Jan 02

REAL MONEY
Rob Rikoon

FINDING COMPANIES THAT HAVE VALUE

When all is said and done, what we are really doing when we plunk down some of our hard earned ducats and buy a stock is simply investing in people. The goal is to find people who know the market in which they are trying to make money. In today's world, an important part of this is finding managers who know the ways in which their markets are shifting, as it seems that all markets are shifting all the time. It takes a certain kind of person capable of working within the right kind of management structure to make me believe that this is a company where I want to put my money. Another way of saying this is I have to make a conscious choice that I want to be a partner in this particular business through thick and thin, with these particular people.

To find companies that truly have underlying value, an investor must examine a combination of elements. The first important thing is to spend time looking at the length of time and cohesiveness that exists in the management team of a company. This means trying to understand the quality of the people who work there. This does not just mean finding out who is the CEO, but involves going further into the organization to other employees, such as researchers and marketing people. An essential issue is whether management is looking forward and is taking into account the myriad of factors that are unique to their business and those that impact their ability to compete in Corporate America. These qualitative issues are relevant in terms of knowing if there is good solid forward thinking about how the company moves forward. I try to ascertain the appropriateness of the financial structure of the company, the positioning of the products it is developing to meet an increasingly competitive future, and the branding or marketing strategy critical to creating recognition and customer loyalty.

FEELING GOOD ABOUT MANAGEMENT

There are several signs that management is doing the right things within their company. Companies who buy back their own stock and companies that are noted on lists like "the top100 companies to work for" are two excellent ways to see if this is a company that believes in itself. If a company qualifies on both fronts, you can believe that inside management which sees value in its stock enough to repurchase shares in the open market and a company that is liked enough by its employees to be listed among the ranks of desirable companies to work for is probably worth investing in for your long term future. Another thing to look at is the management-compensation packages. If the pay packages for top and mid level executives are based on a long-term review of strategic results, we like it a lot more than compensation based on quarterly net income goals, a financial number easily manipulated by those on the inside. The signs that employees are paid based on lasting contributions shows that the company is doing something valuable on the financial side and valuable in terms of providing a beneficial product or service to the public.

One thing that is hard to figure out is where a company is headed in the market place. For example, consider the case of a company like Intel, which has had tremendous competition over the last business cycle but was willing to tighten its belt and to reduce prices to keep market share. As a result of their forward looking, long-range competitive strategy, they continued to expand, even in this down market, by building their next generation of factories and developing a new generation of equipment. This is important because only by making this kind of confident move towards the future can Intel maintain their market share and even expand it when the economy rebounds. Investors should look for companies like this, one that shows by their action that they are willing to invest in and help create the future of their particular industry, and not just looking for short-term profits.

Just so you know how hard it is to evaluate management expertise, here are some mistakes that we have made in trying to figure out if management is on the ball. The first is an experience we had with Compaq Computers, an early innovator in the area of laptops and personal desktop machines. We didn't own a lot of Compaq, but we had to dump it when we became convinced that Compaq's management did not have a plan to compete with Dell Computers, which was delivering machines faster and more efficiently than Compaq. We looked for signs that they were developing a "just in time delivery" system and flawless customer support but it was not there.

We bought United Airlines several years ago because it had tremendous assets and if the airline industry stayed healthy, their share price would have appreciated handsomely. We made a mistake in our thinking about United's management in that the people at the top were not capable of reaching peace with their own unions, even though United's pilots, attendants, and mechanics unions have substantial ownership stakes in the company. None of these parties could see past their individual self interests to a unified strategy in order to compete with the likes of Southwest. We got out of United and moved our money to United Parcel Service. We feel confident that UPS and their employees are on the same page because the employees own a majority of the company and the firm is not subject to the kind of labor unrest as United.

As you evaluate stock purchases for the coming year, keep in mind the idea that traditional methods of research and analysis are not proving themselves as valuable as when companies were more forthright about their challenges and problems. As a result, stock market investing now involves more independent thinking than was required in the past. Many professionals debate and dispute about how new methods of electronic communication, heated competition, and increased disclosure rules are going to change the investment world. The new winning companies will have managers who can think outside of the box, who can act honorably, and who can exhibit fiscal restraint while taking the right kind of long-term risks.

Rob Rikoon is C.E.O. of Rikoon-Carret Investment Advisors, located at 510 Don Gaspar, Santa Fe, NM, Tel. 989-3581.