

FREQUENTLY ASKED QUESTIONS

ADAMS FINANCIAL CONCEPTS

Frequently Asked Questions

Q: Do you open Transaction based accounts? If not, why?

A: We open fee based accounts as a Registered Investment Advisor. Adams Financial Concepts has found fee based managed accounts are more cost effective and are more consistent than the transaction accounts he has managed.

Q: Can I make an appointment?

A: Yes, please call (206) 903-1019 for an appointment.

Q: Do you travel?

A: For accounts \$250,000 and above, A. Michael Adams will travel.

Q: If I live in a State where you are not registered, what do I have to do?

A: Contact us so we can explain the process.

Q: Do you do Seminars?

A: I have in the past and would consider it again if there was an important or critical topic to discuss.

Q: I have noticed your fees are on the higher end of the market, why?

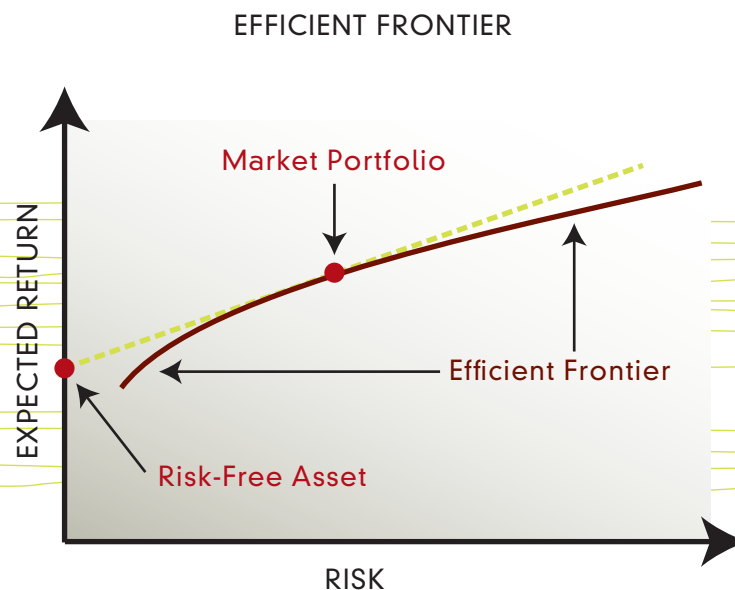
A: We believe that pricing should reflect performance. Warren Buffett states: "The .350 hitter expects, and also deserves, a big payoff for his performance - even if he plays for a cellar-dwelling team. And the .150 hitter should get no reward - even if he plays for a pennant winner. Only those with overall responsibility for the team should have their rewards tied to its results."

Q: Can you mail or email me the newsletters as they come out?

A: Yes, please fill out the form on our Contact us page.

Q: What are "Bottom Up and "Top Down" (Modern Portfolio Theory) Approaches to Investing?

A: These are two systematic approaches (and some combinations of the two) to building portfolios. A. Michael Adams subscribes to building portfolios in the "Bottom Up" approach.



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Frequently Asked Questions (continued)

The "Top Down" (Modern Portfolio Theory) approach was begun when Harry Max Markowitz wanted to quantify stock price movements. He theorized that stock price fluctuations were due to two influences. The first was the overall stock market. When the stock market is moving up, there is a tendency for all stocks to move up; and conversely, when the stock market moves down, all stocks tend to move down. Markowitz termed this portion of the volatility "beta risk." Markowitz further defined company specific risk, or "alpha," as the volatility due to the impact of company specific volatility. Markowitz went further to define what he termed "The Efficient Frontier" and theorized there existed a relationship between return and risk where the higher return was associated with higher risk. Removing the beta portion of volatility would leave a curve defining the Efficient Frontier (see chart previous page).

In 1986 Brinson, Hood, and Beebower (BHB) published a study about asset allocation of 91 large pension funds measured from 1973 to 1985. Their findings showed the great majority of risk (volatility) was due to the beta factor. Subsequent studies of mutual funds and pension funds confirmed this study and depending on the source, generally accepted by Modern Portfolio Theory adherents is that between 85% to over 90% of the risk (volatility) is due to alpha risk and little is due to the beta or company specific risk.

The Top Down approach to investing, then, begins with looking at the economy and making forecasts of which industry will have the best returns and then looks at the specific companies within that industry. The Top Down approach tends to seek a diverse portfolio spread across industries.

On the other hand, the Bottom Up approach to investing overlooks economic conditions and focuses on selecting stocks of companies which have favorable attributes. This approach assumes that companies can do well even when their industry is not doing well. It entails a thorough review of the company: its financials, its products, its competitive position, its management.

In 1997 William Jahnke challenged the results of the Brinson, Hood, and Beebower study. Jahnke using the same data found the 10 year annual returns of the benchmarks for the 91 pension portfolios ranged from 9.47 percent to 10.57 percent (a spread of 1.1 percent). The actual returns of 91 pension portfolios were 5.85 percent to 13.4 percent a spread of 7.55 percent). Based on this, the expected range of 1.1 percent divided by the actual range of 7.55 percent means that asset allocation explained just 14.6 percent of portfolio performance.

The phrase "Don't put all your eggs in one basket" is a strategy of diversification and part of the Top Down (Modern Portfolio Theory) approach to investing. Warren Buffett, perhaps the greatest investor of our time prefers the other approach (Bottom Up) saying, "Put all your eggs in one basket and watch the basket."

Q: What is meant by alpha and beta and the efficient frontier?

A: Alpha Risk: The risk specific to a company regardless of whether the market is up or down. Alpha is a coefficient which measures risk-adjusted performance, factoring in the risk due to the specific security, rather than the overall market. A high value for alpha implies that the stock has performed better than would have been expected given its beta. For example, an alpha of 0.4 means the stock outperformed the market-based return by 0.4%.

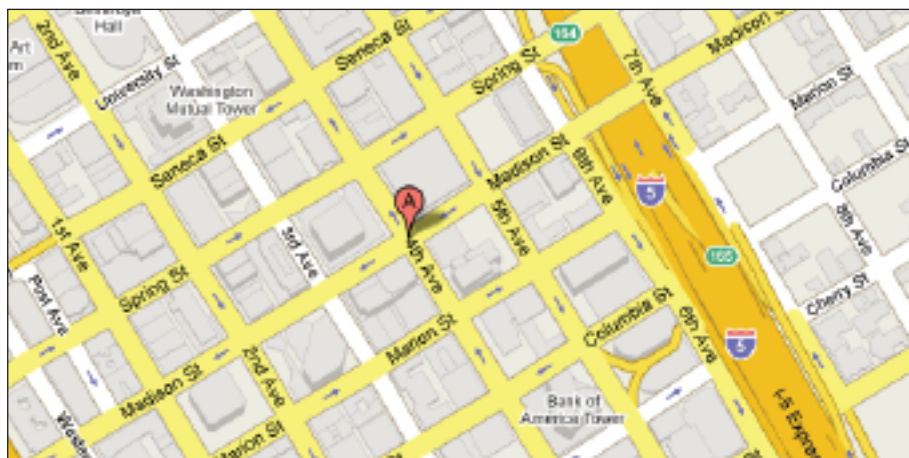
Beta Risk: The risk or volatility relative to the market. A stock with a beta of 1.0 will tend to move higher or lower in tandem with the stock market. A stock with a beta of over 1.0 will tend to move with greater fluctuations than the market and a stock with a beta of less than 1.0 will tend to have a lesser fluctuation than the market.

Efficient Frontier: In Modern Portfolio Theory, the efficient frontier is the line on a risk-reward graph that is comprised of all the efficient portfolios that theoretically are the best return that can be achieved for any given risk level.

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