

EAGLE CAPITAL GROWTH FUND, INC.

Form N-CSR

March 09, 2017

United States

Securities and Exchange Commission

Washington, D.C. 20549

Form N-CSR

Certified Shareholder Report of Registered Management
Investment Companies

Investment Company Act file number: 811-05807

Eagle Capital Growth Fund, Inc.

(Exact name of registrant as specified in charter)

225 East Mason Street, Suite 802, Milwaukee, WI 53202

(Address of principal executive offices) (zip code)

Luke E. Sims, President and Chief Executive Officer

Eagle Capital Growth Fund, Inc.

225 East Mason Street, Suite 802,

Milwaukee, WI 53202

(Name and address of agent for service)

Registrant's telephone number, including area code: (414) 765-1107

Date of fiscal year end: December 31

Date of reporting period: December 31, 2016

ITEM 1. REPORT TO STOCKHOLDERS

Eagle Capital Growth Fund, Inc.
Annual Report

December 31, 2016

Top Ten Holdings (as of December 31, 2016)

Company	Market Value	Percentage of Portfolio	
Franklin Resources, Inc.	\$ 2,374,800	8.0	%
Abbott Laboratories Inc.	\$ 2,304,600	7.8	%
Illinois Tool Works Inc.	\$ 1,591,980	5.4	%
Automatic Data Processing, Inc.	\$ 1,541,700	5.2	%
eBay Inc.	\$ 1,484,500	5.0	%
St. Jude Medical Inc.	\$ 1,443,420	4.9	%
Paychex, Inc.	\$ 1,400,240	4.7	%
T. Rowe Price Group, Inc.	\$ 1,392,310	4.7	%
Cabela's Incorporated	\$ 1,346,650	4.5	%
Stryker Corp.	\$ 1,317,910	4.4	%

Fellow Shareholders,

Our Fund had a very good year, appreciating 12.2% during 2016. This put us slightly ahead of our S&P 500 (total return) benchmark, which ended the year up 12.0%. Because we are worried about elevated price/earnings multiples (see below), our Fund held considerable cash and cash-equivalent reserves during the year, which was a drag on our overall performance. Earning 0.10% in a money market fund contributes little to overall performance.

Our Fund's goal is, and has been, superior long-term investment performance with due regard for the value of capital and the need to protect it. Although we are equity investors, we are risk averse. We have too much regard for the importance of preserving our capital to take any undue risk. We would rather give up a little potential upside than run the risk of a permanent loss of capital.

The current stock market rally has made the market even pricier than it was, something we have worried about throughout 2016. We're led to consider the "appropriate" or "reasonable" level for valuations, rather than accept the current valuations as normal.

We remember the 1997-2001 period very well. Put aside the craziness involving high tech companies; even high quality companies traded at very high price/earnings multiples. When the tech bubble burst in March 2001, it took high quality companies like Coca-Cola (KO) and Johnson & Johnson (JNJ) with it. That period reinforced an iron rule of investing: if you pay too high a price, even for an excellent business, you run the risk of being blindsided.

Any time a company gets to a price/earnings multiple of 20 or above, we revisit our investment thesis. Many average companies are trading at price/earnings multiples well above 20, causing us concern. With some portfolio companies at multiples in excess of 30, we are rethinking all of our portfolio positions. We bought a number of the companies at 12-13x multiples a number of years ago; their valuations have outpaced their operating results. In a number of these situations, we've opted to sell.

Interest rates are a major factor in the analysis above. If we thought that the yield on the 10-year Treasury was going to stay below 2% for an extended time period, then we'd be willing to accept higher price/earnings multiples persistently. Low rates provide a weak alternative to expensive stocks. If the interest rate remained near 2%, many companies could exceed that level of growth with limited risk. We don't try to forecast specific levels for interest rates, but we believe that the general trend for interest rates is up.

We occasionally find a bargain that fits our investment criteria. A recent buy is eBay, Inc. (Nasdaq NMS: EBAY), which runs the eponymous internet auction platform. EBAY trades at a mid-teens multiple of earnings, is growing about 10% a year, and earns a return on invested capital (ROIC) north of 40%. Earning about \$2/share and with \$3/share of cash on its balance sheet, EBAY is inexpensive (15x multiple) with balance sheet flexibility. The EBAY model generates lots of cash and has relatively light capital expenditure requirements; this allows the company to devote its substantial free cash flow towards share repurchases. As long as EBAY shares continue to represent a bargain, we applaud this strategy.

The Fund paid a distribution of \$1.19 per share in December. We paid the distribution in stock, although shareholders had the option to elect for cash. We are happy to report that, for the second year in a row, 63% of shares received stock. That participation rate is a delightful show of confidence, denoting a pleased shareholder base. We're aware of a handful of other funds which pay fund distributions in the same way; not one of them has a participation rate above 40%.

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As always, we love hearing from our shareholders. However, we won't comment on any undisclosed purchases or sales that the Fund has made or is contemplating. With that caveat in mind, all other issues are on the table.

Luke E. Sims

David C. Sims

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January 13, 2017

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Eagle Capital Growth Fund, Inc.
Statement of Assets, Liabilities and Shareholders' Equity
As of December 31, 2016

Assets

Common stock--at market value (cost \$15,038,037)	\$23,870,618	
Money market funds	5,759,024	
Short-term interest receivable	2,008	
Dividends receivable	43,000	
Prepaid fees	13,093	
		\$29,687,743

Liabilities

Accounts payable	\$1,633	
Investment advisor fee payable	21,528	
Accrued expenses	23,500	
		\$46,661
Total net assets		\$29,641,082

Shareholders' Equity

Common stock- \$0.001 par value per share; authorized 50,000,000 shares, outstanding 3,588,977 shares	\$3,589	
Paid-in capital	20,763,929	
Undistributed net investment income	116	
Undistributed capital gains	40,867	
Unrealized appreciation on investments	8,832,581	
Shareholders' equity		\$29,641,082
Net asset value per share		\$8.26

See Notes to Financial Statements.

Eagle Capital Growth Fund, Inc.
Statement of Operations
For the Year Ended December 31, 2016

Investment Income

Dividends	\$445,529	
Interest	11,434	
Total investment income		\$456,963

Expenses

Advisory fees	\$216,660	
Legal fees	1,931	
Insurance	13,094	
Transfer agent	48,305	
Audit fees	22,500	
Directors' fees and expenses	64,000	
Custodian fees	7,612	
Listing fee	15,000	
Other fees and expenses	18,423	
Total expenses		\$407,525

Net investment income \$49,438

Realized Gain and Unrealized Appreciation on Investments

Realized gain on investments:

Proceeds from sale of investment securities	\$22,644,841	
Less: cost of investment securities sold	18,750,192	
Net realized gain on investments		\$3,894,649

Unrealized appreciation on investments:

Unrealized appreciation at end of period	\$8,832,581	
Less: unrealized appreciation at beginning of period	9,505,416	
Net change in unrealized appreciation on investments		\$(672,835)
Net realized gain and unrealized appreciation on investments		\$3,221,814

Net increase from operations \$3,271,252

See Notes to Financial Statements.

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Eagle Capital Growth Fund, Inc.
Statements of Changes in Net Assets

	Year Ended December 31, 2015	Year Ended December 31, 2016
From Operations:		
Net investment income	\$ 118,237	\$ 49,438
Net realized gain on investments	1,404,503	3,894,649
Net change in unrealized appreciation on investments	(1,273,308) (672,835)
Net increase from operations	\$ 249,432	\$ 3,271,252
Distributions to Shareholders from:		
Net investment income	(158,060) (29,562)
Net realized gain from investment transactions	(1,404,502) (3,853,782)
Total distributions	\$ (1,562,562) \$ (3,883,344)
From Capital Stock Transactions:		
Reinvested capital from distribution of shares	986,674	2,465,266
Total Net Assets:		
Beginning of year	\$ 28,114,364	\$ 27,787,908
End of period (including overdistributed income of \$19,760 in 2015 and undistributed income of \$116 and gains of \$40,867 in 2016)	\$ 27,787,908	\$ 29,641,082
Shares:		
Shares issued to shareholders from the distribution	138,190	325,663
Shares at beginning of year	3,125,124	3,263,314
Shares at end of period	3,263,314	3,588,977

See Notes to Financial Statements.

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Eagle Capital Growth Fund, Inc.
Financial Highlights

For the periods ended December 31:	2012	2013	2014	2015	2016
Net asset value at beginning of year	\$7.12	\$7.61	\$8.69	\$9.00	\$8.52
Net investment income	\$0.06	\$0.03	\$0.02	\$0.04	\$0.01
Net realized gain and unrealized appreciation on investments	\$0.79	\$2.07	\$0.66	\$0.04	\$0.99
Total from investment operations	\$0.85	\$2.10	\$0.68	\$0.08	\$1.00
Distribution from:					
Net investment income	\$(0.03)	\$(0.07)	\$(0.02)	\$(0.05)	\$(0.01)
Realized gains	\$(0.33)	\$(0.95)	\$(0.35)	\$(0.45)	\$(1.18)
Total distributions	\$(0.36)	\$(1.02)	\$(0.37)	\$(0.50)	\$(1.19)
Dilution from share issuance	\$-	\$-	\$-	\$(0.06)	\$(0.07)
Net asset value at end of period	\$7.61	\$8.69	\$9.00	\$8.52	\$8.26
Per share market price, end of period last traded price (A)	\$7.10	\$8.19	\$8.70	\$7.59	\$7.35

Total Investment Return:

Average annual return, based on market value:

1 Year	7	%	30	%	11	%	(7	%)	12	%
5 Year	3	%	18	%	15	%	12	%	10	%
10 Year	4	%	7	%	8	%	6	%	7	%
From inception	8	%	9	%	9	%	9	%	9	%

Average annual return, based on net asset value:

1 Year	12	%	28	%
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