



# You Bought A What?!

**S**HOULD I HAVE WRITTEN A COLUMN ON ANNUITIES? I've been in this space for 21 years but have never seen the need to say the obvious, which is that an annuity is just a mutual fund dressed up with some punitively stiff fees. (I am talking only about the most common form of annuity—the deferred annuity sold as an investment account. The other kind, the instant annuity that converts a lump sum into a monthly lifetime payout, is another matter.)

A FORBES reader from Mutual, Ohio recently reminded me that it is sometimes useful to state the obvious, if that will protect investors from making serious mistakes. The reader told me that he had bought a variable annuity and wanted advice on what to do next. The damage, though, was done. Broker-sold annuities levy killer annual fees, in large part to compensate the brokers who sell them. You are required to keep your money in place for a while—seven years is typical. You can get out early only by paying a huge exit fee to make up for the vendor's lost chance to extract that annual fee.

Maybe I was too hard on the poor fellow who wrote in. I instructed him that he should never, ever again make any financial decision. Have a spouse or offspring do it. If no one loves you, have your county court conserve you. Buying a deferred annuity proves you are a serious dupe. Seriously.

The only ones benefiting from annuities are the insurance companies issuing them and the sales reps selling them. Sales reps usually lie. They never tell the whole truth. That is, they may mention the annual fees and the exit penalty, but they rarely clarify how strongly motivated the broker is to push you into this particular product. The sales commission, paid out of those annual fees you are committing to, can easily be 8% to 16% of the amount you invest. And almost never does the salesman disclose the fundamental fact that you'd be better off investing similarly outside the annuity—for example, in a plain old mutual fund.

The tax deferral that comes with deferred annuities is costly, unless you live for centuries. Under present law the tax rate on capital gains and dividends is 15%. The annuity defers this tax, but at the cost of more than dou-

bling the rate. Profits from annuities are taxed as ordinary income, at rates up to 35%. Ouch!

The hot new type is equity-indexed annuities. These give you a sliver of upside potential while promising that your principal will not shrink. I do mean "sliver." And your principal may shrink. There's not much left for potential gain, not when you have paid for the put option (the supposed guarantee against loss) and paid for the broker's golf club membership and kids' college.

Instead of losing money while insurers use yours to buy stocks for themselves, buy good stocks directly and hold them.

France's **Suez Lyonnaise (29, SZE)** is a well-run, diversified (but very cheap) utility. It sells electricity in the Netherlands, Belgium and Luxembourg, and natural gas across Europe and America, with more flexibility than competitors; it is also the world's second-largest water treatment services firm, with

big economies of scale. It sells at discounts to industry norms at 58% of its \$50 billion of annual revenue and 13 times trailing earnings. Yield is 3.6%.

**Millipore Corp. (61, MIL)** provides tools for drug development. Its key technologies are membrane filtration and chromatography that use size exclusion to filter fluids for bacteria and viruses. At 25 times earnings it isn't cheap compared to the market, but it's a bargain for a proven profitmaker in biotech.

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**Mine Safety Appliances (44, MSA)** is the global leader for safety products for workers in hostile environments. It sells gas masks, combat helmets and toxic-detection instruments for construction workers, firefighters, miners and soldiers. This is a growth field as global incomes rise. New products are driving growth further as entries of the last three years deliver a third of sales. Global distribution lets Mine Safety catch more than its share of the growth. At 18 times this year's earnings and 1.8 times revenue, this is a classic growth firm at marketlike valuations.

In July I detailed why, despite popular mythology, there is no housing bubble. If you believe housing won't implode, then **Williams-Sonoma (40, WSM)** is a contrarian's dream. As America's leading retailer for home decor and kitchen needs, it operates five successful retail store concepts and has a heavy repeat customer base. Almost half its revenue comes from catalog and Internet sales. It is a much-better-than-average firm selling at marketlike multiples of 1.4 times revenue and 20 times this year's earnings. **F**



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