# America's Largest Corporations

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L-3 Communications
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[The Corner Office]

# FOUNDERS KEEPERS

## Twenty-seven FORTUNE 500 firms are still run by the CEOs who built them—and they're **tearing up the market.** BY JON BIRGER

OUTSIDE OF being in the FORTUNE 500, Costco, Kinder Morgan, and L-3 Communications don't seem to have much in common. Costco is a warehouse club, Kinder Morgan an oil- and gas-pipeline operator, and L-3 a defense contractor. But they share one characteristic that, it turns out, is a surprisingly powerful indicator of corporate success: All three are still run by their founders.

Overall, 27 FORTUNE 500 companies boast founder-CEOs, a subset comprising the likes of Apple Computer, FedEx, and Cardinal Health. (The list does not include Dell, Nike, Microsoft, and Starbucks, whose famous founders are now chairmen.) The stocks of these 27 companies returned an average of 18.5% annually from year-end 1995 through 2005, which is seven percentage points better than the FORTUNE 500's average return over the same period. Their profit growth has been superior, too, increasing at an average rate of 19.6% a year from 1995 to 2005, vs. 11.7% for the FORTUNE 500.

Of course, 27 companies is a small sample (see fortune.com for the full list), and we might have written this off as a statistical fluke had we not come across the research of an Ohio State University finance professor named Rüdiger Fahlenbrach. Fahlenbrach analyzed the performance of the 2,300 largest U.S. companies from 1993 through 2002, and he discovered that those run by founder-CEOs (11% of the total sample) outperformed the broader stock market by eight percentage points a year.

Fahlenbrach has a few theories on why founder-CEOs seem to be better corporate stewards. One is that they simply care more. Their companies are their life's work, so they're more likely to embrace long-term strategies. (For more on the pressures CEOs face in running companies for the short term, see page 40.) Supporting the theory is Fahlenbrach's finding that founder-run companies have bigger capital budgets and invest considerably more in research and development than nonfounder-run firms.

Fahlenbrach's thesis resonates with founder-CEOs we talked to. "I'm emotionally attached to this company, which means I'm going to do whatever it takes to protect its financial integrity," says Angelo Mozilo, who co-founded mortgage company Countrywide Financial in 1969. "There's no way a babysitter can feel the same way about a child as the parents."

Costco founder Jim Sinegal and Kinder Morgan's Richard Kinder echo Mozilo's passion. "It would be truly devastating to me if this company ever failed," says Sinegal. So he doesn't let near-term cost pressures divert him from what he thinks is good business. He pays above-norm salaries to veteran Costco cashiers and resists the urge to hike markups on in-demand luxury goods that keep Costco shoppers coming back. Kinder, who co-founded Kinder Morgan in 1997, has no patience for the costly executive perks that are so common in corporate America. Kinder Morgan doesn't have corporate jets (its executives all fly coach). It doesn't pay for sports tickets (never mind luxury boxes). And there are no special retirement or benefit packages for senior officers (their base salaries are all capped at $200,000).

Fahlenbrach's other big theory on the founder premium: They tend to be industry experts, not managerial mercenaries. Sinegal started out in the supermarkets as a bagger, Kinder has 20 years in the energy biz, and L-3's Frank Lanza is an engineer by training who rose through the corporate ranks of Loral and Lockheed Martin before co-founding L-3 in 1997. CEOs with résumés like these "tend to stick with what they know," says Fahlenbrach. That means they're less likely to make the kind of disastrous "diversifying" acquisitions that give M&A a bad name. L-3's Lanza says investment bankers are constantly pitching him proposed acquisitions that would move L-3 beyond the defense sector. "But we don't have the marketing or distribution know-how to do that," he says. "We've made a point to stick to our knitting." With L-3's stock up 110% since 2001, Lanza's shareholders are no doubt glad he does. F

# FORTUNE® FIVE HUNDRED 2006

The FORTUNE 500 is the short list of the largest, most influential companies in America. It is the most widely quoted, best-known business list in the world and considered by many as the barometer of business success. Members of the FORTUNE 500 are instantly recognized as key players in Corporate America and as leaders in their industry.

**Ranked #34 in NY state**

**# 253**

## L-3 Communications

Select data excerpts from the FORTUNE 500.

| INDUSTRY | Aerospace and Defense |
|---|---|
| Revenues: | $944.7 (millions) |
| Revenue Rank: | 253 |
| Profits: | $509 (millions) |
| Profit Rank: | 277 |
| Assets: | $11,909.1 (millions) |
| Assets Rank: | 257 |
| Stockholders' Equity: | $4,490.7 (millions) |
| Stockholders' Equity Rank: | 224 |
| Market Value as of 3/17/06: | $10,544.2 (millions) |
| Market Value Rank: | 245 |
| Profits as Percent of Revenues: | 5.4% |
| Profits as Percent of Revenues Rank: | 271 |
| Profits as Percent of Assets: | 4.3% |
| Profits as Percent of Assets Rank: | 272 |
| Profits as Percent of Stockholders' Equity: | 11.3% |
| Profits as Percent of Stockholders' Equity Rank: | 309 |
| Earnings Per Share, 2005: | $4.20 |
| Total Return to Investors, 2005: | 2.2% |
| Total Return to Investors, 2005 Rank: | 269 |

# 5 FORTUNE 500

# 40 THAT CLIMBED

| COMPANY | 2005 rank | Rank gain from 2004 | COMPANY | 2005 rank | Rank gain from 2004 |
|---|---|---|---|---|---|
| LYONDELL CHEMICAL | 121 | +217 | KERR-MCGEE | 320 | +59 |
| ONEOK | 176 | +160 | WELLPOINT | 38 | +59 |
| MGM MIRAGE | 334 | +115 | AMEREN | 324 | +56 |
| ENBRIDGE ENERGY PARTNERS | 335 | +113 | BEAR STEARNS | 202 | +56 |
| GOLDEN WEST FINANCIAL | 326 | +109 | SUNTRUST BANKS | 217 | +56 |
| TOLL BROTHERS | 370 | +107 | BURLINGTON RESOURCES | 298 | +55 |
| APPLE COMPUTER | 159 | +104 | HOVNANIAN ENTERPRISES | 403 | +54 |
| HARRAH'S ENTERTAINMENT | 309 | +87 | LENNAR | 161 | +53 |
| WORLD FUEL SERVICES | 264 | +87 | OCCIDENTAL PETROLEUM | 133 | +53 |
| SEARS HOLDINGS | 33 | +80 | OMNICARE | 406 | +53 |
| ENTERPRISE PRODUCTS | 183 | +77 | L-3 COMMUNICATIONS | 253 | +52 |
| COMMERCIAL METALS | 329 | +75 | SMITH INTERNATIONAL | 390 | +48 |
| WPS RESOURCES | 318 | +75 | UGI | 436 | +48 |
| MOLSON COORS BREWING | 373 | +74 | SLM | 331 | +47 |
| FLUOR | 169 | +72 | FEDERATED DEPT. STORES | 87 | +46 |
| APACHE | 299 | +68 | KB HOME | 254 | +46 |
| REGIONS FINANCIAL | 354 | +66 | TESORO | 132 | +45 |
| C.H. ROBINSON WORLDWIDE | 379 | +63 | BEAZER HOMES USA | 429 | +44 |
| MURPHY OIL | 193 | +62 | PEABODY ENERGY | 453 | +44 |
| TEREX | 355 | +62 | YRC WORLDWIDE | 263 | +44 |

## The Corporations, BY PERFORMANCE

### Fastest-growing companies

# HOW THE COMPANIES STACK UP

**GROWTH IN REVENUES 5 YEARS**

| RANK | | 500 REVENUES RANK | '00–'05 % annual growth in revenues |
|---|---|---|---|
| 1 | CONOCOPHILLIPS | 6 | 51.0 |
| 2 | CAREMARK RX | 60 | 49.4 |
| 3 | WORLD FUEL SERVICES | 264 | 48.2 |
| 4 | TIME WARNER | 40 | 44.7 |
| 5 | COUNTRYWIDE FINANCIAL | 122 | 42.7 |
| 6 | ATMOS ENERGY | 430 | 42.4 |
| 7 | VALERO ENERGY | 15 | 40.9 |
| 8 | WELLPOINT | 38 | 38.8 |
| 9 | L-3 COMMUNICATIONS | 253 | 37.7 |
| 10 | YAHOO | 412 | 36.5 |
| 11 | AMERISOURCEBERGEN | 27 | 36.3 |
| 12 | HOVNANIAN ENTERPRISES | 403 | 36.3 |
| 13 | LYONDELL CHEMICAL | 121 | 35.8 |
| 14 | CONSTELLATION ENERGY | 125 | 35.0 |
| 15 | CENDANT | 114 | 33.0 |
| 16 | NATIONAL OILWELL VARCO | 452 | 32.2 |
| 17 | ENTERPRISE PRODUCTS | 183 | 31.9 |
| 18 | TRIAD HOSPITALS | 432 | 31.8 |
| 19 | CHEVRON | 4 | 31.6 |
| 20 | DEVON ENERGY | 219 | 31.0 |
| | THE 500 MEDIAN | | 6.9 |

L3 communications