Trusting stock pickers is a minefield for any investor

I've been darkly suspicious of Wall Street ever since I tried to launch a robotics venture some years ago.

We had a pretty good idea for a company, complete with cutting edge proprietary technology and a snazzy business plan. But we needed capital. We prepared our pitch (complete with nicely colored flip charts) and dutifully made the rounds of the venture capital and investment banking firms on The Street.

Phil Power

We were regularly greeted by bored newly minted MBA's from Harvard and Stanford who had obviously aced the course in "Patronizing the Entrepreneur." I remember vividly one young man, complete with a beautifully custom tailored blue shirt, white collar, brilliant chrome yellow necktie and mauve suspenders. He listened to us for at least three minutes before dismissing us with a curt, "The market's far too big for your idea; I'd advise you to go back home to, um, Michigan."

So maybe I was a little too eager to take in a piece in the business section of the New York Times on what's happened to Wall Street's stock research analysts. The Times' headline read: "How Did So Many Get It So Wrong? As They Do Little but Shout 'Buy,' Analysts Often Send Investors Astray." In these days of stock market turmoil, it makes important reading.

The article traced the evolution of Wall Street analysts, whose research is supposed to help investors judge the attractiveness of stocks. Analysts used to operate independently; offering investors and brokers detailed recommendations as whether to buy or sell a given stock at a given price. Analysts would "follow" a company over the years, developing an understanding of its technology and product, market prospects and management capability.

Sometimes analysts would recommend investors sell shares; sometimes they would recommend a buy. In the days when the commissions charged by Wall Street firms were relatively high, a far-seeing analyst's recommendation could generate a lot of trades and a lot of income. Analysts – and their firms – were rewarded for good, hard, independent digging.

Two things happened to change this. First, commissions declined, forcing Wall Street to look elsewhere for revenue to cover the costs of research.

More importantly, in recent years Wall Street firms have emphasized investment banking, venture capital, stock underwriting and retail sales of shares underwritten by the firm. In this new environment, potentially negative reports by independent analysts became a cost, not a benefit. Independent research was eroded.

The Times article quoted Robert A. Olstein, a mutual fund manager with 32 years of experience, who likened today's analysts more to race-track touts than to independent researchers. "What passes for research on Wall Street today is shocking to me," said Olstein. "Instead of providing investors with the kind of analysis that would have kept them from marching over the cliff, analysts prodded them forward by inventing new valuation criteria for stocks that had no basis in reality and no standard of good practice."

The Times cited the remarkable lack of "sell" recommendations made by analysts, even in a declining market. Of 8,000 current recommendations made by analysts covering companies in the Standard & Poors 500-stock index, only 29 are sells, according to Zacks Investment Research in Chicago.

■ Individual investors can no longer take analyst recommendations as gospel, especially when the stocks they tout are the same ones underwritten and pushed by their own firms.

More telling and far more troubling were examples cited in the Times story of supposedly independent analysts issuing recommendations on stocks underwritten by their own firms. The vast majority of these were "buy," even when the companies faced tough – even deteriorating – business conditions. Analysts interviewed by the Times denied this represented a conflict of interest, but the denials didn't seem persuasive to me.

In today's economic climate, when so many ordinary investors have made and lost so much money in the stock market and when markets are extraordinarily volatile, the implications of the Times article are far-reaching. Individual investors can no longer take analyst recommendations as gospel, especially when the stocks they tout are the same ones underwritten and pushed by their own firms. Worse, it's tough to get anybody – even your friendly broker – to come clean about which analysts are truly independent and tough minded and which are mere touts.

"Caveat emptor" says the Latin tag: "let the buyer beware."

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Mike Malott

Deadline is too near for lawmaker's pay hike discussion

The very first issue state lawmakers will face when they get to Lansing to start session for the year will be the question of whether to accept the 36-percent pay raises proposed by the State Officers Compensation Commission.

Senators and representatives will have a total of just three session days to take up the issue before the Feb. 1 deadline. Under the rules, the SOCC recommendations automatically take effect unless state lawmakers vote by a two-thirds majority to reject those pay increases.

The salary hikes given out by the seven-member panel this past December included a 36-percent jump for legislators, taking them up to a salary of $77,400 in 2001. They get 3 percent more in 2002. Their expense accounts also jump $2,000 annually to $12,000.

The SOCC also gave 13-percent pay hikes to the justices of the Supreme Court, taking them to $159,960. The lieutenant governor gets 19-percent more, his wage rising to $120,400.

And the governor, who appointed the members of the SOCC, gets a 14-percent salary hike, bringing him to $172,000.

The exorbitant increases have a number of legislators upset, and several have promised to do their best to get the salary hikes tossed out despite the short time frame. Sen. Gary Peters, D-Bloomfield, has promised to introduce a resolution to reject the raises. New House Speaker Rick Johnson, R-LeRoy, has promised that there will be a vote held in the House before Feb. 1.

Rep. Clark Bisbee, R-Jackson, has also announced he'll attempt to put a constitutional amendment on the 2002 ballot to change the way legislative salaries are set. Bisbee's proposal would be to require lawmakers to vote affirmatively to accept such raises.

But the first thing state voters should be asking themselves is how this system got so screwed up.

Didn't we vote, back in 1968, to create the SOCC to come up with a better system for setting lawmakers' wages. The point of the system was to find a way to set salaries that would be fair, would compensate those officials for the work they do, at rates high enough to attract people to the job without getting excessive, and yet make lawmakers accountable for the increases they take.

The idea was to depoliticize the issue. An independent panel would more likely come up with a fair wage, we believed back then, and lawmakers would still be able to vote to override the recommendations if the political appointees on the panel got carried away while handing out raises.

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So why isn't the system working?

Because of the Feb. 1 deadline. It comes around way too soon, and at a time when lawmakers are busy dealing with other things. The leadership is trying to get itself organized. Lawmakers are setting their agendas for the year. They are setting up their offices and hiring staff.

■ The deadline could be a little later to allow the lawmakers a fair chance to really debate the issue and vote on a resolution.

The Feb. 1 deadline is set, not by the constitution, but by implementing legislation.

Some will say there needs to be a deadline in the law, and I think they're right. Without a deadline, the issue of pay raises could go on all year long and take time away from more important business, the business these lawmakers were elected to do, which they are being paid to do.

But it could be March 1. Or April 1. And there is no need for a constitutional amendment to change it.

Lawmakers have set it themselves, and they could change it themselves.

It could be a little later to allow the lawmakers a fair chance to really debate the issue and vote on a resolution. It could be a little later to allow state residents to express their views about the proposed pay hikes to legislators.

As it stands, the arbitrary deadline is a convenient excuse for lawmakers to take pay hikes without having to accept the responsibility. Legislators can say they tried to reject it, but others stalled. Things were too busy. There was just wasn't enough time.

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