STOCKBOY

Columbia Asset Management, L.L.C. *April '18; Yr. 26, Issue I*

CEO's Win the Lottery, But Do Shareholders and Employees?

Tax Cuts for Who and for What?

Congress recently passed a record-breaking tax cut, mostly for businesses. Having studied economics, I'm unconvinced that cutting taxes, and thus increasing the deficit, makes sense--particularly when the economy has already been growing and improving. As investors, we'll see what the stock market thinks of the giant tax cuts in coming months. While the market experienced an early tax-fueled sugar-rush in January as the market vaulted higher, it's been sputtering since. I personally preferred the goldilocks economy we had– not too strong and not too weak. Weak economies have their obvious problems, but very strong economies have their own.

Toys Were Us

Toys R Us recently declared they are closing all their stores and shutting down. Though they were already fading when Bain Capital took Toys private and saddled it with huge debt, David Brandon (of Domino's Pizza and Michigan Athletic Director 'fame') appears to have done very little to help the situation. In fact, it's difficult to understand how Brandon could successfully petition the bankruptcy judge to allow millions of dollars in 'retention bonuses' to Toys R Us executives late last year. Soon thereafter, Brandon announced broad lay-offs of store employees and said Toys wouldn't be able to pay them promised severance pay. Soon after, Brandon broke the shut-down news and employees were let go and bondholders were stuck holding the bag.

Clearly, the internet has changed how we shop and has put great pressure on retail companies such as Toys. However, most retail stores are still doing reasonably well or at least staying above water. Those that aren't either have poor financials or haven't evolved with their customers' tastes. Toys had both problems. Brandon didn't make any notable improvements yet was paid handsomely as Toys burned to the ground. Why underperforming CEO's get overpaid is beyond me.

CEO (over)Pay – Will Knowing Help?

Corporate financial statements now must disclose their CEO's pay versus the firms's average employee. A recent *Stockboy* noted that CEO pay has moved to outrageous levels and gave the counterexample of the famed Herman Miller CEO Max De Pree, who chose to be paid only 20 times (20x) what the average Herman Miller employee made. Now, the average CEO makes well over 200 times that of their typical worker and some companies, such as Boeing, paid 650 times average pay last year. This information has hit the headlines but I'm not sure there's been much made of it by employees and shareholders….yet.

GE

GE has been part of the Dow Jones Industrial Average since its beginning over 100 years ago. Now, as GE's stock hovers in the mid-teens (half of what it was a year ago), some suggest it should be removed from the Dow.

What happened you ask? How could a company that holds leading positions in solid industries such as transportation, medical systems and power systems do so poorly in a growing world economy?? Doesn't GE employ many of the 'best and brightest'???

It's all true and thus GE's downfall has been quite remarkable. I must admit I'm very surprised how far it's fallen and that its former CEO (Jeff Immelt) seemed to have seriously dropped the ball. Immelt certainly seemed to make strategic mistakes in retrospect, but perhaps his larger problem was overseeing an organization that became fat and happy, to its own detriment.

Is it time to give up on GE and just look elsewhere? As a contrarian, I don't think so. In fact, situations such as these are often where you see corporate phoenixes rise from their ashes, at least with time. People love comeback stories and investors often overreact to surprisingly bad news which creates the conditions and circumstances of that comeback.

The keys to a successful turnaround include, first and foremost, a new leader who understands what the problems are and how to fix them. It's also important that the company have strong finances and market positions (which GE does) to have a good chance to turn things around.

With these traits, a company has the wherewithal to take the time to make the proper fixes on their own terms. Otherwise, they're dependent on their lenders, who often are neither patient nor creative.

GE's new CEO, John Flannery, seems to understand the problems GE faces and is taking notable steps to fix things both logistically and symbolically, including layoffs, stopping private jet travel and canceling or delaying unnecessary projects such as a new headquarters. Further, he's taken the opposite tack of the trend on Wall Street as he's slashed executive compensation and bonuses to reflect GE's struggles. This alone is a step in the right direction and an indicator that things are changing at GE.

If or when GE starts to show signs of improvement and regained glory, many of the same investors that have recently sold GE in frustration (or for appearances) will buy GE again, likely at a much higher price and after the 'easy' money has already been made.

Wells Far(to)go

Adding on to their problems from the fraudulent new accounts scandal, Wells Fargo now is being investigated by the state of Massachusetts for knowingly placing clients in higher-cost and/or inappropriate investments. This 'strike two' incident suggests there's a clear culture problem at Wells. The head of Wells' investment management group had this to say to his employees, confirming a lack of self-reflection: "We will get to the bottom of these issues and resolve them. Let's resist any temptation toward cynicism and negativity. Instead, I encourage you to dig deep, stay positive, believe in each other and the good work we do, serve our clients and lead each other forward. Never doubt that we are a great and ethical team serving the important needs of our clients and society. Let's keep marching forward on that noble path." During this year of cascading problems at Wells Fargo, its CEO was paid 291 times more than the average Wells employee.

Et Tu Bank of America?!

Not willing to let Wells have all the 'glory', Bank of America/Merrill Lynch paid $42 million to 'settle' allegations by the state of NY that they had purposely misled and hid important information from many long term clients. Specifically, they hid from institutional clients that Bank of America was making trades through high-frequency trading firms even though those clients specifically asked them not to. What kind of approach to business is that??

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