

# Being a Great Stock-Picker

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There are scores of great stock-pickers --- from Michael Price to Marty Whitman to Bill Miller, and many, many more. Great stock-pickers win over long periods of time, over a myriad of market cycles.

Of course, all great stock-pickers suffer short-term drawdowns. They all endure market cycles where their skills appear to be out of step with the market. But these are temporary bumps in the road. In games of strategy, those who are the most skilled always win if given enough time.

## Great Stock-Pickers Get It

I'm constantly surprised by the number of investors that I talk to who fundamentally misunderstand the stock market.

You can't win a game of strategy if you don't understand the game in the first place. With a flawed understanding of a game that requires skill, a player has only one chance to win: luck. And luck is a dastardly bedfellow, because it begets unwarranted confidence that leads to larger mistakes down the road.

Here I'll explain, briefly, the tenets of "the game" known as the stock market: All stocks are mispriced, some by a little, some by a lot. It is critical that investors understand that stock quotes do not reflect reality. In other words, stock values do not equal business values. At best, a company's stock quote will approximate the underlying business value. Frequently, though, a company's stock quote can diverge 40% to 50% or more from the business value.

For example, the business value at **Boeing (BA)** has not changed much over the last five years. Revenue and profitability metrics have barely budged, but the stock market value has fluctuated far beyond reason: from a low of \$20 billion to more than 3 times that level, or over \$60 billion. The current quote yields a market cap of \$53 billion. Look at the operating metrics and balance sheet change at Boeing over those five years. They have barely budged. It's obvious that the change in Boeing's stock value has vastly exceeded the change in the underlying business.

Boeing is not a unique case. Stock price fluctuation far exceeds business value fluctuation at most companies, including, for example, widely held, well-known behemoths such as **General Electric (GE)** and **Citigroup (C)**. Sales have grown modestly at GE over the last five years (up 20%), while the stock has cut a wide swath, ranging from a nadir near \$23 to a high near \$60. Lately GE has traded at \$37 per share.

Citigroup's stock quote has been less volatile than Boeing and GE, but the five-year high (about \$54) is still double the five-year low (near \$27). Meanwhile, the gross revenue at Citigroup has only slightly increased over the last five years -- it's up less than 5%.

Great stock pickers understand this simple fact: The purpose of the market is to provide liquidity, not to accurately price businesses. The central preoccupation of great stock pickers, then, is to identify and capture the spread when the stock value is materially below the business value.