneth and James Hollen who found a niche worth exploiting in small business health insurance. They started ChannelPoint, an internet-driven software company that aims to cut inefficiency and overhead in establishing health plans for companies with fewer than 50 employees. Until now, the process of providing quotes, reviewing applications, and entering enrollments for these firms took a month and cost the industry $54 billion annually. ChannelPoint's software does the same thing online in a matter of hours. The Hollen brothers project $20 million revenue in 1999. *BENEFIT: Find your niche and use the internet!*

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Forbes provides advice on personal finance

Taxing matters

Saving to the max

If your employer won't let you put a full $10,000 into your 401(k) plan, find out why.

By Ashlea Ebeling

THE CEILING on tax-deductible contributions to a 401(k) account is supposed to be $10,000 this year (and next). But a lot of employees, especially higher-paid ones, never get near this ceiling; they may be capped out at smaller amounts, perhaps shorted by thousands of dollars. The problem afflicts managers at hundreds of companies, such as Land O'Lakes and American General Corp.

That's because their employers get trapped by complex rules designed to protect lower-paid employees. And high pay, in this case, doesn't just mean executives. The restriction snags many earning less than $100,000 per year.

If you are in this unfortunate situation, take another look at your 401(k) plan and find out what your employer is doing to upgrade it. IRS rules released in November should make it easier for your ceiling to go up to $10,000. To take advantage of the new rules, however, your company may have to be a little more generous with its matching contribution. That's why it may take some prodding by you and other workers to get the ceiling raised as high as it can go.

Under the current system, all companies with 401(k) plans must pass complex "nondiscrimination" tests annually. The tests are intended to coerce firms into encouraging lower-paid employees to save more. But complying creates nightmarish paperwork with unpredictable results.

The tests measure two things at each company: the average employee contribution as a percentage of salary, and the average employer match. What's required, in general, is that the averages for highly paid employees don't exceed the averages for other workers by more than two percentage points. Highly paid, here, means those who earn more than $80,000 per year or own more than 5% of the company. If a firm fails a test, it must either reduce contributions made by highly paid employees or add money to other workers' accounts. It isn't hard to guess what often happens: High-paid employees find part of their contributions kicked back to them, generally at year-end.

The new rules allow an escape from all this complexity and uncertainty. They're also intended to convince more companies to offer 401(k) plans. Starting next year, companies can bypass the tests by contributing to non-highly paid workers' 401(k) accounts in one of two ways. The first is to make a company contribution equal to at least 3% of each employee's compensation, regardless of whether the employee contributes.

The other option is to match employees' contributions dollar-for-dollar on the first 3% of their pay, and 50 cents on the dollar on the next 2% of pay—a total match of 4% of salary. With either option, the company can't give highly paid employees a better deal.

Even the latter option would cost many companies more than they now spend, since the typical match currently tops out at 3% of salary. But the benefits of this so-called safe harbor from the nondiscrimination tests may outweigh the costs, says Elinor Merl, a principal with Towers Perrin. That's particularly true for companies that already provide a generous match.

What will irk employers, though, is that the new rules require immediate vesting of the match. The rules also let workers take that money anytime they leave the company. Under current rules, employees often have to forfeit some matching funds if they leave before the end of the year.

Welcome as they are, the safe harbor rules won't turn stingy firms into Santa Clauses. "There are a lot of companies that don't match at all," notes David Gelman, a pension consultant in New York City. "For them, the thought of having to give away 3%, or start matching, is out of the question." But if employees rally around the new rules, companies just might come up with the cash. ■

256 Forbes ■ December 14, 1998

Saving to the max

Forbes reports that the ceiling on 401(k) contributions is $10,000 but many companies prevent their employees from reaching that amount. The problem has been strict IRS "nondiscrimination" rules designed to discourage employers from paying higher match funds to higher-paid employees. The unfortunate result was nightmarish paperwork and a cap on higher-paid employee contributions. Readers learn that the IRS has now eased its rules, allowing employers more options. *BENEFIT: how to get the full benefit of your 401(k).*

INSURANCE

Cheap life insurance can sometimes be just that—cheap.

The incredible shrinking death benefits

By Carolyn T. Geer

GOOD DEAL. Or so it seemed. Citibank offered its credit card customers term life insurance that would pay up to $100,000 in death benefits for as little as $360 a year for a 40-year-old man. No medical examination was required—just a few health questions. The premiums would be automatically billed to customers' Citibank MasterCard or Visa.

Policyholders were not required to reapply every year. Citibank promised that benefits would never go down regardless of the policyholder's health or age.

Between 1987 and 1991 some 100,000 people took the bait.

Many of them soon regretted it. In 1993, less than two years later, Citibank informed more than half its customers that group term benefits were being cut and premiums were being raised. The maximum coverage on all existing policies was reduced to $50,000.

Here's what happened.

The original underwriter of Citibank's policy was a division of Cigna. Citibank formed a trust in Alabama, and Cigna issued a series of group life insurance policies to the trust. Citibank customers were deemed to be members of a group and were therefore eligible for lower-cost coverage under the group policies.

As administrator and marketer, Citibank pocketed as much as 65% of the premiums. Cigna took the rest and was on the hook for the death benefits.

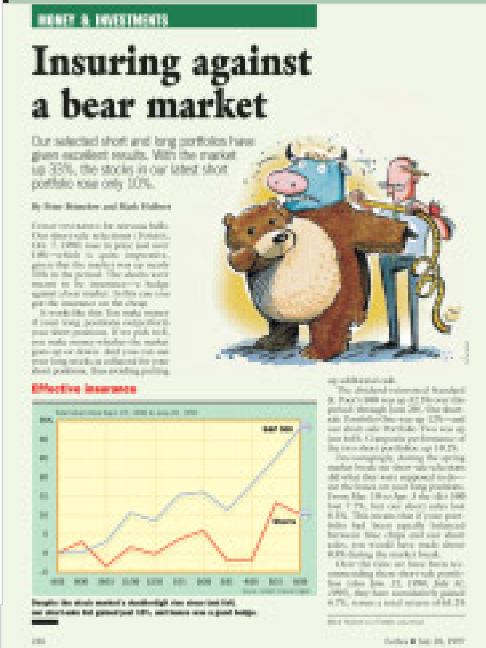
But in 1991 Cigna began complaining that claims for death benefits on the Citibank policies were higher than expected and that it wanted to raise premiums.

Citibank dumped Cigna from the contract and in the fall of 1991 signed on Allianz Life Insurance Co., an affiliate of Allianz, Germany's big insurer. The company immediately

Forbes ■ August 25, 1997 69

No free lunch

Forbes warns of cheap term life insurance offers. Readers learn that Citibank promised $100,000 in death benefits for as little as $360 a year for a 40-year-old man — benefits that would never go down, regardless of the policyholder's health or age. 100,000 people signed up. Later, Citibank cut the benefits in half and raised premiums 15% to 74%, citing higher-than-expected costs (the fine print allowed them to do it). *Benefit: reminder that if it looks too good to be true, it probably is.*



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William Baldwin

Bill Baldwin, Editor

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Forbes GREAT CALLS

A while back, Cheasapeake Energy looked to us like a highflier headed for a fall. Enamored investors had bid up the stock to 67$\frac{1}{4}$, giving the Oklahoma City-based oil and gas company a market capitalization of $2.3 billion.

But Cheasapeake's accounting was aggressive, reporting one of the highest percentages of "undeveloped" reserves ever seen in the industry.

"Is Cheasapeake's oil worth almost five times the average?" we asked. "Doubtful."

We got it right. The company announced a pretax charge of $200 million on poor results from its highly touted Louisiana wells. Falling oil prices took care of the rest. This former highflier has fallen to $1 per share.

Percentage of gain or loss as of January 19, 1999

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