



Two Shades of Green

We may be witnessing a worldwide economic shift of historic proportions. In the second half of the twentieth century, America's industrial and manufacturing economy evolved into an information and service economy. Today, a new source of wealth and productivity appears to be emerging: the eco-economy.

Environmentalism has been a national issue for over 40 years, and conservation and sustainability issues predate the founding of our country. But something is different today. With global warming gaining credence as a genuine threat and oil topping \$108 per barrel, green now begets green: there is economic opportunity in energy efficient, Earth-friendly products and services. And where there is economic opportunity, there is innovation and entrepreneurial problem solving. And there is money to be made by entrepreneurial investors!

YOUR TAX DOLLARS AT WORK

John McCain, Hillary Clinton and Barack Obama all discuss global warming on their campaign websites, which is pretty impressive when you consider that some politicians and members of the press still denigrate the concept as junk science.

That Democrats tout environmentalism is no surprise, but the presumptive Republican nominee's outspoken position has some predicting he will be the most environmental President in history, if elected.

McCain's environmental credentials date back to his time in the Arizona legislature and early days in Washington, when he worked for land conservation and protection of the Grand

Canyon. In 1996, McCain cemented his reputation as a maverick by calling his fellow Republicans to task in a New York Times editorial titled, "Nature is Not a Liberal Plot."

In the editorial, McCain asked, "Have Republicans abandoned their roots as the party of Theodore Roosevelt, who maintained that government's most important task, with the exception of national security, is to leave posterity a land in better condition than they received it?"

McCain organized the first serious Senate hearings on global warming, and worked hard to pry his fellow Senators' heads from the sand, especially the sand of the Middle East. In April of 2007, he spoke on energy policy and reminded his colleagues that, "The United States has coal reserves more abundant than Saudi Arabia's oil reserves. We found a way to cut down acid rain pollutants from burning coal, and we can find a way to use our coal resources without emitting excessive greenhouse gases."

Perhaps more surprising to his associates was McCain's clear declaration: "The burning of oil and other fossil fuels is contributing to the dangerous accumulation of greenhouse gasses in the earth's

atmosphere, altering our climate with the potential for major social, economic, and political upheaval."

Critics contend that McCain has been all hat and no cattle on the topic of global warming, speaking out but rarely acting. During his current presidential campaign, McCain has missed 15 Senate votes on environmental issues, including two that lost by a single vote. It is possible that McCain has only embraced global warming as a campaign issue that would otherwise belong to the Democrats,



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We will be speaking at the 3rd Annual Value Investing Congress West taking place on May 6 & 7, 2008 in Pasadena (between the Berkshire Hathaway and Wesco Annual Meetings). This will be our third time speaking at this event and we highly recommend it. Every event features a stellar line up of speakers who share their investment strategies and talk about their current stock picks.

As Congress speakers we were able to secure a special discount for our guests. If you would like to attend, please register by March 9th with discount code: P8WC1 and you'll get \$200 off the early bird rate, for a total savings of \$1,200. We are told that seats are going quickly, so register as soon as possible. For more information and registration details, please visit www.ValueInvestingCongress.com.

We've seen the Congress grow into a dynamic community of value-oriented investors and we're proud to be a part of the Congress. We hope you'll join us in Pasadena to experience the Congress for yourself!

but his support of carbon cap and trade legislation, opposition to drilling in the Arctic Wildlife Refuge, and long history of voting for environmental accountability have earned him the endorsement of groups like Republicans for Environmental Protection.

The candidates' environmental bona fides may be a moot point; economic necessity could drive the next president, Republican or Democrat, to initiate action on climate change, energy self-sufficiency, water and air pollution, and public lands protection.

FOLLOW THE MONEY

Blogger Mark Pawlosky pointed out in his January 18, 2008 entry that "As one key economic indicator after another - housing, finance, autos, retail - sputters and stalls out, the fledgling eco-economy is purring right along, fueled in no small part by venture capital firms hungry for new opportunities in industries that promise outsized returns on their investments. In the first three quarters of 2007, VCs poured \$2.6 billion into alternative energy and clean-tech firms..." This was more than VCs invested in those areas during all of 2006.



First Solar (FSLR) may be a good example of the opportunity presented by expensive oil and our nation's growing interest in Earth-friendly technologies. The company offers a proprietary thin-film semiconductor technology as an alternative to more expensive silicon. Many companies will grow fast as capitalists invest in the burgeoning eco-economy, but fad investments often lose value just as quickly. Entrepreneurial investors must evaluate the long-term prospects for each company.

Before we jump for joy, let us recall that venture capitalists promoted and buoyed the last "new economy." But of course, there's a tremendous difference between the tech bubble and the eco-economy: there's a real market for solutions to real problems. The importance of John McCain's position on climate change is that he brings the credibility of a skeptic to the issue; it's an "only Nixon could go to China" moment.

Do people really need official confirmation before they believe that they shouldn't waste resources, or pollute their own air and water? Sadly, some people do, but disbelief and/or ignorance have not been the limiting factors in building an eco-friendly economy. Look at how quickly people embraced compact fluorescent bulbs. Yes, these bulbs have their own problems, but the more significant point is that given an economical choice, people want to buy energy-efficient, Earth-friendly products.

Generating economical choices takes time. When Kinko's introduced recycled paper in the mid-1990s, it cost a penny per page more than virgin paper, and customers, even in ecologically activist markets like Portland, Oregon, balked at the price. Over time, recycled and virgin paper came closer in price; now people use recycled without a second thought. The same factors will affect the eco-economy: expensive oil may make the price of competing energy sources more palatable to the public, which will increase production and lower prices.

High oil prices create huge economic incentive to develop economically viable alternatives, which is why we believe high price is the answer to high price. This incentive creates jobs, raises attention, and generates profits for some, although many won't make it. Strong economies include lots of failures; research and development is expensive. Marketing mistakes can torpedo fine products. Only the pursuit of outstanding profits motivates people to take such risks. With America's traditional entrepreneurial zeal and our new political will, we can seize the opportunities presented by the Green economy and make the world a better place in the bargain. ▲

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Theory X and Theory Why

Think about the world in 1960. Senator John Kennedy was running for President, the Beatles were still playing small clubs in Liverpool and Hamburg, men still wore suits and hats when going for a walk in the park, Europe and Japan were still recovering from the devastation of WWII, and the United States was the international center of finance, industry and manufacturing. Despite America's rising wealth and experience, business management techniques in 1960 were little different from those of 1930.

In 1960, Douglas McGregor of the MIT Sloan School of Management published *The Human Side of Enterprise*, in which he asked leaders to reconsider their beliefs about human resource management. McGregor's work played no small part in the rapid increase in American innovation and the eventual rise of Japanese management excellence. McGregor explained what exceptional leaders like David Packard and Bill Hewlett had discovered for themselves - that individuals respond differently to different types of motivation, depending on each individual's personal needs.

Using Abraham Maslow's hierarchy of needs as a point of departure, McGregor described Theory X and Theory Y models of management. Theory X had been the dominant model up to that time, and assumed that human beings inherently dislike work and seek to avoid it. Because of this, people must be coerced or controlled by management, often through threats. According to Theory X, people work only for money and security. Since Theory X assumes that people dislike responsibility and want to be directed, there is no ill will in management's establishment of highly structured, top-down hierarchies. Such structures seem the only logical way to achieve organizational goals.

McGregor recognized that under Theory X, workers would in fact lose motivation as their basic needs for money and security were met, since organizations managing via Theory X would offer no higher-level satisfaction. Theory Y builds on different assumptions and offers a management style more appropriate for knowledge workers, service workers, professionals and managers.

Theory Y assumes that people view work as natural and desirable, learn to accept and seek responsibility, and will eagerly work toward the aims of the organization if their own interests are aligned.

Theory Y also assumes that people are naturally imaginative and creative, and their ingenuity should be tapped for the betterment of all. Companies employing Theory Y tend to be collaborative, innovative workplaces.

At first glance, one might say that Theory Y is automatically superior to Theory X, but of course nothing involving humans is ever that simple. We all have known workers who fit the assumptions of Theory X; some people really do lack self-motivation and respond only to coercion. Also, many types of work require less collaborative management styles. For example, we expect a nuclear power plant to manage operations more strictly than an advertising agency.

McGregor viewed Theory Y as the preferable approach, but conceded that it might be too difficult to execute in very large-scale operations. In 1981, William Ouchi proposed Theory Z, which combined American and Japanese management ideas. Theory Z seems to better recognize diversity of motivation in the workforce. It addresses the basic need of security through long-term employment, then balances collective decision making with individual responsibility for execution. In other words, everyone has a say, but once a decision is made, everyone is expected to support the decision. Theory Z also embraces a more holistic approach to coworkers, including programs to support health and family.

One job of management is optimal application of resources, both mechanical and human. The more one studies Theory X, Theory Y, and Theory Z, the more comfortable one becomes with Theory WHY. Theory WHY is the entrepreneurial investor's application of McGregor and Ouchi's work. In our hearts, we may prefer the assumptions of Theory Y, but in our heads, we seek the best fit of management style and business unit. Excess creativity of workers in dangerous environments or food service production could lead to big trouble. Milton Hershey was legendary in his appreciation of workers (see Inspirational Figures insert), but we suspect that his factory was managed more authoritatively than his research and development kitchens. When evaluating management style, the important question is not which approach the company uses, but why. ▲

Theory X and Theory Y Management

	Theory X	Theory Y
Assumptions	Humans dislike work and avoid it when possible.	People view work as a natural part of their lives.
	Average employees desire direction.	Motivated people direct themselves to the goals of the organization.
	People avoid responsibility.	People learn to accept and seek responsibility.
	People are insecure and need the security of a structured work environment.	People are naturally creative and can flourish in a less structured, problem-solving environment.
Application	Production workers in large-scale, efficiency-driven organizations such as mass manufacturing.	Professional services, knowledge workers and managers in organizations requiring complex problem solving.
Management Style	Authoritarian	Collaborative

Douglas McGregor felt that Theory Y was a preferable approach to management, but conceded it was difficult to use in large-scale organizations. An entrepreneurial investor looks for a good fit of a company's operational needs and management style.

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OUR PHILOSOPHY- West Coast Asset Management's investments are focused in a small number of companies that we thoroughly understand. In our experience, this lowers the risk of losing capital and enables each investment selection to have a meaningful impact on results. We believe the stock market is driven by fear, greed and conflicted interests, which create exceptional buying opportunities for vigilant and nimble investors with a long-term horizon. Our experience has taught us to believe what we see, not what we hear, which is why every investment decision is based on our own hands-on research. We do not limit our investments to companies of a specific sector, size or valuation category - we simply seek the best opportunities to increase wealth and minimize risk. We believe investing is part art, part science, and all craft.