

Financial Statements: Do You Read Them?

(radio transcript)

By Kristian Foden-Vencil

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In a couple of days, it'll be the end of 2009's first quarter. Mutual funds and 401k plans across the country will trot out their quarterly reports, which as dutiful investors we will all read – right? Me neither.

But, as companies increasingly move workers from defined pension plans to 401Ks, more of us are becoming responsible for our own retirement funds.

It's a scary thought, especially as professionals struggle to get good returns.

Kristian Foden-Vencil talked to people who're managing their own retirement money to see how closely they're combing through financial statements.

(street sound): "There is good news and all that believe on the lord Jesus Christ will be saved..."

Nine o'clock on a Thursday morning, the street preachers are out in Portland's Pioneer Courthouse Square along with sidewalk sweepers, tourists and harried workers. It's as good a place as any to ask people whether they'll be digging into their 401k financial statement when it arrives in the post.

Here are Ben Storemont, Kerry Merkley, and Shaun Carhoff.

Ben Storemont: "It feels very abstract."

Kerry Merkley: "You know I probably need to be more educated on what my choices are and what I need to be doing instead of trusting somebody else to do it for me which is what I've pretty much done right now. Because I don't know what I'm doing."

Shaun Carhoff: "I read them in the beginning when they started to come and I started to hear the troublesome stories about the market. Got quickly depressed, tucked them away and never looked at them again. So whenever they come to the house, I just pretend they're not there."

Sound familiar?

But there are people who do read all that fine print and who work the numbers. They read not just their quarterly 401K or mutual fund statements, but they also dig down into annual reports for individual companies and other financial statements. Joe Sherry has been building a retirement nest egg for years. Now he's 51 and a little nervous.

Joe Sherry: "This notion that your whole retirement hinges on how well you speculate, I really can't say that I'm all that pleased with it right now. When times are going well, you think, oh that's a great system, but times don't always go well as we've seen."

To hedge his bets, Sherry has given three quarters of his money to a broker. The rest, he invests himself. He does read through individual company financial reports and has seen some scary drops. But...

Joe Sherry: "In recent times the part I've done myself has done better in this downturn than the part I've had at the brokers."

Kristian Foden-Vencil. "I've heard of the studies where I think it's a monkey throwing a dart at the newspaper and does better than the professionals."

Joe Sherry: "Well if you believe about efficient markets and all that. Any information you have about the stock is already reflected in the price, so it's already a crap-shoot at that point. I don't know whether it makes any sense to have the experts pick for you. A lot of people say you're having someone else do the work for you. But sometimes it's just more time and effort than I can muster to try to keep on top of these things and feel that you're making an intelligent choice."

There is a real monkey by the way. His name is Mr. Adam Monk and he's a stock picker for the Chicago Sun Times.

Another human investor, Fred Bieker says investing keeps him engaged in society. He's a retired Portland doctor who's bullish on Costco. He devours the company's financial reports. But he says, there are other ways he keeps tabs on a company.

Fred Bieker: "Like Costco, if you can go into the store and see how they're doing. Talk to the employees and find out how they're being treated by the company and how they like working for the company. Things like that I find more useful often than the written reports."

Beaverton electrical engineer, Rainer Moehring, also manages his retirement funds pretty closely. But he's very bearish and regards individual company financial statements as little more than a public relations exercise.

Rainer Moehring: "I understand the details of financial statements and I understand what that means in terms of picking good companies versus bad companies in good times. The trouble is the point is going to be reached where the times are so bad that even the good companies are going to get dragged down. And that's happening." (0:19)

Financial statements, like annual reports and quarterly revenue estimates are supposed to be the blue-print of a company's economic health. And some financial advisors say having the skills to read them is essential to managing your own retirement fund or 401K.

But Ralph Cole, of Portland-based Ferguson Wellman Capital Management, says you don't need an MBA, just check a few key lines – like cash flow.

Ralph Cole: “Is this company generating positive cash flow or is it using cash? Especially at a time like this -- when you're in a recession -- you need companies that can still finance their own operations. Are they going to have to go outside themselves to fund themselves? Which is very difficult to do in a time when everyone is scared. And then after that, are they profitable? How much are they going to earn this year, how much are they going to earn next year.”

The next place you should look, says Cole, is the 'management discussion' section, where a company lays out its plans for the next couple of years.

Ralph Cole: “And if you agree with the strategy, then you probably want to go on and start looking at the fundamentals of the company. Does it make sense to go into emerging markets? Do they really have a competitive advantage there? Kind of bigger picture until you start digging out into the balance sheet or income statement.”

Cole says companies can hide things in their paperwork. But contrary to all the headlines, he says, it doesn't happen as often as you'd think. Meanwhile, it's not a bad idea to remember Adam Monk, the cinnamon-ring-tail cebus who's beaten the major indexes four of the last five years.

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