



Numbers Are Easy; Thinking Is Hard

By [Joan Lappin](#)
RealMoney.com Contributor

Market Commentary

In her introductory column, Joan Lappin explains the value of digging through numbers.

A long-term investor, she spotted troubles at Qwest well before the Street.

It's important to be a leader in investing, rather than a follower.

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Greetings, dear reader. I'm thrilled to be joining *RealMoney*, and I'd ask you to please consider this piece an introduction to my way of thinking, which is hardly run-of-the-mill in today's world. If you are an avid reader of stock market information, you know it is heavily focused on the latest trends in everything and anything. Oil inventories, U.S. trade deficits, the state of the U.S. dollar, **Yahoo!'s** (YHOO:Nasdaq) ad numbers, **eBay's** (EBAY:Nasdaq) monthly bookings, interest rates, unemployment rates, etc.

You get the picture. Numbers are easy. They are straightforward. Sometimes they are even factual. They don't require much depth of knowledge. They are what they are.

Well, *sometimes* they are what they are.

My claim to fame is that twice in my long career, I have looked at the same numbers everybody else did with regard to a particular company, and I was able to see what nobody else observed. Decades ago, I spotted some shenanigans at a company called Career Academy, a highflier of the late 1960s. Of course the company insisted to the media that I knew nothing, was totally wrong and so forth. Eighteen months later it was in bankruptcy.

More recently, in 1998, everybody on Wall Street (mainly Jack Grubman and his disciples) was beating **Qwest's** (Q:NYSE) drum.

The company was building out a national fiber optic network, and it really wasn't yet in business, but was reporting earnings anyway. How, you might ask, did it accomplish that?

Well, it was selling the use of some dark fiber (not yet built, lighted or ready for use) to other telecom companies to be used over the next 20 years. That part was OK. But because it promised to deliver the service over the next score of years, it should have put it on the balance sheet as a deferred liability to match deferred revenue. Instead, CEO Joe Nacchio was reporting the revenue and income to be earned over the next 20 years in the current quarter!

Nacchio did not greet my observations with much enthusiasm when Gene Marcial at *Business Week* [ran a story](#) featuring my opinions. Qwest pulled its ads from the local Denver McGraw-Hill TV stations and as our battle of words ensued in the magazine's letters to the editor, there was a coincidental defacing of my Manhattan brownstone. At the time, I suggested the stock was very overvalued. It was. I was the lone wolf for many months, howling that it was, in a manner of speaking, cooking its books.

Why was I alone? Because not many people bother to read the footnotes in financial statements. They don't understand that a set of financial statements is not empirically accurate. It is the result of a series of negotiations over just about every line item between the auditor and the company. Cash is cash. But how you allocate costs to the manufacture of your goods and services depends on many factors. Sales should be sales, but the many restatements of corporate financials since the inception of Sarbanes-Oxley show that when you book a sale, it is open to a lot of interpretation.

Is it when the box leaves the plant?

Is it when the customer accepts the machine as fully installed and operational?

Or is it when any piece of software attached to that machine has been loaded on to it and found to be working in sync with all the products of the other vendors to which it must interface?

Negotiating expense accruals is in the same category, and some view this as an even bigger issue.

And that's the point. Numbers are easy. Everyone pretty much has access to the same numbers in the public domain. That is why Regulation FD (fair disclosure) as mandated by the **SEC** in recent years has been such a boon to everyone who isn't **Fidelity** or **Putnam** or some humongous hedge fund that can force itself on management and demand all kinds of time. Companies must now make the same information available to everyone at exactly the same time. The key isn't the numbers themselves. The key is how you think about those numbers and put them into long-term perspective.

I've been working on Wall Street for decades (more than 40 years). I still come to work every day with enthusiasm at the prospect of matching my wits against the market. I have done it better than most for the vast majority of those years, and I still find the intellectual challenge thrilling and engaging. My goal here will be to impart to you some of the wisdom I have learned plying my trade: first as a media and entertainment analyst for about 15 years, and since 1980, as a portfolio manager.

In this forum I hope to flag companies that are of interest, and others to avoid based on real, fundamental insights. I plan to comment, from time to time, on news of the day from my long perspective when I have insights others have missed.

We manage concentrated portfolios at Gramercy Capital, and we call it "put your money where your mouth is" investing. We are patient long-term investors. With long-term capital gains rates at just 15%, just think of how well you do when you own stocks that double and quadruple if you are just patient enough to let them do their thing and then pay very little on taxes to cash them out.

We are stock pickers because we believe trying to own the averages in the end is inevitably going to produce average results. Or is that an oxymoron?

So remember where we began: Numbers are easy! Knowing how to process those numbers is hard. More than the technicians or those damnable quants and momentum players would like you to believe, chasing last year's or yesterday's winners is rarely the path to success, and following the spot on the tail of the Dalmatian in front of you is not the path to glory, either.

I believe success comes to those who are able to see what others can't and become the lead dog. Let the others follow you. And if they figure it out six or 10 months later, that's OK. Then you have only a few more weeks to go until your investment goes long-term!

Joan Lappin, CFA, is chairman and chief investment officer of Gramercy Capital Management Corp., a registered investment advisor based in New York City, which she founded in 1986. Under no circumstances does the information in this column represent a recommendation to buy or sell stocks. Lappin appreciates your feedback