

Haven't blogged in a while. So I decided to look back and pull out one of my first blog posts, from 2004. An oldie, but goodie !

[The Number](#). I recommend that anyone with an interest in the market jump at the chance to buy it.

In 1990, I sold my company, MicroSolutions which specialized in what at the time was the relatively new business of helping companies network their computer equipment to CompuServe. After taxes, I walked away with about \$2 million. That was going to be my nest egg, and my goal was to protect it at all costs, and grow it wisely.

I set about interviewing stockbrokers and settled upon a broker from Goldman Sachs, Raleigh Ralls. Raleigh was in his late 20s, and relatively new to Goldman. But we hit it off very well and I trusted him. As we planned my financial future, I made it clear that I wanted my nest egg to be invested not like I was 30 years old, but as if I were 60 years old. I was a widows and orphans investor.

Over the next year I stuck to my plan. I trusted Raleigh, and he put me in bonds, dividend-paying utilities and blue chips, just as I asked.

During that year, Raleigh began asking me a lot of questions about technology. Because of my experience at MicroSolutions, I knew the products and companies that were hot. Synoptics, Wellfleet, NetWorth, Lotus, Novell and others. I knew which had products that worked, didn't work, were selling or not. How these companies were marketed, and whether or not they were or would be successful.

I couldn't believe that I would have an advantage in the market. After all, I had read *A Random Walk Down Wall Street* in college. I truly thought that the markets were efficient, that any available knowledge about a company was already reflected in its stock price. Yet I saw Raleigh using the information I gave him to make money for his clients. He finally broke me down to start using this information to my advantage to make some money in the market. Finally after more than a year, I relented. I was ready to trade.

Notice I didn't use the word invest. I wasn't an investor. I just wanted to make money. The reason I was ready to try was that it was patently obvious that the market wasn't efficient. Someone like me with industry knowledge had an advantage. My knowledge could be used profitably. As we got ready to start, I asked Raleigh if he had any words of wisdom that I should remember. His response was simple. "Get Long, Get Loud".

Get Long, Get Loud. As we started buying and selling technology stocks, most of which were in the local area networking field that I had specialized in at MicroSolutions, Raleigh put me on the phone with analysts, money managers, individual investors, reporters, anyone with money or influence who wanted to talk technology and stocks.

We talked about token ring topologies that didn't work on 10BaseT. We talked about what companies were stuffing channels – selling more equipment to their distributors than the distributors really needed to meet the retail demand. We talked about who was winning, and who was losing. We talked about things that really amounted to the things you would hear if you attended any industry trade show panel. Yet after hanging up the phone with these people, I would watch stocks move up and down. Of course as the stocks moved, the number of people wanting to talk to me grew.

I remember buying stock in a Canadian company called Gandalf Technologies in the early 90s. Gandalf made Ethernet bridges that allowed businesses and homes to connect to the Internet and each other via high-speed digital phone lines called ISDN.

I had bought one for my house and liked the product, and I'd talked to other people who'd used it. They had decent results, nothing spectacular, but good enough. I had no idea Gandalf was even a public company until a friend of Raleigh's asked me about it. What did I think about Gandalf Technologies? It was trading at the time at about a buck a share. It was a decent company, I said. It had competition, but the market was new and they had as much chance as anyone to succeed. Sure, I'll buy some, and I would be happy to answer any questions about the technology. The market size, the competition, the growth rates. Whatever I knew, I would tell.

I bought the stock, I answered the questions, and I watched Gandalf climb from a dollar to about \$20 a share over the next months.

At a dollar, I could make an argument that Gandalf could be attractive. Its market was growing, and compared to the competition, it was reasonably valued on a price-sales or price-earnings basis. But at \$20, the company's market value was close to \$1 billion – which in those days was real money. The situation was crazy. People were buying the stock because other people were buying the stock.

To add to the volume, a mid-sized investment bank that specialized in technology companies came out with a buy rating on Gandalf. They reiterated all the marketing mishmash that was fun to talk about when the stock was a dollar. The ISDN market was exploding. The product was good. Gandalf was adding distributors. If they only maintained X percentage of the market, they would grow to some big number. Their competitors were trading at huge market caps, so this company looks cheap. Et cetera, et cetera.

The bank made up forecasts formulating revenue numbers at monstrous growth rates that at some point in the future led to profits. Unfortunately, the bank couldn't attract enough new money to the stock to sustain its price. It didn't have enough brokers to shout out the marketing spiel to entice enough new buyers to pay the old buyers. The hope among the "sophisticated buyers" was that one bank picking up coverage would lead to others doing the same. It didn't happen. No other big investment banks published reports on the stock. The volume turned down.

So I did the only smart thing. I sold my stock, and I shorted it to boot. Then I told the same people who asked me why I was buying the stock that I had shorted the stock. Over the next months, the stock sank into oblivion. In 1997, Gandalf filed for bankruptcy. Its shares were canceled – wiped out – a few months later. I wish I

could take credit for the stock going up, and going down. I can't. If the company had performed well, who knows what the stock would have done?

But the entire experience taught me quite a bit about how the market works. For years on end a company's price can have less to do with a company's real prospects than with the excitement it and its supporters are able to generate among investors. That lesson was reinforced as I saw the Gandalf experience repeated with many different stocks over the next 10 years. Brokers and bankers market and sell stocks. Unless demand can be manufactured, the stock will decline.

In July of 1998, my partner Todd Wagner and I took our company, Broadcast.com, public with Morgan Stanley. Broadcast.com used audio and video streaming to enable companies to communicate live with customers, employees, vendors, anyone with a PC. We founded Broadcast.com in 1995, and we were well on our way to being profitable. Still, we never thought we would go public so quickly. But this was the Internet Era, and the demand for Internet stocks was starting to explode. So publicly traded we would become and Morgan Stanley would shepherd us.

Part of the process of taking a new company public is something called a road show. The road show is just that. A company getting ready to sell shares visits the big mutual funds, hedge funds, pension funds – anyone who can buy millions of dollars of stock in a single order. It's a sales tour. 7 days, 63 presentations. We often discussed turning up the volume on the stock. It was the ultimate "Get Loud." Call it Stockapalooza.

Prior to the road show, we put together an amazing presentation. We hired consultants to help us. We practiced and practiced. We argued about what we should and shouldn't say. We had Morgan Stanley and others ask us every possible question they could think of so we wouldn't look stupid when we sat in front of these savvy investors.

Savvy investors? I was shocked. Of the 63 companies and 400-plus participants we visited, I would be exaggerating if I said we got 10 good questions about our business and how it worked. The vast majority of people in the meetings had no clue who we were or what we did. They just knew that there were a lot of people talking about the company and they should be there.

The lack of knowledge at the meetings got to be such a joke between Todd and I that we used to purposely mess up to see if anyone noticed. Or we would have pet lines that we would make up to crack each other up. Did we ruin our chance for the IPO? Was our product so complicated that no one got it and as a result no one bought the stock? Hell no. They might not have had a clue, but that didn't stop them from buying the stock. We batted 1.000. Every single investor we talked to placed the maximum order allowable for the stock.

On July 18, 1998, Broadcast.com went public as BCST, priced at 18 dollars a share. It closed at \$62.75, a gain of almost 250 percent, which at the time was the largest one day rise of a new offering in the history of the stock market. The same mutual fund managers who were completely clueless about our company placed multimillion orders for our stock. Multimillion dollar orders using YOUR MONEY.

If the value of a stock is what people will pay for it, then Broadcast.com was fairly valued. We were able to work with Morgan Stanley to create volume around the stock. Volume creates demand. Stocks don't go up because companies do well or do poorly. Stocks go up and down depending on supply and demand. If a stock is marketed well enough to create more demand from buyers than there are sellers, the stock will go up. What about fundamentals? Fundamentals is a word invented by sellers to find buyers.

Price-earnings ratios, price-sales, the present value of future cash flows, pick one. Fundamentals are merely metrics created to help stockbrokers sell stocks, and to give buyers reassurance when buying stocks. Even how profits are calculated is manipulated to give confidence to buyers.

I get asked every day to invest in private companies. I always ask the same couple questions. How soon till I get my money back, and how much cash can I make from the investment? I never ask what the PE ratio will be, what the Price to Sales ratio will be. Most private investors are the same way. Heck, in Junior Achievement we were taught to return money to our investors. For some reason, as Alex points out in The Number, buyers of stocks have lost sight of the value of companies paying them cash for their investment. In today's markets, cash isn't earned by holding a company and collecting dividends. It's earned by convincing someone to buy your stock from you.

If you really think of it, when a stock doesn't pay dividends, there really isn't a whole lot of difference between a share of stock and a baseball card.

If you put your Mickey Mantle rookie card on your desk, and a share of your favorite non-dividend paying stock next to it, and let it sit there for 20 years. After 20 years you would still just have two pieces of paper sitting on your desk.

The difference in value would come from how well they were marketed. If there were millions of stockbrokers selling baseball cards, if there were financial television channels dedicated to covering the value of baseball cards with a ticker of baseball card prices streaming at the bottom, if the fund industry spent billions to tell you to buy and hold baseball cards, I am willing to bet we would talk about the fundamentals of baseball cards instead of stocks.

I know that sounds crazy, but the stock market has gone from a place where investors actually own part of a company and have a say in their management, to a market designed to enrich insiders by allowing them to sell shares they buy cheaply through options. Companies continuously issue new shares to their managers without asking their existing shareholders. Those managers then leak that stock to the market a little at a time. It's unlimited dilution of existing shareholders' stakes, death by a thousand dilutive cuts. If that isn't a scam, I don't know what is. Individual shareholders have nothing but the chance to sell it to the next sucker. A mutual fund buys one million shares of a company with your and your coworkers' money. You own 1 percent of the company. Six weeks later you own less, and all that money went to insiders, not to the company. And no one asked your permission, and you didn't know you got diluted or by how much till 90 days after the fact if that soon.

When Broadcast.com went public, we raised a lot of money that certainly helped us grow as a company. But once you get past the raising capital part of the market, the stock market becomes not only inefficient, but as close to a Ponzi scheme as you can get.

As a public company, we got calls every day from people who owned Broadcast.com stock or had bought it for their funds. They didn't call because they were confused during our road show, were too embarrassed to ask questions and wanted to get more information. They called because they wanted to know if the "fundamentals" – the marketing points – they had heard before were improving. And the most important fundamental was "The Number," our quarterly earnings (or in our case, a loss). Once we went public, Morgan Stanley published a report on our company, as did several other firms. They all projected our quarterly sales and earnings. Would we beat The Number?

Of course, by law, we were not allowed to say anything. That didn't stop people from asking. They needed us to beat the forecast. They knew if we beat The Number the volume on the stock would go up. Brokers would tell their clients about it. The Wall Street Journal would write about it. CNBC would shout the good news to day traders and investment banks that watched their network all day long. All the volume would drive up the stock price.

Unfortunately, patience is not a virtue on Wall Street. Every day, portfolios are valued by at closing price. If the value of your fund isn't keeping up with the indexes or your competition, the new money coming in the market won't come to you. It just wasn't feasible for these investors to wait till the number was reported by companies each quarter. The volume had to be on the stocks in you fund. To keep the volume about a stock up, and the demand for the stock increasing, you needed to have good news to tell.

Volume, The Number, whisper numbers, insiders granting themselves millions and millions of options – these are the games that Wall Street plays to keep on enriching themselves at the expense of the public. I know this. I have tried to tell people to be careful before they turned over their life savings and their financial future to someone whose first job is to keep their job, not make you money.

Till I read The Number by Alex Berenson, I never had a book that explained how the market truly worked that I could tell my friends, family and acquaintances to read. I never had a book that would truly warn them that the market was not as fair and honest as mutual fund and brokerage commercials made them out to be. I may be a cynic when it comes to the stock market, but I am an informed cynic, and that has helped me make some very, very profitable decisions in the market.

If you are considering investing in the market, any part of it, or if you are considering giving your hard earned money over to someone else to manage, please, please read The Number first.

Mark Cuban, Dallas, Texas, January 2004