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Apple is from Venus, Wall Street is from Mars

The recent kerfuffle over Apple's earnings report is a prime example of how companies and Wall Street can have very different perspectives. During the conference call, Apple's management spoke about the long-term prospects and opportunities for the company as well as its strengths and plans for new services and product categories. But many of the participating analysts were focused on a single number -- the company's gross margin and what it might be next quarter.

Wall Street firms typically rely on computer models in their investment decision-making process. These are usually spreadsheet-type programs that calculate a company's income statement over the coming quarters based on estimates and assumptions made by the analyst. Numbers such as gross margin are important inputs and analysts are always keen to verify their assumptions and update their models. Projected, or perceived, short-term trends in the spreadsheet -- for revenues, gross margins, earnings or other factors -- may then determine the analyst's rating for the stock: buy, sell or hold.

But the management teams of high-quality companies rarely think about their companies on a short-term basis. And top-notch teams know that Wall Street's focus is frequently not aligned with their own, especially with the current emphasis on short-term hedging and high-frequency trading. In reality, management's job is to manage the company for the long haul, not to satisfy Wall Street's hopes for next quarter. Some of the most spectacular collapses have occurred when management strived to meet Wall Street's expectations each quarter -- Sunbeam and Enron are two such examples.

At the end of the day, computer models are just tools, and are one of several in an analyst's kit. The danger is when they are considered to be the most important tool for reviewing a company. When analysts participate in conference calls with management and sit in front of their computers with their spreadsheet programs up and running, they run the risk of missing what management is really talking about. They may be listening, but they are not hearing what is being said. They are focused on their models and numbers while management is talking about something else entirely -- Venus and Mars conversing, but in different languages about different things.

The jury may still be out on Wall Street, but after listening to management and reading the transcript of the conference call, we are inclined to believe that innovation is still alive and well at Apple -- just not on Wall Street's timetable.

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