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Real Money

The current emotional situation surrounding the markets is so charged that it's useful for investors to step back and focus on the big picture. There are certain people who are trying to take advantage of negative news about the state of the world for their personal gain.

We are in such a period where the number of "bearish", or pessimistic forecasts has increased in number and volume, and they are attracting so much attention that it is necessary to address their arguments. One of the best-known pundits publishes a newsletter which consistently calls for the end of the civilized world, or at least that we are on the verge of a great depression. The first prediction that pessimists raise is that investors are about to have a selling panic attack and no one will have a chance to get out in time. There are, they say, technical indicators that are supposed to point to plunging corporate profits, surging unemployment, and this means we are in for a "massive buyer's strike by investors who have lost all faith in Wall Street." The stock market panic will spread, from the technology sector to Fortune 500 companies, further to overseas markets and then to bonds. Woe to those who do not heed these warnings !

Upon close examination, each of these fear-based pseudo-logical arguments falls apart. I would like to offer a counterpoint to the hysteria that some people are trying to create due to the stock market's decline, now in its third year. It is possible to find examples of companies and even whole industries that have fallen on hard times so that it looks like they are going down the tubes. The technology industry with AOL-Time Warner is one such example. AOL just wrote off 54 billion dollars, the largest single quarterly loss in history. Other companies in similar straits are JDS Uniphase, Xerox, AT&T, and Tyco.

The shock of seeing familiar companies like these and the sheer size of the accounting adjustments has seldom been seen before. At the same time, it is important to remember how huge the capital investments are that businesses require, particularly technology and telecommunications. So, it is very misleading to just look at the dollar amount of a loss taken by a few companies; one must look at the potential gains for economic efficiencies in the long run from capital expenditures in basic infrastructure.

A good example of misleading statements made by writers of fear-based newsletters is "the quarterly profits of 1,146 companies are collectively in a deficit mode." The fact is that it is not unusual for the collective earnings of public companies to be negative during economic downturns. What is more important is to observe how companies react in a deep recession. Companies that become lean during a downturn often position themselves to benefit greatly when economic activity once again picks up, so "collective losses" is essentially a meaningless phrase.

One negative newsletter author pointed to his research of 7,000 publicly traded companies, and he came to the unsubstantiated conclusion that most have basic flaws in their accounting standards and reporting methods. No one can possibly analyze 7,000 publicly traded companies and understand the justifiable accounting differences between firms in different industries. One writer, who is not an analyst himself, states that there are 2,771 companies showing significant deficiencies in their accounting methods, and he intimated that most companies are manipulating their earnings reports. In a post-Enron world, this is a blatant attempt to manipulate public sentiment.

When the newsletter writers and TV personalities replace their rose-colored glasses of the late 1990s with accounting visors today, we know that the mood in the country has changed. Accountants are by and large honest people trained to help in the orderly functioning of business. Similarly, most companies do not out and out lie to investors. Sometimes they try to put a good face on bad situations, which may not be totally ethical, but by no means is our system thoroughly rife with corruption as are some economies around the world. The United States is still the best place in the world to start a business.

Last month, this column was devoted to describing how major brokerage firms manipulate information they give to the public for their own advantage. It is likely that of these kinds of purposefully deceptive activities may result in a downsizing of the financial service industry. Does this mean that the capital markets are drying up and poised to blow away? Not so, as there are or were, so many new brokers, insurance salesmen, investment advisors, and mutual funds that we are overdue for a winnowing out of the industry. With the dawning of the "Information Age," it will be harder for the traditional brokers to monopolize the stock business with backroom deals. Having fewer brokerage firms and mutual funds around might help precipitate industry reforms that would protect the public better than the current self-regulation practiced by the broker-dealer industry.

To counter the argument that our economy is about to crash, we believe that recent economic reports suggest the economy has begun to turn the corner, and that the second half of 2002 should witness a fairly healthy economic recovery. However, as is usually the case in an economic recovery, not all sectors of the economy are strong. The steel industry has lost a tremendous number of jobs, as have other manufacturing businesses. On the other hand, service industry employment continues to grow and the housing market has never been stronger. There are signs that consumer durable orders, indicators of consumer confidence, has turned up.

People who say that the sky is about to fall are able to attract a good deal of attention right now. They serve to crystallize the free-floating anxieties that most people are feeling, and particularly in the aftermath of September 11th and with so much ongoing injustice and bad news about the environment. It is hard to look at current circumstances and feel that, as a society, we will work our way through these problems.

The underlying strengths of the American people and economy are clear and there are still ample opportunities for people who want to get an education to do so. Persons desiring to own their own business can still significantly impact their personal circumstances if they are willing to work hard and plan for the future.

The conditions still exists for fostering the improvement of the quality of life for the great majority of people on earth so we should be grateful and not afraid. There are certain ethical standards that most people in business abide by and this leads me to believe that investing is an act towards a positive goal and not merely precautionary reactions against potential disasters.

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