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Interview with Morris Mark
Founder and President, Mark Asset Management

Keeping the Equity Faith

By Lawrence C. Strauss

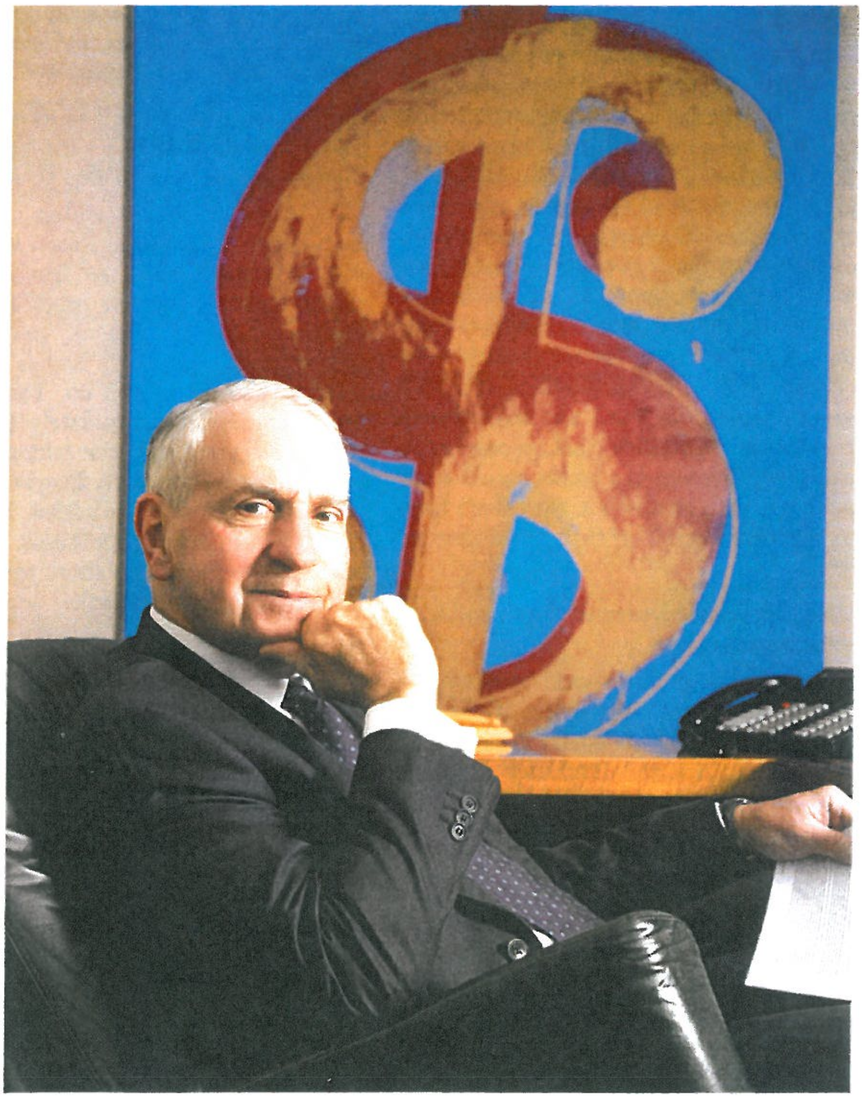
As an equities investor, Morris Mark has been through the wars, having started his career as a junior analyst in the late-1960s. In 1985, the Brooklyn College and Harvard Law School graduate went on to launch his own firm, now called Mark Asset Management. The firm, which primarily invests in equities, oversees about $500 million spread across hedge funds and separate accounts. Mark, 68 years old, is a growth-at-a-reasonable-price investor, avoids leverage, and likes to keep his portfolios concentrated, with the top 25 holdings usually accounting for 70% to 80% of a fund. He stresses the importance of fundamental research, and maintains that stocks are attractive relative to bonds and other alternatives. From April 1987 through early August of this year, the separate accounts managed by the firm had a composite annual net return of 11.82%, compared with about 8.3% for the Standard & Poor's 500 Index.

Barron's interviewed Mark recently at his office on Manhattan's East Side.

Barron's: **How do equities look relative to other types of investments?**

Mark: It seems to me that, risk-adjusted, equities are the single most attractive asset class that anybody could or should look at today. I emphasize risk-adjusted, because two years ago the financial system was at risk. And if the system is at risk, the other places you want to be are cash or government bonds that you have total confidence in. I consider the quality of the leadership at the Federal Reserve to be excellent. Fed Chairman Ben Bernanke really understood the issues, maybe a little late, but he understood them very well, and I believe systemic stability has been restored.

You mentioned in an interview with Kate Welling of welling@weeden late last year that the financial system had been pulled back from the brink, but



"There is no need for equity investors to try to gun their returns by using leverage. Keep your balance sheets simple."—Morris Mark

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Mark's Picks

Company	Ticker	Recent Price
Google	GOOG	$492.36
Coca-Cola	KO	55.81
Walt Disney	DIS	34.02

Source: Bloomberg

that it was still getting fixed. Has it been repaired yet?

No. 1, it will probably never be fixed the way it needs to be fixed. But No. 2, we have maintained confidence in our financial system. There is no run on the bank, and there is no run on money-market funds. Specifically, the spread between the interbank bank lending rates and the Fed-funds rate is less than 20 basis points [0.2 percentage point]. So in that sense, we have systemic stability. If you mean the financial-reform bill that was just enacted by Congress, it's a plus, although there are some things in that legislation that probably never should have been there. But by making derivatives more transparent and by encouraging the standardized versions of derivatives to trade on exchanges or openly over the counter, you will certainly eliminate one of the factors that created this systemic instability in the past. The banks in this country have effectively been recapitalized. As far as I am concerned, we have had the massive real-estate liquidation that people keep expecting, because the banks raised a ton of equity and, as a result, they don't have to aggressively sell off their remaining assets.

What's your assessment of the financial reform package?

Are there things that should be done that haven't been done? Absolutely. If you look at the structure of the equity markets, the SEC [Securities and Exchange Commission] is way behind the curve – and not just because of the Madoff thing, which was important but tangential. But consider things like leveraged indexes and high-speed trading. One very good friend of mine has said that the high-speed traders pull about $20 billion a year out of the system, whereas the people who preceded them, the specialists, only pulled out $200 million.

In commissions?

In hidden commissions, yes, because the spread is wider than it was under the previous system. People think they are using electronic trading at low commissions. But one thing we have learned from this is a simple lesson: Unless it is IBM on a very normal day, buy with limits, and sell with limits. You've got to know your prices, and you have got to act on that basis, because otherwise you just start giving guys market orders, particularly if they are of any size. The computers are faster than we are. They are not smarter, they are faster.

In deciding which companies to invest in, you put a lot of emphasis on finding quality management teams. What's your secret sauce for that?

There is no secret sauce. It is a lot of effort. We go to meetings. We go to conferences. We try to listen to and, if possible, meet with the people that are running the businesses. In the same way that somebody who invests with us is, in effect, going to judge us as a money manager, we view a CEO of a company as a money manager. They have assets and people they are responsible for, and you want to get a sense of their management ability.

You've been around the investment business a long time. What are the biggest changes you've seen on Wall Street?

Like the world, it has gotten a lot faster, because information flows so quickly and, to some degree, so freely. To the extent that you want to react to specific events or specific factors, you have to assume that everybody knows them at least as quickly as you do. The level of professionalism has absolutely improved. People don't get paid for taking guys to baseball games anymore. People don't get paid for perceived value added. Those are pluses. There are some minuses, including too much focus on the short term, but I wouldn't call them endemic.

What lesson did you take away from the financial meltdown of 2008-09?

I've seen really bad markets. I worked at Goldman Sachs from the mid-70s, when we were in the midst of what I thought was the worst market I would ever see, to the mid-80s. As for lessons, No. 1, don't take the system for granted. You can't be myopic and say, "I'm just a company investor, and I'm looking for great businesses." You have got to constantly be alert to what is happening to the system and the structure of the system. Secondly, and fortunately from my perspective, we never employed much leverage. There is no need for equity investors to try to gun their returns by using leverage. Keep your balance sheets simple.

Has the quality of investment research changed much since you got into the business?

Frequently, the best research we see is done by new analysts who are trying to establish their credibility. So they really give you a picture of an industry, a business, or a new industry, whereas many analysts – and don't get me wrong, many of them are fine analysts – are almost forced to keep focusing on what is happening this quarter. And they are forced to constantly be out there saying something and, therefore, they can't sit back and really say what is going on – what is really happening in the semiconductor business, for example.

You have got to go through a lot of stuff to find the best research, and it isn't because the analysts aren't good. It's because there is tremendous pressure to be very, very timely, to be very, very precise on a near-term basis and, indirectly, to generate business.

Let's hear about a few of your holdings.

I'll start with Google [ticker: GOOG].

A big concern for Google is its slowing revenue growth. What is the market missing?

First of all, the market is overlooking that you can buy quality today at no premium. Google is an example of that, as are IBM [IBM] and Coca-Cola [KO], among others. Secondly, the market is overlooking that Google's management is constantly improving its product and is constantly out there being willing to develop something internally or buy something externally to really make Google a better product for its users. And everybody was saying, "They've done a lot of things, but they haven't really paid off," but I don't believe that's totally accurate. One of the things that they did – buying YouTube in 2006, for example – appears to us just about ready to pay off in an extremely big way.

Why now?

For one thing, Internet television is here. As you go into 2011, just about every one of the major [television] sets that are going to be sold will be Internet-ready. Whatever you use, it is going to give you direct access to the Internet on your big screen. Now, I don't believe that means people are going to want to do their e-mail or write their reports sitting on the couch. But the use of YouTube and other things with video is huge. When you can get that on your TV set, there is the ability to leverage it with a lot more advertising.

What about another holding?

It's Coca-Cola, which trades at about 15 times 2011 earnings. Most people expect the company to grow at 10% per annum, and you get about a 3% yield.

On that basis, like a lot of quality stocks, it is attractive. This is a worldwide product. We recently came back from a trip to the Middle East, having been to Israel and Jordan. And in one way, there was no difference between the two countries: you go down the road and there is a Coca-Cola sign. You go to China and they're selling Coca-Cola. So the pervasiveness of the brand franchise and the pervasiveness of the distribution system are crucial, particularly as the world economy expands and as this new emerging middle class gets bigger and, on balance, wealthier.

By the way, this company has come up with a device that's going to be gradually installed in this country. It will give you the choice of more than 100 different drinks out of one fountain. It is not as though the management of Coke isn't aware that tastes are changing and that people are more health conscious or weight conscious. They are in the vitamin water business, for instance. Yes, they did miss the deal for Gatorade, which Pepsico [PEP] owns, but they are turning Powerade into an important business.

So what gets this stock higher? Expansion of its price-earnings multiple or higher earnings growth?

It's a combination thereof over time, and I really expect the rate of return on investment to go up. And if the rate of return on investment goes up, the rate of earnings growth will start to accelerate.

What makes you so sure that Coke's earnings-growth rate can increase? Growth of the global economy?

Yes, with a growing economy and with the implementation of some of the things the company has been doing.

Such as?

Coke Zero tastes just like Coca-Cola. Now, not everybody is going to like it. I've got friends who just love Diet Coke. Well, great. They are going to give you both, and they have the distribution system to give you whatever you want around the world. If you decide you don't want a sweet beverage for whatever reason, Coke has the ability to make a shift. And I think highly of the CEO, Muhtar Kent.

Let's get to one more pick.

I'll finish up with Walt Disney [DIS]. I go back to the premise that you can probably do pretty well owning quality stocks, so I like the risk/reward here. If the economy grows, that's good for Disney. But if I'm not as right as I want to be, we still ought to do all right.

Disney trades at a premium to the other media companies – such as Time Warner [TWX] and Viacom [VNV] – but not at nearly the kind of premium that I believe it deserves when you look at what management has done. I have nothing bad to say about these other companies. But, first of all, look at the franchises that have been acquired by the existing Disney management, including Pixar and Marvel. Second, the structure of the business allows the different profit centers to benefit from the stronger franchises as they evolve and strengthen.

What comes to mind?

Look at ESPN. They have it on the Web, and they have it in just about any paid TV form in this country and around the world. If there is one product you have to have if you're a paid TV distributor, it is ESPN. So they still have nice pricing leverage. And since they have a strong audience demographically, there are a lot of advertising benefits.

Also, their animation business has been completely revitalized with the acquisition of Pixar. You never know if any individual movie is going to do well, but Pixar is extraordinary, and it just makes Walt Disney's overall animation that much better. And every time Pixar comes out with a new character, Disney can create another attraction for its theme parks, and you can't replicate Disney's theme parks.

Barron's: Thanks, Morris. ■