

Merger Profits

In a category that is relatively inaccessible to individual investors, such as the booming mergers and acquisitions market, the AXA Enterprise Mergers & Acquisitions Fund emerges as a viable investment option. Focusing both on announced and potential deals in the U.S. and abroad, the fund is generally diversified across approximately 250 companies in order to capture low-risk returns when the deal is secure or large movements that result from potential takeovers.

Q: What are the core beliefs behind your style of money management?

A: The AXA Enterprise Mergers & Acquisitions Fund is a portfolio with unique structure; we know of nothing similar in the marketplace. The fund captures the best of both worlds as it invests both in announced and potential deals with the goal to preserve capital and to make money for clients regardless of the market environment.

About two-thirds of the fund is invested in announced mergers and acquisitions. When a company announces its intentions to buy another company, we buy the target and hold it until the deal is closed. That is a strategy with a minimal level of risk, which is just above the risk of Treasury Bills, but with higher returns. The investment rationale is that M&A arbitrage is an investment strategy that is not correlated with the equity market. Regardless of the direction of the market, that part of the portfolio is much less volatile, so the risk is lower and the returns are not correlated to the overall market.

The remaining one-third of the portfolio represents companies that we believe could be acquired in the future. We select these companies through a bottom-up research process, identify the private market value and look for a catalyst that will surface that value.

Q: What's the investment strategy and process for achieving those goals?

A: We rely on a team of thirty research analysts that generate and seek out ideas. Each analyst follows specific industries on a global basis regardless of capitalization.

For the announced deals portion of the portfolio, the research process starts after the deal is announced. The initial research involves the spread, the annualized return, the regulatory issues, the financing, the due diligence, the downside if the deal breaks, and the risk. As we analyze the deal, we also look at the buyer, the seller, and the financial conditions. We also look at how the deal is funded and if financing may become an issue. The background is also important; it matters whether it is a friendly or a hostile takeover. The regulatory issues, whether there are overlaps in the business, and whether there are anti-competitive issues, are essential.

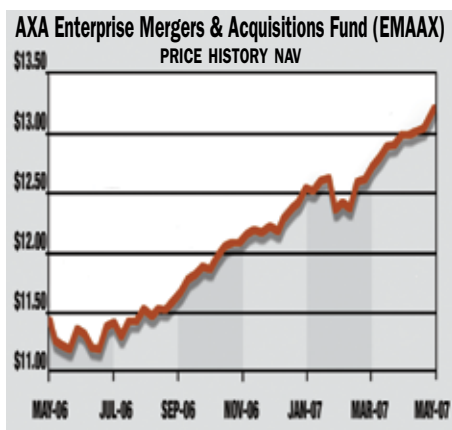
The next step is the analysis of risk versus return, which involves the risk in the case that the deal is not successfully completed, the odds of another buyer coming in, and whether the discussions are preliminary or there is a definitive deal. Overall, we look at the potential risk-adjusted return of the announced deals.



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Prior to joining GAMCO, Ms Pitaro served as an Investment Analyst and an Equity Sales Manager at Lehman Brothers Kuhn Loeb. Ms Pitaro holds an M.B.A in Finance from Columbia University Graduate School of Business, and an M.A. in Anthropology from the Loyola University of Chicago.

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We have had over 30 successfully closed deals in the portfolio just in the first quarter of this year. Currently, the spreads on these deals are closely correlated with short-term interest rates. Our goal is to earn two to three times the return on short-term Treasury bills. Our hurdle rate is the short-term Treasury rate, which is around 5%, and we aim to beat that and achieve a 10% to 15% annualized return.

Q: There are many cross-border deals going on right now. Do you find opportunities there?

A: Yes. According to the prospectus, we can invest up to 20% in non-U.S. stocks and ADRs, and we've been utilizing that opportunity. That has been a very successful portion of the portfolio. For example, last year there was about \$3.7 trillion in deal activity globally. Only about \$1.4 trillion of that amount was in the U.S. The global deals have been fueled by consolidation in Europe and Asia, and we are taking advantage of those opportunities.

Q: Do you share the view that in the low interest rate environment, this type of deal making will flourish for years to come?

A: I absolutely agree. With lower interest rates, financing is readily available, and there is an explosion in mergers and acquisitions. Private equity buyers are willing to pay a premium for companies with steady cash flow and predictable business models.

Q: What's your research process for

the potential deals part of the portfolio?

A: The internal research process is bottom-up and company specific. The idea-generation is done by our team of industry analysts who are looking for the companies that could possibly be acquired. For the 30 years that we've been in business, we have built certain areas of core competency, which means that we know many companies in those industries. For example, we have a strong base in industrial companies, media, entertainment, broadcasting, cable, and food companies.

The analysts meet with the managements, review the annual and the quarterly reports, and look at any available public information to come up with good ideas. We rely entirely on internal proprietary research, and we don't buy any outside research.

Our valuation methodology includes a long-term analysis of the company's earnings as we're not concerned with short-term fluctuations. We look at the private market value or at the price an informed investor would pay for the assets of the company. We also look at the free cash flow you need to continue operating the business. Then we focus on the management, its style and shareholder sensitivity. Finally, we identify a catalyst that we believe will help to surface those values. In this particular portfolio, the catalyst could be a potential takeover, corporate restructuring or something that would help the stock to go up regardless of the market direction.

The analysts prepare models for each company and each industry, trying to ascertain which companies look less expensive relative to their private market value in the case of an acquisition. Ultimately, we're trying to own the companies that are selling at a discount of 50% to that value and where there's a catalyst that could fuel a deal in the next one or two years.

Q: Could you give us some examples of stock picks in each of the two categories, the potential and the announced deals?

A: One example would be Home Depot announcing that it would buy Hughes Supply. We bought shares of Hughes Supply at \$45.50. A few months later, the deal closed at \$46.50, and we made a one-dollar profit. We also received a dividend before the deal closed, so our annualized return was 10% with minimum risk. The strategy in this case is to hold the stock until the deal closes.

In the potential deal category, we owned a company called Aztar. We like the gaming industry because it is a good franchise business with very strong cash flows. Aztar owned the Tropicana properties in Atlantic City and Las Vegas. We held the stock for some time because we believed that someone could take it over, given the consolidation in the gaming industry.

In 2006, Pinnacle offered to buy the stock at \$38 a share. Then Colony Capital offered \$41, Ameristar Casinos offered \$42, and Columbia Entertainment \$47, etc. It became a bidding war, in which the stock price went from \$38 to \$54 a share. There was fierce competition for Aztar because of the 34-acre parcel on the Vegas strip and the potential to acquire the last remaining spot there for a new resort or casino. Ultimately, it was bought by Columbia Entertainment for \$54 in cash in May, so that investment worked out beautifully.

Q: What is your approach towards portfolio construction?

A: The portfolio is built on a stock-by-stock basis and we give the heaviest weightings to our best ideas. We don't use any index; rather we attempt to earn an absolute return, which is typically two to three times the 90-day Treasury bill return in any market condition.

No stock represents more than 5% of the portfolio with rare exceptions. Typically,

our largest holdings are in the 2.5% to 3% range. Currently the portfolio consists of about 250 holdings, so it is a well-diversified portfolio.

Within the portfolio, we emphasize the stocks that offer the lowest amount of risk and the highest level of certainty of deals closing. We take small positions in stocks after a deal is just announced if we like the stock, but haven't done the complete due diligence that we need to increase that position. As the deal moves closer to actually closing, and after the regulatory hurdles have cleared, then we might take a bigger position although the spread might be narrower.

In the announced deals portion of the portfolio, there is higher turnover because the deals are closing in an average of 60 to 180 days, so the holding period for these securities is relatively short. But in potential deals portion we have a longer-term approach and these companies tend to stay in the portfolio for a longer period of time.

Q: What would trigger a sell decision, in addition to a deal closing?

A: Most positions are sold when a deal is completed; however, if we think that we have made a mistake, or if we don't see the upside anymore, we'll examine the case again, and we'll go back to our research. We have to make sure that all the elements are still in place. Depending on the results of the analysis, we may increase the position or sell it. So far we've had a very high ratio of closing deals with very few deals breaking.

Q: Do you believe that such diversification adds return? Also, isn't it difficult to track and know in depth 250 names?

A: We've always kept a large number of names in the fund, partially because of the potential deals portion. We may like a certain industry without being sure which company in the industry could be bought, so we might own several companies in

the same industry. Typically, if one of the companies is taken over, it does extremely well and fuels stock price growth in the other companies. For example, we owned not just Aztar, but also a couple of other gaming stocks, which did extremely well because of the expectation that more deals would follow.

In terms of the announced deals, we like to be diversified and there are a lot of deals right now. So there is a lot of choice and our strategy is to cherry pick among the best but we don't mind having smaller positions. We increase them when we feel more secure in the deal and in the completeness of our due diligence. Also, there are cases such as Aztar, when a bidding war creates a very high rate of return, so we don't mind keeping a big number of stocks knowing that some of them will provide a terrific rate of return. Overall, we're comfortable with the diversification.

Q: How do you control and measure the risk?

A: I believe that the thorough research on the individual companies helps to control the risk. Knowing and analyzing the business and looking down before you look up, helps to minimize the risk.

For the majority of the portfolio, where the return is not correlated to the market, we don't have the equity market risk. In the long term, the returns are less volatile than stock market returns, so the risk is much lower. The potential deals portion is much more correlated to the market, but its beta is still lower than that of the market.

The strategy to buy those companies at a discount of 50% to the intrinsic value of the business also leads to a margin of safety in the case of a mistake. Over the last twenty years, approximately 3% of announced deals globally were not completed, while less than 1% of deals that we invest in have not closed. **T**

AXA Enterprise Mergers & Acquisitions Fund

Symbol	EMAAX
Website	www.enterpriseinvestments.com
Address	AXA Enterprise Funds 3343 Peachtree Road, NE Suite 450 Atlanta, GA 30326-1022
Tel. No.	800-432-4320
Inception	02/28/2001

PORTFOLIO	
Total Net Assets*	\$805
Avg Mkt Cap (\$ Weighted)*	\$9,900
Average Price/Earnings Ratio	25.5x
Average Price/Book Ratio	4.13x
Turnover Ratio	227%

INVESTMENT INFORMATION	
New Investment	Open
Min Initial Investment	\$2,000
Min Subsequent Investment	\$50
Min Initial IRA Investment	\$250

RISK (AGAINST S&P 500 DAILY REINV INDEX - 3 YEARS)	
Alpha	0.41
Beta	0.44
R-Squared	0.67
Ann. Std Deviation	3.85
Sharpe Ratio	1.81

RETURNS VS. S&P 500 DAILY REINV INDEX		
	EMAAX	Index
1 Year (Cum.)	14.98%	22.79%
3 Year (Ann.)	10.89%	13.03%
5 Year (Ann.)	8.76%	9.45%

RETURNS VS. RUSSELL MID CAP TR INDEX		
	EMAAX	Index
1 Year (Cum.)	14.98%	23.76%
3 Year (Ann.)	10.89%	19.14%
5 Year (Ann.)	8.76%	15.31%

FEES AND EXPENSES	
Max Sales Charge - Front**	4.75%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee***	2.00%
Total Expense Ratio	1.66%

MANAGEMENT INFORMATION	
Mario J. Gabelli	Lead Portfolio Manager
Regina Pitaro	Managing Director

*millions **for amount invested less than \$100,000

*** 1 month after purchase

Data through: 05/31/07

Source: Company Documents; Lipper

Ticker staff searches for mutual funds for their consistency in performance and durability of investment style.

Our interview covers investment philosophy and strategy, research process, portfolio construction and risk control for funds. Through an interview we uncover long-term strategies and processes that help to generate long-term returns.

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