Sentinel Trust Company

On Watch

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Private Flight Options

WILLIAM R. BERGER, CFA, CPA
LISSA GANGJEE, J.D., CFP®
Senior Client Relationship Officers

In This Issue:

IF YOU ARE LOOKING FOR THE BEST PRIVATE-JET TRAVEL bang-for-your-buck, there are five options to consider: private jet hours ("on-demand"), blocks of time ("block charter"), a fractional card, a fractional interest, and purchasing your own private plane.

The biggest factor in making this decision is the number of hours you plan to fly annually, as the cost per hour decreases dramatically with every hour flown. Accordingly, if you aren't flying more than 250 hours per year, chances are one of the many leasing options may be more effective than buying your own plane.

Story continued inside.

Private Flight Options continued.

On Demand

At one end of the spectrum, on demand aircraft are turnkey, hourly, private jet rentals which do not require a contract commitment. So, you buy what you need when you need it, but you will pay a premium for the flexibility. Most services require two-hour prior notice for availability. Generally there is complete flexibility within the lessor's fleet, which means you may charter any type of jet. Some even offer pick-up and limo service. However, if you are flying one way or staying at your destination for a long period of time, you will need to pay a "deadhead" fee in order to return the aircraft to its origination point. As crews and aircraft vary, so can the quality of experience. On demand aircraft are generally appropriate for someone flying privately up to 50 hours per year, but be prepared to spend up to $100,000-$150,000 for the privilege. Providers include ExcelAire, Executive Jet® Management, and Jet Aviation.

Block Charter

Moving along the continuum, block charter aircraft allow you to pre-purchase aircraft hours at discounted rates without being hemmed in by a contract term. That is, your hours never expire. The more hours you pre-purchase, the greater the discount and, generally speaking, a block charter is a better deal than purchasing on demand. As with on demand, there is a choice of aircraft type and a deadhead fee will apply. Aircraft owners are usually licensed resellers of unused fractional shares or charter brokers who sell blocks of time at a discounted rate, not an aircraft owner himself. So, quality of crews and aircraft vary and there is no depreciation available to a block charter purchaser. Block charter deals are usually best for those who know they will fly 25-75 hours per year and are willing to pre-pay $50,000-$250,000 for those hours. Providers include Bluestar and Sentient.

Fractional Cards

Fractional cards allow you to purchase one-sixteenth (the equivalent of 50 hours), eighth, quarter, or whole segments of ownership. Flying time is charged against hours accrued on your card. There is a contract term, which means you will need to use or lose your flight hours during the 12 contracted months, and fleets are limited. The upsides of fractional interest cards include that you typically will not pay a deadhead fee; the quality of crews and aircraft is consistently high; and the cards are relatively easy to use. On the downside, you are not permitted to depreciate the asset for tax purposes. Fractional cards are the best option for someone flying 25-100 hours annually who does not mind an annual contract term. Annual costs range from $100,000-$400,000. Providers include MarquisJet and FlexJet.

Fractional Ownership

In many respects, fractional ownership allows you the benefits of owning your own plane without financing the costs of hanger or tie-down time because someone else is, theoretically, using the plane (and paying for it) when you are not. There is no deadhead fee. Contract terms generally are five years and you may be able to depreciate the cost if the plane is used for business purposes. The quality of crews and aircraft are consistently high, but your fleet is limited. Fractional ownership is best for someone flying 50-250 hours annually and who is willing to pay $600,000-$1.1 million for the privilege. Providers include NetJets, Citationair, and FlexJet.

Complete Ownership

Buying a private plane may become cost-beneficial, that is you will have the lowest operating cost per flight hour, if you are flying more than 250 hours annually, though it will cost you upwards of $5 million when you take into account the purchase, direct operating costs (fuel, maintenance resources, etc.) and fixed costs (pilot, crew, insurance, hangar, training, charts, etc.). There currently is a glut of good-quality, used aircraft available, so it is a good time to be in the market. You might be able to recoup your purchase price (net of depreciation) upon sale. Advantages include no deadhead fee as the plane stays with you wherever you go; you control who rides on your aircraft; you hand-pick your staff; and you outfit, equip, style and decorate the aircraft according to your tastes. You may only use the plane you buy, though, and cannot go up-market for long-haul flights and down-market for short hops. Depreciation may be allowable for business use, but be ready for an IRS audit – it is almost a given – and keep excellent records of the plane's use.

When buying a plane you should find an honest, reputable consultant to help you locate the right aircraft, negotiate the best deal, and set up the correct ownership infrastructure. You should own a private plane in a standalone entity in order to limit liability. Furthermore, the entity should lease, rather than directly hire, your pilot and crew for the same reason. You should consider outsourcing maintenance, upkeep and recordkeeping to a qualified aviation management firm. In order to limit significant financial exposure related to unexpected maintenance requirements (e.g., your plane requires a new engine that costs one-third of the plane's total value), you should source a quality insurance policy before buying the plane. Lastly, given today's low interest rates, it might be worth financing the cost if you think you can better invest those funds elsewhere.

When considering your private aviation options, cost effectiveness of your purchase is key. Other variables you might consider are typical city origins and destinations; distance flown; passenger loads (in order to determine the best size and class of aircraft); typical mission (roundtrip vs. one way); whether you need to employ multiple aircraft simultaneously; flexibility of travel requirements to minimize blackouts or peak periods; passenger predictability and punctuality; and your desire for consistency in service and performance standards. Regardless of the solution that's right for you, there are many service providers at every point along the private aviation continuum who can provide the quality of service, safety and cost effectiveness you desire

International Micro-Cap Value Stocks:

Tiny Niche or Something More?

BRUCE L. SWANSON, PH.D.
Chief Investment Officer

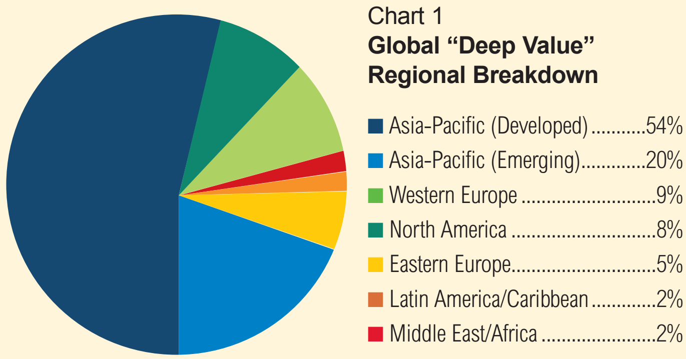
Please ignore this article if you believe that U.S. Large Cap Multinationals represent all the stock market exposure you really need or that the secret to investment outperformance is to make long-term investments in great companies. Please continue if you believe there is a big difference between a great company and a great investment; price matters - the best way to outperform is to buy something for much less than it is worth; and opportunities vary across countries and sectors over time as asset prices respond to the extremes of sentiment and liquidity.

Conventional Wisdom vs. A Different Perspective

With equity market capitalizations of between $10 million and $250 million, global micro-caps account for only $1.6 trillion, or 3.2% of the world equity market. Non US micro-cap stocks represent only 2.7% the world equity capitalization, with non-US micro-cap value stocks representing only 1.35% of the world equity market. Conventional wisdom holds that this segment of the equity market should be ignored because it is immaterial.

However, academic research has concluded that exposure to small cap and value factors is an ongoing source of alpha (outperformance). Our experience is that active management within the extreme-value international micro-cap space can indeed generate significant additional returns.

Chart 1
Global "Deep Value" Regional Breakdown



Additional segmentation is helpful in understanding the investable opportunities in the international micro-cap value space. The 23,000 global micro-cap stock universe accounts for 63% of all investable equities. The nearly 20,000 international micro-caps account for 85% of the global micro-cap universe and 54% of all global equities. There are 5,100 investable global micro-cap value stocks, as identified with a simple filter (price-to-earnings ratio less than 10). Of these, 95% or 4800 are international. This means international micro-cap value stocks total 13% of all global equities and 65% of the 7400 global value stocks.

A Deeper Dive

A more granular analysis reveals that "extreme value" is really found only in the smallest 3% of firms by capitalization. This is where price, the notion of shopping for something really cheap relative to value, comes into play in identifying opportunities. Unfortunately, conventional small-cap funds and self-described micro-cap funds rarely provide this exposure, at least in a concentrated form.

Using an extreme-value balance-sheet metric, 93% of all non-US firms with a net liquidating ratio (current assets less total liabilities, divided by market capitalization) above 1.0 had market capitalizations less than $250 million. 82% have capitalizations less than $100 million and less than 3% had market capitalizations in excess of $500 million. Using an extreme-value income metric: 81% of all non-US firms with Enterprise Value divided by Earnings Before Interest, Taxes, Depreciation and Amortization ratios less than 3.0 had market capitalizations less than $250 million; and less than 10% had market capitalizations in excess of $500 million.

Country/Region Breakout

Considerable regional variation exists, with Developed Asia seemingly awash in cheap stocks (8.0% of all stocks passed the value filter), while North America (1.5%) and Middle East/Africa (1.4%) presented fewer opportunities. Of all major countries, value stocks were least likely to be found in the US (1.3%), Sweden (1.1%) and Switzerland (0.3%). The best "value markets" were Japan (13.1%), Singapore (11.9%), Romania (9.5%), Hong Kong (9.1%), Argentina (7.3%), Vietnam (6.8%), Russia (5.8%) and Malaysia (5.8%). Micro-cap exposure is required to access deep-value opportunities, as such stocks accounted for at least 84% of all deep-value stocks for every region.

The charts highlight the radically different country and regional portfolio weights that might result from the application of a value-based process (Chart 1) versus a conventional value-indifferent market cap weighted approach (Chart 2). Chart 3 reveals the concentration of deep-value stocks among the smallest firms, those with market capitalizations under $250 million, often under $100 million. A hypothetical global value equity portfolio would have an Asian weight of 74% and a US weight of only 5.6%, far below its 35.2% capitalization weight. Micro-cap stocks would account for nearly 86% of the portfolio.

Of course, sheer numbers of companies, no matter how they are sliced and diced, do not themselves justify investing in a segment of the market. Real life portfolios would never approach these extremes of geographic mix or micro-cap exposure. However, if you can ferret out opportunities in the deep-value small-cap segment of the international markets, our experience is that significant returns are possible.

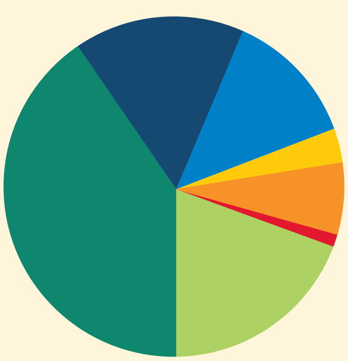


Chart 2
Conventional "Cap-Weighted" Regional Breakdown

- North America 39%
- Western Europe 21%
- Asia-Pacific (Developed) 17%
- Asia-Pacific (Emerging) 14%
- Latin America/Caribbean 5%
- Eastern Europe 3%
- Middle East/Africa 1%

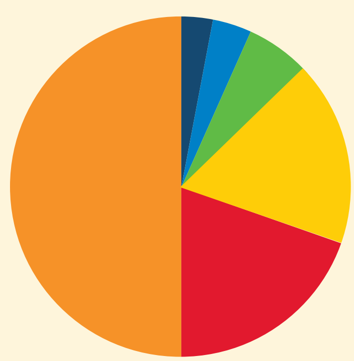


Chart 3
Global "Deep Value" Stocks - Market Cap Breakdown ($Millions)

- $1,000 ....3%
- $500-1,000 ....4%
- $250-500 ....7%
- $100-250 ....16%
- $20-100 ....50%
- $10-20 ....20%

Engaging the Next Generation in Your Family Foundation

LISSA GANGJEE, J.D., CFP®
Senior Client Relationship Officer

A family foundation can be a perfect venue for engaging younger family members in the stewardship of a family's wealth and philanthropic mission. While there is never one path to success, there are some easy ways to increase the next generation's involvement.

Encourage them to contribute their time by volunteering for an organization related to the foundation's mission. Before they begin, discuss appropriate behavioral decorum. Use the experience to begin intergenerational conversations about money and giving in their communities.

Invite a next-generation family member to intern or work on the foundation's staff. Make sure to set up clear policies, including a job description and compensation guidelines. Consider the age-appropriateness of employment options. Offer a variety of roles within the organization – from administrative to strategic work.

Organize educational opportunities for the next generation by creating opportunities for mentorship, peer networking, site visits, internships, participation in committees, as well as attendance at board meetings, conferences and workshops. Invite the targeted young people to plan and manage their own events with the help of a guide. Encourage peer networks both within and outside the family foundation; these are often invaluable for young people to support and challenge each other in their thinking about wealth and social philanthropy.

Ask the family's young people, who are not yet trustees, to allocate discretionary or small matching grants in accordance with their own personal giving. If appropriate, these funds may be outside the foundation's primary funding areas. Ensure, however, that these "side pockets" are not used as a means to avoid dealing with ideological differences on the board.

Create a junior board by convening a committee of the family's young people to recommend how the foundation should allocate a pool of foundation funds. Offer support from a foundation staff member or mentor, but allow the next generation to manage its own grant-making process as a group. Clarify the short and long-term goals for the next generation's involvement in the foundation and the junior board. Is it a promotion track? What are the opportunities for new leadership in the foundation?

Ask one or more next generation members to participate as trustees of the foundation board. Prepare them for success by providing adequate board training. When possible, ask more than one next-generation member to participate simultaneously in order to ensure they have a strong voice and are not silenced because of their youth. This step may necessitate or even provoke a cultural shift within the foundation – requiring meetings to be held on weekends or school vacations, simplifying more traditionally used jargon, and being creative in the ways the foundation makes itself fun and accessible.

Regardless of the path chosen, one of the most valuable aspects of involving the next generation is the opportunity for intergenerational dialogue. Often, young people who are part of family foundations are looking for broader conversations with their families and peers about their identities in relation to money. By involving young people in philanthropic endeavors, the results will almost certainly be a more educated, engaged and savvy next generation, prepared to better shoulder the blessings and burdens of wealth.

Sentinel Trust Company provides custom integrated planning, investment, fiduciary and administrative solutions to affluent families and their closely held businesses and entities.

Founded in 1997 as the successor to two 40-year old, investment-focused family offices, today Sentinel offers the stability of an institutional firm, the entrepreneurial spirit of a young firm, the personal feel of a family office and the in-house technical skills of independent planning and investment management firms.

For further information, please contact Anthony DeToto, Senior Vice President, at adetoto@sentineltrust.com or 713.559.9578.

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Contributing to this issue:

David A. Bristol, Jr.
William R. Berger, CFA, CPA
Anthony J. DeToto
Lissa Gangjee, J.D., CFP®
D. Fort Flowers, Jr., CFA
Ross W. Nager, CPA
Tina J. Schockling, CFA
Bruce L. Swanson, Ph.D.

For additional information about the topics presented in this newsletter, or to be placed on our mailing list for future editions, please contact Anthony DeToto at adetoto@sentineltrust.com or call 713.559.9578.

2001 Kirby Drive, Suite 1200

Houston, Texas 77019-6081

713.529.3729

www.sentineltrust.com